The new Food Supply Chain Law: key highlights

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On December 15, the Official State Gazette (BOE) published Law 16/2021, amending (once again) Law 12/2013, on measures to improve the functioning of the food supply chain (the Food Supply Chain Law or LCA, after its initials in Spanish).

The new law contains major new legislation for all the businesses participating in the food industry (affecting foreign companies for the first time). Here we analyze its key elements.

The past two years have seen a true revolution for the legislation on contracts in the food supply chain. This latest change was preceded by two other recent ones. The first, created in Royal Decree-Law 5/2020 of February 25, 2020 which we analyzed in this Garrigues Agribusiness commentary, made sweeping changes. And a few months later, Law 8/2020 brought a second change.

The stated purpose of this latest reform of the LCA, made in Law 16/2021, is to transpose into Spanish law the requirements in Directive (EU) No 2019/633 of the European Parliament and of the Council, of April 17, 2019. Although, one more time, the Spanish legislation goes far beyond the requirements in the directive and in the comparable legislation of a large majority of the member states and concerns itself with another type of rules of a protective nature, which bear no similarity to the EU instrument.

Our analysis of the various items of new legislation has to mention the following elements:

Broadened scope

Generally speaking, the new law continues to be applicable, in the same way as its predecessors, to the commercial relationships arising between operators participating in the food supply chain.

Having said that, for the first time a few parameters and rules have been introduced that considerably broaden its material, personal and geographic scope:

a. Geographic scope (Foreign Companies)

One of the amendments that we expect will have a greater practical impact is the inclusion for the first time of the specific territorial scope, with the introduction of rules with an extraterritorial reach affecting foreign companies.

Under the directive, any legislation on unfair trading practices (but only these practices) had to apply to commercial relationships between a supplier and buyer where

i. i. both are established in Spain or,

ii. one is established in Spain and the other in an ***EU member*** state, if the legislation of another member state is not expressly chosen.

In addition to that, an *ius cogens* rule has been also included so that the LCA will always apply where one of the parties is established in Spain and the other in a ***non EU country***, for matters relating to the "prohibitions contained in this law and the associated penalty rules determined for them in title V".

b. Material scope

- **New definition of "agricultural or food products"**

  After previously being defined only by reference to their intended purpose or use (products "intended to be ingested"), now they include additionally any products which are on the list in annex I to the Treaty on the Functioning of the European Union. This means that the LCA's scope will for the first time be considered to include products that are not intended to be ingested, such as, for example, cork, flax, hemp, tobacco or ornamental flowers, among others.

- **Disappearance of the former requirement for an imbalance**

  Another new feature is that the LCA has shed its former main restriction, which placed outside its scope scenarios in which no positions were in imbalance. Now, regardless of whether or not an imbalance exists, the LCA will be applicable in all transactions having a price above a threshold, which has been calculated to be reasonable, currently set at €1,000 under Law 7/2012, of October 29, 2012.

  It has kept outside its scope certain scenarios in which the lawmakers consider intervention and protection are not needed (in particular, transactions in which payment takes place in cash on delivery of the product).

c. Personal scope

Similarly, the number of entities subject to the law has been increased, by also including:

- **Catering, Hospitality and Accommodation**

  For the first time the personal scope has been broadened to include hospitality, catering and food service businesses, which now come under the legislation in the LCA where their gross revenues are at or over ten (10) million, and accommodation businesses (e.gr. hotels, cruise lines, etc) have also been brought within its scope where their gross revenues are at or over fifty (50) million euros.

- **Cooperatives and other associative agricultural entities**

  As a general rule, the law does not apply to supplies of products from a member of an agricultural association to such association, as long as members are required by bylaws to sell their products to their association. This would be the rule fir first, second or higher degree (agricultural) cooperatives, for agricultural product processing companies (SATs), for entities with a separate legal personality recognized as producer organizations (OPFHs), or to civil law partnerships and business companies primarily owned by the entities mentioned above, whenever they receive product from their members.

  Those associations do, however, have to instead fulfill the rules in article 8.1, consisting basically of the obligation to enter into a written contract with each member, containing the minimum elements determined in article 9, unless those entities' bylaws or agreements determine, before the delivery takes place, the procedure for determining the value of the product delivered by its members, the schedule for payment, and it is also specified that such agreements have to be notified in a verifiable manner.

It needs to be noted that this amendment introduces a very important new transparency requirement in the relationships between the associative entities (cooperatives and other common interest entities) and their members, as well as a potential trigger for disputes between them in relation to determining the value of the product and fulfilling any security that members may require.

It is important to notice that the special regime affects solely to the supplies between the member and the association, so that the subsequent sales from the association to its clients would be subject to the general rules, obligations and prohibitions.

I. Contracts in the food supply chain

The new law defines an agrifood contract (*contrato alimentario*) as a contract relating to the sale of food products at a certain price, which may involve either a purchase or a supply transaction.

It lays down in this respect that the contract must be formalized before the obligations start to be performed, signed by both parties and a copy must be held by each party. Therefore, unsigned documents would not be valid to these purposes.

This obligation to formalize contracts in writing (together with the other obligations introduced by the law for the first time) applies to any new transactions that will be carried out following the entry into force of the law, namely, **on or after December 16, 2021.**

For their existing contracts, operators **have been given until May 1, 2022 to adapt their terms to the law.**

The necessary terms in the contract are laid down in a broad set of minimum terms notably including the elements described below.

a. Determination of the price and the actual production cost

Although the EU directive being transposed stresses the freedom that the parties should have to negotiate the elements of the contract, including price, the law has stuck with the interventionist rules introduced for the first time by Royal Decree-Law 5/2020, which first wrote into Spanish law a ***prohibition for the buyer to "buy at a loss"*** or below the previous operator's costs (the comments we made here are still useful).

A number of amendments have been made to the restrictions on free negotiation by the parties of the buying price, in the following changes made to the two articles with provisions on this subject:

- **Article 9.1.c for primary producers**

This article, which has been in the LCA (though with some changes) since RD-Law 5/2020, states, among other requirements, that the price that a primary producer or a grouping of these producers has to receive under an agrifood contract must always be higher than the aggregate sum of the costs incurred by the producer or actual production cost.

Now an applicable rule has been added to that article which we believe to be useful from a practical standpoint for the businesses concerned, and we had in fact been recommending in conjunction with various associations in the industry. It involves allowing the producer to calculate those actual costs and for compliance with them to be verified, not for each transaction separately, instead by reference to all the sold produce of the same type for all

or part of their economic or production cycle, "which shall be allocated in the way that the supplier considers best fits the quality and characteristics of the products under each contract".

This amendment undoubtedly means greater flexibility for producers in relation to determining their production costs, which brings the law closer, on this point at least, to real-world agribusiness scenarios. The legislative technique is not free from defects which will cause interpretation doubts, although the intention is aligned, in this case, with the functioning and the needs of a large majority of agribusiness subsectors (which are neither linear or uniform in either the conditions of their products, or in the setbacks that may arise in a seasonal cycle).

- **Article 12 ter for other links in the chain**

The same flexibility is not given, however, in article 12.ter (the article defining the prohibition on buying at a loss for subsequent links in the chain), as would have been desirable.

That article only contains a few amendments geared mainly towards avoiding scenarios where, barring a few exceptional circumstances, the price determined in the final sale to the consumer is below the buying cost for the seller (this scenario had not been prohibited as such in the law, until now

Therefore, we continue to have serious technical problems needing to be solved. A few particularly obvious ones we could mention are a lack of clarity over the point in time that must be used to verify that the price is in line with the "costs incurred by the producer or actual production cost", given that these costs may be changeable (as they actually are in fact, and very). Do the costs that existed when the contract was signed have to be used? How else will buyers be able to know, when signing a contract, whether or not they are compliant with the law? What happens therefore if costs change after the contract is signed and before the product is ready for delivery? How then can they be called "actual costs"? A very careful drafting of the relevant clause will be of the essence to solve all these problems and to meet the real needs of the parties.

The law seems to be drafted considering only products that exist when the purchase contract is signed. It fails to take into account that in cattle farming, fishing and even more so in crop farming, products are bought before they are produced (at a time when the actual production cost is unknown –if their costs relating to electricity, water, plant health products or wages later go up–). What happens where the contract was signed with a price that covered costs, but those costs go up? Does a clause that was originally valid become null and void? Does that buyer become eligible for a penalty? These are a few of the main questions that the law still has to resolve and that the operator will have to solve in their contracts with the assistance of an expert advisor.

b. Payment terms and conditions

This point (maximum ***payment periods***) has probably caused the highest number of penalties of all due to the automaticity of their application and the strictness with which they are interpreted. The new article 9.1.d) gives another turn of the screw and now expressly prohibits the debtor from receiving any compensation, advantage or discount for fulfilling the terms in the contract (namely, for shortening its payment periods), as well as placing any conditions on payment.

c. Nullity as an expressly defined effect

A new article with greater consequences than might first appear is the new article 9.3, which expressly states that any clauses and terms precluded by article 9.1.c) are null and void. This article relates to determining the price and prohibits paying the primary producer a price below production cost.

Until now there were doubts as to whether administrative penalties were the only consequence of a breach of the law, or civil law penalties could also be imposed (on the understanding that nullity may be applicable to contracts precluded by mandatory laws). Therefore, this new article has two effects:

i. the first is clarifying that an infringement of article 9.1.c) carries nullity of the clause as a matter of law, plus a potential right to claim for damages and losses; and

ii. the second and no less important effect is clarifying by logical inference that an infringement of other articles in the law carries no more than an administrative penalty, but not nullity (including the very similar article 12 ter which also prohibits buying at a loss, although with the other operators coming after the primary producer).

d. Rules on sales negotiations

The law introduces a new article 9 bis relating to the negotiation of annual contracts. This section contains provisions that are particularly unusual in Spanish law. This could be the first time that the law (apparently) lays down a mandatory requirement that after a negotiation has started, an agreement must necessarily be reached no matter how far apart the parties' intentions. It does not stipulate either what must happen if, although negotiations have started, the parties fail to reach an agreement.

Moreover, it also states that, where an agrifood contract exists that stipulates renewal, the new terms of sale must be negotiated before the end of the term of the then valid contract or in a two month period following the end of its term. Within this period, the previous contract will remain valid, although it may be covenanted that the new terms of sale will be retrospectively valid from the expiration date for the previous terms and conditions.

On reflection, if the rule in this article 9.bis is ever actually applied in practice (a seemingly unlikely occurrence), it could cloud the environment or context for the parties' contract negotiations (and require them to take huge legal precautions and for pre-ensuring compliance with the legislation during their negotiating activities, which for trade to run smoothly in an industry, lawmakers should make easier and swifter to achieve, instead of creating obstacles).

e. Creation of an Agrifood Contract Register

In a new article 11 bis, the Food Supply Chain Law provides for the creation by the Ministry of Agriculture, Fishing and Food of a digital register on which must be entered any agrifood contracts made with primary producers and organizations of producers of this type, along with their amendments.

In view of the size of the industry in Spain and the number of commercial transactions that are signed every day, an extraordinary amount of paperwork will arise for businesses after this article 11.bis comes into force (special transitional rules are provided, until this new register is fully up and running).

f. Promotion clauses

A new article 12 bis includes rules on so-called promotional activities, containing detailed provisions on the limits that have to be covenanted in contracts in relation to what the law refers to as promotions. There is also an express description of the information that the end consumer must have in these cases.

II. Unfair trading practices

Another notable element is the inclusion of the catalog of trading practices regarded as unfair by the UTP Directive.

This really was the only element laid down by Directive (EU) 2019/633. However, the Spanish law has again gone further on this point in that it has considered it absolutely necessary to ensure bidirectional fairness in trading practices between any companies of any size. The directive, by contrast, aware of the real-world scenarios in the industry, starts out from the assumption that the catalog of activities regarded as unfair must be seen from the seller's standpoint, who is usually the first producer, so this approach is the minimum element to be included in the national laws.

The law includes in the catalog of practices the so-called black and grey practices of the UTP Directive. In other words, a set of practices –a few already contemplated in Spanish law– that EU lawmakers have concluded must be treated as unfair regardless (black practices) or may be unfair unless they have been expressly agreed by the parties in clear and unambiguous terms in their commercial relationships (grey practices).

- The first type, namely the black or especially prohibited unfair trading practices, as stipulated in the new article 14.bis.1, notably include the following, as an example or as a selection of those we consider to be most important in practical terms:

  i. where one of the parties to the agrifood contract requires payments from the other that are not related to the sale of the products (letter d);

  ii. where one of the parties to the agrifood contract cancels an order for perishable agricultural or food products with less than thirty (30) days' notice before the specified time (letter b); or, for example,

  iii. the buyer requires the supplier to pay for the deterioration or loss, or both, of agricultural and food products that occurs on the buyer's premises or after ownership has been transferred to the buyer, where such deterioration or loss is not caused by negligence or fault of the supplier (letter e).

  This last case will make it even more necessary for agrifood contracts to state the point when ownership and risk are transferred, because clauses determining a discount for deteriorated products after that point will no longer be allowed.

  Additionally, letter c) includes a prohibition of any unilateral change to the terms of the supply agreement for agricultural and food products; an element which, moreover, does not need to be stated because it is prohibited across the board in Spanish law (see article 1,256 of the Civil Code).

- The grey unfair trading practices (article 14 bis.2) are only prohibited if the parties have not previously agreed to them and this is stated clearly. The most notable examples include:

i. one of the parties being charged payment as a condition for stocking, displaying or listing its agricultural and food products, or making such products available on the market (letter a);

ii. one of the parties requiring the other to pay for the advertising of agricultural and food products that are sold by that first party (letter c); or, for example,

iii. the buyer returning unsold agricultural and food products to the supplier without paying for those unsold products or without paying for the disposal of those products, or both (letter f).

III. Infringements and penalties

In its provisions on penalties, the law adds the new practices not permitted by the legislation as described above as well as the resistance, the obstruction, or the refusal to cooperate with steps by public authorities and the disclosure of trade secrets.

Clarification is provided of the rules relating to the more serious classifications of repeated acts or omissions, by specifying that they will exist where the commission of a second or further infringement takes place involving a repeat infringement with another committed within a two (2) year period, from which it may be inferred that the infringement may simply be of the same type and equally serious, without having to involve exactly the same activity by the party concerned. Additionally, article 25 contains a detailed catalog of rules for graduating penalties.

A point very worth noting is the presumption in the new article 23.4 that the ***infringing party is the buyer***, unless proven otherwise, with respect to infringements relating to not formalizing a written agrifood contract, failing to fulfill the minimum terms requirement or failing to include the price in the contract, as required in article 9.1.c), which are all elements that operators will have to take well into account.

Added to this is the specification that the commission of any of the defined infringements cannot turn out to be more beneficial for the infringer than if they had fulfilled the law, which means that the final amount of any imposed monetary ***fines cannot be lower than the economic gain*** obtained by the infringing party.

IV. Confidentiality and advertising

From one angle, the new law creates an environment in which the confidentiality of ***whistleblowers*** (articles 29) is protected to encourage whistleblowing without commercial retaliation. Whistleblowers will also have various expressly defined rights, such as being able to know the status of the handling process of the report, the steps that have resulted from that process and any potential decisions.

The opposite policy has been adopted (by facilitating the distribution and disclosure of information) for infringing parties and penalties. Together with the financial penalties, the law has retained the public disclosure of decisions imposing serious and very serious penalties, which will include identification of the infringing party, the imposed penalty and the infringement giving rise to the penalty.

V. Other elements

a. Special arrangements

New special arrangements have been included for some specific products, such as that applicable for bananas from the Canary Islands, in a new additional provision seven in which drafting Garrigues has actively participated.

b. Reports on prices of food products

New paragraphs in article 20.1 provide for the future publication of certain reports and indexes for prices and production costs. The law does not expressly clarify whether they will be binding or are to be the mandatory reference to be taken into account for the purposes of article 9.1.c and article 12 ter (a matter which might, moreover, have compatibility issues with the legislation on the EU internal market and compatibility issues with EU competition legislation, in that they may be treated as "minimum prices" set by the government). Nonetheless, a coherent construction of this section with other sections of the law would require that it should be seen only as illustrative information for mere reference (bearing in mind also that the new article 9.1.c states clearly that producers will determine their prices and allocate their costs as they see fit, which would not be compatible with a different interpretation of these cost and price indexes).

The same reasoning would not apply, however, to additional provision three, under which the Ministry of Agriculture, Fishing and Food must publish within six (6) months from the full entry into force of the law the rules on the various factors or concepts coming into play for determining production costs in relation to calculating the minimum price under article 9.1.c., considering that these are rules (definitions) and not figures or amounts.

Entry into force

Law 16/2021 of December 14, 2021 entered into force on December 16, 2021, the day after its publication date in the Official State Gazette.

The obligation to register agrifood contracts as set out in article 11 bis of Law 12/2013 will enter into force when the register is fully up and running, in line with its implementing regulations, as specified in final provision six.

Lastly, the provisions in the new article 8.1 of that law for cooperatives and other common interest entities comes into force six (6) months after the entry into force of that law (namely, on June 16, 2022).

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