Chapter 3

How to Procure and Purchase U.S. Grains and Grain Co-Products

This chapter will examines some of the key issues and actions an importer needs to consider and take when procuring and purchasing U.S. grains and their co-products.

These issues include the components of a contract, the use of standard contract forms, the use and role of agents and brokers, and the basic documents often required in the international shipment of grain. After studying this chapter you should be better equipped to purchase the best value grains in a competitive environment.

The first step in procuring feed grains from the United States is simple and often overlooked. In order to be able to make an effective value-based comparison between various grains, a potential importer should thoroughly understand and be able to clearly express clearly what type and quality of grain they require for its eventual end use. Next, the importer should have a detailed understanding of the quality characteristics for the grain on offer, along with a working knowledge of the underlying U.S. quality grades and standards that will apply. With this information an importer will be equipped to evaluate the value to them of various grain qualities and prices available from suppliers. The importer then can proceed to the next step of identifying a responsible supplier and making an informed purchasing decision.

FINDING A U.S. GRAIN OR GRAIN CO-PRODUCTS SUPPLIER

There are several ways an importer can discover the names and contacts of potential exporters of U.S. grains.

First, there are always the obvious well-known traders of international grain (such as ADM, Bunge, Cargill, and Louis Dreyfus – i.e. ABDC).

Second, you can inquire with a local or international trade association (such as the North American Export Grain Association or the U.S. Grains Council, both of which are addressed in more detail below) or a local chamber of commerce.

Third, you could contact the U.S. Department of Agriculture (also addressed in more detail below).

Fourth, a broker or local agent can assist you in finding a reputable seller and in facilitating a transaction with them.

Finding a Supplier

When contacting a potential supplier an importer should be prepared to provide commercial references, banking references, a description of the importer's business or international commodity trading experience, and any other information that demonstrates an ability to negotiate and fully execute an international grain purchase.

It is also reasonable for the importer to ask for similar information from the supplier to allow the importer to be comfortable with the supplier's ability to perform.

The following associations are available to assist importers by placing them in contact with interested suppliers:

U.S. GRAINS COUNCIL (USGC)

U.S. Grains Council
20 F Street NW, Suite 900,
Washington, D.C. 20001 U.S.A.
Phone: (202) 789-0789
Fax: (202) 898-0522
Email: grains@grains.org
Website: www.grains.org

The USGC is a private, non-profit organization with the goal of developing and expanding export markets for U.S. produced feed grains and their co-products through an international network of offices. All of these offices can assist importers with the search for a U.S. supplier.

An importer or potential importer can contact the USGC for assistance in either developing the technology to process feed grains for industrial uses or in providing information on the products themselves. The USGC will direct inquiries to one of their many internal experts on trade and utilization or to one of the 100-plus firms and organizations comprising its membership. The USGC also maintains offices in certain different countries plus consultants in many more to help importers with their feed grains needs.

The Council was founded in 1960 to develop and promote exports of U.S. feed grains and their co-products. It is one of the few organizations whose membership is truly representative of both producers and agribusiness interests. They have successfully coordinated and unified the efforts of both groups into a policy promoting the global expansion for the utilization of feed grains and their co-products. This manual is part of that effort.

USGC membership is comprised of over 140 organizations, including state checkoff boards, agribusinesses, and producer groups, who together form a unique partnership with the goal of building global markets for U.S. grains. Many of these members can be supplier of grain and can assist you in procurement and purchasing.

For more information about USGC members, and contact details, see the membership directory at: https://grains.org/membership/member-directory/#member_area_of_business=95 .

NORTH AMERICAN EXPORT GRAIN ASSOCIATION (NAEGA)

North American Export Grain Association
1400 Crystal Drive, Suite 260
Arlington, VA 22202 USA
Phone: 202-682-4030
Fax: 202-682-4033
Email: info@naega.org
Website: www.naega.org/

The North American Export Grain Association (NAEGA) is a not-for-profit industry trade association promoting policies, rules and commercial practices that support efficient international trade in grains, oilseeds and their derived products.

NAEGA members are exporters of U.S. grain and oilseeds in international markets. Established in 1912, NAEGA's members include private and publicly owned companies and farmer-owned cooperatives who export agricultural production to customers around the world. Our work benefits consumers, farmers and people working the trade.

NAEGA's mission is to promote and sustain the development of commercial export. Through a reliance on member action and support, NAEGA acts throughout the world to promote policies, rules and commercial practices that support international trade in grains, oilseeds, and their derived products. Providing for competitive, informed, robust, responsive, responsible, reliable, resilient, safe, and secure supply chains for agricultural commodities and food products is the core value of NAEGA.

UNITED STATES DEPARTMENT OF AGRICULTURE (USDA) - ATTACHES AND COMMERCIAL OFFICERS

The U.S. Embassy or consular office in most countries will house an agricultural attaché or commercial officer who is the overseas representative of the U.S. Department of Agriculture (USDA) Foreign Agricultural Service (FAS).

The agricultural attaché can offer the local importer a broad range of information regarding U.S. government-assisted export programs as well as assistance in finding a number of U.S. feed grains suppliers.

In addition to the above sources, interested importers might contact their local commercial banker or the branch office of a U.S.-based commercial bank for a list of potential suppliers.

USING AN AGENT OR BROKER

An importer also can utilize an agent or broker to assist securing a supplier and in the negotiation of the contract. Commodities brokers and agents serve as a point of connection between buyers and sellers and can help facilitate the purchase of grain. However, is important to know the difference.

An **"agent"** is a person or firm is authorized to act on behalf of the party that contracts with the agent; in our case either the supplier or the buyer. As an agent has authority to act they should not be representing both the supplier and buyer, and the party contracting with the agent should set clearly defined limits on, among other things, the agent's authority and territory, compensation, and the time period that the agency arrangement covers. Generally, an agent will have actual or constructive custody of the goods being supplied.

The party (supplier or buyer) that hires the agent is known as the "principal." Typically a principal will engage with an agent over a period of time, not for a particular potential transaction.

A **"broker"** is a person, firm or electronic trading platform that is engaged on behalf of others, at least partially on a commission basis, to negotiate or facilitate the formation of contracts for goods of which the broker has no actual or constructive custody of the goods being supplied.

The broker identifies potential suppliers and buyers and helps them work towards a contract, has no authority to bind either party or act on their behalf except as a supplier or buyer may give the broker specific instructions from time to time. Further, once the supplier and buyer enter into a contract, or if negotiations fail, neither the buyer nor supplier have any continuing relationship with the broker.

Using and Agent or Broker

It is important to note the difference between a broker of physical cash commodities and a broker of derivatives, futures, options and other exchange traded instruments, which are more highly regulated.

Brokers assist in the negotiation of a contract, working to put together the terms of trade that are agreeable to both parties. Upon the successful completion of negotiating a contract, a broker sends a written confirmation of the agreed contract terms and conditions to both the buyer and the seller. When the broker's contract confirmation is received, both parties should check the details for accuracy, and raise any omissions or errors with the broker immediately. This is extremely important, as it is the terms and conditions within the brokers contract confirmation that will often prevail or be persuasive in the case of any dispute over the terms or existence of a contract between the supplier and buyer.

Grain brokers may be a sole proprietor or can work at large brokerage firm or exchange. They may work within a locally or regionally defined market. Individual brokers may also be focused on a particular commodity or commodity group.

A grain broker typically takes fee or commission for each deal successfully arranged. This fee may be based on the quantity of the transaction, e.g. "per unit of grain" (i.e. bushels, metric tonnes, etc…), a "flat fee", or a "percentage fee" based on the value of the transaction. A broker should disclose these fees up front so that buyers and sellers are aware of the terms and whether the fees are acceptable. In most physical cash grain trades it is the seller who will pay brokerage fees.

Brokers who charge high fees may also offer special services as an incentive for parties who might otherwise turn down a relationship with the broker due to cost.

When selecting a broker it is important to use a reputable person or firm with whom a trusted relationship can be developed. Also ensure that they understand and have access to the latest applicable standard contracts and/or trade rules, as well as quality grades and standards.

PURCHASING UNDER DIRECT NEGOTIATION

Most end users and importers like to play an active role in the negotiation of contract terms and conditions for the purchase grain. They engage in direct negotiation with one or more suppliers.

Direct purchasing allows the buyer and the seller to negotiate alternatives that either may find more attractive and can significantly impact price and relative value of the commodity supplied. Importers can actively compare prices and determine the best time and supplier from which to purchase.

For example, an exporter may be able to provide an importer with a discounted price for accepting a shipment period that better suits the exporter's logistical situation.

COMPONENTS OF A CONTACT

Under contract laws in the U.S. the essential requirements of a contract are: 1) an offer, 2) acceptance of that offer, and 3) consideration. The law in most states in the U.S. also requires that contracts for the sale of goods between merchants with a value in excess of $500 be in writing.

In nearly all cases however this "writing" requirement can be met by any kind or writing; physical or electronic, including an exchange or emails.

"Consideration" is the value exchanged by both parties. In a grain sale the seller gives value in the form of grain, and the buyer gives value in the form of U.S. dollars or other money. While a contract requires some consideration, courts in the U.S. (and most arbitrators) will not look at the value of the consideration or whether it is reasonable. Any consideration will do.

An offer and acceptance can be shown by an exchange of emails or even text messages so long as the exchanges show that the parties have agreed on the basic terms of the transaction, such as price, quantity, quality, delivery terms, and the shipment or delivery period. Agreeing to only these basic terms is not, however, a recommended practice. The parties should agree in detail on the all of terms of their transaction, as described in mor detail below.

Occasionally the parties may dispute the existence of a contract, and its existence (or non-existence) and terms must be proven by evidence. On these occasions, a court or arbitrator(s) may be required to determine whether two parties had, in fact, entered into a contract. It will become the panel's or tribunal's role to make an objective finding of fact based on the evidence presented by the parties, on the balance of probabilities.

In order to avoid such disputes, effective communication and supporting records and evidence need to be maintained.

A more complete list of contract components commonly incorporated into a purchase/sale for agricultural commodities are likely to include:

Common Contract Terms & Conditions

- Name and details of Buyer
- Name and details of Seller
- Broker *(if any…)*
- Date and Time of Contract
- Kind and Quality Grade of Commodity
    - Type of Quality Inspection *(at Origin or Destination)*
    - Who does the sampling and grading (*e.g. U.S. Federal Grain Inspection Service)*
- Quantity
    - Type of Weights *(at Origin or Destination)*
    - Packaging *(Bulk, Bagged, etc…)*
    - Who determines the quantity (*e.g. U.S. Federal Grain Inspection Service)*
- Delivery or Shipment Period
- Transportation Specification
- Price - Price Basing Point *(e.g. FAS, FOB, CFR, CIF Location)*
- Payment Terms
    - Including who pays taxes, Levies and Statutory Charges
- Certificates and Documents, including who provides the certificates
- Applicable Trade Rules or Standard Form Contract Terms
- Applicable Dispute Resolution & Arbitration Terms
- Other Terms and Conditions specific to the transaction *(e.g. force majeure, circles, extension of delivery)*

Note that if the parties incorporate standard trade rules or a standard form of contract, they often do not have to specifically negotiate many terms of their contract, such as dispute resolution or arbitration, what constitutes an event of default, force majeure or extension of delivery. That's one of the beauties of using standard terms and forms.

Common Contract Terms & Conditions

Counterparties – Buyer / Seller

It is important to note on the written contract confirmation, both the Buyer and the Seller, clearly state the full legal name of the entities, along with complete contact information, including; their full physical address and place of business, telephone, fax, email.

Broker or Agent

If a broker or agent is engaged to facilitate the trade, their legal name, along with their full physical address, telephone, fax, email.

Time

It is also advised to note on the written confirmation the date, as well as the time, that the contract was concluded.

Kind and Quality Grade of Commodity

The contract should clearly state the kind, type or class, and quality of the commodity. For U.S. grain, most parties reference USDA grades. For co-products the contract should state a detailed description of the goods.

Also included here should be the type of inspection, and whether this is to occur at "Origin" or at "Destination". For all grain exported out of the United States grain quality is determined by an official USDA Inspector working for the Federal Grain Inspection Service (FGIS) according to established U.S. Grades and Standards. These official grades and standards govern the classification and grading of grain based on a number of qualitative factors.

The importer should clearly specify the maximum and/or minimum grade determining factors required and confirmed by an official export grain inspection certificate issued by the FGIS or an FGIS-authorized state agency.

The contract may also specify non-grade determining factors to which the parties have agreed, and identify the sampling, testing and certificate-issuing entity authorized to perform these tests.

For example: "U.S. No. 2 or better yellow corn, maximum 15.0% moisture. Aflatoxin maximum 20 parts per billion as determined by independent lab."

The more precise the quality description, the better the chance the importer will be pleased with the quality obtained. However, an overly restrictive quality requirement can lead to a much higher purchase price.

Quantity

The contract must specify the quantity desired and the exact unit of measure; (metric ton, long ton, short ton, hundredweight, etc…).

Common Contract Terms & Conditions

The quantity term is also likely to include a contract tolerance. For example +/-5% or +/-10% of the stated contract quantity, at the discretion of the seller or buyer. This tolerance allows the buyer (in FAS or FOB contracts) or the seller (in CFR or CIF contracts) the flexibility necessary to charter an appropriately sized vessel for the grain cargo, and to have the cargo loaded to the approval of the captain of the vessel. The contract should also specify the method that will be used to establish the price of the quantity above or below the mean contract amount. In most cases this tolerance is priced at the original contract price.

For example: "50,000 metric tons (5 percent more/less at contract price) at buyer’s option”

Also included here should be the type of weight certification that is to occur, and whether this is to occur at “Origin” or at “Destination”. Generally, for all grain exported out of the United States weights are determined upon loading by (or under the supervision of) an official USDA FGIS Inspector. The weight certificate is final at load and issued by FGIS or an FGIS-supervised state agency.

Occasionally, the weight determined at discharge will govern. In these rare cases, initial payment is still made for the shipped weight at load port, and an adjustment is made once the discharge weight is known. The discharge weight must be determined under procedures acceptable to the seller such as an independent surveyor. When an importer purchases grain using discharge weights as final, the exporter will usually add a premium to the price that reflects the normal estimated loss of grain in a discharge operation. Selling on discharge weights also raises difficult issues if the goods are lost or damaged, in whole or in part, during the voyage.

Shipment Period

The shipping period (or in some cases, the arrival period) should be clearly stated in the contract terms.

Delays, extensions or charges for late shipment/delivery are covered under the provisions of the NAEGA and Grain and Feed Trade Association (GAFTA) contracts, discussed later in this chapter.

For example: "50,000 metric tons (5 percent more/less at contract price) for shipment September 1 through September 20, 2003."

Transportation or Shipping Terms and Vessel Types

Tied closely with the shipment period and quantity are the shipping terms and the type of vessel that will carry the cargo. In a free on board (FOB) contract the importer provides the freight (i.e. charters the vessel, and the contract should specify:

Common Contract Terms & Conditions

1. The U.S. port or range of ports where the grain will be delivered, as well as the number of berths within the port from which the seller may deliver the cargo.

2. The type of vessel (a self-trimming bulk carrier, tween decker or tanker, for example) and a rate of loading (sometimes called a load rate guarantee), including a determination of when lay time will commence and how lay time will be counted to determine the total allowed loading time.

3. A statement declaring which party will assume the cost of spout stowing and trimming the cargo.

4. A demurrage/despatch rate.

5. A pre-advice period (the minimum number of days before arrival that the buyer will advise the seller of the vessel's expected arrival).

6. The rate of carrying charges the buyer will pay the seller in the event the buyer's vessel fails to file in the agreed upon period.

Many of these details are covered in the standard NAEGA No.2 Export Contract discussed later. The charter party - the contract for the use of the vessel between the importer and the vessel owner - will also cover some of these items.

If the contract requires the seller to provide the freight as a cost included in the purchase – a so-called cost and freight (CFR) - the contract normally includes a daily discharge rate at the destination port in place of the load rate guarantee, and specifies a minimum arrival draft at the discharge port and berth, maximum vessel age and any specific restrictions at the discharge port. The contract may also require the seller to provide insurance covering the cargo against loss or damage during the voyage. This type of sale is called a cost, insurance and freight (CIF) sale. The contract should spell out the minimum requirements for the cargo insurance. The general terms governing these types of shipments are covered in detail in the GAFTA contracts discussed later in this chapter.

For example: "FOB unstowed/untrimmed basis one (1) self-trimming bulk carrier, one (1) safe port/one (1) safe berth U.S. Gulf of Mexico. Load guarantee 5,000 metric tons WWD SHEX EJU with demurrage/despatch $8,000/$4,000/day. Buyer to give 10 days pre-advice of vessels probable readiness to load. Carrying charges shall accrue at the rate of 0.20 USD/metric ton per day, inclusive of interest."

Common Contract Terms & Conditions

Price

The contact will state an agreed upon price to be paid per unit of the commodity (e.g. metric ton or mt), usually stated in U.S. dollars.

The contract should also include another term related to the pricing of the quantity tolerance; that is how to handle pricing of the amount above or below the mean contract quantity.

The contract may also allow for component pricing. This is also sometimes referred to as a basis priced contract, or basis pricing. It refers to the separate pricing of the basis (a premium or discount often expressed in cents/bushel) which is used to adjust the price of an identified underlying commodity futures contract at the time the contract is priced. This is discussed at a later point in this manual.

Payment Terms

The most common form of payment is the confirmed, irrevocable, documentary letter of credit payable at sight. Other forms of payment exist, obviously, and depend in part on how financially secure and reputable the counterparties may consider each other to be.

The contract can also address which party is responsible for export and import taxes, levies and any statutory charges, though if the contract uses Incoterms® as its delivery terms (e.g. FOB, CFR or CIF) the Incoterms® address these issues.

Certificates and Documents

Closely associated with payment are the documents that the seller needs to present to the buyer in order to be paid, as well as which party is responsible for the costs of such documents. Courts have gone so far as to refer to export sales as sales of documents, not goods.

Common Contract Terms & Conditions

For example: "Prices to be quoted in U.S. dollars per metric ton." "Payment by irrevocable letter of credit payable at sight to be confirmed in the seller's favor by a first class New York bank in time to be in the seller's possession, in good order, 15 days prior to beginning of shipment period or within 10 days of contracting and payable against the following documents:

- Commercial invoice
- Full set of clean, on board ocean bills of lading issued to order of shipper
- Official weight and grain inspection certificates
- Certificate of origin
- Phytosanitary certificate"

A list of these documents and a brief explanation of each is included later in this chapter.

FOREIGN EXCHANGE RISK

A buyer and a seller who are in different countries rarely use the same currency. Payment is usually made in the buyer's or seller's currency or in a third mutually acceptable currency. In the international grain trade payments are normally made in U.S. Dollars.

One of the risks associated with foreign trade is the uncertainty of exchange rates in the future. The relative values of the two currencies could change between the time the trade is concluded and the time payment is made or received. If either the buyer or the seller are not properly protected, a change in the relative value of their local currency against the currency of payment could cause the seller to receive less, or the buyer to pay more, than originally expected.

For example: If the buyer has agreed to pay US$6,000,000 for a shipment of corn and the euro was valued at US$1.20 at the time of the transaction; the seller would expect to pay €5,000,000.

If later at the time of payment the euro had decreased in value to US$1.15, payment under the new rate would be €5,217,391.30, meaning a loss of $217,319.30 for buyer.

However, if at the time of payment the euro had increased in value to US$1.25, payment under the new rate would be €4,800,000, and the buyer would realize a discount of €200,000.

Nonetheless, many exporters and importers are not interested in speculating on foreign exchange fluctuations and prefer to avoid risks by adding certainty in the final payment amount.

Foreign Exchange Risk

One of the simplest ways to avoid the risks associated with fluctuations in exchange rates is to quote prices and require payment in U.S. dollars. Then both the burden of exchanging currencies and the risk are placed on the buyer. However, such an approach may result in losing export opportunities to competitors who are willing to accommodate their foreign buyers by selling in the counterparties' local currencies. This approach could also result in nonpayment by a foreign buyer who finds it impossible to meet agreed-upon obligations owing to a significant devaluation of his local currency against the U.S. dollar. While losses due to nonpayment could be covered by, for example, export credit insurance, such "what-if" protection is meaningless if export opportunities are lost in the first place because of a "payment in U.S. dollars only" policy. Selling in foreign currencies, if foreign exchange risk is successfully managed or hedged, can be a viable option for U.S. exporters who wish to enter the global marketplace and remain competitive there.

Importers should also be aware of any problems with potential currency convertibility. Not all currencies are freely or quickly converted into U.S. dollars. The U.S. dollar is widely accepted basis as the international trading currency; and as such, companies most frequently can often secure payment in dollars.

If the buyer asks to make payment in a foreign currency, the seller should consult an international banker before negotiating the sales contract and confirm the currency's convertibility. Banks can offer advice on any foreign exchange risks associated with a particular currency.

The most direct and common methods of hedging foreign exchange risk is a forward contract with an international bank. This enables the exporter to exchange a set amount of foreign currency at a pre-agreed exchange rate with a delivery date at some time in the future. Likewise, an importer can also establish a set amount of foreign currency payment at a pre-agreed exchange rate with a delivery date at some time in the future.

Determining a currency forward rate depends on interest rate differentials for the currency pair in question. The mechanism for computing a currency forward rate is straight forward and depends on interest rate differentials for the currency pair (assuming both currencies are freely traded on the forex market).

Foreign Exchange Risk

A currency forward contract is a binding contract traded in forex markets that lock in an exchange rate for a currency pair; i.e locking in an exchange rate for the purchase or sale of a currency on a future date. Currency forward contracts are over-the-counter (OTC) instruments, as they do not trade on a centralized exchange, and are also known as “outright forwards.”

Currency forward contract settlement can either be on a cash or a delivery basis, provided that the elected option for settlement is mutually acceptable and has been specified beforehand in the contract.

Unlike exchange-traded currency futures, the other major benefit of an OTC currency forward contract is that its terms are not standardized, and the terms and conditions can be specifically customized and tailored to a notional currency amount, and for any maturity or delivery period. In addition, and unlike listed currency futures and options contracts, currency forwards don't require up-front payments when used by large corporations and banks.

These contracts and financial instruments are generally used for hedging foreign exchange exposure.

U.S. REGULATIONS:

U.S. exporters and all purchasers of goods from the U.S. are subject to regulations which can place restrictions on the export or re-export of commodities to certain people, companies, organizations, governments and destinations. Exporters must present to the carrier or the U.S. Customs service a "shipper's export declaration" which names the ultimate and intermediate destinations of the cargo. The cargo cannot be delivered to any country that is not named on the declaration.

In addition, U.S. laws require that a "destination control statement" be stated on the originals and all copies of the bill of lading and commercial invoice. This means the importer must agree to accept documents bearing the destination control statement.

> **For example:** The United States law prohibits export and distribution of commodities to Cuba, Iran, North Korea, unless authorized by the U.S. government.
>
> [*The list of these countries is subject to change and does often change. All exporters and importers should be aware of these limitations.*]

U.S. exporters also are subject to U.S. regulations on restrictive trade practices or boycotts. Exporters may agree with and may be required to specifically reject requests that the exporter to refuse to do business with certain entities or countries, or otherwise participate in a boycott. Most of these prohibited or penalized boycott requests related to the Arab world boycott of Israel and Israeli goods and companies.

STANDARD FORM CONTRACT TERMS AND CONDITIONS

To help facilitate efficient markets and trade, the grain industry has developed several standard form contracts. It is estimated that more than 80% of the world`s trade in grain is shipped by contracts which incorporate one of these standard contract forms in whole or in part.

Standard Form Contracts

Standard form contracts are commonly a part of any export transaction of U.S. origin commodities. Importers should read and thoroughly understand the terms and conditions within these standard form contracts prior to initiating any discussions with potential trading partners that could incorporate such standard contract forms.

The two organizations who most commonly provide standard contract forms used in exports of U.S. origin grain are:

NORTH AMERICAN EXPORT GRAIN ASSOCIATION
1400 Crystal Drive, Suite 260
Arlington, VA 22202 USA
Phone: 202-682-4030
Fax: 202-682-4033
Email: info@naega.org
Website: www.naega.org/

We introduced you to NAEGA and what it does earlier in this chapter. NAEGA's standard contract is the so-called No.2 contract, which is an export contract on FOB delivery terms. Most parties that contract with reference to the NAEGA No. 2 contract also agree to incorporate its Addendum No.1. Addendum No.1 is called a Load Rate Guarantee addendum and so, among other things, specifies load rates and demurrage and dispatch rates. The NAEGA No. 2 contract and its Addendum No.1 are discussed in this chapter in more detail below.

GRAIN AND FEED TRADE ASSOCIATION
9 Lincoln's Inn Fields
London, WC2A 3BP
Phone: +44 20 7814 9666
Fax: +44 20 7814 8383
Email: post@gafta.com
Website: www.gafta.com

Standard Form Contracts

The Grain and Feed Trade Association (GAFTA) is an international, London headquartered trade association consisting of traders, brokers, superintendents, analysts, fumigators, arbitrators and other professionals in the international grain trade.

GAFTA is headquartered in Holborn, London and currently operates four more offices in Beijing, Geneva, Kyiv and Singapore.

GAFTA has many form contracts which are tailored to different trade terms and different origins and destinations. Some of the contracts used most often in the international grain trade include GAFTA contracts 27, 30, 64 and 100. GAFTA contracts 27 and 30 are discussed in this chapter in more detail below.

NAEGA NO. 2 CONTRACT – FREE ON BOARD

NAEGA No. 2 is the standard form contract for bulk grain sold on a Free On Board (FOB) basis from the United States and North America. This is NAEGA's only form contract other than NAEGA's Addendum No.1, which works together with the NAEGA No.2 contract.

See Appendix A for a copy of the NAEGA No. 2 form.

Some important features of the NAEGA 2 contract include:

Weight: Clause 5 states that the quantity is to be final at the port of loading in accordance with the customary weight certificates. In the U.S. these certificates are provided by FGIS, and in Canada by the Canadian Grain Commission (CGC). Note also the weight tolerance of 5% more or less at the buyers option in clause 4, and that the conversion of pounds to kilograms is specifically called out in clause 5.

Quality and condition final: Clause 7 states that the quality and condition are final at the port of loading in accordance with official inspection certificates. Delivery of higher grades of the same type and description is permissible.

Vessel nomination and delivery: Clause 8 states that the buyer is to provide or nominate to the seller the name of the vessel, its capacity and its date of readiness at the load port. This pre-advice must be made prior to the minimum number of days specified in the contract in order to allow the seller to have the cargo available for prompt loading. The pre-advice should be in writing and delivered to the seller by any means of rapid communication as stated in Clause 15. It is also the buyer's responsibility to advise the seller of any change in the vessel's date of readiness.

NAEGA NO. 2

The buyer may substitute a vessel once if the new vessel is of approximately the same size and type and can be ready around the same time. If the substitute vessel is damaged to the point of incapacitation, this clause allows an additional substitute vessel so long as it is also the same type, of approximately the same size, and in a position agreeable to both parties. Should the vessel arrive before the delivery period begins, the vessel may file its berth application and take its turn in the loading berth's line-up. However, the seller is not obligated to load the vessel before the delivery period begins.

Clause 8 states that delivery shall be made at the discharge end of the loading spout, in other words, FOB unstowed and untrimmed. All export elevators in U.S. loading ports charge fees for facility and/or use of the wharf, based on the vessel's tonnage, the cargo amount and/or the number of days berthed. The rates for facility charges are stated in the elevator’s tariff (addressed next), change regularly and may be different for each export facility in a specific port.

Elevator tariff: The first paragraph of Clause 8 of NAEGA 2 states that delivery is subject to the elevator tariff to the extent that the elevator tariff does not conflict with the terms of the contract. When the buyer's vessel files a berth application and is accepted by an elevator, the elevator tariff becomes part of the contract between the elevator and the vessel. Under this contract the vessel owner agrees to abide by the regulations of and pay the charges in the elevator tariff. The vessel’s berth application is usually accompanied by documents which include but are not limited to the following:

1. Certification by the USDA that the vessel's cargo holds are clear.

2. Certification by the National Cargo Bureau (NCB) of the vessel's readiness in all compartments.

3. Evidence that the vessel has entered at a U.S. custom house.

4. Evidence that the vessel has been tendered to and accepted by the charterer (buyer).

5. Written description of the vessel and the proposed stowage, also known as the stowage plan.

Once the berth application is accepted by the elevator, the vessel is assigned a berth in chronological order in relation to other vessels, based on when the vessel filed. However, the elevator tariff generally states that the elevator can change that order if operating difficulties arise or in order to operate more efficiently.

NAEGA NO. 2

The elevator can also require continuous loading of a vessel through 24-hour periods, with the overtime expenses charged to the vessel or split between the vessel and the elevator. Under most elevator tariffs if a vessel refuses to work overtime, it can be asked to vacate the berth in favor of the next vessel willing to work overtime.

Price: Clause 10 covers the price. The seller and buyer also need to agree on the load port(s) and berth(s) port/berth options allowed by the importer should be stated here. Clause 10 also addresses the methods used to establish a settlement price for any quantity loaded and shipped above or below the mean quantity but within the tolerance stated in clause 4.

As the quantity tolerance facilitates the vessel loading, many grain contracts simply specify that the tolerance will be settled at the contract price.

Advice of shipment: When the cargo is delivered to the vessel, the seller must advise the buyer of the delivery "without undue delay" as specified in Clause 13. This notice includes the vessel name, bill of lading date(s), quantity and quality. Some people call this notice a tender. In a CFR or CIF contract this notice is sometimes called a vessel appropriation.

Insurance: Clause 14 requires the buyer to purchase marine and war risk insurance with first-class approved companies and/or underwriters. The buyer must then make sure that the insurer provides the seller with confirmation of this coverage at least five days prior to the expected readiness of the vessel. Recall that in clause 8 the buyer must provide the seller with a "preadvice" of the vessel's probable readiness to load. The timing of the confirmation of insurance ties into this preadvice If the insurer does not provide a timely insurance confirmation, the seller may purchase the necessary insurance and charge the cost to the buyer's account.

Buyer’s failure to take delivery: Clause 18 specifies that the buyer is in breach of contract if the vessel “fails to file” before the delivery period expires. This reference to filing goes back to the language in the 5th paragraph of clause 8 concerning when a vessel is considered to be filed with the load elevator. If the vessel files late, the seller must hold (or “carries”) the grain for a limited period of time though at the buyer's expense. The expenses to hold or “carry” the grain are called “carrying charges.” Under NAEGA No.2 carrying charges are calculated as laid out in clause 19.

NAEGA NO. 2

Carrying charges, normally expressed as a fixed amount per ton or bushel per day, typically represent storage and insurance charges and can be inclusive or exclusive of interest on the delayed payment of the sales. Interest charges are assessed from and including the first day following the last day of the delivery period of the vessel. Charges for storage and insurance are calculated from the first day following the last day of the shipment period on only that portion of the cargo that has not been loaded, as verified on a daily basis by the stevedore's loading log.

Strike clause: The strike clause, Clause 20, applies if the seller cannot supply the commodity at the agreed-upon time due to certain events specifically listed in clause 20(b). To invoke this clause, the seller must promptly notify the buyer of the problem and, if requested by the buyer, provide a certificate from NAEGA certifying that clause 20 is properly invoked, and the duration and existence of the event. The benefit to the seller of invoking clause 20 is that the seller's obligation to deliver is suspended while the event (or “cause” as the term is used in clause 20) preventing or delaying delivery continues.

Arbitration: Clause 30 specifies that settlement of any disputes which may arise from or in connection with the contract should be settled by arbitration in the city of New York under the International Arbitration Rules of the American Arbitration Association (AAA). Each party appoints one arbitrator from the list of grain arbitrators maintained by NAEGA. These two party-appointed arbitrators then select a third arbitrator from NAEGA’s list of Special Grain Arbitrators. The arbitration panel’s decision is essential final as there is no appeal procedure within the AAA and the right to appeal to the courts is extremely limited.

Load guaranty: Addendum No. 1 loading rate guaranty is an optional part of the standard NAEGA 2 contract, requiring the seller to guarantee delivery to the vessel of an agreed, minimum tonnage during each weather working day of 24 hours (subject to the exceptions in Clause 1 of Addendum No. 1). If the seller fails to deliver at the agreed rate, the seller will pay the buyer a penalty, called demurrage, at an agreed rate. If the seller delivers the cargo at a faster rate than guaranteed, the buyer will pay the seller a premium, called despatch, at an agreed rate, usually half the rate of demurrage. Both the demurrage and despatch are paid for each day, pro-rated, of the time lost or saved. Addendum No. 1 includes such items as filing times, holiday time, overtime responsibilities, payment terms, documents necessary for claims and interest charges for failure to make payment on time. Importers should be fully aware of all the terms and conditions of this important and useful contract addendum as it is almost always included with the NAEGA 2 contract.

GAFTA 27 AND GAFTA 30

GAFTA publishes several standard form contracts.

GAFTA 64 is FOB Terms; however, NAEGA No. 2, along with its related Addendums, are more commonly used when grain is being shipped from North American locations.

GAFTA No. 30 is a standard contract for less-than-full cargo (parcels) bulk shipments of grain from the United States that are purchased under CFR or CIF terms, while GAFTA No. 27 is the CFR or CIF contract form for full cargoes. As mentioned, GAFTA has many standard contract forms. Buyers and sellers also often use the GAFTA 100 for bulk CFR and CIF sales when originating grain from other origins.

GAFTA 27 and GAFTA 30

A copy of current GAFTA Contracts can be found on their website at: https://www.gafta.com/All-Contracts

Some important features of GAFTA contracts include:

Quality and condition final: Under GAFTA No. 27, Clause 5 and GAFTA 30, Clause 6, quality can be determined by sealed sample, at discharge, or at load as evidenced by an official certificate of inspection at the time of loading. Where determined by an official inspections certificate at load, that certificate is final. Delivery of higher grades of grain of the same type and description is permissible.

Quantity: Under GAFTA 30, the tolerance is at the seller's option, with two percent more or less at the contract price and a further three percent more or less to be settled at the CFR or CIF market price on the final bills of lading date. If more than one shipment is made under one contract, each shipment is to be considered a separate contract, but the quantity tolerance of the mean contract quantity will not change.

Under GAFTA 27, the tolerance is 5 percent more or less at contract price and an additional 5 percent, at the seller's option, to be settled at the C&F or CIF market price on the final bill of lading date. It is also common, particularly under U.S. government export promotion programs, for all tolerances to be priced at the contract price.

GAFTA 27 and GAFTA 30

Weights: Under both contracts, Clause 18 for GAFTA 30 and clause 16 for GAFTA 27, specifies that the cargo quantity is weighed and determined at discharge. These GAFTA contracts also incorporate the GAFTA weighing rules 123, which users of these contracts should read and understand. Any deficiency from the bill(s) of lading weight (shipped weight) will be settled by the seller to the buyer; any excess, from the buyer to the seller. In each case, settlement is at contract price. In practice many or perhaps most grain contracts using GAFTA form contracts will agree to have weight, like quality, determined at the load port by a certificate issued by an official agency of the exporting country, or a recognized surveyor.

Extension: If the seller fails to ship the cargo within the specified shipment period the seller has an additional eight consecutive days in which to ship the cargo as long as the seller notifies the buyer by the first business day that follows the expiration of the original shipment period. The shipment date is determined by the shipped on board date stated on the bill(s) of lading. The extension clauses are Clause 10 in GAFTA 27 and Clause 11 in GAFTA 30.

These clauses also specify a formula to compensate the buyer for the extension, based on a percentage of the CFR or CIF price, and this amount is deducted from the original contract price at time of payment.

Strike clause: Both of these GAFTA contracts include a force majeure clause which suspends the seller's obligations during the period of the force majeure event. This is clause 21 in both GAFTA 27 and GAFTA 30. The event must fit within the specific events stated in the force majeure clause, and the seller must provide the buyer with notice within the time periods stated in this clause, along with a statement of the reasons supporting their declaration of force majeure. If the force majeure event continues for more than 21 days after the end of the shipment period, then the buyer has the option to cancel the unfulfilled portion of the contract, but to do so the buyer must notify the seller no later than the first business day after the end of this 21 day period.

Arbitration: Clause 28 of GAFTA 27 and GAFTA 30 specify that all disputes arising from the contracts will be settled by arbitration in London, England, in accordance with the arbitration rule No. 125 of GAFTA. Under this rule, the parties each appoint their own GAFTA-approved arbitrators who in turn choose a third arbitrator. GAFTA arbitration rulings can be appealed within GAFTA to a GAFTA-appointed panel of arbitrators. A party can also ask the English courts to review the award by the GAFTA appeal panel, though the courts are not obligated to take up an appeal. English courts will only hear an appeal of an arbitration award if the award presents novel or particularly important issues. Asking an English court to hear the appeal of an arbitration award is referred to seeking a "leave to appeal." See Appendix F for a copy of arbitration rule No. 125 of GAFTA.

GAFTA 27 and GAFTA 30

Insurance: Unless terms are CIF, the buyer is responsible for securing marine insurance. Clause 20 of GAFTA 30 and GAFTA 27 sets out the minimum insurance coverage that the seller must purchase. The requirements are detailed, and incorporate the GAFTA insurance terms No. 27. As of January 2022 the minimum coverage is "WA," which means "with particular average" , along with war, strikes, riots and civil commotion coverage.. WA insurance includes coverage if the vessel sinks, is stranded, on fire or in a collision (so-called FPA or free of particular average coverage), but adds coverage for damage caused by seawater or inclement weather. ARI or "all risk" is even more comprehensive as it covers all risks of physical loss or damage from external causes.

Appropriation (advice of shipment): FOB contracts require the seller to notify the buyer of delivery, while C&F and CIF contracts require the seller to notify the buyer of shipment. Clause 12 of GAFTA 30 and GAFTA 27 provide the appropriation clause in detail. Such a clause is required to insure that the buyer has timely notice of the vessel name, the date of the bill(s) of lading, the quantity loaded and the contract number to which the shipment applies. Remember that in a CFR or CIF transaction the buyer often will have little insight into what is happening at the load port as the seller is responsible for not only loading the goods onto the vessel, but also chartering in the vessel. Buyers therefore will sometimes hire a surveyor to monitor the loading operations.

BASIC DOCUMENTS ASSOCIATE WITH THE GRAIN TRADE

This section will take a closer look at some of the basic documents used in the international feed grains trade. These documents constitute the core of the transaction and are the mechanism by which title, or ownership, and the right to possession of the of the cargo is transferred from one party to another.

The specific documents required for any given shipment depend on U.S. Government regulations, the destination country's import regulations, importer's requirements, and mode of transportation, along with the contracts terms of sale and method of payment.

Slight discrepancies or omissions in documentation may prevent goods from being exported, may result in the shipper not getting paid, or may even result in seizure of the goods by U.S. or destination customs agents.

Basic Documents Associated with the Grain Trade

While completion of much of the documentation is routine for freight forwarders or customs brokers, the exporter is ultimately responsible for accuracy of the documentation.

The Draft: A draft is an instrument by which one party directs another party to make payment and/or acceptance. They are more often used when payment does not involve the use of a documentary letter of credit. In a draft, the exporter, who is requesting payment, is the drawer, and the importer, who is responsible for paying the draft, is called the drawee. In order to be negotiable, a draft:

1. Must be in writing and signed by the drawer;
2. Must contain an unconditional promise or order to pay a certain sum of money;
3. Must be payable on demand or at a fixed, determinable future time;
4. Must be payable to order or to bearer;
5. Must name the drawee or otherwise indicate the drawee with reasonable certainty.

Drafts can be drawn payable on demand and are called sight or demand drafts. Drafts also may be time drafts, which are payable at a later date. The type of draft depends on the payment or finance method used by the importer. The draft covering the export of grain and co-products from the

United States is generally expressed in U.S. dollars but may also be expressed in other currencies. The draft may be payable either to the drawer or exporter, but more often it is payable to the seller's bank. Exhibit 1 in Appendix G gives an example of a sight draft.

Commercial Invoice: The most common invoice used in the grain trade is the commercial invoice, which is a bill for the purchased grain. It describes the goods being sold and the amount to be paid by the importer, including any charges in connection with the shipment of the grain and typically states the terms of shipment (FOB, CIF or C&F).

The invoice should be dated and contain the name and address of both the exporter and the importer, the name of the vessel (or carrier), the port or location of loading and, in the case of a CIF or CFR transaction, and the name of the destination.

Basic Documents Associated with the Grain Trade

There may be additional requirements in order to comply with customs and exchange controls in the importer's country, including the use of an additional customs invoice. The description of the goods sold in the commercial invoice must correspond exactly with the description contained in the letter of credit if this payment method is used. The commercial invoice also should be consistent with the information contained in other documents accompanying the invoice. See Exhibit 2 in Appendix G for a sample commercial invoice.

In addition, some countries require a legalized or consular invoice to accompany the commercial invoice and other shipping documents. This invoice is simply a commercial invoice that must be presented, legalized and given a visa or stamp by the embassy or consular office of the importer's country.

Bill(s) of Lading: The bill(s) of lading is issued by the vessel owner and typically is signed by the vessel master or agents for the vessel, The bill of lading serves three functions. First, it is a receipt for the goods loaded. Second, it is a document of title as it gives the holder of the bill the right to possession of the goods (in the case of a bill of lading made out "to the order of" the consignee, or a bearer or blank consigned bill of lading), or to the person named as the consignee (in the case of a so-called straight bill of lading). Third, it is evidence of a contract of carriage between the vessel owner and the holder or named consignee. There are many standard form bills of lading. One often used in U.S. grain exports is the Baltimore Form C bills of lading. Whatever form is used, the bills of lading should show the name of the shipper, the vessel or carrier transporting the goods, the type of grain being exported, the port or location of shipment, the date that the goods were loaded on board, the destination, the consignee and the party to be notified upon arrival of the grain.

Bills of lading can be issued in two forms: "straight" (non-negotiable) or "to order" (negotiable). Some countries prohibit the issue of "to order" bills of lading. In such cases, the seller normally consigns the "straight" bill of lading to an agent or bank at the destination, with instructions to release the bill(s) of lading to the buyer only upon confirmation of payment. The shipping company should not surrender the bills of lading without the agreement of the agent or bank. If the "straight" bills are consigned to the buyer, the buyer can take possession of the goods upon identification without being required to present the bills of lading themselves.

Basic Documents Associated with the Grain Trade

Most bills of lading used in exporting feed grains are charter party bills of lading which are negotiable, in other words are consigned “to the order” or a named entity or just “to order." They are issued by the vessel owner in two or three original sets, each of which is negotiable. Thus, any one set gives the holder title to the goods. The presentation of any properly endorsed original will allow a holder to pick up the merchandise at the port of destination. The bills of lading may be endorsed in blank or endorsed to the buyer, his agent or some other third party.

Insurance Policy or Certificate of Insurance: The contract between the buyer and the seller should specify the extent and the value of insurance coverage for the feed grain, which party is required to obtain the policy or certificate and who must pay for the insurance. The coverage available under marine policies can range from specific risks, such as fire, collision or sinking, to general "all risks" coverage. However, all risks coverage does not necessarily cover war, strikes, riots and civil commotion. Such circumstances could require special endorsements or policies, such as war risk insurance.

Official Export Inspection Certificate: Under the U.S. Grain Standards Act, grain being exported must be officially inspected by USDA-licensed inspectors from either the Federal Grain Inspection Service (FGIS) or an FGIS-authorized state agency, who will then issue an official certificate showing the commodity type, class, grade, quality, condition and quantity of grain and the loading location. Some importers may also require a copy of the official grain inspection log, which is a record of the individual lots of grain that comprised the cargo. A sample inspection certificate is shown as Exhibit 4 in Appendix G.

Official Grain Weight Certificate: In addition to the official inspection certificate, FGIS or an FGIS-authorized state agency will issue an official weight certificate which indicates the net weight, date and place of issue, the name of the carrier, location of the grain, kind of grain and the date and time the loading started and finished. A sample weight certificate is shown in Exhibit 5 of Appendix G.

Phytosanitary Certificate: A phytosanitary certificate is issued by the USDA's Animal and Plant Health Inspection Service (APHIS) or an authorized state agency. The document certifies that the grain being shipped is free of quarantine pests and generally conforms to the phytosanitary requirements of the importer's country. A sample phytosanitary certificate is shown as Exhibit 6 of Appendix G.

Certificate of Origin: A certificate of origin is normally issued by the exporter and certified by a recognized chamber of commerce and certifies that the grain is a product originating in the United States of America. The certificate identifies the seller or the agent and the name of the carrier, and it gives a general description of the commodity. A sample certificate of origin is shown as Exhibit 7 in Appendix G.

Basic Documents Associated with the Grain Trade

Landing Certificate: While landing certificates are not required by the importer, the exporter may require this document.

When utilizing commercial U.S. government programs (namely, the GSM-102 credit guarantee programs and the Export Enhancement Program), exporters are required to obtain and maintain official records that can demonstrate to USDA the commodity actually arrived at the importer's designated destination. The records or documents must be in English or be accompanied by a translation acceptable to USDA.

Records acceptable to meet this requirement include an original certification of entry signed by an authorized customs or port official of the importing country, by the importer, by an agent or by a representative of the vessel or shipping company which delivered the commodity to the importing country or by a private surveyor in the importing country.

Important points which must be included in a landing certificate are:

1. Certification that the commodity entered the importing country;
2. Identification of the export carrier;
3. Quantity of the commodity sold;
4. Kind, type, grade and/or class of the agricultural commodity;
5. Date and place of unloading of the commodity in the importing country.

U.S. Export Requirements

The U.S. Government requires export documentation for a number of different reasons including national security, control of products in short supply, compiling export statistics, administration of export laws, protection of endangered species, and to protect U.S. export markets by ensuring product quality of specific exports.

The main document required by the United States government is the Shippers Export Declaration (SED).

Importing Country Requirements

Each destination country has different set of requirements regarding the documentation that must accompany any import shipment.

Importing countries require these documents for the administration of their import laws, assessment of taxes, and protection from hazardous pests and diseases.

Basic Documents Associated with the Grain Trade

Some of the more frequently required documents are: commercial invoice, bill of lading, phytosanitary certificate (for plants or plant products), veterinary health certificate (for animals or animal products), packing list, and certificate of origin.

Other import regulations that may affect a shipment are packaging and labeling requirements, and recycling laws.

Importer's Requirements

The importer may require documents in addition to the documents required by their government. An importer may need a specific document in order to receive an import permit from the local government, or to obtain financing from a financial institution.

Possible documents requested are: pro forma invoice, inspection certificate for grade and condition, or a statement of processing methodology (depending on the level of processing involved).

Other Documents: Some other documents often required by importers include:

- a certificate of fumigation, often provided by a certified fumigation company or marine chemist;

- a certificate from a private laboratory for quality tests not covered under the official grain inspection certificate;
- an official stowage examination certificate, stating that the vessel holds were duly examined prior to loading and found to be substantially clean;
- a crop year certificate, usually issued by the supplier, certifying that the feed grain loaded was grown in a certain crop year;

Basic Documents Associated with the Grain Trade

An experienced freight forwarder can assist shippers in determining what documents are required and can complete much of the documentation on the shipper's behalf.

Additional sources for determining documentation requirements for any given shipment are: bank, destination country's consulate, and;

- USDA's Foreign Agricultural Service http://www.fas.usda.gov/
- Animal and Plant Health Inspection Service - http://www.aphis.usda.gov/
- Food Safety and Inspection Service (http://www.fsis.usda.gov/

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