

Licensing Under the Perishable Agricultural Commodities Act: Is a USDA Apology Enough to Rescue a PACA Licensee?

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The United States District Court for the Southern District of Ohio was recently presented with a strange set of facts regarding a purported licensee under the Perishable Agricultural Commodities Act (PACA). The issue was whether an acknowledged mistake by the United States Department of Agriculture (USDA) – accompanied by a written USDA apology, no less – was sufficient to retroactively reinstate the licensee status of a produce producer. The court considered a number of arguments brought by a secured creditor, and ruled that the USDA had the power to correct a mistake. As is common in PACA cases, the ruling potentially has the effect to ensure that the produce producer gets paid in full, while other creditors are left to fight over any remaining assets.

The case, *Dusty Acres v. JAO Distributors, Inc.*, 2015 WL 4910970 (S.D. Ohio August 10, 2015), involved a farmer and producer of fresh produce operating under the trade name Dusty Acres. Dusty Acres had a PACA license issued by the USDA as of May 21, 2012. Dusty Acres was required to renew the license with the USDA annually. Produce producers with PACA licenses are provided with critical protection in the event the purchaser of the produce becomes financially distressed and is unable to pay its many creditors. PACA is a federal statute that creates a "floating trust" in the proceeds of the produce sales. Produce producers who have properly complied with PACA have claims to the trust funds superior to all other claimants, including secured creditors. The purpose of PACA is to protect farmers from catastrophic loss when brokers or other produce producers become financially distressed. For a detailed discussion of PACA trusts, see *Farmer Favoritism, Statutory Protections for Creditors in Agricultural Bankruptcy Cases*.

Dusty Acres allowed its PACA licensee status to expire on the anniversary date of May 21, 2013. A representative of the USDA notified Dusty Acres of the expiration, and Dusty Acres thereafter submitted a renewal application to the USDA via fax on August 3, 2013. Dusty Acres did not follow up on the matter and assumed it was once again a PACA licensee in good standing. During the months of August and September 2013, Dusty Acres sold \$251,017 worth of produce to distributor JAO Distributors, Inc. (JAO). JAO ceased operating in October 2013 and a receiver was later appointed. While JAO did not file bankruptcy, the case involved claim priority issues similar to those in a bankruptcy matter. Namely, JAO creditor Fifth Third Bank, which had a security interest in the produce, argued that its security interest entitled it to be paid the produce proceeds prior to any other creditor, including Dusty Acres. The claim priority fight therefore came down to whether Dusty Acres was a PACA licensee in September and October 2013. If Dusty Acres was a licensee, it would be entitled to the proceeds. If it was not a PACA licensee, Fifth Third Bank would take priority over the funds.

Unfortunately for Dusty Acres, the USDA mistakenly did not process its August 3, 2013 application. In February 2014, Dusty Acres' counsel contacted the Director of the USDA National Licensing Center, PACA Division regarding the mistake. The Director responded with a written letter acknowledging that Dusty Acres' application was handled "inappropriately"

and offering an apology. The Director further stated in the letter that, because the mistake was on the part of the USDA and not Dusty Acres, the USDA was reinstating Dusty Acres' license retroactively as of May 2013.

Fifth Third Bank filed a motion for summary judgment in the U.S. District Court for the Southern District of Ohio asserting, on a number of different grounds, that Dusty Acres was not a PACA licensee, and that Fifth Third Bank's claim was entitled to priority. The court addressed each argument in turn. Fifth Third Bank first argued that the USDA did not have the power to retroactively reinstate a license and that providing the USDA with such power would allow the USDA to "unlawfully usurp" the legislative power of Congress. The court responded that the issue involved a mistake, not an attempt by the USDA to rewrite a statute or administrative rule. The court thus held that the USDA is permitted to correct its own mistake via the retroactive action it took. Next, Fifth Third Bank argued that Dusty Acres was precluded by equitable estoppel from making its arguments because Dusty Acres placed confidence (or more accurately, misplaced confidence) in the USDA to process its application and because Dusty Acres allowed the license to expire in the first place. The court stated that these arguments were not well-taken. The court found that Dusty Acres was not provided with any indication by the USDA that there was an issue with its renewal application. The court further noted that JAO believed Dusty Acres was a licensee during the relevant time period and there was no evidence that Fifth Third Bank detrimentally relied on the apparent license termination.

The court also addressed a number of public policy arguments asserted by Fifth Third Bank. Essentially, Fifth Third Bank argued that Dusty Acres should bear the loss of the USDA's mistake because otherwise creditors such as Fifth Third Bank would be required to conduct inquiries into whether the public record accurately stated a PACA licensee's status. On this point, the court held that the USDA's action in addressing the mistake as not plainly erroneous or inconsistent with regulations and therefore the court would defer to the USDA's determination that a retroactive reinstatement was appropriate. Finally, Fifth Third Bank argued that it was entitled to the funds as a bona fide purchaser. The court analyzed this argument in the context of trust funds, noting that a bona fide purchaser must give value for trust property, and must have no actual or constructive notice of the breach of trust. The court held that these were factual issues that could not be resolved at summary judgment. The court therefore denied Dusty Acres' cross motion for summary judgment on that matter.

It thus remains to be seen in the case whether Fifth Third Bank will prevail on the bona fide purchaser fact issue. However, the case clearly illustrates the importance of a produce producer dutifully maintaining its PACA licensee status. While a written letter from the USDA protected Dusty Acres in this case, other purported licensees may not be so lucky. It stands to reason that requesting confirmation from the USDA that a license renewal has been processed is prudent produce producer practice.