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Rynn & Janowsky AGRICULTURAL LAW NEWSLETTER

BEWARE: PACA TRUST LANGUAGE ON YOUR INVOICES MAY NOT GUARANTEE PROTECTION

In 1995, Congress amended the PACA trust provisions to provide a second -- significantly simpler - invoice method of protecting a supplier's PACA trust rights. Growers and shippers of perishable agricultural commodities enthusiastically embraced this "ordinary and usual invoice" method, principally because it is easy. It *appears* to merely require that suppliers print specific PACA trust language on their invoices.

This is an oversimplification of the law. As numerous suppliers have discovered from objections filed to their claims, the "devil is in the details." The newly minted and most troublesome "gotcha" is taken directly from the language of the statute: only "*licensees* may use ordinary and usual billing" to perfect their PACA trust rights.

The second "detail" that often draws an objection is payment terms, such as 14 days or 21 days, that differ from the USDA's "full payment promptly" standards. Debtors argue with some success that where payment terms are "extended" beyond the "prompt pay" standard, the PACA trust provisions require the parties to (1) agree *in writing* to these terms *prior to the transaction* and (2) to state accurately the payment terms on their invoices.

1. <u>Invoice Language Is For Licensees Only</u>

Although objections relating to the licensing are still winding their way through the courts, they are likely to be fatal to a claim, because the PACA trust provisions appear to *expressly* limit the invoice method of perfecting claims to USDA licensees. Consequently, if you are not a USDA licensee, the $100,000 claim that you think is protected by the PACA trust provisions may not be. The solution for non-licensees is: (1) obtain a license from the USDA or (2) comply with the cumbersome notice method of preserving trust benefits by giving the buyer a written notice of intent to preserve the benefits of the trust within the very short time periods mandated by the PACA. Of course, prior to applying for a USDA license, it is important to consider the obligations and responsibilities that accompany a license.

2. <u>Payment Terms Beyond 10 Days - Seller's Trust Claim at Risk</u>

A more routine, but significant, objection to PACA trust claims is triggered by payment terms that differ from the USDA's prompt pay requirements (the most common is 10 days from acceptance). Generally, the court claims procedure will require that PACA trust creditors attach any *written* agreement reflecting the parties' payment terms. When a supplier with payment terms in excess of 10 days is unable to produce the agreement, objections inevitably follow.

And while there are several

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circuit court of appeal decisions holding that lack of a written agreement is not fatal when a licensee has the statutory language on the invoice, there is no Ninth Circuit (covering Western U.S.) opinion directly on point. The simple remedy is to insist on 10-day prompt payment terms and indicate so on your invoices.

3. Written Agreement with Buyer to Accept Payments Over Time May Void Trust Rights

Finally, a seller's payment terms should *never* exceed 30 days; if they do, the seller loses the protection of the PACA trust. This issue frequently arises when a buyer is behind in payments. The buyer informs the seller that it will pay $20,000 a week, until the entire $60,000 is paid in full. Because the buyer is months in arrears, the seller quickly agrees, but demands that the agreement be reduced to writing. Most debtors will argue that by entering into this agreement, the seller waived his PACA trust rights, because the agreement extends payment terms well beyond the maximum "30 days after receipt and acceptance of the commodities."

The preferred, although by no means ironclad, alternative is to inform the buyer that payment terms are 10 days from acceptance (or whatever they may be) and those terms will not extended. You may also advise the buyer that because of the costs of litigation, you will delay filing a lawsuit pending receipt of the payments.

4. Conclusion

In summary, if you are not a USDA licensee and you are using the invoice method of perfecting your PACA trust rights, you should immediately consult an attorney knowledgeable about PACA trust matters. Some other action may be required to qualify for PACA trust protection. If your payment terms exceed 10 days or they vary from the USDA's prompt payment standards, you should strongly consider changing them. Otherwise, you should (1) secure a written agreement extending payment terms from your customer prior to any transaction and (2) print the payment terms on your invoices. Finally, never enter into a written extended payment plan with a buyer unless you have first consulted with an attorney knowledgeable in PACA trust matters.

HOW TO PROTECT YOUR CARGO CLAIM

If you are exporting your product using an ocean carrier, you have likely encountered various situations involving in-transit damage to the goods upon arrival and the problematic claims procedure that follows. Because most perishable shipments are uninsured, it is important to protect your claim even before the product leaves the warehouse.

1. COGSA Will Apply

The shipment of goods of any kind from the United States overseas is governed by The Carriage of Goods By Sea Act (COGSA) 46 U.S.C. 1300 et seq. This statute governs the transaction from the time the goods are loaded on board the ocean carrier to the time they are discharged from the vessel. However, COGSA generally applies from the time of receipt until delivery by virtue of common extensions found in the bill of lading.

Because different elements of proof and defenses exist under COGSA, there are certain steps that may be taken, rendering your cargo claim less susceptible to defenses by the ocean carrier. Below is a checklist that may allow for a greater likelihood of success against the carrier. Providing your consignee or agent overseas with this checklist may keep you out of court and leave more dollars in your pocket.

2. Steps to be Taken Before Shipment

(1) Get a pre-shipment inspection.

(2) Make sure to place a Ryan Recorder or other temperature-recording device inside the container.

(3) When the truck arrives, make sure the container is pre-cooled to the proper temperature.

3. Steps to be Taken After Arrival of the Cargo:

(1) After arrival of the container, immediately inspect the cargo before signing the delivery receipt.

(2) Provide written notice of the damage to the carrier.

(3) Immediately contact a surveyor to assess the loss or damage.

4. Make Sure Your Surveyor Includes the Following Information:

(1) The date the shipment arrived at destination and the date it was made available for survey.

(2) The date the survey was performed and the date the report was written.

(3) The number of packages present and available for survey.

(4) All label information and markings on packages, as well as lot numbers.

(5) Pulp temperatures taken in random places with notations as to where the temperatures were taken.

(6) Sampling procedures should be described and show that they were randomly selected.

(7) Each defect must be described in detail. General conclusions are not acceptable.

(8) The percentage of the cargo damaged should be described.

(9) Temperature recording devices such as the Ryan Recorder, Partlow Chart, or Temperature Download should be retrieved by the surveyor. A clear copy of one or each of these records should be attached to the survey. If the surveyor is unable to secure these devices, the report should reflect the surveyors efforts to attain these records and state why the chart was not attained. Note, newer reefer containers come with a temperature download chart that may be attained from the carrier. These list hourly temperatures during the voyage and are very helpful when making a claim. If these are not available, make sure to ask for a copy of the Partlow chart at the time you make the claim.

(10) Make sure the surveyor takes color photographs of the damaged cargo.

5. Arrange to Have Rejected Cargo Sold at Destination.

6. Make Sure Your Consignee Sends You the Ryan Recorder to be Calibrated by the Manufacturer.

7. Check Your Bill of Lading for the Statute of Limitations.

8. Keep all Your Records, Notes and Correspondence in a Claims File.

Retain good records of all telephone conversations. Make sure your consignee follows these steps and keeps good records as well. Planning ahead can only assist you in the future.

9. Contact an Attorney

Counsel familiar with COGSA claims should be contacted as soon as you learn there is a problem with the cargo. An attorney can assist the exporter in making certain the best possible evidence to support a claim is preserved.

FORBIDDEN FRUIT PACA CLAIMANTS TO PARTICIPATE IN DISTRIBUTION OF POST & TABACK'S ASSETS

The Honorable Jed S. Rakoff, U.S. District Court Judge for the Southern District of New York in Manhattan, issued a decision in the long awaited action pending against Post & Taback. The decision is a huge victory for the 18 claimants represented by *Rynn & Janowsky*, all of whom had claims against Post & Taback based on inspection conducted by inspectors that were guilty of bribery in the Operation Forbidden Fruit scandal.

Judge Rakoff's decision validates those Operation Forbidden Fruit PACA claims arising from the fraudulent inspections conducted between March 29, 1999 to October 27, 1999 (which covers the first and last dates that the former Post & Taback employee was found to have paid bribes to the inspectors in the criminal proceeding). Although an expanded period of time would have been more favorable because it would have allowed additional transactions to be included, the decision still recognizes as valid *over $400,000 worth of claims* of PACA claimants represented by *Rynn & Janowsky*.

The proceeds from the sale of Post & Taback's docks on the Hunts Point Market together with the accounts receivable collected have realized approximately $2 million for distribution to the claimants which amount to approximately 70 cents on the dollar.

MEDIATION OF COMMERCIAL DISPUTES

Background

Mediation in one form or another has been around since the beginning of civilization, and is used extensively for dispute resolution in many cultures. However, mediation was not part of the common law process and, until recently, was utilized only for certain types of disputes, notably labor-management grievances.

Today, mediation is used in all types of disputes, including those involving produce transactions. This is attributable to court congestion and to dissatisfaction with the adversarial process generally.

Experience shows mediation is one of the least expensive and least disruptive processes for resolving disputes. It has also proven to be the most effective way to preserve whatever relationship exists between the disputing parties.

What Does Mediation Involve?

Mediation is the next step beyond direct negotiations. It involves a *neutral third party* who attempts to "facilitate" settlement negotiations between the disputing parties.

Various Forms of Mediation Share the Following Important Characteristics:

1. *Mediation is entirely voluntary* (although written agreements or statutes may require mediation before commencing other dispute resolution procedures, such as arbitration or the filing of a lawsuit).

2. *Mediation is generally nonbinding.*

Advantages Over Litigation

1. Mediation can take place at any stage of the dispute including before or after a lawsuit is filed.
2. The parties actually participate in resolving their dispute.
3. Mediation is speedier.
4. It costs less money to mediate.
5. Confidentiality is absolutely essential to mediation.
6. The parties select the mediator.
7. Creative solutions to a dispute are possible.

In sum, business disputes are increasingly being resolved through mediation. And while mediation does not always occur prior to a party filing a lawsuit, mediation is almost always more advantageous than proceeding to a trial for all the reasons described in this article.

SHIPPERS, GROWERS' AGENTS, COMMISSION MERCHANTS: DO NOT OVERLOOK THE IMPORTANCE OF ACCURATE AND ADEQUATE ACCOUNTINGS

1. The Marketing Agreement is Not the Answer to All Problems

Many produce marketers think that once they revise and update their marketing agreements, they have nothing more to worry about with growers. Few marketing agents give enough thought to the format and detail to be included in their accountings to growers, which can be a very costly oversight. As fiduciaries, growers' agents are duty-bound to provide true, accurate and complete accountings to their growers showing costs, charges and the results of their marketing efforts.

The scope of the agent's marketing authority and the terms under which it will market the crops should already have been clearly spelled out in a marketing agreement. Charges for services or materials to be supplied by the agent in connection with the crop to be marketed should also be delineated in the agreements. In California, a detailed schedule of commission merchant charges for services and supplies must also be included in the annual Produce Dealer's license renewal application submitted by the marketer to the California Department of Food and Agriculture.

2. Pooling Accountings Deserve Special Attention

An agent, who wishes to pool a grower's produce with that of another or others for purposes of marketing and accounting, must obtain each grower's written consent before doing so. Otherwise, a grower is entitled to an accounting on a lot-by-lot basis, of all the produce it entrusted to the agent for marketing.

The marketing agreement should also indicate when the grower should expect to receive a final accounting, and at what intervals interim accountings will be produced. Too often the parties neglect to discuss and agree upon how much detail the accounting to the grower will provide. Pooled accountings are typically in a summary format, and do not always provide the grower with requisite information concerning price adjustments or charge backs to the pool for claims or expenses.

Prior to the season, it would be wise for growers' agents and growers to review the type of reporting and the detail provided by the agent's software program, and to agree in advance on the format and the sufficiency of the detail to be provided. Otherwise, the more onerous statutory requirements will apply.

3. When Marketing Agreements Are Silent About Data Required in Accounting, State and Federal Law Apply

If marketing agreements are silent as to the type of data to be included in the weekly or final accountings, section 56273.1 of the California Food and Agricultural Code specifies 14 different categories of information which must be set forth in accountings to growers. The accountings must include all of the following: 1) the date of shipment; 2) the terms of the original sale; 3) the commodity, variety, size and grade; 4) the quantity of units shipped; 5) the quantity disposed of, if not sold; 6) the original sales price; 7) the adjusted price, if applicable; 8) the reason for the adjustment; 9) inspection certificates required to substantiate adjustments; 10) amounts billed and collected from buyers for services rendered to buyers; 11) the gross and net returns received from buyer; 12) authorized commission merchant charges; 13) any additional amounts paid to the grower by the commission merchant to support the original price; and 14) the net amount due to the grower.

Likewise, the Perishable Agricultural Commodities Act ("PACA") regulations [7 C.F.R. §46.32(b)] states that accountings to growers must be "prompt, accurate and detailed." This means that, at a minimum, the accounting must itemize all expenses or charges incurred for the various operations conducted by the agent and detail the disposition of all produce handled by the agent, including sales, adjustments, rejections, consignments, sales through brokers, and status of claims filed against or collected from carriers. Moreover, PACA requires that complete records be retained by agents in connection with all produce transactions in sufficient detail as to be readily understood and audited.

4. Consider the Following Items When Entering Pre-Season Marketing Relationship

(1) If sales are to be made on anything other than a straight F.O.B. basis (e.g., consignment, open, delivered or price-after-sales), the grower's approval must be obtained before the season gets underway.

(2) Any participation by the marketing agent in a rebate or promotional allowance program with payments refunded to certain customers must be pre-authorized by growers if they are to be funded from grower returns.

(3) The rate to be charged to buyers for services and materials to be provided by agent (e.g., precooling, gassing, palletizing, etc.), must be disclosed to grower even if grower will neither provide, nor participate, in revenues generated from the provision of such services or supplies.
Where produce will be accounted for on a pooled basis, the accounting should disclose how charges to the pool and pool average prices have been computed.

(4) If "culls" or "sort outs" are marketed, the accounting must also obviously include such sales.

(5) If produce accepted for marketing has quality or condition problems, the nature and extent of the problem must be documented prior to sale, preferably with the grower's acknowledgment. Otherwise, the produce will be presumed to be in pristine condition when shipped.

(6) If the agent supplements a grower's sales return by waiving its commission, or adding money to a grower's return or applicable pool, the supplemental or "support" payment MUST BE DISCLOSED to the grower. Reporting returns that are inflated provides the grower with a false and misleading perception of sales results, and is just as inaccurate as under reporting sales returns to growers. Accountings should **always** truly and correctly depict the actual sales results. Any commission rebates, credits, or other payments or concessions an agent is willing to extend to its growers to help them out, must always be disclosed, and appropriately identified in the accounting.

(7) Marketers may not hold back or retain a certain percentage of grower's sales revenues realized to bolster their lower returns in weaker markets. If there are to be any retentions or "hold backs" withheld from interim grower payments (e.g., for "bad debt" or "adjustment" reserves), this arrangement must be disclosed to growers and agreed upon prior to the season.

(8) Should a grower seeks to impose a special or unique accounting obligation upon a marketing agent which is too costly or burdensome for the agent to fulfill, the agent must expressly decline to undertake the added reporting obligations. The grower can either choose to allow the agent to market and account

for its produce without the extra accounting task, or select another marketer willing to accept the added accounting responsibility. Agents must make sure that they can carry out all the duties they promise the grower will be undertaken.

5. Conclusion

Agents who carefully consider how and when sales results will be reported to their growers before the season gets underway generally do not run into problems or disputes with their growers after the season is behind them. Any marketer who has been confronted by legal challenges brought by an unhappy grower knows how costly this type of case can be to defend. Consequently, the importance of reviewing the format and detail of the grower accounting as well as an appropriate grower agreement cannot be overemphasized.

Within the Firm

Patricia Rynn and **Jason Read** currently serve as arbitrators on the Arbitration Panel of the Fruit and Vegetable Dispute Resolution Corporation, a private, non-profit organization, whose membership consists of firms involved in the marketing of fruits and vegetables within the NAFTA countries.

Lewis Janowsky is awaiting the first decision to be issued by the U.S. District Court where Hunts Point receiver, Koam Produce, Inc. appealed a USDA reparation order in favor of DiMare Homestead, Inc. Mr. Janowsky represents DiMare.

Bart Botta presented oral argument before the Seventh Circuit Court of Appeals in Chicago in the case of *Patterson Farms Foods v. Crown Foods*. The forthcoming opinion from the court should decide under what circumstances a written payment plan with a debtor may void PACA trust rights.

Marion Quesenbery is a frequent contributor to Western Grower & Shipper Magazine. Her most recent article was entitled, "Mediation Offers Options" and appeared in its July 2002 issue.

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