

BRIEFING PAPER ON PROPOSED PACA TRUST REGULATION

THE PACA TRUST PROVISIONS

The purpose of the trust provisions of the Perishable Agricultural Commodities Act (PACA) is to assure that produce and its proceeds are used to pay produce suppliers. Congress decided the best way to accomplish this goal was to establish a trust. In a trust relationship, the trustee must hold the trust property for the beneficiaries of the trust.

The terms of the PACA trust are set forth in the PACA statute. The PACA statute first identifies what makes up the trust by stating that produce and proceeds of produce, that is, the money derived from sales, must be held in trust. This section also states who the beneficiaries are: unpaid suppliers until full payment is made. The exact wording of the statute is:

“Perishable agricultural commodities received by a commission merchant, dealer, or broker in all transactions, and all inventories of food or other products derived from perishable agricultural commodities, and any receivables or proceeds from the sale of such commodities or products, shall be held by such commission merchant, dealer, or broker in trust for the benefit of all unpaid suppliers or sellers of such commodities or agents involved in the transaction, until full payment of the sums owing in connection with such transactions has been received by such unpaid suppliers, sellers, or agents.” 7 U.S.C. §499e(c)(2).

The next section of the statute sets out what suppliers must do to remain trust beneficiaries – they must give written notice to the buyer of their intent to preserve the trust within 30 days after payment is due. If they do not give this notice, they lose their trust rights. This section also addresses when the 30-day notice period begins: either after the payment due dates in the regulations (normally 10 days from delivery), or “after expiration of such other time by which payment must be made, as the parties have expressly agreed to in writing before entering into the transaction.” USDA regulations state that “such other time by which payment must be made” can be no more than 30 days from delivery of the product. If the parties agree to a payment term in writing greater than 30 days, then the supplier loses its trust rights. So, under the statute and regulations, a supplier loses its trust rights by failing to give the proper notice of intent, or agreeing to payment terms in writing before the transaction that exceed 30 days.

WHY IS USDA PROPOSING TO AMEND THE CURRENT REGULATIONS?

When buyers fail to pay, suppliers attempt to work out a payment schedule rather than immediately filing a lawsuit or a PACA complaint. These are called post-default agreements, meaning that they occur after the buyer has the produce and the payment term has been breached. There is no further credit extended to the buyer; the supplier is simply trying to collect a bad debt. However, some courts interpreted

post-default agreements as extensions of terms. They concluded that because post-default agreements extend payment terms beyond 30 days, then any supplier with a post-default agreement waives its trust rights.

After these courts decisions, every past due produce bill became a minefield. Any discussion, email, or fax regarding the debt potentially meant a loss of trust rights. Suppliers who knew about the court rulings either had to immediately file a federal court suit after default, or have lengthy consultations with lawyers about what could and could not be said to defaulting buyers. Unsuspecting suppliers fell into a trap whenever the buyer failed to pay on time. As soon as the supplier agreed to a payment plan to avoid litigation, the trap was sprung and the supplier lost its trust rights. The court rulings were effectively making the PACA trust less useful and defeated the purpose of the trust by finding a waiver whenever a buyer failed to pay, which is the only time the trust is needed. The USDA Fruit and Vegetable Industry Advisory Committee, United Fresh, and many other allied partners requested USDA issue regulations to remedy these problems.

ANALYSIS OF THE PROPOSED USDA REGULATION

In response, USDA recently issued a proposed regulation for comment by August 9, 2010. After examining the proposed regulation, the proposal adopts a post-default waiver rule at odds with the trust provisions. A proposed regulation always includes a preamble in which the government explains the basis for the proposed rule. In the preamble to this proposed regulation, USDA explains the court decisions and says,

It is our interpretation of the statute and regulations that post-default agreements are not an extension of the 30-day maximum time period for pre-transaction agreements that would result in a waiver of the seller's trust rights; post-default payment agreements are an attempt to collect a debt. ... We do not believe that a seller's perfected trust rights should be lost because the seller enters into a payment arrangement, in an attempt to collect a debt, after the buyer has violated the PACA's prompt payment requirement.

USDA then states that only extensions of credit before the transaction, as stated in the statute, waive trust rights. USDA also explains that it has always ruled in the past that post-default agreements do not extend payment terms in deciding whether a buyer has violated PACA by failing to pay on time. Finally, USDA says that the law is that a supplier who meets the PACA trust requirements remains a beneficiary until the debt is paid in full.

These comments support a rule saying post-default agreements do not waive trust rights. Instead, USDA has proposed a rule that includes a post-default waiver very similar to the rulings of the courts that it means to correct. USDA proposes that if there are post-default agreements, they must be in writing and cannot exceed 180 days from the date of default. So if the post-default agreement is not in writing or exceeds 180 days, the supplier waives its trust rights. There is no explanation how the statute supports this new waiver of trust rights, and there is nothing in the

statute or legislative history to support it. Nor is there any explanation why there should be such a limitation. On the other hand, USDA's proposed post-default waiver contradicts the trust provisions as USDA explained in the preamble -- once a supplier fulfills the eligibility requirements (i.e. giving notice and not exceeding a 30-day term before the transaction) then the supplier remains a trust beneficiary until there is full payment.

UNITED FRESH ACTION PLAN

United Fresh has established a *PACA Trust Working Group* to look at this proposed regulation and develop a set of formal comments to submit to USDA. In addition the group will encourage industry stakeholders to send comments to USDA regarding their views on this important issue. The goal is to ensure that the PACA Trust provisions continue to be a robust industry tool for the commercial sale of fresh produce.

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