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DEPARTMENT OF AGRICULTURE

Agricultural Marketing Service

[Document Number AMS-FV-09-0047]

7 CFR Part 46

Perishable Agricultural Commodities Act: Impact of Post-Default Agreements on Trust Protection Eligibility

AGENCY: Agricultural Marketing Service, USDA.

ACTION: Final rule.

SUMMARY: The Department of Agriculture (USDA) is amending the regulations under the Perishable Agricultural Commodities Act (PACA) to allow, if there is a default in payment as defined in the regulations, a seller, supplier, or agent who has met the PACA trust eligibility requirements to enter into a scheduled agreement for payment of the past due amount without foregoing its trust eligibility. USDA is also amending 7 CFR 46.46(e)(2) by adding the words “prior to the transaction.” This change clarifies that the 30-day maximum time period for payment to which a seller can agree and still qualify for coverage under the trust refers to pre-transaction agreements.

DATES: *Effective Date:* April 13, 2011.

FOR FURTHER INFORMATION CONTACT: Phyllis L. Hall or Josephine E. Jenkins, Trade Practices Section, 202-720-6873.

SUPPLEMENTARY INFORMATION:

Background of PACA Trust Provisions

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

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, and reduced to 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.

Over the past few years, several federal courts have invalidated the trust rights of unpaid creditors because these creditors agreed in writing, and in some cases, by oral agreement, after default on payment, to accept payments over time from financially troubled buyers. In general, these courts have invalidated the seller’s previously perfected trust rights because the agreements were deemed to extend payment terms beyond 30 days.¹

¹ See, *Paris Foods Corp. v. Foresite Foods, Inc.*, No. 1:05-cv-610-WSD, 2007 WL 568841 (N.D. Ga. Feb. 20, 2007); *Bocchi Americas Assoc. v. Commerce Fresh Mktg., Inc.*, No. Civ. A. H0402411, 2005 WL 3164240 (S.D. Tex. Nov. 28, 2005); *American Banana Co. v. Republic Nat. Bank of N.Y.*, 362 F.3d 33 (2nd Cir. 2004); *Patterson Frozen*

The court decisions at issue have held that any post-default agreement, whether oral or written, that extends the buyer’s obligation to pay the seller’s invoices beyond 30 days after receipt and acceptance of the produce abrogates the produce seller’s PACA trust rights. These decisions have held that (1) when a seller enters into the post-default agreement, the agreement modifies any valid payment agreement entered into prior to the transaction and therefore voids the trust protection,² and (2) post-default agreements that allow for installment payments exceeding 30 days from receipt of produce violate the PACA prompt-pay provisions.³

Many of the court decisions at issue have been based on an interpretation of § 46.46(e) of the regulations (7 CFR 46.46(e)). Section 46.46(e)(1) (7 CFR 46.46(e)(1)) requires that parties who elect to use different times for payment must reduce their agreement to writing before entering into the transaction. Current § 46.46(e)(2) (7 CFR 46.46(e)(2)) states that the maximum time for payment for a shipment to which a seller can agree and still qualify for coverage under the trust is 30 days after receipt and acceptance of the commodities. It is our interpretation that § 46.46(e)(2), like paragraph (e)(1) of the regulations (7 CFR 46.46(e)(1) and (e)(2)), addresses pre-transaction agreements only.

This interpretation of our regulations is consistent with the Secretary’s unwillingness to impute a waiver of trust rights as illustrated in the policies established by the Secretary and upheld by the courts in the context of the trust provisions of the Packers and Stockyards Act (7 U.S.C. 181 *et seq.*), after which the PACA trust provisions are largely modeled.⁴ In the context of the PACA trust, the right to make a claim against the trust are vested in the seller, supplier, or agent who has met the eligibility requirements of paragraphs (e)(1) and (2) of § 46.46 (7

Foods, Inc. v. Crown Foods, Int’l, 307 F.3d 666, 667 (7th Cir. 2002); *Greg Orchards Produce, Inc. v. P. Roncone J.*, 180 F.3d 888, 892 (7th Cir. 1999); *Idahoan Fresh v. Advantage Produce, Inc.*, 157F.3d 197, 205 (3d Cir. 1998); *In re Lombardo Fruit and Produce Co.*, 12 F.3d 806, 809 (8th Cir. 1993); and *Hull v. Hauser’s Foods, Inc.*, 924 F.2d 777, 781-82 (8th Cir. 1991).

² See *American Banana Co.*, 362 F.3d at 33; *Patterson Frozen Foods*, 307 F.3d at 669.

³ *American Banana Co.*, 362 F.3d at 46.

⁴ See, e.g., *In re Gotham Provision Co., Inc.*, 669 F.2d 1000, 1007 (5th Cir. 1982).

CFR 46.46(e)(1) and (2)). The seller, supplier, or agent remains a beneficiary of the PACA trust until the debt owed is paid in full as stated in section 5(c)(4) of the statute. An agreement to pay the antecedent debt in installments is not considered payment in full. Thus, we do not believe that a post-default payment agreement should constitute a waiver of a seller's previously perfected trust rights.

Notice of Proposed Rulemaking

In response to the Fruit and Vegetable Advisory Committee's request that the Secretary of Agriculture address the impact of post-default payment agreement on PACA trust eligibility, a proposed rule to amend PACA regulations was published in the **Federal Register** on June 8, 2010, [75 FR 32306].⁵ The proposal sought to amend Title 7, Part 46 to ensure that qualified PACA trust beneficiaries maintain their trust protection after entering into a post-default agreement. The comment period initially closed on August 9, 2010. However, the comment period was reopened and extended an additional 30 days. The reopening of the comment period was published in the **Federal Register** on August 23, 2010, [75 FR 51693]. The comment period closed a second time on September 22, 2010.

The proposal sought to amend 7 CFR 46.46(e)(2) by adding the words "prior to the transaction." This change would clarify that the 30-day maximum time period for payment for a shipment to which a seller can agree and still qualify for coverage under the trust relates back to paragraph (e)(1) which refers to pre-transaction agreements.

The proposal also added a new paragraph (e)(3) to 7 CFR 46.46. The new paragraph provided that in circumstances of a default in payment as defined in § 46.46(a)(3), a seller, supplier, or agent who has met the eligibility requirements of § 46.46 paragraphs (e)(1) and (2) could agree in writing to a schedule for payment of the past due amount and still remain eligible under the trust. The post-default payment agreement could not extend beyond 180 days from the default date.

Comments

AMS received 130 timely comments. The commenters substantially approved of the proposed rule, except in regard to the limits on the length of post-default payment agreements and on collection activities. They expressed concerns that the suggested wording in the proposed

regulation may itself create the same confusion, uncertainty, and need for costly litigation that the new regulation aims to eliminate. Eighty-nine of the 130 commenters offered alternative language for the amendment, four of which included the rationale for the suggested alternative language. These 89 commenters favored the removal of the requirement of a written post-default agreement and recommended the deletion of the last three sentences of § 46.46(e)(3) of the proposed rule which (1) set a 180-day limitation on post-default agreements, (2) limited collection activities in cases of bankruptcy and civil actions, and (3) stated that the remaining unpaid amount under the scheduled payment agreement continued to qualify for trust protection.

Twenty-three of the 130 comments raised legitimate concerns about the proposed changes to the regulations, stating:

1. It is contrary to the law—only full payment ends a supplier's trust rights. The commenters suggested that the proposed rule conflicts with the statutory language that a trust creditor remains eligible for trust benefits until it has received full payment.

2. The regulation cements a post-default waiver rule in the regulations. The commenters reason that if the Secretary acknowledges in the regulations that some post-default agreements can forfeit trust rights, this could be interpreted by the courts to prohibit all post-transaction agreements.

3. The proposed regulation will result in more problems than currently exist. The comments noted that there is no problem in the industry with post-default agreements to collect trust assets outside of litigation, so, no regulatory action is required over such agreements.

4. Routine past due collection efforts will jeopardize trust rights. The language in the proposed rule would necessitate that every time there is a past due debt, sellers will have to consult a PACA lawyer.

5. All claims in trust cases would be subject to extensive litigation about post-default collection efforts. Commenters noted that initially, produce suppliers try to resolve past due payments over the phone, thus, under the proposed rule, every subsequent trust claim will be the subject of the same expensive litigation to determine if there was a forfeiture due to an oral post default agreement.

We recognize the serious nature of the concerns the comments raise: That the proposed regulation, as written, is contrary to the plain language of the statute that trust creditors remain

eligible until fully paid; that the proposed regulation could be interpreted broadly to prohibit all post-transaction agreements; that it creates new problems; that routine collection activities could jeopardize trust rights and give rise to extensive litigation. Because we agree with these comments, we are revising the regulation.

Twenty-eight of the 130 commenters specifically requested that the 180-day cap for post-default payment plans be stricken from the proposed rule, indicating that it may be unrealistic under a multitude of circumstances, and that the time limitation would create new challenges to the trust eligibility of a creditor who attempts to collect on a past due debt. We agree.

In addition, we agree that Congress intended that the seller, supplier, or agent remains a beneficiary of the PACA trust until the debt owed is paid and, recognizing that a 180-day limitation would create a new time limitation and new opportunity for litigation and misinterpretation of the regulations. Therefore, we are removing the 180-day limitation of post default agreements from the final rule.

Commenters noted that initially, produce suppliers try to resolve past due payments over the phone, thus, under the proposed rule, every subsequent trust claim will be the subject of the same expensive litigation to determine if there was a forfeiture due to an oral post default agreement. Because we agree with the comments that it is typical for produce suppliers to attempt to resolve past due payments over the telephone and, a requirement for a written post-default agreement would be burdensome and unnecessary, we are removing the requirement that a post-default agreement must be in writing from the final rule.

It is our interpretation of the statute and regulations that post-default agreements are not an extension of the 30-day maximum time period for pre-transaction agreements that would result in a waiver of the seller's trust rights; post-default payment agreements are an attempt to collect a debt that remains due until fully paid. The Secretary has long recognized a significant difference between the relative positions of buyers and sellers before a transaction, versus their positions after a buyer defaults on payment. The Secretary has observed that "produce sellers are not in an equal bargaining position with produce purchasers who are in possession of the produce seller's perishable agricultural

⁵ To view the proposed rule and the comments we received, go to <http://www.regulations.gov>.

commodities.”⁶ After a buyer has defaulted on payment, the seller is at the buyer’s mercy since produce deteriorates rapidly, leaving no collateral. Any agreement reached after default is not an arm’s length transaction. The trust is intended to provide protection to the unpaid seller whose bargaining position has changed for the worse after delivering its produce to a buyer. We do not believe that a seller’s perfected trust rights should be lost because the seller enters into a payment arrangement, in an attempt to collect a debt, after the buyer has violated the PACA’s prompt payment requirement.

We also agree with the comments from a California law firm that specializes in PACA law regarding the proposal to limit collection activities in cases of bankruptcy and civil actions. The commenter reminded us that limits on collection activities in cases of bankruptcy and civil actions are “already amply controlled under existing laws and procedures administered by the United States district and bankruptcy courts* * *.” Because laws already exist to ensure that a buyer in bankruptcy and civil actions cannot continue to make preferential payments to select creditors, we are eliminating the third and fourth sentences in § 46.46, paragraph (e)(3) of the final rule.

One commenter, a New Jersey based attorney specializing in PACA, recommended that the Secretary withdraw the proposed new regulation and solicit further suggestions for alternate language. USDA opted not to implement this recommendation. This commenter also included a suggestion for changes to § 46.46 (c)(1), § 46.2(aa)(11). The commenter suggested a new paragraph in § 46.46 to address payment terms with a debtor who has entered into a post-default agreement. We do not adopt the suggestion, as it presents significant problems of implementation and interpretation by bringing separate, subsequent transactions into the analysis. USDA also opted not to adopt this suggestion because it is beyond the scope of the proposed rule.

The courts have expressed concern that post-default agreements could undermine the enforcement of the prompt pay provisions of the PACA. No commenters echoed the courts’ concerns. When a buyer defaults on payment for produce, it has committed a violation of section 2(4) of the PACA (7 U.S.C. 499b(4)). The defaulting

buyer’s license is then subject to suspension or revocation, or the buyer may be assessed a civil penalty for its violations of the PACA. Allowing a seller who has perfected its trust rights to enter into a post-default payment agreement with the defaulting buyer does not negate the buyer’s violations of the Act. The trust is a means to protect the seller’s right to payment for produce, not to enforce the prompt payment provisions of the Act. The Secretary can still initiate an enforcement action against the buyer to seek the appropriate sanction for violations of the Act without regard to any post-default agreement entered into between the unpaid seller and the buyer in default.

Based on full consideration of comments received during the initial and reopened comment periods, USDA has determined that it is appropriate to simplify the language of the final rule in order to avoid creating any additional confusion, uncertainty, and unnecessarily protracted, costly litigation about post-default agreements and collection efforts. New § 46.46(3) will be amended to delete the last three sentences of the proposal, and permit post-default agreements made in any manner. Furthermore, accepting partial payments after default would not affect a seller’s trust rights.

No comments addressed the proposal to amend § 46.46(e)(2) by adding the words “prior to the transaction.” This change would clarify that the 30-day maximum time period for payment for a shipment to which a seller can agree and still qualify for coverage under the trust relates back to paragraph (e)(1) which refers to pre-transaction agreements. Therefore, this change is finalized as proposed.

Executive Orders 12866 and 12988

This final rule has been determined to be not significant for the purposes of Executive Order 12866, and therefore, has not been reviewed by the Office of Management and Budget. This final rule has been reviewed under Executive Order 12988, Civil Justice Reform, and is not intended to have retroactive effect. This final 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 final 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 final 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. The Small Business Administration (SBA) has defined small agricultural service firms (13 CFR 121.601) as those whose annual receipts are less than \$7,000,000. There are approximately 14,400 firms licensed under the PACA, a majority of which could be classified as small entities.

The final regulations would clarify that a trust beneficiary who has perfected its trust rights does not forfeit those rights by entering into a post-default agreement to accept partial or installment payments on the amount past due. This language would provide companies of all sizes with clear regulatory guidance on this matter, thereby reducing the time and expense associated with litigating matters involving post-default agreements and trust right preservation under the PACA. Therefore, we believe that this final rule will not have a significant economic impact on a substantial number of small entities.

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 final 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/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, Definitions, Accounts and records, Duties of licensees, Statutory trust.

For the reasons set forth in the preamble, 7 CFR part 46 is amended as follows:

PART 46—[AMENDED]

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

⁶ See *In re: Scamcorp, Inc.*, 57 Agric. Dec. 527, 563 (1998).

Authority: 7 U.S.C. 499a–499t.

■ 2. In § 46.46, paragraph (e)(2) is revised, paragraphs (e)(3) and (4) are redesignated as paragraphs (e)(4) and (5), and a new paragraph (e)(3) is added as follows:

§ 46.46 Statutory trust.

* * * * *

(e) * * *

(2) The maximum time for payment for a shipment to which a seller, supplier, or agent can agree, prior to the transaction, and still be eligible for benefits under the trust is 30 days after receipt and acceptance of the commodities as defined in § 46.2(dd) and paragraph (a)(1) of this section.

(3) If there is a default in payment as defined in § 46.46(a)(3), the seller, supplier, or agent who has met the eligibility requirements of paragraphs (e)(1) and (2) of this section will not forfeit eligibility under the trust by agreeing in any manner to a schedule for payment of the past due amount or by accepting a partial payment.

* * * * *

Dated: April 5, 2011.

Ellen King,

Acting Administrator, Agricultural Marketing Service.

[FR Doc. 2011–8718 Filed 4–11–11; 8:45 am]

BILLING CODE 3410–02–P

DEPARTMENT OF AGRICULTURE

Food Safety and Inspection Service

9 CFR Parts 391, 590, and 592

[FDMS Docket Number FSIS–2006–0025]

RIN 0583–AD40

New Formulas for Calculating the Basetime, Overtime, Holiday, and Laboratory Services Rates; Rate Changes Based on the Formulas; and Increased Fees for the Accredited Laboratory Program.

AGENCY: Food Safety and Inspection Service, USDA.

ACTION: Final rule.

SUMMARY: The Food Safety and Inspection Service (FSIS) is amending its regulations to establish formulas for calculating the rates that it charges meat and poultry establishments, egg products plants, and importers and exporters for providing voluntary, overtime, and holiday inspection, and identification, certification, and laboratory services. The 2011 basetime, overtime, holiday, and laboratory services rates in this final rule will be

applied on the effective date. For future years, FSIS will use the formulas established to calculate the annual rates. FSIS will publish the rates annually in **Federal Register** notices prior to the start of each calendar year and will apply them on the first FSIS pay period at the beginning of the calendar year. The Agency is also increasing the codified flat annual fee for its Accredited Laboratory Program for FY 2012 and FY 2013.

DATES: This final rule is effective May 22, 2011.

FOR FURTHER INFORMATION CONTACT: For further information concerning policy issues contact Rachel Edelstein, Director, Policy Issuances Division, Office of Policy and Program Development, FSIS, U.S. Department of Agriculture, Room 6065 South Building, 1400 Independence Ave., SW., Washington, DC 20250–3700; telephone (202) 720–0399, fax (202) 690–0486.

For further information concerning fees contact Michele Torrusio, Director, Budget Division, Office of Management, FSIS, U.S. Department of Agriculture, Room 2159 South Building, 1400 Independence Avenue, SW., Washington, DC 20250–3700; telephone (202) 720–8700, fax (202) 690–4155.

SUPPLEMENTARY INFORMATION:

Background

The Federal Meat Inspection Act (FMIA) (21 U.S.C. 601 *et seq.*) and the Poultry Products Inspection Act (PPIA) (21 U.S.C. 451 *et seq.*) provide for mandatory Federal inspection of livestock and poultry slaughtered at official establishments and of meat and poultry processed at official establishments. The Egg Products Inspection Act (EPIA) (21 U.S.C. 1031 *et seq.*) provides for mandatory inspection of egg products processed at official plants. FSIS bears the cost of mandatory inspection provided during non-overtime and non-holiday hours of operation. Official establishments and official egg products plants pay for inspection services performed on holidays or on an overtime basis.

Under the Agricultural Marketing Act of 1946 (AMA), as amended (7 U.S.C. 1621 *et seq.*), FSIS provides a range of voluntary inspection, certification, and identification services to assist in the orderly marketing of various animal products and byproducts. These services include the certification of technical animal fats and the inspection of exotic animal products, such as antelope and elk products. The AMA provides that FSIS may assess and collect fees to recover the costs of the

voluntary inspection, certification, and identification services it provides.

Also under the AMA, FSIS provides certain voluntary laboratory services that establishments and others may request the Agency to perform. Laboratory services are provided for four types of analytic testing: Microbiological testing, residue chemistry tests, food composition tests, and pathology testing. Again, the AMA provides that FSIS may collect fees to recover the costs of providing these services.

FSIS also accredits non-Federal analytical laboratories under its Accredited Laboratory Program. Such accreditation allows laboratories to conduct analyses of official meat and poultry samples. The Food, Agriculture, Conservation, and Trade Act of 1990, as amended, mandates that laboratory accreditation fees cover the costs of the Accredited Laboratory Program. This same Act mandates an annual payment of an accreditation fee on the anniversary date of each accreditation.

Proposed Rule

On October 8, 2009, FSIS published a proposed rule to amend its regulations to establish formulas for calculating the rates it charges meat and poultry establishments, egg products plants, and importers and exporters for providing voluntary, overtime, and holiday inspection, and identification, certification, and laboratory services (74 FR 51800). FSIS also proposed to keep the annual fee for its Accredited Laboratory Program at \$4,500 for FY 2009, 2010 and 2011, and increase it to \$5,000 for FY 2012 and FY 2013 (74 FR 51802).

As FSIS explained in the proposed rule, historically, the Agency amended its regulations annually to change the rates and fees. However, because the rulemaking process is lengthy, the fiscal year repeatedly would partially elapse before the Agency could publish a final rule to amend its rates and fees. As a result, the Agency was unable to recover the full cost of the services it provided.

To address the delays in recovering the cost of services, in January 2006, FSIS amended its regulations to provide for multiple annual rate and fee increases in one action (71 FR 2135). With this rulemaking, the rates and fees for 2006–2008 were increased and FSIS established criteria for determining the rate and fee increases on a multi-year basis. While this solution enabled the Agency to increase rates and fees each year, estimates used to establish the annual rates and fees were imprecise and have left the Agency collecting too little, and thus, not fully recovering its