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DEPARTMENT OF AGRICULTURE

Agricultural Marketing Service

7 CFR Part 46

[Document Number AMS-FV-15-0045]

RIN 0581-AD50

Regulations Under the Perishable Agricultural Commodities Act (PACA): Growers' Trust

Protection Eligibility and Clarification of "Written Notification"

AGENCY: Agricultural Marketing Service, USDA.

ACTION: Proposed rule.

SUMMARY: The U. S. Department of Agriculture (USDA), Agricultural Marketing Service (AMS), is proposing to amend the regulations under the Perishable Agricultural Commodities Act (PACA or Act) to enhance clarity and improve the administration and enforcement of the PACA. The proposed revisions to the regulations would provide greater direction to the industry of how growers and other principals that employ selling agents may preserve their PACA trust rights. The proposed revisions would further provide greater direction to the industry on the definition of "written notification" and the jurisdiction of USDA to investigate alleged PACA violations.

DATES: Written or electronic comments received by *[Insert date 60 days after date of publication in the Federal Register]* will be considered prior to issuance of a final rule.

ADDRESSES: You may submit written or electronic comments to "PACA Regulatory Enhancements," AMS, Specialty Crops Program, PACA Division, 1400 Independence Avenue S.W., Room 1510-S, Stop 0242, Washington, D.C. 20250-0242; Internet:

<http://www.regulations.gov>; or fax: 202-690-4413.

FOR FURTHER INFORMATION CONTACT: Josephine E. Jenkins, Chief, Investigative Enforcement Branch, 202-720-6873; or PACAIinvestigations@ams.usda.gov.

SUPPLEMENTARY INFORMATION: The Perishable Agricultural Commodities Act (PACA) was enacted in 1930 to promote fair-trading in the marketing of fresh and frozen fruits and vegetables in interstate and foreign commerce. It protects growers, shippers, distributors, and retailers dealing in those commodities by prohibiting unfair and fraudulent trade practices. The PACA also provides a forum to adjudicate or mediate commercial disputes. Licensees who violate the PACA may have their license suspended or revoked, and individuals determined to be responsibly connected to such licensees are restricted from being employed or operating in the produce industry for a period.

Growers' Trust Protection Eligibility

Growing, harvesting, packing, and shipping perishables involve risk: costs are high; capital is tied up in farmland and machinery; and returns are delayed until the crop is sold. Because of the highly perishable nature of the commodities and distance from selling markets, produce trading is fast moving and often informal. Transactions are often consummated in a matter of minutes, frequently while the commodities are in route to their destination. Under such conditions, it is often difficult to check the credit rating of the buyer.

Congress examined the sufficiency of the PACA fifty years after its inception and determined that prevalent financing practices in the perishable agricultural commodities industry were placing the industry in jeopardy. Particularly, Congress focused on the increase in the number of

buyers who failed to pay, or were slow in paying their suppliers, and the impact of such payment practices on small suppliers who could not withstand a significant loss or delay in receipt of monies owed. Congress was also troubled by the common practice of produce buyers granting liens on their inventories to their lenders, which covered all proceeds and receivables from the sales of perishable agricultural commodities, while produce suppliers remained unpaid. This practice elevated the lenders to a secured creditor position in the case of the buyer's insolvency, while the sellers of perishable agricultural commodities remained unsecured creditors with little or no legal protection or means of recovery in a suit for damages.

Deeming this situation a "burden on commerce," Congress amended the PACA in 1984 to include a statutory trust provision, which provides increased credit security in the absence of prompt payment for perishable agricultural commodities. The 1984 amendment to the PACA states in relevant part:

It is hereby found that a burden on commerce in perishable agricultural commodities is caused by financing arrangements under which commission merchants, dealers, or brokers, who have not made payment for perishable agricultural commodities purchased, contracted to be purchased, or otherwise handled by them on behalf of another person, encumber or give lenders a security interest in such commodities, or on inventories of food or other products derived from such commodities, and any receivables or proceeds from the sale of such commodities or products, and that such arrangements are contrary to the public interest. This subsection is intended to remedy such burden on commerce in perishable agricultural commodities and to protect the public interest.

(7 U.S.C. § 499e(c)(1)).

Under the 1984 amendment, perishable agricultural commodities, inventories of food or other derivative products, and any receivables or proceeds from the sale of such commodities or products are to be held in a non-segregated floating trust for the benefit of unpaid sellers. This

trust is created by operation of law upon the purchase of such goods, and the produce buyer is the statutory trustee for the benefit of the produce seller. To preserve its trust benefits, the unpaid supplier, seller, or agent must give the buyer written notice of intent to preserve its rights under the trust within 30 calendar days after payment was due. Alternatively, as provided in the 1995 amendments to the PACA (Pub. L. 104-48), a PACA licensee may provide notice of intent to preserve its trust rights by including specific language as part of its ordinary and usual billing or invoice statements.

The trust is a non-segregated “floating trust” made up of all of a buyer’s commodity-related assets, under which there may be a commingling of trust assets. There is no need to identify specific trust assets through each step of the accrual and disposal process. Since commingling is contemplated, all trust assets would be subject to the claims of unpaid sellers, suppliers and agents to the extent of the amount owed them. As each supplier gives ownership, possession, or control of perishable agricultural commodities to a buyer, and preserves its trust rights, that supplier becomes a participant in the trust. Section 5(c)(2) of the PACA states in relevant part:

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)).

Thus, trust participants remain trust beneficiaries until they have been paid in full.

Under the statute, the District Courts of the United States are vested with jurisdiction to

entertain actions by trust beneficiaries to enforce payment from the trust. (7 U.S.C. § 499e(c)(5)).

Thus, in the event of a business failure, produce creditors may enforce their trust rights by suing the buyer in federal district court. It is common in this type of trust enforcement action for unpaid sellers to seek a temporary restraining order (TRO) that freezes the bank accounts of a buyer until the trust creditors are paid. Many unpaid sellers have found this to be a very effective tool to recover payment for produce. Often, a trust enforcement action with a TRO will be the defining moment for the future of a buyer-debtor firm. Since the TRO freezes the bank accounts of the buyer, the buyer must either pay the trust creditors or attempt to operate a business without access to its bank accounts. This aggressive course of action by unpaid sellers is generally pursued when the sellers are concerned that trust assets are being dissipated.

In the event of a bankruptcy by a produce buyer, that is, the produce “debtor,” the debtor’s trust assets are not property of the bankruptcy estate and are not available for distribution to secured lenders and other creditors until all valid PACA trust claims have been satisfied. The trust creditors can petition the court for the turnover of the debtor’s trust-related assets or alternatively request that the court oversee the liquidation of the inventory and collection of the receivables and disburse the trust proceeds to qualified PACA trust creditors.

Because of the statutory trust provision, produce creditors, including sellers outside the United States, have a far greater chance of recovering money owed them when a buyer goes out of business. However, because attorney’s fees are incurred in trust enforcement cases, it is not always practical to pursue small claims that remain unpaid. Nonetheless, because of the PACA trust provisions, unpaid sellers, including those outside the United States, have recovered hundreds of millions of dollars that most likely would not otherwise have been collected.

The PACA trust provisions protect not only growers, but also other firms trading in fruits and vegetables since each buyer in the marketing chain becomes a seller in its own turn and can preserve its own trust eligibility accordingly. Because each creditor that buys produce can preserve trust rights for the benefit of its own suppliers, any money recovered from a buyer that goes out of business is passed back through preceding sellers until ultimately the grower also realizes the financial benefits of the trust provisions. This is particularly important in the produce industry due to the highly perishable nature of the commodities as well as the many hands such commodities customarily pass through to the end customer.

In 1995, Congress amended the PACA (Pub. L.104-48), changing several requirements of the PACA trust. Changes include no longer requiring sellers or suppliers to file notices of intent to preserve trust benefits with USDA, and allowing PACA licensees to have their invoices or other billing documents serve as the trust notice. The primary reason for removing the notice filing requirement was to reduce the paperwork burden on sellers and suppliers and eliminate USDA's expense in processing trust notices and administrating the provision.

To preserve trust protection under the PACA, the law offers two approaches to unpaid sellers, suppliers, and agents. One option allows PACA licensees to declare at the time of sale that the produce is sold subject to the PACA trust, providing protection in the event that payment is late or the payment instrument is not honored. This option allows PACA licensees to protect their trust rights by including the following language on invoices or other billing statements:

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.

(7 U.S.C. § 499(c)(4)).

The second option for a PACA licensee to preserve its trust rights, and the sole method for all non-licensed sellers requires the seller to provide a separate, independent notice to the buyer of its intent to preserve its trust benefits. The notice must include sufficient details to identify each transaction and be received by the buyer within 30 days after payment becomes due.

Under current 7 CFR § 46.46(e)(2), only transactions with payment terms of 30 days from receipt and acceptance, or less, are eligible for trust protection. Section 46.46(e)(1) of the regulations (7 CFR § 46.46(e)(1)) requires that any payment terms beyond “prompt” payment as defined by the regulations, usually 10 days after receipt and acceptance in a customary purchase and sale transaction, must be expressly agreed to in writing before entering into the transaction. A copy of the agreement must be retained in the files of each party and the payment due date must be disclosed on the invoice or billing statement.

Since 1984, the district courts have had jurisdiction to entertain actions by trust beneficiaries to enforce payment from the trust. Recent court decisions have invalidated the trust claims of unpaid growers against their growers’ agent because the growers did not file a trust notice directly with the growers’ agent. Growers’ agents sell and distribute produce for or on behalf of growers and may provide such services as financing, planting, harvesting, grading, packing, labor, seed, and containers. The growers have argued that it is not necessary to file a trust notice with their growers’ agent because growers’ agents are required to preserve the growers’ rights as a trust beneficiary against the buyer (7 C.F.R. § 46.46(d)(2)). Some courts have ruled that while

the growers' agent is required to preserve the growers' trust benefits with the buyer of the produce, the grower has the responsibility to preserve its trust benefits with the growers' agent.

AMS proposes that section 46.46 of the regulations be amended by revising paragraphs (d)(1) and (d)(2), redesignating paragraph (d)(2) as (d)(3), adding a new paragraph (d)(2) and revising (f)(1)(iv). These amendments would clarify that growers, or other types of principals, who employ agents to sell perishable agricultural commodities on their behalf are among the class of "suppliers or sellers" referenced in section 5(c) of the PACA (7 U.S.C. 499e) and as such must preserve their trust benefits against their agents. The revision of (f)(1)(iv) would identify additional types of documents that can be used in a notice of intent to preserve trust benefits.

If licensed under the PACA, the grower may choose to preserve its trust rights by invoicing the growers' agent based on shipping and/or billing documents. The shipping and/or billing documents must include the requisite trust language provided in section 5(c)4 of the PACA. Non-licensed growers may choose to preserve their trust rights by issuing a notice of intent to preserve trust benefits as outlined under section 46.46 of the PACA regulations.

Clarification of "Written Notification"

The PACA was amended in 1995 to require written notification as a precursor to investigations of alleged violations of the PACA. Within recent years, produce entities have challenged the USDA's jurisdiction to conduct investigations based their narrow reading of the definition of "written notification" stated in section 46.49 of the Regulations (7 C.F.R. § 46.49). The proposed amendment of section 46.49 is needed to make clear that public filings such as bankruptcy petitions, civil trust actions, and judgments constitute written notification. Moreover, AMS proposes to clarify that the filing of a written notification with USDA may be

accomplished by myriad means, including, but not limited to, delivery by: regular or commercial mail service, hand delivery, or electronic means such as email, text, or facsimile message. Furthermore, a written notification published in any public forum, including, but not limited to, a newspaper or internet website, will be considered filed with USDA upon its visual inspection by any office or official of USDA responsible for administering the Act. Clarification of the meaning of “written notification” would ensure that PACA licensees and entities operating subject to the PACA understand the breadth of documentation that could trigger USDA’s authority to initiate an investigation of alleged PACA violations.

Section 46.49 would be amended by revising paragraphs (a), (b), (c) and (d) to clarify the meaning of “written notification” as the term is used in section 6(b) of the PACA. Further, to reflect current industry practices and advancements in electronic communication, section 46.49(d) would be amended to allow the Secretary to serve a notice or response, as it relates to paragraph (d), by any electronic means such as registered e-mail that provides proof of receipt to the electronic mail address or phone number of the subject of the investigation.

Executive Orders 12866 and 13563

The proposed rule has been reviewed under Executive Order 12866 supplemented by Executive Order 13563 and it has been determined that this proposed rule is not considered a significant regulatory action under section 3(f) of Executive Order 12866 and, therefore, it was not reviewed by the Office of Management and Budget.

Executive Order 12988

This proposed rule has been reviewed under Executive Order 12988, Civil Justice Reform, and is not intended to have retroactive effect. This proposed rule will not preempt any State or

local laws, regulations, or policies, unless they present an irreconcilable conflict with this rule.

There are no administrative procedures that must be exhausted prior to any judicial challenge to the provisions of this proposed rule.

Effects on Small Businesses

Pursuant to requirements set forth in the Regulatory Flexibility Act (RFA) (5 U.S.C. 601 *et seq.*), USDA has considered the economic impact of this proposed rule on small entities. The purpose of the RFA is to fit regulatory actions to the scale of businesses subject to such actions in order that small businesses will not be unduly or disproportionately burdened. Small agricultural service firms are defined by the Small Business Administration (SBA) as those having annual receipts of less than \$7,500,000, and small agricultural producers are defined as those having annual receipts of less than \$750,000 (13 CFR 121.201). There are approximately 14,500 firms licensed under the PACA, a majority of which could be classified as small entities. Historically, the produce industry has been an entry-level job market. There is a constant turnover involving the closing and opening of businesses. Produce firms generally start as small business entities.

The Agricultural Marketing Service (AMS) believes that the proposed amendments to the PACA regulations would help growers and other sellers and suppliers of produce protect their rights under the PACA trust, and the potential recovery of millions of dollars in unpaid produce debt. Moreover, AMS believes that the proposed amendments more accurately reflect the intent of Congress when it amended the PACA to require written notification as a precursor to investigations by the Secretary of Agriculture. The proposed revisions include language that clarifies a grower's responsibility to preserve its benefits under the PACA trust, as well as

language that clarifies what constitutes “written notification” for purposes of investigating alleged violations of the PACA.

AMS believes the proposed revisions would increase the clarity of the PACA regulations and improve AMS’s enforcement of the PACA. AMS believes that this proposed rule would not have a significant economic impact on a substantial number of small entities.

Executive Order 13175

This proposed rule has been reviewed in accordance with the requirements of Executive Order 13175, consultation and Coordination with Indian Tribal governments. The review reveals that this proposed regulation will not have substantial and direct effects on Tribal governments and will not have significant Tribal implications.

Paperwork Reduction Act

In accordance with OMB regulations (5 CFR part 1320) that implement the Paperwork Reduction Act of 1995 (44 U.S.C. Chapter 35), the information collection and recordkeeping requirements that are covered by this proposed rule are currently approved under OMB number 0581-0031.

E-Government Act Compliance

USDA is committed to complying with the E-Government Act, which requires Government agencies in general to provide the public the option of submitting information or transacting business electronically to the maximum extent possible. Forms are available on our PACA Web site at <http://www.ams.usda.gov/rules-regulations/paca> and can be printed, completed, and faxed. Currently, forms are transmitted by fax machine, postal delivery and can be accepted by e-mail.

List of Subjects in 7 CFR Part 46

Agricultural commodities, Brokers, Penalties, Reporting and recordkeeping requirements.

For the reasons set forth in the preamble, AMS proposes to amend 7 CFR Part 46 as follows:

**PART 46--REGULATIONS (OTHER THAN RULES OF PRACTICE) UNDER THE
PERISHABLE AGRICULTURAL COMMODITIES ACT, 1930**

1. The authority citation for part 46 continues to read as follows:

Authority: 7 U.S.C. 499a – 499t.

2. Amend § 46.46 by revising paragraphs (d) and (f)(1)(iv) to read as follows:

§ 46.46 Statutory trust.

* * * * *

(d) *Trust maintenance.* (1) Licensees and persons subject to license are required to maintain trust assets in a manner so that the trust assets are freely available to satisfy outstanding obligations to sellers of perishable agricultural commodities. Any act or omission which is inconsistent with this responsibility, including dissipation of trust assets, is unlawful and in violation of section 2 of the Act (7 U.S.C. 499b). Growers, licensees, and persons subject to license may file trust actions against licensees and persons operating subject to license. Licensees and persons subject to license are bound by the trust provisions of the Act (7 U.S.C. 499(e)).

(2) Principals, including growers, who employ agents to sell perishable agricultural commodities on their behalf are “suppliers” and/or “sellers” as those words are used in section 5(c)(2) and (3) of the Act (7 U.S.C. 499e(c)(2) and (3)) and therefore must preserve their trust rights against their agents by filing a notice of intent to preserve trust rights with their agents as set forth in paragraph (f) of this section.

(3) Agents who sell perishable agricultural commodities on behalf of their principals must preserve their principals' trust benefits against the buyers by filing a notice of intent to preserve trust rights with the buyers. Any act or omission which is inconsistent with this responsibility, including failure to give timely notice of intent to preserve trust benefits, is unlawful and in violation of section 2 of the Act (7 U.S.C. 499b).

* * * * *

(f) * * *

(1) * * *

(iv) The amount past due and unpaid; except that if a supplier, seller or agent engages a commission merchant or growers' agent to sell or market their produce, the supplier, seller or agent that has not received a final accounting from the commission merchant or growers' agent shall only be required to provide information in sufficient detail to identify the transaction subject to the trust.

* * * * *

3. Revise § 46.49 to read as follows:

§ 46.49 Written notifications and complaints.

(a) Written notification, as used in section 6(b) of the Act (7 U.S.C. 499f (b)), means:

(1) Any written statement reporting or complaining of a violation of the Act made by any officer or agency of any State or Territory having jurisdiction over licensees or persons subject to license, or a person filing a complaint under section 6(a), or any other interested person who has knowledge of or information regarding a possible violation of the Act, other than an employee of an agency of USDA administering the Act;

(2) Any written notice of intent to preserve the benefits of, or any claim for payment from, the trust established under section 5 of the Act (7 U.S.C. 499e);

(3) Any official certificate(s) of the United States Government or States or Territories of the United States; or

(4) Any public legal filing or other published document describing or alleging a violation of the Act.

(b) Any written notification may be filed by delivering the written notification to any office of USDA or any official of USDA responsible for administering the Act. Any written notification published in any public forum, including, but not limited to, a newspaper or an internet website shall be deemed filed upon visual inspection by any office of USDA or any official of USDA responsible for administering the Act. A written notification which is so filed, or any expansion of an investigation resulting from any indication of additional violations of the Act found as a consequence of an investigation based on written notification or complaint, also shall be deemed to constitute a complaint under section 13(a) of the Act (7 U.S.C. 499m(a)).

(c) Upon becoming aware of a complaint under section 6(a) or written notification under 6(b) of the Act (7 U.S.C. 499f (a) or (b)) by means described in paragraph (a) and (b) of this section, the Secretary will determine if reasonable grounds exist to conduct an investigation of such complaint or written notification for disciplinary action. If the investigation substantiates the existence of violations of the Act, a formal disciplinary complaint may be issued by the Secretary as described in section 6(c)(2) of the Act (7 U.S.C. 499f(c)(2)).

(d) Whenever an investigation, initiated as described in section 6(c) of the Act (7 U.S.C. 499f(c)(2)), is commenced, or expanded to include new violations of the Act, notice shall be

given by the Secretary to the subject of the investigation within thirty (30) days of the commencement or expansion of the investigation. Within one hundred and eighty (180) days after giving initial notice, the Secretary shall provide the subject of the investigation with notice of the status of the investigation, including whether the Secretary intends to issue a complaint under section 6(c)(2) of the Act (7 U.S.C. 499f(e)(2)), terminate the investigation, or continue or expand the investigation. Thereafter, the subject of the investigation may request in writing, no more frequently than every ninety (90) days, a status report from the Director of the PACA Division who shall respond to the written request within fourteen (14) days of receiving the request. When an investigation is terminated, the Secretary shall, within fourteen (14) days, notify the subject of the termination of the investigation. In every case in which notice or response is required under this paragraph, such notice or response shall be accomplished by personal service; or by posting the notice or response by certified or registered mail, or commercial or private delivery service to the last known address of the subject of the investigation; or by sending the notice or response by any electronic means such as registered e-mail, that provides proof of receipt to the electronic mail address or phone number of the subject of the investigation.

Dated: December 8, 2016

Elanor Starmer
Administrator
Agricultural Marketing Service

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