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VEGGIE WARS

PACA LAW UPDATE

Presenter

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PACA Legal Update

- Basic Training
- Skirmishes between PACA Beneficiaries
- Personal Liability Land Mines
- Disarming Non-Dischargeability
- Factoring Companies – Friend, Foe, Frenemy?





BASIC TRAINING: What is PACA?

- Perishable Agricultural Commodities Act
- Administered by United States Department of Agriculture
- Federal law established in 1930

- Code of Conduct/Rules of Fair Trade For Produce Industry
- Licensing
- Complaint process
- Unfair conduct
 - **FOCUS: Section 5 – PACA Trust (1984 Amendments)**

PACA Unfair Conduct vs. PACA Trust

Section 2 Unfair Conduct – VIOLATIONS:	Section 5 PACA Trust – FOCUS OF CASE DECISIONS
Make, for a fraudulent purpose, any false or misleading statement in connection with any transaction involving any perishable agricultural	
Fail to deliver good under contract	
Discard, dump, or destroy without reasonable cause	
Unfair, unreasonable, discriminatory, or deceptive practice in connection with the weighing, counting	
Misrepresent by word, act, mark, stencil, label, statement, or deed, the character, kind, grade, quality, quantity, size, pack, weight, condition, degree of maturity, or State, country, or region of origin of any perishable agricultural commodity received, shipped	
Fail or refuse truly and correctly to account and make full prompt payment	
Fail to maintain the trust assets	

How and why was PACA enacted?

- In 1930, Congress originally enacted PACA to provide protections to produce sellers (selling on short payment terms) in cases where a buyer failed to make payment as provided by contract
- State court collection lawsuits did not adequately provide protection
- Public interest to protect food supply and interstate commerce
- Fair and ethical trading
- Ensure orderly trading through supply chain

Who is subject to PACA?

PACA LICENSEE

- Person or entity licensed by the USDA-PACA

OR

DEALER: PERSON OR ENTITY

- Dealer in "wholesale and jobbing quantities"
- Buys or sells 2,000 pounds of perishable agricultural commodities in any given day
- In interstate or foreign commerce

AND

RETAILERS

- Dealer in "wholesale and jobbing quantities" †
- Purchase \$230,000 or more worth of fresh or frozen fruits and vegetables in a calendar year
- May include restaurants

FROZEN FOOD BROKERS

- Dealer in "wholesale and jobbing quantities" †
- Negotiate \$230,000 or more worth of fresh or frozen fruits and vegetables in a calendar year

What are the PACA Trust Provisions

Seller's Rights:

- Puts sellers of fresh and frozen fruits and vegetables in a **super priority status** in PACA Trust Assets in the event their buyers become insolvent or file for bankruptcy protection

What are the PACA Trust Provisions

Buyer must hold in **trust** until supplier is fully paid:

- all inventories of food or products derived from perishable agricultural commodities
- any receivables or proceeds from the sale of such commodities or products

What is the “PACA Trust?”

- Statutory trust designed to protect unpaid suppliers of perishable agricultural commodities
- Creates a ***trust relationship*** between unpaid seller and buyer
- Provides sellers with “super-priority” collection rights

What is the “PACA Trust?”

The PACA Trust shares the same basic legal components as any trust relationship:

- Trustee: the person responsible for managing the trust: owners, officers, principals. The trustee has the highest standard of care known as a *fiduciary* duty. [Buyer]
- Beneficiary: the person who will benefit from the trust. [Supplier]
- Trust Assets: the property belonging to the trust.

Trustee's fiduciary duties

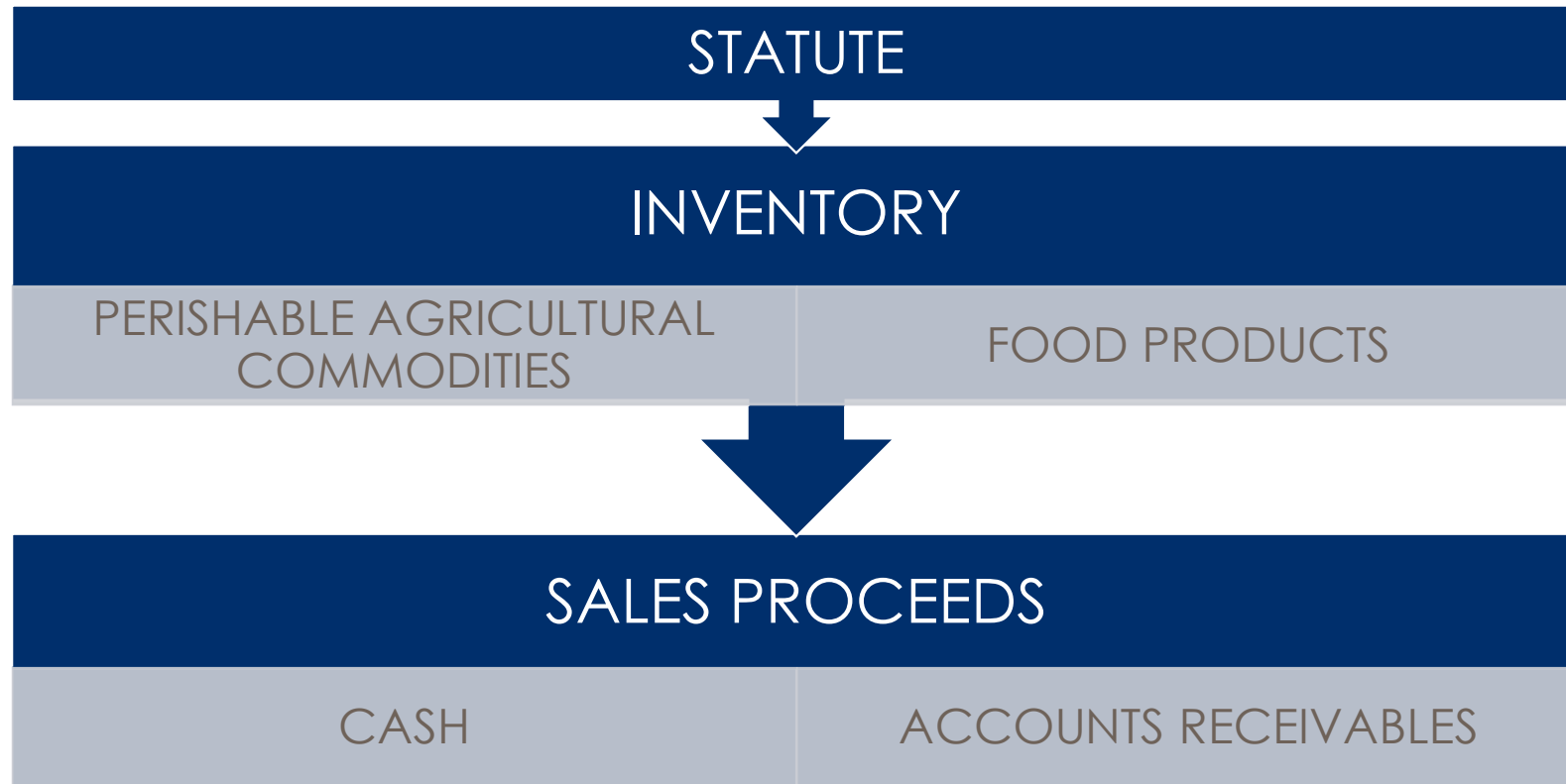
Trustee owes buyer *fiduciary duties*:

- Trustees are principals of the company in control of money
- Trustee will be liable to the Trust Beneficiary for not maintaining sufficient assets to timely and fully seller's PACA trust claim.
- Depending on degree of control of PACA trust assets, principals of buyer cannot discharge debt

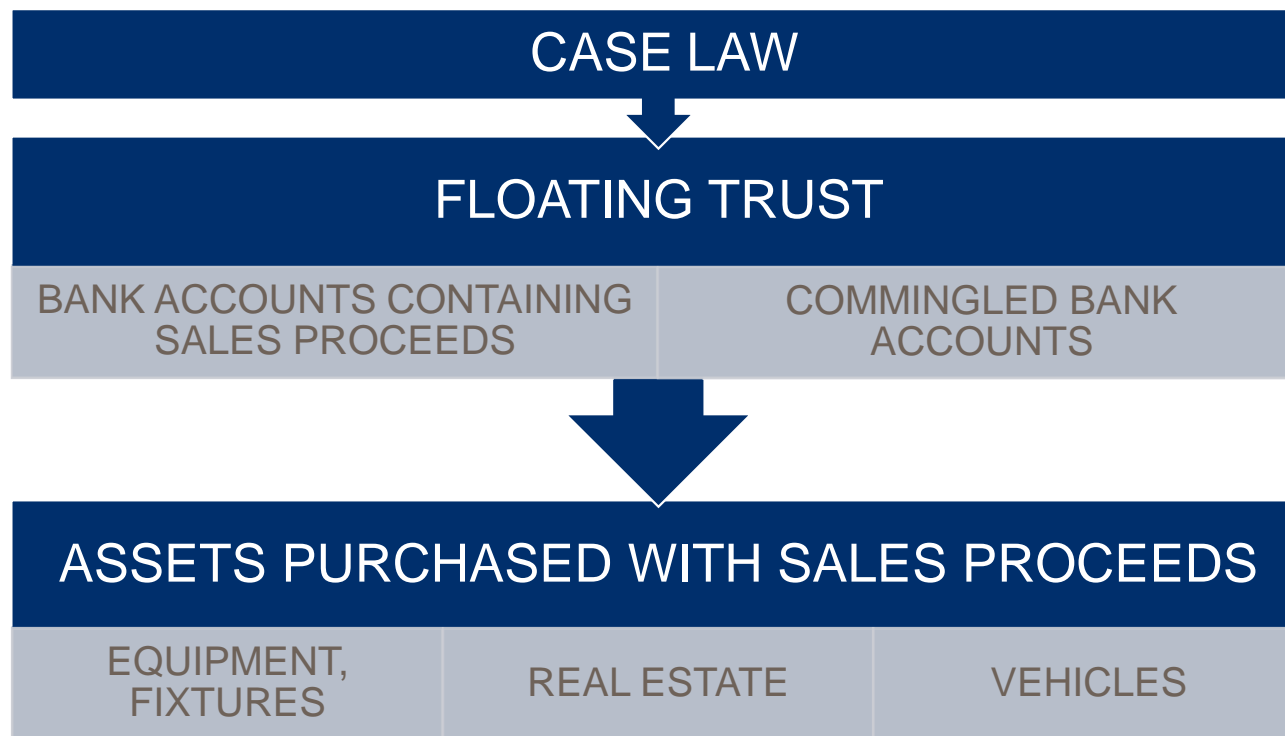
What are PACA Trust assets?

- Presumptively all the buyer's assets

What is a PACA Trust Asset?



What is a PACA Trust Asset?



What commodities are covered?

COVERED

- Fresh fruit and vegetables
- Frozen fruits and vegetables
- Adding chemicals to retard oxidation
- Water, blanching, hot oil spray
- Battering and coating

MAYBE

- Puree
- Dates
- Nuts

NOT COVERED

- Processing to change character
- Fresh fruit concentrate
- Dehydrated
- Cooked in oil

What are the elements of a valid PACA Trust claim?

COMMODITIES

- Covered fresh or frozen perishable agricultural commodities

INTERSTATE OR FOREIGN COMMERCE

- Perishable agricultural commodities moves or in contemplation of moving in interstate or foreign commerce

BUYER IS LICENSED OR SUBJECT TO LICENSE

- Dealers, wholesales, jobbers, commission merchants, brokers, and possibly retailers

PAYMENT TERMS

- Default PACA Prompt = 10 days
- CANNOT exceed 30 days

NOTICE TO BUYER

- Send written notice of intent to preserve PACA Trust rights within 30 days of when payment is due
- PACA LICENSEE: include statutory language on invoices

What is included in a PACA Trust claim?

Costs in connection with the sales transaction:

- Precooling and palletizing
- Gassing
- Freight
- Cold Storage
- Temperature recorders

- Attorney's fees (if provided for by contract, i.e. invoice or credit application)
- Interest/Finance charges

Preserving PACA Trust Rights

- *Send separate written notice to buyer of intent to preserve PACA trust rights within 30 days of when payment is due. 7 U.S.C. sec. 499e(c)(3)*
- *PACA licensees include this exact language on the face of each invoice (7 U.S.C. sec. 499e(c)(4)):*

The perishable agricultural commodities listed on this invoice are sold subject to the statutory trust authorized by Section 5(c) of the Perishable Agricultural Commodities Act, 1930 (7 U.S.C. §499e(c)). The seller of these commodities retains a trust claim over these commodities, all inventories of food or other products derived from these commodities, and any receivables or proceeds from the sale of these commodities until full payment is received.

Skirmishes between PACA beneficiaries

A wide-angle photograph of a rural agricultural landscape. The foreground and middle ground are dominated by neat, parallel rows of young, vibrant green plants, likely soybeans, growing in dark soil. To the right, a paved road runs parallel to the field. A red car is driving away from the viewer on this road, creating a cloud of dust or mist behind it. In the background, there are utility poles with power lines, a few trees, and a white building with a red roof, possibly a farm or processing facility. The sky is filled with soft, grey clouds, suggesting an overcast day.

PACA Trust Creditors of Lenny Perry's Produce, Inc. v. Genecco Produce, Inc. **853 Fed.Appx. 769.(2d Cir. 2021)**

- U.S.D.C., Western District of New York => Second Circuit
- Defendants-Appellants Genecco Produce, Inc. ("GPI") and principal appealed a judgment entered against them in favor of Plaintiff-Appellees, PACA trust creditors of the bankrupt produce buyer Lenny Perry's Produce ("LPP").
- Plaintiffs filed an adversary complaint to recover monies GPI owed to LPP.
- GPI and LPP each purchased and sold produce to the other resulting in GPI appearing in the bankruptcy as both a PACA Trust creditor and a PACA Trust debtor of LPP.
- Defendants argued that GPI's debt to LPP should be fully offset by its debts to LPP, a result which would lead to GPI recovering more than its pro rata share of the PACA Trust assets.
- By recommendation by Bankruptcy Court, the District Court for the Western District of New York held, inter alia, that (1) GPI's debt to LPP was an asset of the LPP PACA Trust that could not be completely offset by LPP's debt to GPI, but (2) GPI could, as a creditor of LPP, recover its pro rata share of the PACA Trust ("GPI's Share") and use that to offset its liability to the PACA Trust.
- The Second Circuit affirmed and returned the case the Bankruptcy Court for determination of a sum certain to be paid by GPI to the PACA Trust after the offset for GPI's Share.



Personal Liability Land Mines

S. Katzman Produce Inc. v. Yadid **999 F.3d 867 (2d Cir. 2021)**

- U.S.D.C., Southern District of New York => Second Circuit
- Defendant Eliran Yadid appeals a judgment - jointly and severally liable with his codefendants Orel Produce, Inc., and his dad, Moshe Yadid to pay PACA creditors \$473,268.82, plus interest and attorneys' fees.
- The court granted plaintiffs' MSJ holding Eliran liable on the ground that he was a person in control of the trust assets.
- Orel was wholly owned by Moshe, who was its only officer.
- Son claims Dad made all the decisions; took instructions from Dad.
- Son signed contracts and personally guaranteed equipment finance; signed checks including payments to produce suppliers; withdrew cash, paid himself a weekly \$900 salary and transferred \$40k 2018 into his personal bank account; claims dad instructed him and "he received no personal benefit."
- Son claims he worked part time, ran errands, made sales, signed checks when dad was unavailable.
- Son maintained near-daily text message contact with Plaintiff's controller as he attempted to work out Orel's debts; participated in meetings on behalf of Orel, without his father present, to make financial arrangements for the Company, and applied for a loan on behalf of Orel, overseeing the distribution of the loan proceeds.
- The suppliers contended that the son was an officer and director of the dealer corporations and had ordered produce from them and assured them that they would be paid.
- Under traditional trust principles: "[a]n individual who is in the position to control the trust assets and who does not preserve them for the beneficiaries has breached a fiduciary duty and is personally liable for that tortious act. ... [A] PACA trust in effect imposes liability on a trustee, whether a corporation or a controlling person of that corporation, who uses the trust assets for any purpose other than repayment of the supplier."
- Affirmed district court's ruling that Eliran as a matter of law is responsible for dissipation of \$40,000 of Orel's assets.
- Genuine issues of fact to be tried as to whether he had sufficient control of Orel's assets to make him liable for misuse of PACA trust assets, and that summary judgment was thus inappropriate.



Disarming Non-Dischargeability

In re Forrest

47 F.4th 1229 (11th Cir. 2022)

- U.S.B.C., Middle District of Florida => Eleventh Circuit => **Petition for Certiorari filed 11-30-22**
- The Forrests were owners of Central Market of FL, Inc. – failed to pay for \$261,504.15 for produce from Spring Valley Produce, Inc.
- The Forrests filed for Chapter 7 to discharge business debt.
- SVP filed adversary complaint objecting to discharge of debt under 11 U.S.C. § 523(a)(4) (defalcation while in a fiduciary capacity)
- Court looked at early Supreme Court cases - the Fiduciary Capacity Exception does not apply to trusts implied by contract but applies to technical trusts or trusts in the technical sense but doesn't define technical trust.
- Test to deterring fiduciary capacity:
 - ✓ A trustee, who holds
 - ✓ An identifiable trust res, for the benefit of
 - ✓ identifiable beneficiaries
 - ⊖ Fails trust-like duties of segregating trust assets and duty to refrain from using trust assets for non-trust purpose
- Resembles a constructive or resulting trust - PACA did not impose sufficient trust-like duties to create technical trust, and it did not impose duty to refrain from using trust-assets for non-trust purpose – not an exception to discharge.
- Affirmed.

Factoring Companies – Friend, Foe, or Frenemy?



In re Spiech Farms, LLC, **840 Fed.Appx. 861 (6th Cir. 2021)**

- U.S.B.C., Western District of Michigan => U.S.D.C., Western District of Michigan => Sixth Circuit
- Produce Pay is an agricultural financing company providing capital financing and market and trade programs to growers and distributors.
- Spiech was already indebted to Chemical Bank for \$4 million through existing secured loans, Spiech sought assistance from Produce Pay as a “multi-service finance company.”
- Spiech and Produce Pay entered into a “Distribution Agreement” that allowed Spiech to obtain short-term loans from Produce Pay as a partial advance on payments that Spiech was supposed to receive from its existing customers.
- Chemical Bank learned that Produce Pay filed a financing against Spiech’s assets and called the loans.
- Spiech filed for Chapter 11 bankruptcy relief.
- Produce Pay asserted a PACA Trust claim against the bankruptcy estate for \$1,002,273.70 to recover the cash advances it made to Spiech.
- After evidentiary hearing, bankruptcy court rejected Produce Pay’s claim and found that Produce Pay was not the supplier or seller produce because: (1) the Agreement did not explicitly identify what produce would be sold; (2) Produce Pay only learned what produce was “for sale” after it was registered on Produce Pay’s on-line platform; (3) by the time Produce Pay “bought” the produce, it was already delivered to Spiech's customers; and (4) Produce Pay did not receive a document of title until after a customer possessed the produce and title transferred to the customer.
- Court looked to the Second, Fourth, Fifth, and Ninth Circuits’ “transfer-of-risk test” to determine if it was a sale or a loan. The transfer-of-risk test entails four factors: “[1] the right of the creditor to recover from the debtor any deficiency if the assets assigned are not sufficient to satisfy the debt, [2] the effect on the creditor's right to the assets assigned if the debtor were to pay the debt from independent funds, [3] whether the debtor has a right to any funds recovered from the sale of assets above that necessary to satisfy the debt, and [4] whether the assignment itself reduces the debt.”
- Court found that Spiech did not sell Produce Pay its accounts receivables because Produce Pay assumed no risks with receivables collections. Spiech was tasked with collecting the accounts receivables and remitting one-half to Produce Pay. If Spiech's customers defaulted and Spiech did not remit the proceeds to Produce Pay within 30 days, Spiech was responsible for paying Produce Pay an increased “commission,” making default lucrative for Produce Pay and transferring the risk back to Spiech.
- Affirmed.

Produce Pay, Inc. v. Izguerra Produce, Inc. **39 F.4th 1158 (9th Cir. 2022)**

- U.S.D.C., Central District of California => Ninth Circuit
- Produce Pay is an operator of an online platform for buying and selling wholesale produce.
- In its complaint, Plaintiff-Appellant Produce Pay alleged that Defendant-Appellee Izguerra Produce, Inc. violated several provisions of the PACA and it also brought several state-law claims.
- After dismissing Produce Pay's PACA claims, the district court declined to exercise supplemental jurisdiction over the state law claims. Produce Pay's on-line platform connects growers in Mexico with distributors.
- Produce Pay obtains title to produce, but produce is shipped directly to distributor.
- Upon receipt distributor inspects and informs Produce Pay how much of the produce is marketable; distributor then sells on consignment and remits net proceeds to Produce Pay.
- Produce Pay takes a "marketplacings commission"
- Izguerra agreed to be a distributor on Produce Pay's on-line platform. Izguerra bore risk of not selling at "expected price" and receivable uncollectibility.
- April 2019, Izguerra bought 1,600 25-pound cartons of avocados on the on-line platform; Produce Pay invoiced Izguerra for \$70,560; outstanding balance was \$63,786.56.
- The district court granted Izguerra's motion to dismiss with prejudice concluding that as a matter of law Produce Pay was not a seller of wholesale produce and thus not entitled to PACA protections.
- District court applied the transfer-of-risk test articulated and factoring relationship involving in *S&H Packing & Sales Co. v. Tanimura Distributing, Inc.*, 883 F.3d 797, 813 (9th Cir. 2018) (en banc) and in *In re Spiech Farms, LLC*, 840 F. App'x 861, 863 (6th Cir. 2021).
- However, Produce Pay did not factor Izguerra's accounts receivable; it did not "loan" the avocados to Izguerra, did not take a security interest in Izguerra's receivables, and did not file a financing statement.
- Produce Pay properly and plausibly alleged the elements of a PACA claim: (1) the commodities sold were perishable agricultural commodities, (2) the purchaser was a commission merchant, dealer, or broker, (3) the transaction occurred in contemplation of interstate or foreign commerce, (4) the seller has not received full payment on the transaction, and (5) the seller preserved its trust rights by including statutory language referencing the trust on its invoice.
- Held that plaintiff plausibly pled that it was "seller" entitled to PACA's protections. Reserved and remanded.

Produce Alliance, LLC v. West Central Produce, Inc.
2022 WL 1285041, (9th Cir. 2022)

- U.S.D.C., Central District of California => Ninth Circuit
- West Central Produce entered into a Consent Order to allow for the orderly liquidation of West Central's PACA Trust Assets, and agreed to not remove, withdraw, transfer, conceal, pay, encumber, assign, sell or otherwise dissipate
- Consent Order defined Trust Assets to include "assets comingled with, purchased with maintain, or otherwise acquired with such proceeds"
- West Central acquired an assignment of certain produce suppliers' interest in PAA trust claims with checks from West Central bank accounts.
- Bank accounts contained funds that were commingled with the proceeds of non-Produce related goods.
- Assigned Litigation Rights became impressed with PACA trust because they were acquired with PACA trust assets.
- West Central then sold the Assigned Litigation Rights with a deep dispute to factoring company Produce Capital Group, Inc.
- ProCap asserted a PACA trust claim for \$4.1 million.
- Court affirmed district court's order voiding the transaction because it violated the Consent Order.

Questions

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