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ARTICLE

CURRENT ISSUES INVOLVING STATUTORY TRUSTS UNDER THE PERISHABLE AGRICULTURAL COMMODITIES ACT

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In 1984, Congress amended the Perishable Agricultural Commodities Act by enacting statutory trust provisions. The trust provisions were based on similar trust provisions found in the Packers and Stockyards Act. Congress' intent in enacting the trust provisions was to combat the prevalent slow, and no, pay practices of the fresh produce industry. This article discusses the areas of dispute which have arisen from enactment of the trust provisions: attorneys' fees, interest, injunctive relief, and substantial versus strict notice requirements. The author then discusses the judicial decisions which have addressed these areas of dispute. In conclu-

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sion, the author contends that, despite initial judicial reluctance to enforce the Perishable Agricultural Commodities Act trust provisions, the courts appear to be proceeding in a manner consistent with Congressional intent.

INTRODUCTION

The Perishable Agricultural Commodities Act (PACA) of 1933[1] was enacted to promote fair trade in fresh fruit and vegetable marketing. The PACA broadly defines unfair trade practices and sets forth legal penalties for fraudulent marketing practices.[2]

In 1984, Congress amended the PACA to provide additional protection to unpaid sellers or suppliers of perishable produce by creating a statutory trust for their benefit. The amendment impresses a trust on the perishable commodities received by the purchaser, all inventories of food or other products derived therefrom, and receivables or proceeds from the sale of such commodities and products. The trust continues until the unpaid suppliers who give timely notice to preserve their trust rights receive full payment from the purchaser.

The PACA statutory trust provisions were patterned after a similar trust incorporated into the Packers and Stockyards Act[3] (PSA) in 1976. Both the PSA trust and the PACA trust protect unpaid sellers from delinquent purchasers by elevating the claims of trust beneficiaries above secured lenders and creditors. Thus, trust beneficiaries move to the head of the line when the defaulting purchasers' assets are distributed to creditors.[4]

Reclassifying the debtor/creditor relationship in the fresh produce industry reflects Congressional concern over the status of unpaid sellers as unsecured creditors who seldom recover from insolvent or bankrupt purchasers.[5] Congress deemed nonpayment of sellers "a burden on commerce," and "contrary to the public interest" when it enacted the

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[1] Perishable Agricultural Commodities Act of 1933, PUB. L. NO. 98-273, § 1, 98 Stat. 165 (1933) (codified as amended at 7 U.S.C. §§ 499 *et seq.*).

[2] 7 U.S.C. § 499(b) (1988).

[3] Ch. 64, § 1, 42 Stat. 159 (1921) (codified at 7 U.S.C. §§ 181-229 (1988)).

[4] *In re* Fresh Approach, Inc., 48 B.R. 926, 931 (Bankr. N.D. Tex. 1985). *See also*, *In re* Samuels & Co., Inc. 526 F.2d 1238 (5th Cir. 1976) (an unpaid cash seller of cattle already delivered to a purchaser is subordinate to a good faith purchaser holding a perfected security interest in the livestock) *cert. denied sub nom.* Stowers v. Mahon, 429 U.S. 834 (1976). It was partially in response to the *Samuels* result that Congress enacted the statutory trust provisions of the Packers and Stockyards Act.

[5] H.R. REP. NO. 543, 98th Cong., 2d Sess. 2, 4 (1984), *reprinted in* 1984 U.S.C.C.A.N. 405, 407.

PACA trust amendments.[6] Congress also intended to assure speedy payment to trust claimants, in addition to giving trust claimants priority over banks and other secured parties.[7] The concern with prompt payment was explicitly stated in the House Report:

> The Committee believes that the statutory trust requirements will not be a burden to the lending institutions. They will be known to and considered by prospective lenders in extending credit. *The assurance the trust provision gives that raw products will be paid for promptly* and that there is a monitoring system provided for under the Act will protect the interests of the borrower, the money lender, and the fruit and vegetable industry.[8]

The United States Department of Agriculture (USDA) further emphasized the importance of prompt payment in the fresh produce industry in the preamble to the PACA trust regulations. The PACA trust was characterized as "a self-help tool that will enable them [suppliers and sellers of fruits and vegetables] to protect themselves against the abnormal risk of losses resulting from slow pay and no-pay practices by buyers or receivers of fruits and vegetables."[9]

Additionally, the PACA states that trust benefits will be lost unless they are preserved within time limits established by the USDA.[10] The regulations establish short time limits for filing PACA trust claims; time limits intended to encourage buyers and sellers to agree on prompt payment in the absence of a written contractual agreement.[11]

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[6] The PACA trust amendment states:

> "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) (1988).

[7] *In re* W. L. Bradley Co. Inc., 78 B.R. 92 (Bankr. E.D. Pa. 1987).

[8] H.R. REP. NO. 543, *supra* note 5, at 4 (Emphasis added).

[9] 49 Fed. Reg. 45,735, 45,737 (1984) (codified at 7 C.F.R. Part 46).

[10] 7 U.S.C. § 499e(c)(3) (1988).

[11] 7 C.F.R. § 46.46(f) (1991). The regulations predicate eligibility to participate in the trust on compliance with the time limits set forth in 7 C.F.R. §§ 46.2(z) and (aa). In the absence of an agreement extending the time for payment, a purchaser violates the PACA unless full payment is made within 10 days after receipt of the produce. 7 C.F.R. § 46.2(aa)(5). The parties may expressly agree to a different time period for

I. Judicial Interpretations of the PACA Trust

The House of Representatives, in its report, declared that legal precedents established under the PSA were to be used as guidance in interpreting the PACA trust provisions.[12] Despite Congress' direction, some courts have expressed reluctance to enforce PACA trusts.[13] Other courts have gone beyond reluctance by ruling adversely on actions seeking to establish and enforce PACA trust claims. In so doing, these courts have ignored the Congressional intent to encourage prompt payment in produce transactions, disregarded elementary principles of statutory construction, and declined to exercise their equitable powers.

This paper will present a critical analysis of federal decisional law affecting some of the practical aspects of enforcing PACA trust rights. The decisions discussed have addressed issues such as the availability of injunctive relief to private party PACA trust claimants and the awarding of attorneys' fees and interest as a component of the PACA trust. Several court decisions have also determined the class of PACA beneficiaries entitled to relief and the effect of noncompliance with the statutory and regulatory requirements for the preservation of trust rights. The emerging body of law in these areas will have a significant impact on unpaid produce suppliers who must consider whether litigation to collect trust assets is economically feasible.

II. *In re Milton Poulos, Inc.*

In *In re Milton Poulos, Inc.*,[14] several fresh fruit and vegetable sellers joined as plaintiffs (hereinafter "beneficiaries") to assert their PACA trust rights in the assets held by Milton Poulos, Inc. After Poulos filed a Chapter 11 bankruptcy petition, the beneficiaries filed a motion for relief from the automatic stay and for turnover of property not part of the debtor's estate. After months of litigation, the bankruptcy court granted relief from stay, confirming that PACA trust as-

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payment up to a maximum of 30 days and still be eligible for trust protection. 7 C.F.R. §§ 46.46(f)(1) and (2). In addition, the trust claimant's notice of intent to preserve trust benefits must be received by USDA and the debtor no later than 30 days after the expiration of time for payment. 7 C.F.R. § 46.46(g).

[12] H.R. Rep. No., *supra* note 5, at 12.

[13] *See, e.g.*, *In re* D.K.M.B., Inc., 95 B.R. 774, (Bankr. D. Colo. 1989) (wherein the court noted the "Draconian impact" of the PACA trust on the bankruptcy estate before mandating strict compliance with the PACA regulations); *see also*, *In re* Aande Foods, Inc., 110 B.R. 346 (Bankr. N.D. Ill. 1989) (wherein the court states that the consequences of the trust are unfair to secured creditors).

[14] 94 B.R. 648 (C.D. Cal. 1988) [hereinafter *Milton Poulos I*].

sets were not part of the bankruptcy estate.[15] In its Memorandum, the trial court identified each of the beneficiaries and the amounts due each as part of the trust corpus. The court also noted that several other entities had potential claims but were not participating in the motion.[16] The court denied the award of any interest, attorneys' fees or costs to the beneficiaries and stated its rationale as follows: "Assuming the court has the equitable power to grant the unpaid creditor's claims, the court has determined that awarding interest, fees and costs would unfairly deplete the bankruptcy estate at the expense of all other creditors."[17]

A separate order was concurrently entered, directing the parties to return to court, to settle the distribution of the trust funds. At the distribution hearing, two additional trust claimants (hereinafter "claimants") first appeared. The original beneficiaries objected because the claimants had expressly declined to join the motion for relief from stay and thereby avoided the burdensome costs of the litigation. Nonetheless, the court allowed both claimants to share in the trust assets.[18]

The beneficiaries appealed to the Ninth Circuit Bankruptcy Appellate Panel (BAP) challenging: (1) the inclusion of claimants in the trust distribution, and (2) the denial of an award of interest, attorneys' fees, and costs. The BAP upheld the trial judge's opinion in its entirety in *Milton Poulos II*.[19]

The BAP decision was then appealed to the Ninth Circuit Court of Appeals.[20] The court affirmed the BAP's ruling that nonparticipating claimants were entitled to a *pro rata* share of trust assets.[21] The court also decided that attorneys' fees are to be awarded to the beneficiaries out of the trust fund.[22] The court did not address the BAP's denial of an award of interest on amounts recovered under the trust.

A. *Nonparticipating Claimants*

According to the *Milton Poulos III* Court, failure to participate in the motion for relief from stay did not preclude the claimants from a

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[15] *Id.* at 653.
[16] *Id.* at 649.
[17] *Id.* at 653.
[18] *Id.*
[19] *In re* Milton Poulos, Inc., 107 B.R. 715 (1989) [hereinafter *Milton Poulos II*].
[20] *In re* Milton Poulos, Inc., 947 F.2d 1351 (9th Cir. 1991) [hereinafter *Milton Poulos III*].
[21] *Id.* at 1353.
[22] *Id.*

pro rata share in the trust assets. In affirming the trust claims of the nonparticipating claimants, the Court of Appeals further held that they had properly perfected their trust rights.[23] This holding was based on a USDA "certification letter" which acknowledged the "trust claimants and amounts perfected." The court was also influenced by the declarations of the claimants which asserted that their claims were legitimized by the USDA certification letter. The correspondence from the USDA and the claimants' declarations were thus treated as evidence in identifying members of the trust beneficiaries class.[24] In so holding, the Appellate Court did not acknowledge the lower court's failure to request, nor did it require, the nonparticipating claimants to prove the validity of their claims.

The court's conclusion is erroneous because it wrongly characterizes the USDA-prepared list of trust claimants as conclusive. In practice, the USDA routinely prepares a list of the number, identity, and extent of potential PACA claims against any given debtor. Generally, the information is not disclosed unless and until the debtor goes into bankruptcy or faces foreclosure and liquidation. After disclosure, the list is accompanied by a form letter stating that the trust claims *appear* to qualify for trust protection and that PACA claims are superior to those of other creditors *absent valid defenses.* The USDA may list any given trust claimant upon receipt of a notice of intent to preserve trust benefits, followed by a cursory examination to determine whether the dates of the notices and invoice dates are timely.

Although, USDA certification of trust claims is relevant and persuasive evidence regarding the identity of the class beneficiaries, it is not a final determination of whether PACA trust rights were perfected. The USDA's evaluation of the PACA trust claims is preliminary and open to legal and factual challenge by the debtor and other interested parties. Furthermore, USDA certification is not determinative on the issues of statutory and regulatory compliance. To establish the validity of purported trust claims and withstand challenges by other claimants, the trustee, or the debtor, a claimant must furnish additional documentary and corroborative evidence of the claim. For example, the court in *C. H. Robinson v. B. H. Produce, Inc.*,[25] disqualified several trust claim-

[23] The court did not consider that there are other defenses to PACA trust claims, aside from alleging a defective notice of intent to preserve trust benefits. For instance, certain invoices listed on the trust notice may have already been paid, or may be subject to credits and offsets by the debtor.

[24] *Milton Poulos III*, 947 F.2d at 1353.

[25] 723 F. Supp. 785 (N.D. Ga. 1989).

ants, despite the fact that their trust notices were "certified" by USDA. The court stated: "[t]his certification by the USDA is persuasive in the absence of *other evidence*, but it is not binding on the court if evidence shows that the notices were not in compliance with the statute."[26]

The *Milton Poulos III* decision is also disturbing because a PACA claimant must initiate legal action to collect trust funds. As aptly noted by the court in *Matter of United Fruit and Produce Co., Inc.*,[27] "PACA contains no mechanism for the administration and distribution of trust assets."[28] As with any other commercial litigation, PACA trust beneficiaries must carefully weigh the potential recovery of PACA trust assets against the likely expense of attorneys' fees incurred to obtain release of the trust monies. Under *Milton Poulos III*, trust litigants can be forced to share trust assets with other claimants who choose to "sit on the sidelines" until a court recognizes the validity and existence of a PACA trust. Potential PACA beneficiaries may well be reluctant to shoulder the burden of litigation when numerous other potential PACA claims would swallow up the debtor's assets and only a *pro rata* distribution of the trust would result.

The USDA does not serve an adjudicative function in assessing the validity of PACA claims. Therefore, a judicial decree ordering distribution of trust funds to claimants who expressly refused to intervene in the action taken against the debtor is difficult to understand.[29]

The court in *United Fruit* purported to follow the rationale of *Milton Poulos* when it declined to accept that all PACA trust claimants listed by the USDA had perfected their claims. In *United Fruit*, the court noted that the USDA listed thirty unpaid sellers who appeared to qualify for trust protection. However, only twenty filed proofs of claim, and only sixty percent of the claims qualified for PACA trust protection.[30] While holding that all creditors in compliance with PACA could share in the PACA trust, the court directed the bankruptcy trustee to

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[26] *Id.* at 796 (Emphasis added). *See also*, *In re* Marvin Properties, Inc., 76 B.R. 150 (9th Cir. BAP 1987) *aff'd*, 854 F.2d 1183 (9th Cir. 1988) (benefits of PACA trust not preserved merely because USDA has acknowledged receipt of trust notice. Filing of such a notice is one step toward perfecting trust rights, but unpaid sellers must also comply with every other statutory requirement to establish valid trust claims).

[27] 119 B.R. 10 (Bankr. D.Conn 1990).

[28] *Id.* at 11.

[29] In contrast to *Milton Poulos III*, the U.S. District Court in Gullo Produce Co. v. A. C. Jordon Produce Co., 751 F. Supp. 64 (W.D. Pa. 1990), took a more judicious approach by using non-intervention as one reason for excluding two trust claimants from its order of distribution.

[30] *United Fruit*, 119 B.R. at 11-12.

examine the claims for compliance with statutory notice requirements.[31] Presumably, a claimant who did not file a proof of claim with the bankruptcy court would be denied a share of the trust.[32] Unfortunately, the *Milton Poulos* court does not demand even this minimal level of participation before distributing PACA trust funds to any claimant appearing on USDA's list.

Milton Poulos also leaves open the issue of when a claim must be filed. Despite the apparent finality of the lower court's decision, the late claimants were included in a subsequent order granting relief from stay. Conceivably, this permits an indefinite time for potential claimants to step forward, whether or not they participated in the litigation.

In the absence of a statute of limitations for filing PACA trust claims, the courts may acknowledge trust claimants appearing after judgment, but before distribution of trust assets. This rule undercuts the primary purpose of the trust amendment: to promote prompt payment.

B. *Attorneys' Fees and Interest*

The PACA trust provisions do not contain an explicit right to interest, attorneys' fees and costs. However, several courts have either construed the statute broadly to include attorneys' fees or have relied on established exceptions[33] to the American Rule[34] to permit recovery of attorneys' fees.

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[31] *Id.* at 12.

[32] Although most of the PACA trust claimants in *United Fruit* filed proofs of claim with the bankruptcy court, the general majority of trust beneficiaries seek to enforce their trust rights by filing a motion for relief from the automatic stay and for turnover of the trust assets, or by filing an adversarial complaint against the debtor.

[33] *See, e.g.*, Aleyeska Pipeline Service Co. v. Wilderness Service, 421 U.S. 240, 257-59 (1975). Although the Supreme Court did not allow attorneys' fees in this instance, the Supreme Court did confirm the historic equity of federal courts to grant attorneys' fees in the interests of justice, independent of statutory authorization. *See also*, Mills v. Electric Auto Lite Co., 396 U.S. 375 (1970) (implied restrictions on the power to do equity are disfavored).

[34] The American Rule does not allow the prevailing party to recover attorneys' fees from the losing party, absent statutory authority. The court in *In re* W. L. Bradley, 78 B.R. 92 (Bankr. E.D. Pa. 1987) followed the American Rule and interpreted the PACA trust amendments restrictively to disallow attorneys' fees.

1. Attorneys' Fees

In *Pennsylvania Agricultural Cooperative Mktg. Ass'n v. Ezra Martin Co.*,[35] attorneys' fees were awarded under a PSA trust. The *Ezra Martin* court focused on 7 U.S.C. section 196(b), which states in part:

> All livestock purchased by a packer in cash sales, and all inventories of, or receivables or proceeds from meat, meat food products, or livestock products. . .shall be held by such packer in trust for the benefit of all unpaid cash sellers of such livestock until full payment has been received by such unpaid sellers. . . .[36]

The court construed "full payment" to include costs incurred by trust beneficiaries seeking to enforce their rights.[37] This conclusion was based on the logic that the PSA trust legislation was "clearly remedial," and should therefore be construed broadly to effectuate its purpose.[38] Accordingly, the court defined the phrase "full payment" expansively and granted unpaid livestock suppliers the broadest possible protection.

The court in *In re Monterey House, Inc.*,[39] examined the reasoning of the *Ezra Martin* court in reviewing a claim for attorneys' fees under the PACA trust amendments. In language similar to the PSA, the PACA trust amendment requires debtors to hold trust assets until "full payment of the sums owing in connection with such transactions has been received by" unpaid suppliers.[40] Furthermore, a purchaser must make prompt payment or be subject to a reparation order by the Secretary of Agriculture. Reasonable fees and expenses incurred by the prevailing party may be included in the reparation order.[41] If a lawsuit is required to enforce the reparation award, the complainant is entitled to reasonable attorneys' fees and costs. The court consequently adopted the method of statutory construction used in *Ezra Martin* and ruled that attorneys' fees may be awarded to PACA trust beneficiaries.[42]

Following the rationale of *Ezra Martin* and *Monterey House*, there appears to be statutory support for an award of attorneys' fees under the PSA and PACA trusts. Just as the threat of reparation orders are intended to encourage prompt payment, the PACA trust is similarly

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[35] 495 F. Supp. 565 (M.D. Pa. 1980).
[36] 7 U.S.C. § 196(b) (1988).
[37] *Ezra Martin*, 495 F. Supp. at 570.
[38] *Id.*
[39] 71 B.R. 244 (Bankr. S.D. Tex. 1986).
[40] *Id.* at 246.
[41] 7 U.S.C. § 499g(b) (1988).
[42] *Monterey House*, 71 B.R. at 248.

intended to remedy the financial dilemmas caused by "slow pay" and "no pay" practices. Moreover, USDA's trust regulations refer to the same time limits used for other parts of the PACA.[43] The statutory language creating the trust is broad, calling for full payment of the amount owed "in connection with" produce transactions.[44] When this language is liberally interpreted there is no need to resort to an analysis of the American Rule and its exceptions. An award of attorneys' fees is, therefore, consistent with the statutory purposes of the PACA.

An alternative approach to the issue of attorneys' fees was used in *Milton Poulos III*.[45] The *Milton Poulos* court applied the "common benefit" exception to the American Rule to justify an award of attorney's fees. The court recognized that the attorneys retained by the trust beneficiaries were:

> directly responsible for the availability of the funds from the statutorily created trust. Through their efforts, the bankruptcy court declared the trust valid and enforceable, thereby permitting the funds to be dispersed among the trust claimants. As the efforts of these attorneys resulted in a common fund for the group, we hold that they are entitled to recover their attorneys' fees out of the fund.[46]

Thus, two avenues to attorneys' fees exist; expansive interpretation of PACA trust amendments and a resort to the common benefit exception to the American Rule.

2. Interest

The threshold issue in determining whether to award interest is identification of a trust corpus, made up of assets that are not part of a debtor's bankruptcy estate. Interest on the trust should be granted as an integral part of the trust itself upon identification of the trust assets.

The first reported PACA decision on the issue of prejudgment interest was *Monterey House*.[47] The *Monterey House* court looked to earlier decisions interpreting the PSA trust. The court found that the earlier decisions had uniformly awarded prejudgment interest.[48] The *Monterey House* court accordingly awarded PACA trust beneficiaries pre- and

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[43] 7 C.F.R. § 46.46(f) (1991) (incorporating by reference the time limits for prompt payment set forth in 7 C.F.R. § 46.2(aa) (1991)).

[44] 7 U.S.C. § 499e(c)(2) (1988).

[45] 947 F.2d at 1353.

[46] *Id.*

[47] 71 B.R. 244 (Bankr. S.D. Tex. 1986).

[48] *Id.* at 248. *See also, In re* G & L Packing Co., 20 B.R. 789 (Bankr. N.D.N.Y. 1982), *aff'd*, 41 B.R. 903 (N.D.N.Y. 1984); *Ezra Martin*, 495 F. Supp. 565.

postjudgment interest as part of their trust claims.[49]

In *In re W. L. Bradley, Inc.*,[50] the court was unwilling to award attorneys' fees under the PACA, but recognized prejudgment interest as part of a trust claim. The *Bradley* court noted that: (1) statutory silence on prejudgment interest does not preclude prejudgment interest, and (2) without statutory authorization, the courts should consider the Congressional purpose in recognizing the underlying obligation.[51] As the *Bradley* court noted, the right to interest "is ultimately derived from the statute."[52] The court discussed Congressional concern with prompt payment in transactions governed by the PACA, and the harm that unpaid sellers may suffer resulting from slow pay practices and delays. The court also relied on the inherent equitable power of the federal courts to award prejudgment interest.[53]

Bradley has been followed by all subsequent PACA decisions, both published[54] and unpublished,[55] with the exception of *Milton Poulos I*. The *Milton Poulos I* court declined to exercise its equitable powers to award prejudgment interest, declined to follow PSA and PACA precedents, and ignored *Bradley*[56] because such an award "would unfairly deplete the bankruptcy estate at the expense of all other creditors."[57] On appeal, the BAP affirmed, finding no abuse of discretion by the lower court.[58] The court's decision overlooked Congressional intent to prevent slow pay practices in the fresh produce industry and instead favored "other estate creditors."

A determination as to the amount of funds, receivables, and other assets making up the trust, and hence not part of the estate, should be made independently of any claims that may be made by the estate's

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[49] Postjudgment interest in the federal district courts is available pursuant to 28 U.S.C. § 1961(a) (1991).

[50] 78 B.R. 92 (Bankr. E.D. Pa. 1987).

[51] *Id.* at 93, (citing Poleto v. Consolidated Rail Corp., 826 F.2d 1270 (3d Cir. 1987) and Rodgers v. United States, 332 U.S. 371 (1947)).

[52] *Bradley*, 78 B.R. at 94.

[53] *Id.* (citing Marshall v. Burger King Corp., 509 F. Supp. 353 (E.D.N.Y. 1981)).

[54] *See, e.g.*, Gullo Produce Co. v. A. C. Produce Co. Inc., 51 F. Supp. 64 (W.D. Pa. 1990).

[55] *See, e.g.*, Lyng v. Hancock-Nelson Mercantile, Inc., (*In re* Hancock-Nelson Mercantile, Inc.) Ch. 11, Case No. BKY 3-86-256, Adv. No. 2-86-105 (Bankr. D. Minn. Feb. 19, 1988).

[56] *See generally*, Campbell, *The Perishable Agricultural Commodities Act Regulatory Program*, § 4.12A, *in* 1 AGRICULTURAL LAW at 222 (J. Davidson ed. Supp. 1989) (wherein several decisions are discussed).

[57] *Milton Poulos I*, 94 B.R. at 653.

[58] *Milton Poulos II*, 107 B.R. at 719.

creditors in the bankruptcy proceeding. PACA trust beneficiaries are precisely that: beneficiaries of a trust, not creditors of the bankrupt debtor's estate. The PACA trust provisions were enacted to give PACA trust beneficiaries priority over estate creditors until the PACA trust assets are identified, distributed, and exhausted. Limiting the scope of the trust corpus out of concern for the estate creditors, ignores, in part, the statutory preference created by Congress.

Attorneys' fees, interest and costs may be significant expenses if protracted litigation is needed to enforce the trust. Interest and fees may be factors that alter the distribution of funds even when *pro rata* shares are allocated from a trust fund that will not satisfy all claims. Therefore, PACA trust claimants should always include attorneys' fees and interest as a component of their claims.

III. *Frio Ice, S.A. v. Sunfruit, Inc.*[59]

The Eleventh Circuit Court of Appeals issued this highly significant PACA decision in late 1990, and permitted PACA beneficiaries to enforce trust rights by injunction and through orders to segregate trust assets.[60]

A. *Factual Background*

Frio Ice sold nineteen shipments of asparagus to Sunfruit. When a dispute arose over the type of contract governing the transaction, Sunfruit refused to pay for the asparagus, and Frio Ice preserved its PACA trust benefits under 7 U.S.C. section 499e(c)(3). Frio Ice obtained a preliminary injunction requiring Sunfruit to place $229,831.14 in an interest-bearing trust account.[61]

Four months later, the District Court for the Southern District of Florida, *sua sponte* vacated the preliminary injunction. The court concluded, first, that PACA failed to grant federal courts jurisdiction to provide injunctive protection to private parties.[62] Second, the court ruled that no statutory authorization existed for an order segregating trust assets to prevent the dissipation or transfer of the trust *res*.[63]

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[59] 918 F.2d 154 (11th Cir. 1990) [hereinafter *Frio Ice II*], *rev'g* Frio Ice, S.A. v. Sunfruit, Inc., 724 F. Supp. 1373 (S.D. Fla. 1989) [hereinafter *Frio Ice I*].

[60] *Frio Ice II*, 918 F.2d at 160.

[61] *Frio Ice I*, 724 F. Supp. at 1376.

[62] *Id.* at 1378.

[63] *Id.* at 1376-77.

B. The Jurisdictional Issue

In ruling that the Secretary of Agriculture had exclusive authority to bring injunctive actions for the benefit of PACA claimants, the district court narrowly construed the jurisdictional provisions of the PACA:

> The several district courts of the United States are vested with jurisdiction specifically to entertain (i) actions by trust beneficiaries to enforce payment from the trust, and (ii) actions by the Secretary to prevent and restrain dissipation of the trust.[64]

The court interpreted this language to mean that jurisdiction extends *only* to suits for injunctive relief brought by the Secretary.[65]

The Court of Appeals reversed, ruling that the language of the statute gave district courts jurisdiction to issue private plaintiff injunctions.[66] The appellate court relied on *Califano v. Yamasaki*,[67] which states that federal courts have the equitable power to issue injunctions unless Congress has clearly withdrawn the remedy.[68]

The *Frio Ice* court further stated that, by using the general term "actions" in subsection (i) of the jurisdictional provisions of the PACA, Congress meant that the courts could entertain all civil actions to enforce a PACA trust, including actions by trust beneficiaries to obtain legal and equitable relief. Subsection (ii) was not viewed as limiting jurisdiction, but instead was giving the Secretary of Agriculture standing to sue when trust assets were being dissipated.[69] The court also stated that statutory language should be interpreted to resolve ambiguities and to permit the courts to exercise their powers in equity to the fullest extent.[70]

C. Segregation of Trust Assets

In holding that the district court could establish a separate bank account for the effective segregation of trust assets,[71] the *Frio Ice* court declined to follow *DeBruyn Produce Co. v. Victor Foods, Inc.*[72]

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[64] 7 U.S.C. § 499e(c)(4) (1988).

[65] *Frio Ice I*, 724 F. Supp. at 1379 (Emphasis added).

[66] *Frio Ice II*, 918 F.2d at 158.

[67] 442 U.S. 682 (1979).

[68] *Id.* at 705. In this case, the U.S. Supreme Court upheld the granting of injunctive relief under a jurisdictional provision of the Social Security Act which did not mention injunctive actions at all: 42 U.S.C. § 405(g) (1988).

[69] *Frio Ice II*, 918 F.2d at 158.

[70] *Id.* at 157. *See also*, Porter v. Warner Co., 328 U.S. 395 (1946).

[71] *Frio Ice II*, 918 F.2d at 159.

[72] 674 F. Supp. 1405 (E.D. Mo. 1987).

In *DeBruyn*, the court ruled that the PACA trust was preserved if the buyer made appropriate bookkeeping entries to identify trust assets.[73] However, the court refused to segregate trust assets in a supervised bank account, finding no authority expressly in the statute or impliedly in the legislative history.[74]

In comparison, the *Frio Ice* court decided that a court could segregate trust assets, under its inherent equitable powers, unless Congress clearly precluded such relief.[75] The court thereupon found no intent to preclude equitable segregation in the PACA or its legislative history. Consequently, the segregation of trust assets has emerged as an important, and often the exclusive, way to prevent the dissipation of the PACA trust.[76]

D. *Injunctive Relief in the Second Circuit*

Cases from the Second Circuit indicate that its Court of Appeals would probably follow *Frio Ice* if faced with similar facts. In *Dole Fresh Fruit Co. v. United Banana Co. Inc.*,[77] officers and employees of the debtor were restrained from dissipating trust assets.[78]

In *JSG Trading Corp. v. Tray-Wrap, Inc.*,[79] the court declined to segregate assets because the plaintiff did not produce evidence of dissipation. Without such evidence, the plaintiff could not establish the likelihood of irreparable harm and was not granted injunctive relief.[80] Even so, the court stated that it would be willing to grant injunctive relief to a private litigant, enjoining the dissipation of trust assets, if the likelihood of dissipation could be shown.[81] In dicta, the court did express reluctance to order the segregation of trust assets to prevent dissipation, preferring an order to "keep adequate records regarding the trust *res*."[82] This is similar to the questionable bookkeeping remedy of *DeBruyn*.

The *JSG* decision was made in the context of a contract dispute involving a solvent purchaser as the defendant, and a plaintiff who was

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73 *Id.* at 1407.
74 *Id.* at 1409.
75 *Frio Ice II*, 918 F.2d at 159.
76 *Id.*
77 821 F.2d 106 (2nd Cir. 1987).
78 *Id.* at 109.
79 917 F.2d 75 (2nd Cir. 1990).
80 *Id.* at 80.
81 *Id.* at 78-79.
82 *Id.* at 78.

seeking segregation of trust funds pending the outcome of its underlying contract claims. These facts make *JSG* distinguishable from the insolvent debtor situation.

The *JSG* decision also underscores the importance of establishing the traditional elements for preliminary injunctive relief in the federal courts: (1) likelihood of success on the merits; (2) irreparable harm; (3) balance of hardships; and (4) public interest.[83]

IV. Substantial Versus Strict Compliance

An apparent split has developed between the Eighth Circuit and the Ninth Circuit over the issue of whether strict compliance with the notice requirement of PACA is necessary to preserve trust benefits. Strict construction of the PACA trust regulations was employed in *In re Marvin Properties, Inc.*,[84] while substantial compliance has been held to be sufficient in *Hull Co. v. Hauser's Foods, Inc.*[85]

In *Marvin*, the Ninth Circuit Court of Appeals ruled that an unpaid seller lost PACA trust benefits when it did not give written notice of its intent to preserve trust benefits directly to the debtor.[86] The seller had filed a notice of intent to preserve trust benefits with the Secretary of Agriculture, and a copy of the Secretary's acknowledgement was mailed to the debtor. The debtor did not dispute that it had actual knowledge of the filing in this manner. Even so, the court decided that the debtor's actual notice was inadequate to perfect the PACA trust under section 499e(c)(3). Section 499e(c)(3) expressly requires the seller to give notice directly to the buyer:

> The unpaid supplier, seller, or agent shall lose the benefits of such trust unless such person has given written notice of intent to preserve the benefits of the trust to the commission merchant, dealer, or broker and has filed such notice with the Secretary. . . .[87]

The case of *In re D.K.M.B., Inc.*,[88] relied on the *Marvin* decision as authority for the proposition that there must be strict compliance with the notice provisions of the PACA regulations to preserve PACA trust

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[83] For a thorough discussion of the elements required to be established for injunctive relief in the context of litigation to enforce the PACA trust, *see* Rynn, *Injunctive Relief Under the 1984 Trust Amendments to the Perishable Agricultural Commodities Act: A Necessary Means of Trust Enforcement*, 23 U.C. Davis L. Rev. 625 (1990).

[84] 854 F.2d 1183 (9th Cir. 1988).

[85] 924 F.2d 777 (8th Cir. 1991).

[86] *Id.* at 1186.

[87] 7 U.S.C. § 499e(c)(3) (1988).

[88] 95 B.R. 774 (Bankr. D.Colo. 1989).

benefits.[89] Unlike *Marvin*, the *D.K.M.B.* case involved an unpaid supplier who did give notice to the purchaser of the supplier's intent to preserve PACA trust benefits. Strict compliance was lacking, however, because the written notices omitted some of the information required under the PACA regulations.[90]

The court rejected the seller's argument of substantial compliance with the statute and regulations. To the court, nothing less than strict compliance would preserve the trust. The existence of a PACA trust would keep most of the debtor's funds out of the bankruptcy estate "without regard to the claims of other creditors" and "would effectively prevent the equitable distribution of debtor's assets among its creditors." This result would frustrate "the Congressional intent behind the Bankruptcy Code, which is to provide an orderly, fair, and equitable distribution of a debtor's assets among its creditors."[91]

The court in *In re Lombardo Fruit & Produce*[92] relied upon *D.K.M.B.* to require strict statutory compliance. The PACA allows parties to agree to payment terms up to thirty days from the date of delivery, provided the agreement is expressed in writing prior to the transaction.[93] According to the *Lombardo Fruit* court, the parties did not comply with the above mentioned statutory prerequisite with an undated letter to the debtor extending payment terms to thirty days.[94]

Another recent case calling for strict compliance with the PACA is *In re John DeFrancesco & Sons, Inc.*[95] Here the trust notices were addressed to the individual principals of the corporate purchaser rather

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[89] *Id.* at 779.

[90] This regulation states:

> "(3) An appropriate notice of intent to preserve trust benefits must be in writing, must include the statement that it is a notice of intent to preserve trust benefits, and must include information which establishes for each shipment:
>
> (i) The name and addresses of the trust beneficiary, seller-supplier, commission merchant, or agent and the debtor, as applicable,
>
> (ii) The date of the transaction, commodity, contract terms, invoice price, and the date payment was due,
>
> (iii) The date of receipt of notice that a payment instrument has been dishonored (if appropriate),
>
> (iv) The amount past due and unpaid."

7 C.F.R. § 46.46(g)(3) (1991).

[91] *D.K.M.B.*, 95 B.R. at 779.

[92] 106 B.R. 593 (Bankr. E.D. Mo. 1989).

[93] 7 U.S.C. § 499e(c)(3)(ii) (1988).

[94] *Lombardo Fruit*, 106 B.R. at 600.

[95] 114 B.R. 335 (Bankr. D. Mass. 1990).

than the corporation itself. This was ruled to be insufficient evidence that the corporation was given notice of intent to preserve the PACA trust.[96]

In contrast to the "strict compliance" line of cases discussed above, there are cases where the courts have seen fit to enforce a PACA trust if "substantial compliance" with the statute and regulations by the unpaid seller are found. The bankruptcy court ruled in *In re Carlton Fruit Co. Inc.*,[97] that the seller's failure to include all of the information required by the PACA regulations in its notice to the purchaser was not fatal to the imposition of the PACA trust.[98] *Carlton Fruit* was similar to *D.K.M.B.*, except that only the buyer could have supplied the missing information, and the court found that the seller had done everything possible to otherwise comply with the notice requirements.[99]

A better case for substantial compliance was made by the U.S. District Court in *In re Aannde Foods, Inc.*[100] The unpaid seller complied with the PACA notice requirements when it sent to the purchaser copies of letters addressed to the U.S. Department of Agriculture. The delivery of these copies was treated as sufficient notice[101] to the purchaser, and the court rejected the argument that such notice was not strict compliance under *D.K.M.B.*[102]

In re Richmond Produce[103] states the most cogent analysis of the "substantial compliance" versus "strict compliance" approach to the PACA trust statute and regulations. Among the issues before the court was an argument that a notice of intent to preserve trust benefits is ineffective if such notice is given in anticipation of default, but before a default occurs.[104] This argument was based in part on the strict construction approach to the PACA enunciated in *Marvin*. The court disagreed, interpreting *Marvin* to mean that a PACA trust claim must fail

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[96] *Id.* at 338.

[97] 84 B.R. 810 (Bankr. M.D. Fla. 1988).

[98] *Id.* at 812.

[99] *Id.*

[100] 110 B.R. 346 (Bankr. N.D. Ill. 1989).

[101] The notice was worded as a "request" to preserve trust benefits rather than a "notice of intent", but the court did not consider this to be a fatal defect in the notices. Nor was it fatal to the action that the notices did not state when payments for the goods were due. The unpaid seller had attached copies of its invoices to the notices and the invoices set forth payment terms of net ten days. With no evidence that the parties had agreed to other payment terms, the statute supplied the time for payment and omission of this term did not make the notices defective. *Id.* at 352.

[102] *Id.*

[103] 112 B.R. 364 (Bankr. N.D. Cal. 1990).

[104] *Id.* at 369-70.

when a trust claimant fails to comply with plain statutory language. In *Marvin*, "the Ninth Circuit Court of Appeals did not comment as to whether PACA should be given a liberal or strict construction," and the opinion "does not stand for the general proposition that PACA must be strictly construed. Rather, it stands for the proposition that the plain unambiguous requirements of the statute may not be disregarded."[105] Correctly noting that a liberal construction of the statute should be given to effect its remedial purposes, the court employed a liberal construction of the PACA to hold that the early notices were not premature, ineffective, or in conflict with the statutory timing requirements.[106]

The debtor also challenged the sufficiency of some of the trust notices and described several alleged deficiencies resulting from failure to include all of the information mandated by the regulations at 7 C.F.R. section 46.46(g)(3). In response, the court considered and rejected the strict compliance analysis of the *D.K.M.B.* opinion. In refusing to follow *D.K.M.B.*, the court pointed out that the PACA is not inherently inconsistent with the Bankruptcy Code. The legislative history for Bankruptcy Code section 541 (defining the bankruptcy estate) explicitly refers to the statutory trust established under the Packers and Stockyards Act and explains that section 541 would not affect other statutes creating "a trust fund for the benefit of a creditor of the debtor."[107]

The *Richmond Produce* opinion also undercuts the strict compliance approach by noting that the PACA statutory provisions do not require that notices state the long list of information demanded by the regulations. Since the statute did not require regulations regarding the contents of notices, the court did not defer to the regulations as it might have otherwise done. Because the notices identified transactions at issue, and there was no showing that anyone was misled by the omitted information, the court held that substantial compliance was sufficient to preserve each claimant's PACA trust rights.[108]

Finally, the substantial compliance approach was adopted in the Eighth Circuit Court of Appeals in *Hull Co. v. Hauser's Foods, Inc.*[109] The court rejected the strict compliance approach in favor of liberal construction of the PACA statute to effectuate its remedial pur-

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[105] *Id.* at 370.

[106] *Id.*

[107] *Id.* at 371-72 (citing H.R. REP. NO. 95-595, 95th Cong., 1st Sess., 367-68 (1977), and SENATE REPORT NO. 95-989, 95th Cong., 2d Sess., 82-83 (1978)).

[108] *Richmond Produce*, 112 B.R. at 372.

[109] 924 F.2d 777 (8th Cir. 1991).

poses. Specifically, the court ruled that the trust notices, together with the seller's unpaid invoices attached thereto, provided all the information required by the regulations, thereby preserving trust benefits.[110] The court also disregarded an alleged oral agreement between buyer and seller to extend payment terms to forty-five days after delivery. If such an agreement had been written, it would have disqualified the seller from seeking trust protection under 7 C.F.R. section 46.46(f)(1). The court refused to recognize the oral agreement when the only effect would be to defeat the legislative purpose and void the trust.[111]

Consequently, the *Hull Co.* case and the substantial compliance approach to preserving PACA trust rights stands as an appellate counterweight to the strict compliance view of the PACA regulatory burden articulated by the courts following the *Marvin Properties* decision in the Ninth Circuit. As long as some courts see the PACA trust to be fundamentally at odds with the legislative scheme expressed in the Bankruptcy Code, the courts will have enough precedent to use strict construction to frustrate all but the most careful PACA trust claimants. On the other hand, courts that weigh the legislative purpose of the PACA trust equally with the legislative intent behind the Bankruptcy Code will rely upon *Richmond Produce* and *Hull Co.* to justify a more liberal construction of the PACA's requirements.

Conclusion

For many unpaid produce suppliers, the incentive to enforce their PACA trust rights was being eroded by courts who perceived a clash between the PACA statutory trust amendments and the Bankruptcy Code. By requiring "strict compliance" with the PACA requirements, the courts effectively sheltered the debtor's estate from PACA trust claimants. Some courts have declined to exercise their equitable powers to award attorneys' fees and interest to trust beneficiaries.

To eliminate a "race to the courthouse," the courts have taken the reasonable position that PACA trust assets should be available to all trust beneficiaries. However, this approach can be unfair to those trust claimants who take the initiative by retaining legal counsel to establish the existence and validity of the trust. The trust claimants who fail to take the initiative seem unjustly enriched; They avoid the costs and uncertainties of the litigation to establish the trust, yet benefit equally with the earlier claimants. The *Milton Poulos* decision will eliminate

[110] *Id.* at 783.
[111] *Id.* at 782.

some of the inequity if other courts adopt its reasoning and award attorneys' fees to prevailing trust beneficiaries. On the other hand, *Milton Poulos* permits the practice of "sitting on the sidelines" until others have established the existence of the trust as a common fund. As a solution to this problem, Congress could supply a statute of limitations which would bar PACA trust claimants who fail to intervene in actions to enforce the trust after being served with notice of pending litigation.[112] USDA could respond to *Milton Poulos* by revising the language in its correspondence giving debtors notice of the existence of potential PACA trust claims. These so-called "certification letters" should contain an express statement to the effect that the letter is not conclusive evidence that claimants have properly perfected their trust rights.

The most positive recent development has come from the Eleventh Circuit where the Court of Appeals has upheld the rights of PACA trust claimants to seek injunctive relief to enforce the PACA trust. *Frio Ice* may have finally settled this issue by declaring that federal courts have jurisdiction to hear suits for equitable relief by private parties and affirming that such relief may take the form of a court order to segregate and halt the dissipation of trust assets.

Finally, the Eighth Circuit Court of Appeals has endorsed the argument that substantial compliance with the PACA statutory provisions and regulations is sufficient to preserve trust benefits. PACA trust claimants can be optimistic and hope that this liberal approach to the construction of the PACA will spread to the other federal circuits, including the bankruptcy courts.

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[112] At least two cases have dealt with an asserted statute of limitations in the context of the PACA trust. In an unreported decision, it was held that a statute of limitations does not apply to actions for equitable relief such as an action by the Secretary of Agriculture for an injunction to restrain dissipation of a PACA trust. Lyng v. Frydman, No. C86-1210Y (N.D. Ohio Feb. 3, 1987). In another case, it was held that the nine month statute of limitations set forth in 7 U.S.C. § 499f(a) limits only administrative actions for reparations before the Secretary of Agriculture and does not apply to a civil action in federal district court to enforce payment of a PACA trust. *In re* So Good Potato Chip Co., 124 B.R. 298 (Bankr. E.D. Mo. 1991).