IN THE UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF ARKANSAS
FAYETTEVILLE DIVISION

In re: VEG LIQUIDATION, INC. f/k/a ALLENS, INC. and ALL VEG, LLC, Debtors

No. 5:13-bk-73597
Jointly Administered
Ch. 11

ALLENS, INC. and ALL VEG, LLC
v.
HARTUNG BROTHERS, INC.

Objection to PACA Claim

ORDER

On January 13, 2014, Allens, Inc. [the debtor] filed *Debtors' Omnibus Objection to PACA Claims* [omnibus objection] that included multiple grounds for objection to the PACA proof of claim of Hartung Brothers, Inc. [Hartung] in the amount of $8,172,200.56. Those grounds for objection, as condensed by the Court, are as follows: (1) that nearly half of Hartung's claim was not entitled to PACA trust protection because that amount was incurred for expenses other than produce–what the debtor refers to as contemplated expenses [contemplated expenses objection]; (2) that Hartung violated its fiduciary duties by overcharging the debtor to procure a secret profit and by inflating its PACA claim with the alleged contemplated expenses [fiduciary duties objection]; (3) that Hartung's ability to recover attorney fees was based on a contractual condition precedent that was not satisfied at the time of the claim and that Hartung provided insufficient documentation of attorney fees with its PACA claim [attorney fees objection]; and (4) that the debtor's books and records reflected that the debtor owed $149,645.08 less than the amount shown in Hartung's PACA proof of claim [books and records objection]. On March 27, 2014, the debtor filed a notice of withdrawal of the portion of its fiduciary duties objection related to Hartung's alleged procurement of a secret profit. The notice stated that the debtor reserved its right to proceed with the remainder of the fiduciary duties objection related to Hartung's alleged inflation of its PACA claim.

The debtor's objection to Hartung's PACA claim was set for hearing and heard on June 9 and 10. At the conclusion of the debtor's case on June 9, the debtor made an oral motion to amend *Debtors' Omnibus Objection to PACA Claims* to conform with the evidence presented at the trial, pursuant to Federal Rule of Civil Procedure 15(b). Specifically, the debtor sought two amendments: first, that its books and records objection be amended to reflect a greater amount in dispute, and second, that the Court consider an additional objection to Hartung's PACA claim on the basis that a portion of Hartung's PACA claim is not entitled to PACA claim protection under 7 U.S.C. § 499e(c). Both parties filed post-trial briefs on June 30.

Several grounds for objection raised by the debtor in its omnibus objection do not require the Court's analysis. The debtor never addressed at the hearing or in its post-trial brief the portion of its attorney fees objection regarding insufficient documentation. Accordingly, the Court finds that the debtor abandoned this portion of its attorney fee objection. *See Faulkner v. Kornman* (*In re The Heritage Organization, LLC*), 2012 WL 136898, at *14 (Bankr. N.D. Tex. 2012). In addition, the debtor did not argue at the hearing or in its post-trial brief that Hartung breached any fiduciary duty owed to the debtor. *Id.* Therefore, the Court finds that the debtor also abandoned this portion of its fiduciary duties objection. The remainder of the allegations contained in the debtor's fiduciary duties objection–that Hartung's PACA claim was inflated by the inclusion of non-produce expenses–was subsumed by the debtor's separate contemplated expenses objection. The Court previously overruled the substance of the debtor's contemplated expenses objection in a prior order in this bankruptcy case by finding that a buyer is obligated by statute to pay all sums owing in connection with a PACA transaction, including freight, fuel surcharges, and interest.[1] The Court adopts that finding here and overrules the debtor's contemplated expenses objection.

[1] To review those findings, see *Allens Inc. and All Veg, LLC v. D&E Farms, Inc.*, No. 5:13-bk-73597 [doc. 1045] (Bankr. W.D. Ark. July 30, 2014).

The matters remaining for determination are: (1) the debtor's oral Rule 15(b) motion, which encompasses the debtor's proposed new objection under 7 U.S.C. § 499e(c), (2) the proposed amended books and records objection, and (3) the debtor's attorney fees objection. For the reasons stated in this order, the Court denies the debtor's oral Rule 15(b) motion as to its proposed new objection under 7 U.S.C. § 499e(c) and grants the oral motion as to the amendment of the debtor's books and records objection. Substantively, the Court overrules the debtor's amended books and records objection and also overrules the debtor's attorney fee objection. The Court will address each, below.

The Court has jurisdiction over this matter under 28 U.S.C. § 1334 and 28 U.S.C. § 157, and it is a core proceeding under 28 U.S.C. § 157(b)(2)(B). The following order constitutes findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052, made applicable to this proceeding under Federal Rule of Bankruptcy Procedure 9014.

LEGAL ANALYSIS

1. The Debtor's Rule 15(b) Oral Motion

At the hearing, the debtor asked the Court to allow it to amend its omnibus objection pursuant to Federal Rule of Civil Procedure 15(b). Hartung opposed the motion and challenged the applicability of Federal Rule of Civil Procedure 15 at the hearing and later in its post-trial brief. Hartung correctly noted that Federal Rule of Bankruptcy Procedure 7015 designates Rule 15 as applicable in adversary proceedings–but that the debtor's objection to Hartung's PACA claim is a contested matter under Federal Rule of Bankruptcy Procedure 9014. In line with Hartung's argument, Rule 7015 is not listed among those rules that Rule 9014(c) designates as applicable in both adversary proceedings and contested matters. Nevertheless, many courts find that Rule 7015 is applicable in contested matters, at a court's discretion, because of Rule 9014(c)'s language stating that "[t]he court may at any stage in a particular matter direct that one or more of the other rules in Part VII shall apply." *See, e.g.*, *In re MK Lombard Group I, Ltd.*, 301 B.R. 812, 816 (Bankr. E.D. Penn. 2003) ("The trend of the cases appear to

apply Rule 7015 to contested matters."). The Court follows those courts' reasoning and finds that it is appropriate to apply Rule 7015–and, accordingly, Rule 15–in this matter.

Rule 15(b) addresses the amendment of pleadings during and after the trial:

> (1) **Based on an Objection at Trial.** If, at trial, a party objects that evidence is not within the issues raised in the pleadings, the court may permit the pleadings to be amended. The court should freely permit an amendment when doing so will aid in presenting the merits and the objecting party fails to satisfy the court that the evidence will prejudice that party's action or defense on the merits. The court may grant a continuance to enable the objecting party to meet the evidence.
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> (2) **For Issues Tried by Consent.** When an issue not raised by the pleadings is tried by the parties' express or implied consent, it must be treated in all respects as if raised in the pleadings. A party may move–at any time, even after judgment–to amend the pleadings to conform them to the evidence and to raise an unpleaded issue. –But failure to amend does not affect the result of the trial of that issue.

The Eighth Circuit has stated that "[t]he goal of Rule 15(b) is to promote the objective of deciding cases on the merits rather than on the relative pleading skills of counsel." *Am. Family Mut. Ins. Co. v. Hollander*, 705 F.3d 339, 348 (8th Cir. 2013). For this reason, amendments pursuant to Rule 15(b) are to be "'liberally granted where necessary to bring about the furtherance of justice and where the adverse party will not be prejudiced.'" *Id.* (quoting *Am. Fed'n of State, Cnty, and Mun. Emps v. City of Benton, Ark.*, 513 F.3d 874, 883 (8th Cir. 2008)).

Rule 15(b)(2) allows a court to grant a motion to amend if the non-moving party has consented explicitly or impliedly. Consent is not a consideration in the present case because Hartung clearly asserted its opposition to any amendment of the issues throughout the trial.[2] Alternatively, a court may grant a Rule 15(b) motion if the court

[2] Counsel for Hartung expressed this opposition during his opening statement, his closing argument, in response to the debtor's counsel's oral Rule 15(b) motion, and by issuing a standing objection at the outset of trial to any evidence relevant to the debtor's proposed amended objections. Counsel for Hartung also renewed the objection

finds that the non-moving party will not be prejudiced. *Hardin v. Manitowoc-Forsythe Corp.*, 691 F.2d 449, 457 (10th Cir. 1982). To determine whether an amendment would cause prejudice, courts consider "'whether (the party has) had a fair opportunity to defend and whether (the party) could offer any additional evidence if the case were to be retried . . . .'" *Nielson v. Armstrong Rubber Co.*, 570 F.2d 272, 276 (8th Cir. 1978) (quoting *Monod v. Futura, Inc.*, 415 F.2d 1170, 1174 (10th Cir. 1969)).

In making its oral Rule 15(b) motion, the debtor sought to accomplish two things: (1) to introduce a new ground for objection related to statutory noticing requirements under 7 U.S.C. § 499e(c), and (2) to increase the dollar amount of its books and records objection listed in its written omnibus objection. The Court will examine these amendment requests separately to determine whether Hartung would be prejudiced by the granting of the debtor's oral Rule 15(b) motion.

A. The Debtor's Proposed New Objection Under 7 U.S.C. § 499e(c)

The debtor alleges that a portion of Hartung's PACA proof of claim is not entitled to PACA trust protection because Hartung failed to satisfy the PACA noticing requirements under 7 U.S.C. § 499e(c). That statute mandates that a licensee seller must provide

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throughout the trial.

Nevertheless, the debtor asserts that Hartung implicitly consented to trying the proposed 7 U.S.C. § 499e(c) issue when Hartung entered evidence into the record to rebut the debtor's evidence. The Court finds this argument to be without merit given Hartung's persistent and thorough objection to the Rule 15(b) motion. Under the debtor's argument, a party opposing a Rule 15(b) motion would have to remain silent as to the new allegations or forfeit its objection to the Rule 15(b) motion. This would limit the objecting party's ability to demonstrate prejudice (for instance, by showing the court that additional discoverable evidence may exist). In addition, in the event the court took the Rule 15(b) motion under advisement–as this Court did–and later granted the Rule 15(b) motion post-trial, it would be too late for the opposing party to present any evidence to refute the new allegation.

notice to the buyer of its intent to claim PACA trust rights as to a debt in one of two ways: by serving notice upon the buyer within 30 days of the payment due date, under § 499e(c)(3), or by including specific PACA trust language within the seller's invoices, under § 499e(c)(4). For the second method, providing notice through invoices, the statute requires the seller to list other specific provisions, including payment terms, within the invoices to render the notice effective as to PACA trust rights.

Hartung asserts that it attempted to satisfy both methods, first by including the required PACA trust language in its invoices, and second by sending separate e-mailed notices to Josh Allen on August 27, October 8, and October 28 of 2013. However, the debtor argues that some of Hartung's invoices were deficient because of incorrect payment terms and that Hartung never sent its last e-mail notice on October 28, resulting in a portion of the debt owed to Hartung failing to acquire PACA protection under either method of notice.

With respect to the debtor's argument that Hartung will not be prejudiced by the debtor's Rule 15(b) motion as to this issue, the debtor cites two forms of notice by which it alleges that Hartung became aware or should have become aware that the debtor intended to pursue the additional objection regarding PACA noticing requirements. First, the debtor conducted a deposition of Daniel Hartung, president of Hartung, on April 30, 2014, in which counsel for the debtor questioned Daniel Hartung regarding incorrect payment terms listed in some of the invoices related to the debt in question. According to the debtor, this line of questioning should have put Hartung on notice that it intended to pursue an unpleaded ground for objection to Hartung's PACA claim. However, the eight pages of deposition transcript submitted to the Court show that the debtor's counsel never mentioned the possibility of amending its objection. In addition, the deposition transcript shows that the debtor never broached the subject of the August 27, October 8, and October 28 e-mails; whether those e-mails separately satisfied PACA noticing requirements; or whether the October 28 e-mail, in fact, existed. The debtor's belief that the deposition constituted some form of notice relies on the supposition that Daniel

Hartung never sent the October 28 e-mail, and that Hartung (the company) should have been alerted to the course of the debtor's investigation and concluded that the debtor would ultimately discover that Hartung had otherwise failed to preserve its PACA trust rights. In effect, the debtor argues that Hartung should have reached a conclusion on April 30 that the debtor apparently had not yet reached itself. The Court finds that the April 30 deposition did not constitute notice that the debtor intended to pursue an unpleaded ground for objection.

Second, on June 3, 2014, six days before trial, the debtor's counsel sent an e-mail to Hartung's counsel in which she stated that she was unable to find the October 28 e-mail among the other documents and requested that Hartung's counsel direct her to it. The e-mail concluded by stating: "As you know, without a proper trust notice there is a proper preservation issue under 7 USC 499e(c)(4) because the Carrot invoices list Net 10 payment terms, but the contract terms are actually Net 20." Hartung does not dispute that this e-mail provided notice that the debtor intended to pursue an additional ground for objection to its PACA claim. However, Hartung argues that the notice was provided less than a week before trial, leaving it little time to gather additional evidence to defend against the unpleaded objection. The result, Hartung argues, is that despite the prior notice, it will suffer surprise and prejudice if the debtor now is permitted to amend its objection to Hartung's PACA claim.

For the following reasons, the Court agrees with Hartung. As previously stated, the Eighth Circuit looks at two factors to determine whether the non-moving party would be prejudiced: (1) whether that party had a fair opportunity to defend, and (2) whether that party could offer any additional evidence if the case were to be retried. The debtor's proposed additional ground for objection would require the Court to determine whether Hartung failed in *both* of its attempts to preserve its PACA trust rights. Whether Hartung failed to provide the correct payment terms in its invoices is a question of statutory compliance. The Court is unaware of any additional evidence needed to make that determination. However, for the question of whether Hartung preserved its rights by

notice provided in the e-mails, the Court is faced with competing allegations surrounding the alleged October 28 e-mail.

Both the debtor and Hartung relied primarily on the testimony of two witnesses throughout the trial: Daniel Hartung, president of Hartung, and Josh Allen, the debtor's CEO in 2013 who also previously had a long-standing role in the debtor's operations. The two witnesses had worked together since at least 2004 and were each other's primary contact for their respective companies. Together, they were responsible for negotiation of the parties' contracts as well as general communication regarding the debtor's account with Hartung. The demeanor of Daniel Hartung and Josh Allen at the hearing indicates that they had a friendly working relationship.

Daniel Hartung testified that in the light of the debtor's impending financial troubles, he had decided in 2013 to provide "belt and suspender" notice to the debtor regarding Hartung's PACA trust rights. In addition to including PACA notice language on Hartung's 2013 invoices to the debtor, he stated that he also sent e-mails to Josh Allen on August 27, October 8, and October 28 with attached spreadsheets providing separate notice of Hartung's PACA trust rights. For both the August 27 and October 8 e-mails, Daniel Hartung was able to produce the e-mails and spreadsheets as well as the verification messages providing the date and time that Josh Allen viewed those e-mails. However, while he was able to locate spreadsheets dated October 28 that would have been attached to the e-mail he allegedly sent on that date, he was unable to find the e-mail itself. He recalled that he was in Europe using a newly-acquired iPad on October 28 and that he had no reason to believe he had not sent the e-mail. Although he received automated verification e-mails for the other two e-mailed notices he sent to Josh Allen, he testified that he was unfamiliar with how to request a "read receipt" for e-mails sent on the iPad.

October 28 was also the date that the debtor filed its voluntary Chapter 11 bankruptcy petition, and Josh Allen testified that he received 500-600 e-mails per day during that

period of time. He stated that he did not read the majority of e-mails he received on October 28, and that he could not remember whether he received an e-mail from Daniel Hartung on that date. However, he testified that he was unable to find the e-mail when he later searched for it. Josh Allen did not state when he searched for the e-mail or whether he knew of a reason why he was unable to find the e-mail when he searched.

The existence of the October 28 e-mail is determinative to the debtor's proposed new objection. Not surprisingly, the parties interpret Hartung's failure to produce the e-mail differently: the debtor argues that the absence of the e-mail is conclusive evidence that it never existed, and Hartung argues that the six-day notice was insufficient time for it to conduct more than a simple search of Daniel Hartung's e-mails. While the debtor alleges that Hartung should have been prepared to defend such a fundamental objection, even with little prior notice, it offers no explanation to the Court for its own shortcomings– namely, that it failed to include this ground for objection in its timely written objection, did not later seek to amend its objection in the five months before trial, and ultimately only disclosed its intentions as Hartung's counsel and Daniel Hartung were preparing to travel from different states to convene for trial in Arkansas. Finally, the evidence before the Court supports at least the possibility that the contested e-mail exists. Based on these considerations, the Court finds that Hartung would be prejudiced if the debtor were permitted to proceed with its newly proposed objection under 7 U.S.C. § 499e(c).[3] The Court denies the debtor's oral Rule 15(b) motion as to this proposed objection.

B. The Debtor's Proposed Amendment of the Books and Records Objection

Pursuant to Rule 15(b), the debtor also requests that it be permitted to amend the amount

[3] The debtor also argued that Hartung could have requested a continuance of the trial in order to conduct more discovery regarding the 7 U.S.C. § 499e(c) issue. However, in the context of a Rule 15(b) motion that is prejudicial to the non-moving party, that party has no obligation to seek a continuance. *See Hardin v. Manitowoc-Forsythe Corp.*, 691 F.2d 449, 457 (10th Cir. 1982) ("In the absence of a showing of prejudice, the objecting party's only remedy is a continuance to enable him to meet the new evidence.").

of its books and records objection that appeared in its written omnibus objection. The debtor previously objected to $149,645.08 of Hartung's PACA claim based on calculations made from its own books and records. In response to counsel for Hartung's request for an accounting in late April 2014, counsel for the debtor e-mailed Hartung's counsel an accounting on May 29, 2014, that reflected that the amount of objection had risen to $605,006.38. Thus, the debtor argues that Hartung had notice that the debtor would pursue an increased objection amount. The debtor also argues that its requested amendment of the objection amount is only an adjustment of the books and records objection already made in its timely filed omnibus objection, which Hartung had notice of since January 13, 2014. In response, Hartung argues that the delayed notice of the debtor's intended amendment is prejudicial, although it also contends that the debtor's objection lacks a factual basis according to Hartung's own accounting and a review of case law performed once it received the May 29 e-mail.

The debtor's counsel stated at the hearing that the proposed amended objection was "based on the exact same law, exact same notice to Hartung" as the original books and records objection filed on January 13, 2014. However, the Court cannot independently verify that the basis of the original books and records objection is the same as that of the proposed amended objection. The debtor broadly applied the term "books and records objection" in its omnibus objection to multiple PACA claimants whose claims the debtor disputed for various accounting reasons. As written, the debtor's original books and records objection was little more than a bare assertion of an amount in dispute– $149,645.08. In addition, according to statements made by Hartung's counsel, the debtor provided no accounting of the objection until May 29, at which time Hartung was also notified by e-mail for the first time that the objection amount had increased to $605,006.38. For this reason, the Court dismisses the debtor's argument that the original books and records objection served as notice to Hartung of the issues in dispute.

The debtor's second alleged form of notice, the e-mail sent on May 29, provided Hartung eleven days' notice of the basis of its objection and the increased objection amount. Like

with its 7 U.S.C. § 499e(c) objection, the debtor offered no reason for the delay in notifying Hartung or the Court of its intention to pursue an amended objection. Nevertheless, despite misgivings the Court has toward the debtor's conduct in presenting its objection to Hartung less than two weeks before trial–particularly in the light of the debtor's counsel's practice of eleventh hour disclosures in other hearings in this bankruptcy case–the debtor's amended books and records objection appears ripe to proceed. The crux of the proposed amended objection is the difference in how each of the parties accounted for the application of the debtor's payments to Hartung's invoices in 2013. The underlying facts are not in dispute–the parties are in agreement as to the amounts shown in Hartung's invoices for the sale of peas and carrots to the debtor. The parties are also in agreement as to the amounts paid to Hartung by the debtor. Moreover, Hartung points to no specific outstanding evidence that would change the determination of this issue if it had received more than eleven days to prepare. Instead, the question is a matter of law regarding the manner in which Hartung applied the debtor's payments. Accordingly, the Court concludes that Hartung will not be prejudiced by the debtor's amendment of its books and records objection and grants the debtor's oral Rule 15(b) motion.

2. Amended Books and Records Objection

The substance of the debtor's books and records objection relates to how the debtor's payments to Hartung should have been applied to Hartung's 2013 invoices. For the 2013 growing season, Hartung applied the debtor's incoming payments chronologically to invoices, beginning with the oldest invoice. Once the oldest invoice was paid in full, Hartung applied subsequent payments to the next oldest invoice. Daniel Hartung testified that this was compliant with the parties' established method of payment by which invoices were paid in full as they became due. By this method of applying payments, Hartung deemed one invoice in the amount of $1,191,122.18 fully paid, one invoice in the amount of $1,126,693.80 partially paid, and the remaining eighteen invoices unpaid at the time the debtor filed bankruptcy on October 28, 2013. The PACA portion of Hartung's proof of claim, in the amount of $8,172,200.56, consisted of the

remaining amount due on the partially paid invoice and all amounts due on the unpaid invoices.

The debtor alleges that Hartung's method of payment application was improper because the debtor had provided specific instructions to Hartung to apply payments in a different manner. Each of Hartung's invoice included a breakdown of the total amount owed, including some or all of the following components: produce (peas or carrots), freight, freight fuel escalator, harvest, and harvest fuel escalator. The debtor's payments submitted to Hartung by check or direct deposit in 2013 were accompanied by payment vouchers or automated e-mails that listed the invoices(s) for which the payment was intended and specified that the payment be applied to the produce component only of those invoices. By this method of accounting, the debtor alleges that some of the funds that Hartung applied to freight or harvest components in its oldest invoices should have been applied to the produce component of later invoices that Hartung deemed either partly or wholly outstanding. The debtor cites to case law in Wisconsin, the controlling jurisdiction listed in the parties' contracts, for the proposition that Hartung was required to apply payments according to the instructions of the debtor.

The most fundamental reason why the Court must overrule the debtor's amended books and records objection is because the debtor's method of payment allocation has no practical effect but for the debtor's contemplated expenses objection, which the Court has already overruled. Under the contemplated expenses objection, the debtor alleged that only the produce component of each invoice was entitled to PACA trust protection. According to the debtor's argument, all other components–including freight, freight fuel escalator, harvest, and harvest fuel escalator–are contemplated expenses that should be relegated to status of general unsecured debt in the debtor's bankruptcy case. Within that context, the debtor's different method of allocating payments may have reduced the amount of Hartung's PACA claim. However, the Court overruled the debtor's contemplated expenses objection.

Pursuant to that finding (although subject to the Court's determination on the debtor's other grounds for objection), the entire sum of each invoice was entitled to PACA protection, and, for the purpose of determining the amount of Hartung's PACA claim, it is irrelevant to the matter currently before the Court whether the debtor's payments were applied to one invoice versus another invoice. The debtor's liability for Hartung's PACA trust claim amounts is equal to the total allowed pre-petition amount owed to Hartung minus all pre-petition payments made by the debtor. The Court has no evidence to show that Hartung's PACA proof of claim does not follow that basic equation.

Even if the debtor succeeded on its contemplated expenses objection, the Court would still overrule the debtor's amended books and records objection. The debtor's sole argument rests on the following quote from a Wisconsin Supreme Court case: "[w]here a debtor owes a creditor multiple debts, a payment by the debtor should be applied to one or another of the debts as the debtor directs." *Moser Paper Co. v. North Shore Pub. Co.*, 266 N.W.2d 411, 415 (Wis. 1978). *Moser* dealt with a debtor and creditor who agreed as to the application of a payment but were faced with the objection of a second creditor who sought the payment to be reallocated to its advantage. *Moser* and subsequent cases explored the circumstances under which an intervening second creditor, for equitable reasons, has the right to demand allocation in a particular way, notwithstanding the debtor's or creditor's desire or agreement to have it allocated differently.

Clearly, the facts before this Court differ from *Moser* because there is no intervening second creditor–the allocation dispute is between the debtor and Hartung. A Wisconsin bankruptcy court similarly determining a payment allocation dispute between the originating debtor and creditor recited *Moser*'s statement of law, but with the important recognition that a prior agreement between the parties would control. *Howe v. Scannell* (*In re Scannell*), 60 B.R. 562, 564 (Bankr. W.D. Wis. 1986). That court stated: "Wisconsin law is clear that when a debtor owes a creditor multiple debts, the creditor must apply all payments in accordance with any instructions made by the debtor at or before the time of payment, *unless a prior contrary agreement of the parties specifies the*

manner of application." *Howe*, 60 B.R. at 564 (emphasis added).[4]

The debtor argues that no such agreement or course of dealing as to payment allocation existed between the parties. In support of that argument, the debtor elicited testimony at the hearing regarding the difference in payment terms between the parties' prior 2004 agreement and the 2012 agreement presently in effect. Both Daniel Hartung and Josh Allen testified that the 2004 agreement, which was not entered into evidence, stated that all service costs were to be paid within 10 days of the debtor's receipt of an invoice from Hartung and that all produce costs were to be paid by September 15 of each year. The 2012 agreement changed the payment terms by providing that both produce and service costs would be paid within 10 days of receipt of an invoice. As written, the difference in terms suggests that the parties changed payment methods prior to the 2012 growing season and therefore had no long-term course of dealing as to payment application. However, Daniel Hartung testified that accounting difficulties had led the parties to disregard the written payment provision of the 2004 agreement, and that "from 2004 until 2013, every invoice was paid in its entirety, everything on it, delivered peas to the plant, and done. There was never any breakout. Produce was not paid separate ever." He stated that the parties changed the payment terms in the 2012 agreement to reflect in writing what the parties already had been doing for years. The amended provision within the 2012 agreement stated, in part: "Payments for produce and services due under this agreement shall be due ten (10) days after ALLEN'S receipt of invoice from Hartung."

Upon direct examination by Hartung, Josh Allen agreed that the debtor had paid Hartung

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[4] In addition, there is one further potential contradiction between the debtor's use of *Moser* and the facts presently before this Court. *Moser* and similar cases make the point that, absent contradictory circumstances, the debtor has the right to designate how payments are applied *at or before the time the payment is made* to the creditor. In the absence of that instruction, the creditor is free to allocate the payment as it desires. Upon questioning by Hartung, Tasha Farmer testified that for at least two of the debtor's 2013 payments to Hartung, the vouchers that provided allocation instructions were tendered to Hartung one to two weeks after the payments had been made.

in a consistent manner for years:

> Q: And in 2012, did Allens pay Hartung using a single instrument for both produce and services?
> A: Each and every invoice.
> . . .
> Q: And is it in full payment of the invoice, inclusive of produce–
> A: Yes, it is.
> Q: –freight and fuel?
> A: Yes.
> Q: Thank you. You can set that document aside. Is that how Allens paid all of its invoices from Hartung in 2012?
> A: Yes.
> Q: Thank you. **And is that how Hartung and Allens had done business in prior years?**
> A: **Yes.**
> Q: **So that Allens' instrument for payment would include the cost of the produce, as well as related services?**
> A: **Yes.**

To provide further evidence of an agreement or established method between the parties, Hartung entered into evidence an e-mail chain between Daniel Hartung and Josh Allen dated June 20, 2013, in which Daniel Hartung questioned the first payment received from the debtor that was allocated for produce only. That e-mail stated:

> Accounting just brought in copies of the payment we just received. For some reason AP is instructing us to apply the payment to the produce (carrots) on each invoice and not the services or freight? Our policy is to pay the oldest invoices first in full and then go to the next one due. Is there something I need to know here? This just doesn't look right? Could you please call me yet today so we can get this posted correctly.

(Original line spacing omitted.) Josh Allen's response the same day stated that he thought "it was a system error" and that "[t]oday we split freight and raw product apart then pull them back." Josh Allen testified that he could not recall having further conversations with Daniel Hartung regarding the payment allocation issue after his June 20 response.

From the testimony of Daniel Hartung and Josh Allen, as well as other evidence entered

into the record, the Court concludes that at least since 2004, the parties had established the practice of invoices being paid in full, despite contradictory language in the 2004 agreement.[5] Even without the evidence of the parties' long term course of dealing, the payment provision within the 2012 agreement (which was in effect in 2013) made it clear that the produce and other components of each invoice were due at the same time. The debtor's instructions for its payments to be applied to the produce component only–and leaving the other components unpaid–was in violation of that provision of the parties' written contract.

In addition, there is no evidence to contradict Hartung's assertion that its method of applying the debtor's partial payments to the oldest invoice first was in compliance with the parties' agreed practices. The debtor attempted to refute Hartung's argument in two ways: first, by arguing that Hartung had failed to present any conclusive evidence of an agreement to that effect, and second, by presenting its own evidence to show that the debtor's payments always had been associated with specific invoices for accounting purposes. That evidence included testimony by Josh Allen and Tasha Farmer, a current employee of the debtor who was responsible for issuing payments in 2013, as well as a payment receipt issued by the debtor in 2012 that listed the invoice for which payment was intended. However, the fact that the debtor's payments were always designated for particular invoices is not inconsistent with Hartung's alleged long-term practice of applying payments to invoices chronologically. The evidence from the hearing indicates that up until 2013, the debtor had always paid each invoice in full, generally "in a reasonable amount of time" to avoid arrears on the account, according to Josh Allen. If the debtor designated payment of particular invoices as they became due (to prevent arrears), the logical result was that those payments were deemed paid by Hartung in

[5] The fact that the 2004 agreement included a provision stating that all amendments would be made in writing did not prevent the parties from waiving the statute of frauds requirement under Wisconsin state law through an established course of dealing over the years. *See Royster-Clark, Inc. v. Olsen's Mill, Inc.*, 714 N.W.2d 530, 535-40 (Wis. 2006).

chronological order. There is no evidence that the debtor instead regularly paid Hartung's invoices nonsequentially (i.e., designating full payment for later invoices first, then earlier invoices later).

Taking all of these factors together, the Court finds that Hartung applied payments in 2013 based on the prior agreement of the parties through contractual provisions and course of dealing. Josh Allen's dismissal of the debtor's produce-only payment allocation as an "error" in his June 20 e-mail, coupled with the fact that the parties engaged in no otherwise meaningful discussion about the issue, leads the Court to conclude that the parties did not decide together to change that agreement in 2013. Therefore, Hartung was not required to allocate payments according to the unilateral instruction of the debtor. For this reason, as well as for the reason that this objection became irrelevant upon the denial of the debtor's contemplated expenses objection, the Court denies the debtor's amended books and records objection to Hartung's PACA proof of claim.

3. Attorney fees objection

Both the peas and carrots contracts between the parties included the following provision:

> 20. ENFORCEMENT OF PROVISIONS: Each party agrees to pay and discharge all reasonable costs, attorney fees, and expenses which may be incurred or made by the other enforcing the covenants and agreements of this Agreement.

The debtor objects to a claim of attorney fees by Hartung based on its interpretation that only a party who brings an action against the other and prevails is entitled to attorney fees. The debtor argues that at the time that Hartung filed its PACA claim, Hartung's request for attorney fees was premature because no party had yet prevailed. The debtor further suggests that based on the alleged contingency provision, Hartung's right to attorney fees could not vest until after the default, therefore preventing the attorney fees from being considered a sum owing in connection with a produce transaction. For these reasons, the debtor asserts that Hartung's attorney fees are not entitled to PACA trust

protection.

The debtor does not dispute that Hartung's PACA proof of claim served as bringing an action to enforce the terms of the parties' contracts. In addition, according to this Order, Hartung is the prevailing party as to all of the debtor's grounds for objection to Hartung's claim. Therefore, Hartung has a contractual right to attorney fees and costs, regardless of whether Hartung's right to those fees vested upon the debtor's default or later. Courts have found that where a creditor has that contractual right, the attorney fees are considered sums owing in connection with a produce transaction and are, therefore, deemed part of a creditor's PACA trust claim. *Coosemans Specialties, Inc. v. Gargiulo,*485 F.3d 701, 709 (2d. Cir. 2007); *Middle Mountain Land and Produce Inc. v. Sound Commodities Inc.*, 307 F.3d 1220, 1222-23 (9th Cir. 2002).[6] The Court finds that Hartung's attorney fees that have accrued and are accruing during the course of this bankruptcy to litigate its PACA claim are entitled to PACA trust protection. Accordingly, the Court overrules the debtor's attorney fees objection.

Conclusion

For the foregoing reasons, the Court denies the debtor's objections to Hartung's PACA proof of claim.

IT IS SO ORDERED.

Ben Barry
United States Bankruptcy Judge
Dated: 10/09/2014

[6] Also see *Allens Inc. and All Veg, LLC v. D&E Farms, Inc.*, No. 5:13-bk-73597 [doc. 1045] (Bankr. W.D. Ark. July 30, 2014), fn.2, for a more comprehensive discussion of those cited cases.

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