Dairy Heifer Contracting: Motives, Forms, and Arrangements

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Should a dairy producer enter a heifer-raising arrangement in which a grower raises the producer's heifers? Contracting when dealing with animals poses some special problems as the dairy producer is entrusting a grower with the herd's future. Not all animals turn out perfect, and the dairy producer must recognize that the grower does not have total control of the resulting product. A trusting relationship must be developed between the grower and producer, and the grower's results will be an important factor in developing that trust.

The purpose of this fact sheet is to identify important points a producer should consider when examining heifer contracting. Three topics are discussed: (1) reasons for entering a contract, (2) forms of contracting, and (3) the arrangement between the producer and the grower.

Reasons for Entering a Heifer-Raising Contract

Both the producer and the grower must gain from the heifer-raising arrangement; otherwise, they should not enter the agreement. The probability of having a successful raising arrangement increases if the producer knows the motives of the grower and the grower knows the motives of the producer.

Motives of the Dairy Producer

A producer's motives for entering a heifer-raising contract depend on whether the costs of raising heifers are high or low. A producer may have high raising costs if heifers are spread over many locations or are located far from the milking herd. In this situation, labor costs will be high because of travel time and other logistical problems. High costs may also result if it takes more than 24 months to raise heifers to first calving. Periods over 24 months of age to first calving generally increase heifer-raising costs by an average of $1.60 per day. In addition, high costs may occur if the producer is feeding poor quality forages. In a high-cost situation, a producer can use a heifer-raising arrangement to lower heifer-raising costs.

A producer raising heifers efficiently will have low raising costs. A "low cost" producer will not decrease raising costs by entering a heifer-raising contract. Generally, a grower cannot raise heifers at a lower cost than an efficient producer. A producer will have to pay a grower at least the cost of raising heifers; otherwise, the grower loses money. Even though growing costs will not be reduced, a producer with low raising costs may still find it advantageous to enter into a heifer-raising contract. Benefits from other areas may more than offset increased raising costs. Below are three potential benefits:

1. **Reducing investment outlays during an expansion**. Expanding the milking herd means that more heifers will be in the herd. These heifers often require additional housing. A producer can postpone or eliminate the need to invest in additional heifer housing by contracting with a grower to raise heifers. Funds that would have been used to build heifer housing can be used to invest in the milking herd or to reduce debt required for the expansion. A producer may be housing heifers in an area that could be used for milking cows. In this case, moving heifers to a grower would allow a producer to expand the herd with little investment in housing facilities.
2. **Streamlining labor requirements**. Eliminating heifer raising may allow a producer's labor force to focus on the milking herd. This focus may simplify laborers' job requirements by allowing them to perform assigned jobs more efficiently. Gains in labor efficiency may lead to an increase in the productivity of the milking herd.
3. **Reducing the nutrient load at one location**. Moving heifers to a grower reduces manure at the producer's locale, especially if the milking herd and heifers are housed at the same site. Eliminating heifer manure reduces inflows into the producer's manure storage system, reducing the number of times the storage must be emptied during a year. Moreover, the grower may be better able to use manure for crop production than the producer.

Motives of the Grower

Growers want to generate income by raising heifers for producers. The income needed by the grower depends on the situation. Some growers have existing facilities that are usable for raising heifers. These individuals may view contracting as a way of using existing facilities to supplement their income. Other growers may wish to make heifer raising an important income generator. These individuals may invest in facilities to increase the size of the heifer-raising enterprises.

Two factors affect the returns of the grower and should therefore be considered when deciding the payment provisions of the contract. The first is the number of heifers to be raised. A small number of heifers limits the return to the grower. Higher payments may be required in these cases. The second factor is the grower's facilities. Some growers will use existing housing, such as an old dairy facility, to raise heifers. These growers may not plan to replace the housing once it reaches the end of its useful life. Because replacement is not needed, contract heifer payments do not have to cover the facility's replacement cost. Other growers may invest in heifer housing and must cover the cost of the facility.

Forms of Contracting

Heifer contracts vary between each producer and grower. These contracts can be divided into four forms based on payment provisions:

1. **Per Day**

   The grower is paid on a per day basis. The current range of payment is between $1.45 and $1.70 per day. The grower generally provides and pays for all feed, labor, facilities, emergency veterinary services and supplies (e.g., costs incurred from the treatment of injury or illness), and other variable costs (Table 1). The producer generally pays for artificial insemination and routine veterinary services and supplies, including things such as vaccinations, parasite control, and other preventative health measures. If the heifer dies, the grower is paid up to the point the heifer dies and the producer accepts the loss of the heifer's value.

2. **Per Pound**

   Heifers are weighed when they are delivered to the grower and again when they are brought back to the producer. For example, the grower is paid on 1,000 lb of gain if a heifer weighs 200 lb when it is brought to the grower and 1,200 lb when it is returned to the producer. Per pound prices range from $0.65 to $0.85. If the price is $0.75, the grower would be paid $750 (1,000 lb x $0.75). The grower usually pays all feed, utility, bedding, and fixed costs. Artificial insemination and routine veterinary services and supplies are paid by the producer (Table 1). If a heifer dies, the grower loses the input costs of the heifer, while the producer loses the value of the heifer.

3. **Sell/Buy Back**

   The producer sells the calves to the grower and retains the right to repurchase the same animal prior to freshening. A variation to this arrangement allows the producer to buy back the same number of heifers as sold; however, the repurchased animals do not have to be the same heifers sold to the grower. As an example, the grower may purchase one-week-old heifers at $120 per head from the producer. The producer then purchases springing heifers for $1,200 per head from the grower. The repurchase price may be a market price or negotiated price. The grower pays all costs associated with raising the heifers and bears all death losses (Table 1).

4. **Full Contract**

   The producer provides the grower with all variable inputs, such as feed and medical supplies. The producer dictates to the grower how the heifers will be cared for and the conditions under which the heifers are managed. The grower provides the facility, utilities, and labor. The producer covers the grower's costs for labor and facilities as part of the grower's charge for rearing the heifers (Table 1). Death losses are born by the producer.

Table 1. Who is responsible for costs under alternative contracting forms?[1]				
	Contracting Form			
Who Pays For:	**Per Day**	**Per Pound**	**Sell/Buy Back**	**Full Contract**
Calf	Producer	Producer	Grower	Producer
Feed	Grower	Grower	Grower	Producer
Veterinary				
Routine[2]	Producer	Producer	Grower	Producer
Emergency[3]	Grower	Grower	Grower	Producer
Artificial insemination	Producer	Producer	Grower	Producer
Utilities	Grower	Grower	Grower	Grower
Bedding	Grower	Grower	Grower	Grower
Building	Grower	Grower	Grower	Grower
Labor	Grower	Grower	Grower	Grower

[1]The producer ultimately covers the grower's costs as part of the grower's charge for rearing the heifers.
[2]Routine veterinary costs include things such as services and supplies for vaccinations, parasite control, and other preventative health measures.
[3]Emergency veterinary costs include services and supplies necessary to treat illness or injury.

Choosing a Form

The four forms differ in three dimensions. Choice between the forms is influenced by the producer's and grower's desires along each dimension.

The first dimension is control. Control refers to how many of the heifer-raising practices a producer dictates to the grower. At one extreme is the full contract where the producer dictates all feeding, health, and breeding practices to the grower (Figure 1). At the other extreme is the sell/buy back form where the producer does not own the animal, and the grower is usually responsible for all feeding, health, and breeding practices. In the middle are the per day and per pound forms. Under these forms, the grower may be responsible for most of the day-to-day decisions. For example, the grower usually decides the rations to feed the heifers and where feed will be purchased. The producer, however, may dictate certain feeds that must be fed to the heifers.

The second dimension is who bears death losses. Under the full contract form, death loss is entirely the producer's risk (Figure 1). Under the sell/buy back form, the grower absorbs death losses. When a heifer dies under the per pound form, the producer loses the value of the heifer, while the grower loses the variable costs of raising the heifer. Under the per day form, the producer loses the value of the heifer. In addition, per day payments are usually made to the grower up to the day in which the animal dies. Therefore, the producer does not receive a return for the per day payments. If this is a major concern, the per day form can be modified so that the grower absorbs these losses. For example, the producer could stipulate that the grower will not receive per day payments for the last two weeks of a dead heifer's life.

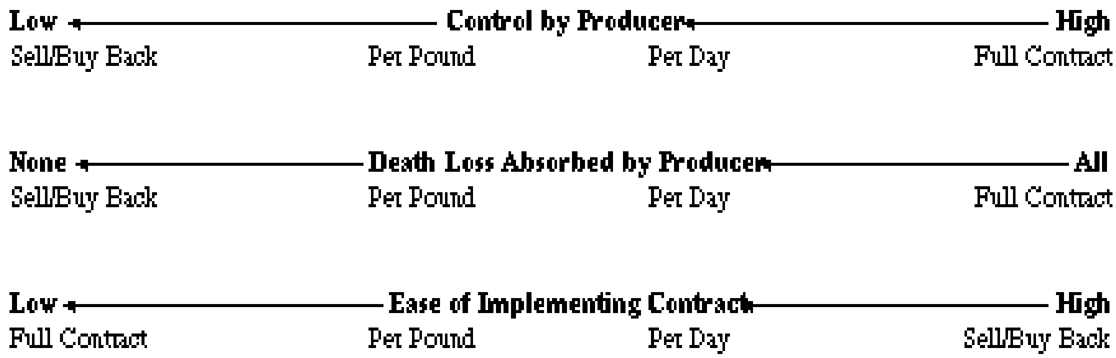

Figure 1. Comparison of contracting forms.

The third dimension is ease of implementing the contract. The two items that must be considered are: (1) supervision required by the producer, and (2) the ease of making heifer exchanges between the producer and grower. At the low extreme is the full contract form (Figure 1). This form requires the producer to provide a great deal of supervision. At the high extreme is the sell/buy back form. Under this form, the producer does not supervise the grower and exchanges can be made at preset prices. In the middle are the per day and per pound forms. Both forms require some supervision. The per day agreement is easier to implement than the per pound form because the heifers do not have to be weighed when they are exchanged.

Most producers should not use the full contract form. The supervision costs outweigh the benefits from additional control. Also, most producers will likely prefer the per day form to the per pound form. The per day form is easier to implement because heifers are not weighed when exchanges are made. However, the per day form causes the producer to bear more of the death losses. Given that few producers desire the full contract form and that the per day form is preferred to the per pound form, most producers will be choosing between the per day and sell/buy back forms. Examining the above dimensions can aid in choosing between these two forms.

The Agreement

A producer and grower who deal with each other consistently and fairly will increase the chances that both are satisfied with the contracting arrangement. Evidence of financial responsibility may be requested by the grower before entering into a contract, and payment must occur on time. A written agreement aids in laying out the framework for this relationship. When beginning the contractual arrangement, the first choice is which of the four forms to use. This choice will determine the payment type and who retains ownership of the heifers. Other items requiring consideration are:

Payment terms: The rate at which the grower will receive payment must be determined. For example, a per day charge must be determined if the per day form of contracting is used. Besides the rate, two other issues under payment terms may be considered:

1. *Rate adjustment*. Under certain conditions, the rate may be adjusted up or down. For example, the costs to the heifer grower increase as feed prices increase. The grower may require a higher rate when feed costs are high. These rate changes can be specified in the contract.
2. *Payment timing*. The arrangement should state when payments are expected. This issue is particularly important under the per day payment form. One alternative is to pay the grower at the end of each month. Another alternative is to pay the grower when the animal is returned to the producer.

Artificial insemination practices: In general, the following issues must be dealt with:

1. Who determines sires for the heifers?
2. Who is responsible for insemination (e.g., the grower, the producer, or a technician of the producer's choice)?
3. Who pays for the semen and insemination costs?
4. Who conducts pregnancy examinations?

Generally, the grower selects the bulls, is responsible for insemination, and pays for insemination under the sell/buy back form. These questions are negotiable under the per pound and per day agreements.

Health practices: The agreement can specify routine veterinary practices that should be performed. For example, the agreement can specify deworming, hoof trimming, external parasite control, vaccination practices, and pregnancy examination. In addition, the party responsible for paying the costs of these routine practices should be specified in the agreement. The agreement should also stipulate that the dairy producer must provide a healthy animal to the grower and meet the grower's demands for proper care prior to receiving the animal. The grower should have written procedures that the dairy producer must follow with all calves before sending them to the grower.

Other heifer-raising practices: Producers may specify any other practices they desire. For example, some producers may wish to specify the source of feedstuffs for the heifers.

Commingling of heifers: Some growers may commingle heifers from several producers. Producers may request that their heifers be kept separate from other heifers. If heifers are commingled, an aggressive health and vaccination program must be used.

Death losses: To a large extent, the party that absorbs death losses is determined by the contract form. However, specific terms can be negotiated. Under the per day agreement, determining when payments will stop needs to be stated. Payments often stop at the death of the animal; however, the payment could be stopped for the last two weeks the heifer was alive. This shifts more of the death loss risk to the grower.

Transportation: The basic question is who provides transportation of the heifers to and from the grower.

Animal identification: Animal identification is a must for determining charges under the per day and per pound arrangements. Identification may also be required if the grower raises heifers for several different producers. A permanent type of identification, such as tattooing or freeze branding, will aid in identification. In addition, a record of when the heifer arrives and leaves the grower should be maintained.

Length, renewal, and termination considerations: These specifications indicate how long the heifer-raising contract will be in effect, how it will be renewed at the end of the contract, and how it will be terminated. Of particular importance is indicating how the grower and producer will extend or end the contract. Knowing these issues will aid in future planning for both the grower and the producer.

Arbitration: In certain cases, disputes may arise between the grower and the producer. How these issues will be handled can be outlined in the contract. Often, independent parties are identified in the contract. These parties will seek to find a reasonable solution to the dispute.

The above issues should be resolved in a written form of agreement. In addition, the producer and grower should include heifer performance measures in the contract. This portion of the contract will outline general criteria for indicating whether or not heifers are performing up to standard. The following points should be addressed:

5. How long will the heifers be with the grower?
6. What is an acceptable percentage of death loss?
7. What is an acceptable percentage of non-breeders?
8. How large (weight, hip height, height at withers, or heart girth) are heifers when they are returned to the producer?

Having an understanding of these issues will aid in evaluating whether the arrangement has been successful. Some benchmarks for heifer performance are presented in Table 2.

Table 2. Performance benchmarks for Holstein heifers raised from 400 to 1,250 lbs.	
Item	**Benchmark**
Feed efficiency:	
Rate of gain	1.75 lb per day
Growth:	
Age at first calving	24 months
After calving weight	1,250 lb
Reproductive performance:	
Services per conception	1.5
Conception rate	75%
Death loss	Less than 3%

Source: Cady, Roger A. and Gayle Willett. Case Study of Contract Raising. Presented at NARES Conference on Calves, Heifers, and Dairy Profitability: Facilities, Nutrition, and Health, January 11, 1999.

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