PACA Pitfalls: Waiving PACA Protection Through Arbitration Provisions

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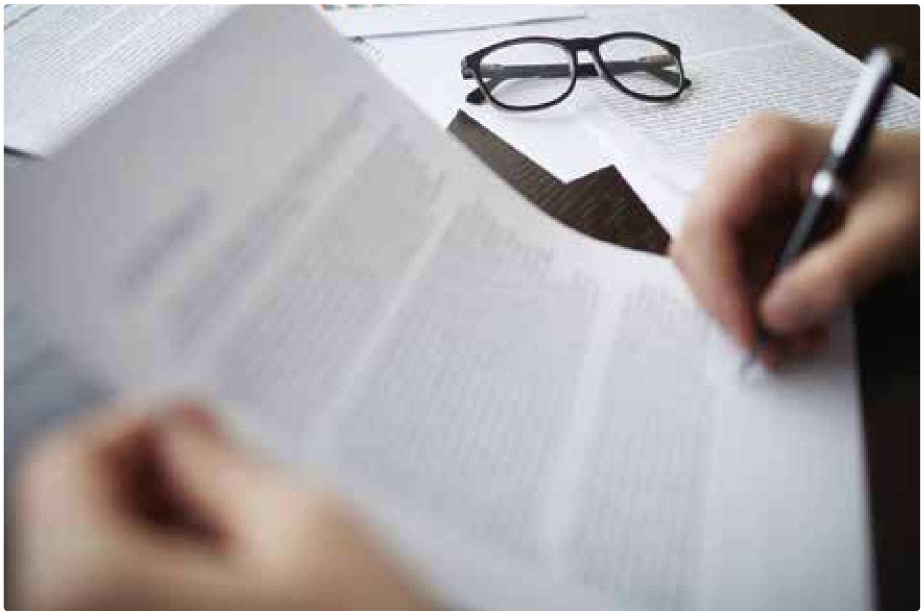

In order to establish a cost effective and efficient method of resolving disputes, it has become increasingly common in the agricultural industry to enter into agreements that contain alternative dispute provisions, such as mandatory submission of contract disputes to mediation or arbitration ("ADR Provisions"). These ADR Provisions have gained in popularity because they afford the contracting parties the ability to fashion flexible solutions to disputes in a shorter timeline and economical scale than may be available through litigation. However, these provisions, when included in agreements that cover marketing of fruits and vegetables, have a significant hidden cost: they may disqualify the parties from certain protections under the Perishable Agricultural Commodities Act, 7 United States Code §§499 et seq. ("PACA").

PACA was enacted in 1930 by the United States government at the request of the agricultural industry to ensure fair trade by shippers, dealers, brokers, wholesalers, retailers, and wholesale grocers within the chain of commerce of fruits and vegetables. The United States Department of Agriculture, PACA Branch (the "PACA Branch") has been tasked with developing policies and procedures, which can be found at 7 Code of Federal Regulations §§46 et seq. Among other things, PACA set up a licensing system for industry members marketing agricultural commodities in foreign and interstate commerce, and a set of rules establishing a trust protection for sales proceeds for qualifying commodities.

One of the benefits of PACA is the availability of an efficient dispute resolution system for licensees. The PACA Branch administers four different methods of dispute resolution to address three tier system to resolve disputes by and among licensees: 1) "Good Delivery" Hotline; 2) Informal complaint; 3) mediation services; and 4) Formal complaint. The Good Delivery Hotline is typically used to resolve quality disputes. An Informal complaint submitted in writing with a $100 fee and will result in an investigation of the claims by a PACA Branch investigator who provides a conclusion with the parties in an attempt to settle the dispute. The PACA Branch also offers mediation, which is the use of an experienced, third party neutral who meets with both parties to a dispute in an effort to reach a voluntary resolution. Finally, PACA licensees can also initiate a Formal Complaint by submitting a notarized written application available on the USDA's PACA website (www.ams.usda.gov) and a $500 filing fee. The Formal Complaint process will result in a binding decision in less than a year that can be converted into a judgment by the applicable civil court for enforcement purposes.

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However, recent decisions by the United States Supreme Court and the Secretary of Agriculture have held that ADR Provisions may disqualify the parties from applying to the PACA Branch for dispute resolution under PACA. Specifically, the United States Supreme Court has held that [a]n agreement to arbitrate is enforceable and irrevocable (without mutual consent) unless the entire contract itself is unenforceable or revoked. Perry v. Thomas, 482 U.S. 483, 490 (1987). In an opinion in 1996, the Secretary of Agriculture determined that the Federal Arbitration Act requires that the arbitration provisions in a valid and enforceable contract preempt PACA dispute processes. Green Acres Turf Farms, Inc. v. Kelly Distributing, Inc., et al. (1996) 55 Agric. Dec. 1298.

Another disadvantage to ADR is that it may cut off the shipper's timely recourse to enforce the PACA statutory trust. That trust is an extraordinary tool for collecting from receivers who fail to pay. It is available when

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the invoice contains the PACA legend and when the terms of payment are "PACA-10 days", or when they are fixed at 30 days or less by written contract before shipment. When the PACA statutory trust is fixed, the receivable is considered to be the shipper's money, held in trust by the receiver for the shipper. If the receiver files in bankruptcy, the receivable is removed from the bankrupt estate and paid to the shipper. If the receiver is not in bankruptcy, the shipper may apply to the federal district court for an order that the trust moneys be turned over to the shipper. However, an ADR provision may block the shipper from applying to any court for legal remedies until the ADR process is exhausted. By then, the trust moneys may be dissipated

The lesson to be learned from these decisions is that the parties should pay particular attention to the ADR Provisions, which are usually included in the section of the contract that is reserved for "boilerplate" language. If the parties to an agreement that includes responsibilities for marketing fruits and vegetables wish to remain subject to PACA jurisdiction, the ADR Provisions should be excluded, or carefully written to preserve the right of the parties to the trust protection and PACA's dispute resolution processes.