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Payment Protection for Canada's Fresh Fruit and Vegetable Industry: Backgrounder

WHAT IS THE PROBLEM?

Growing, harvesting, packing and shipping perishables is risky. The unique characteristics and volatile financial environment of the fresh produce sector make it vulnerable to payments disruption, with the highly perishable nature of the product an important contributing factor. Low profit margins are the norm for producers and many rely on a single buyer to purchase their entire crop.

The rate of business insolvencies in the produce sector is lower than the national average, yet compared to other suppliers, fruit and vegetable producers are hit particularly hard when a buyer declares bankruptcy as repossession of shipments is impossible. A single bankruptcy can devastate not only the producer, but all the businesses connected to them and hits rural communities particularly hard.

Recognizing the industry's unique nature, the Government of Canada included special protection for suppliers of perishable products in the *Bankruptcy and Insolvency Act* more than two decades ago. Unfortunately, the conditions required are so complicated and limiting that few produce suppliers can actually access the security provided by the law. In practice, fresh produce suppliers have no protection in Canada when buyers declare bankruptcy.

In the United States, produce shippers are protected by a statutory deemed trust established through the Perishable Agricultural Commodities Act (PACA). The PACA trust helps suppliers of perishable products ensure prompt payment by buyers by making suppliers' interests in a debtor's assets derived directly from the sale of produce superior to those of other creditors, including secured creditors ("super priority"). Those assets available to trust creditors would be limited specifically to inventory, cash on hand and accounts receivable derived from the sale of the produce. Canadian companies exporting into the United States have had the same rights as American suppliers to recover payments easily and quickly if a buyer refuses to pay or declares bankruptcy with unpaid bills to produce suppliers, but this preferred status is under threat.

In order to address the gaps between the two countries, the Canada-U.S. Regulatory Cooperation Council (RCC) mandate agreed to by President Obama and Prime Minister Harper in 2011 included commitments towards establishing comparable approaches toward the common goal of protecting Canadian and U.S. fruit and vegetable suppliers from buyers that default on their payment obligations.

CANADA-U.S. TRADE IMPLICATIONS

Integrated supply chains with the United States are key to ensuring a year-round supply of affordable fresh produce for Canadian consumers. Canada sells about 40% of its fruit and vegetable production to the United States – about $1.5 billion in sales in 2012 – and Canada imported nearly $3.5 billion from the U.S. in the same year.

While Canadian firms receive the same benefits as U.S. entities when operating in the US, the lack of reciprocity is a growing trade irritant for US suppliers and affects the price and quality of fresh fruit and vegetables available to Canadians. According to a U.S. Department of Agriculture (USDA) licensee survey, U.S. shippers already add a 5 to 15 percent price premium to fresh fruit and vegetable bound for Canada in order to compensate for the riskier environment. And, Canadian producers routinely bypass the Canadian domestic market in order to take advantage of the superior protections offered in the United States. In order to shed its reputation as a secondary or inferior market, Canada must provide payment protections comparable to those offered in the United States.

U.S. frustration with the lack of reciprocity has reached a breaking point and steps are being taken within the U.S. government to remove the preferred access to PACA that Canadian firms receive if the Canadian government doesn't soon demonstrate movement towards establishing a limited statutory deemed trust. An announcement of the removal of Canadian preferred PACA access could happen any day.

Removal of reciprocity will affect import and export volume and prices, and could result in Canadian job losses. Though the biggest loser will likely be Canadian consumers, who will face increased prices, decreased quality, and reduced selection and variety in the produce aisle.

MARKET IMPORTANCE

In addition to providing a diverse supply of healthy food for Canadian consumers, Canada's fresh fruit and vegetable sector makes an important contribution to national economic output and employment. In 2013, the fresh fruit and vegetable sector supported 147,900 jobs and creates $11.4 billion in real GDP.

Canada's domestic farm gate receipts for fresh fruit and vegetables, excluding potatoes, in 2012 were $2.72 billion. Including potatoes would add more than $1 billion to 2012 farm gate receipts. Seventy-five percent of Canada's 10,000 fruit and vegetable producers are small businesses with average sales of less than $85,000 per year.

Over 85% of the value of Canada's vegetables and fruit are grown in Quebec, Ontario, and B.C. Rural communities in these provinces are at greatest risk from produce buyer insolvency.

CURRENT GOVERNMENT REVIEW

Under RCC, Agriculture Canada and industry reviewed and commissioned studies into current and traditional tools including a modern insurance model for financial risk mitigation, but none proved viable. Industry Canada is currently undertaking a statutory review of the *Bankruptcy and Insolvency Act* (BIA) and the *Companies' Creditors Arrangement Act*, including looking at the specific protections for fruit and vegetable suppliers and how these may be changed to satisfy the RCC commitments. The Fresh Produce Alliance (FPA) submitted a brief to the review requesting the establishment of a PACA-like trust in Canada. This proposal was also supported in the submissions to Industry Canada from the Canadian Federation of Independent Business, the Canadian Federation of Agriculture, and dozens of Canadian and U.S. companies operating in Canada. The Minister of Industry is expected to table a report to Parliament in the fall after which its recommendations will be studied by a Parliamentary committee.

PRODUCE INDUSTRY SOLUTION

The fruit and vegetable industry believes that the most effective way to provide protection to produce sellers is through the establishment of a limited statutory deemed trust, modeled on what currently exists in the United States. This would provide effective and inclusive protection that takes into account the unique characteristics of trade in perishable products. Assets available to trust creditors would be limited specifically to produce accounts receivable, and any cash and inventory from the sale of the produce. A trust does not require any government funding or administration.

Urgent action is needed. The fruit and vegetable industry is looking for the support of the Canadian government to establish a deemed trust mechanism in order to provide transparency and security to the buyers and sellers of fresh produce. Secure payments in the fresh produce sector will:

1. Protect rural communities,
2. Support thousands of Canadian businesses of all sizes,
3. Ensure affordable, high-quality produce for Canadian consumers and
4. Prevent disruptions of domestic and cross-border agrifood supply chains.

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