

BE A SMART MARKETERSM

A special publication brought to you by CAWG's Member Services & Communications Committee

June 2009



Overview

CAWG HELD 2009 SMART MARKETER WORKSHOPS IN LODI, SANTA ROSA, AND PASO ROBLES FEATURING PRESENTATIONS BY DALE STERN WITH STERN, VAN VLECK & MCCARRON LLP, AND AGGIE D'ESTERHAZY, MARKET ENFORCEMENT BRANCH CHIEF WITH THE CALIFORNIA DEPARTMENT OF FOOD AND AGRICULTURE.

Dale Stern began his presentations with a series of rhetorical questions then went on to suggest answers to each of them, and much more.

“What if the date for payment has come and gone without a check? What do you do?”

The answers are many and depend on a lot of factors, such as how much is owed, the grower's relationship with the winery, and the number of years he has been doing business with the winery. “Ask yourself: Is it still the same people at the winery or has the winery been bought out and now you are dealing with all new people? Who is calling the shots? Is it the person you talked with on the phone (e.g. the field rep or winemaker), or an accountant in Boston or Tennessee or somewhere else across the country?” Stern asked.

The way in which that series of questions is answered will help guide a grower in deciding how quickly and assertively to act against a non-paying winery. Stern stressed the importance of good communications and maintaining a non-confrontational attitude as long as possible.

“So for me, the first step is to communicate. And I even would go so far as to say if the payment is due on a Friday and you don't have it in hand, call up on Monday and say you are just checking in. Don't say things that will destroy your relationship. Avoid making threats that you are going to call your attorney or go to Market Enforcement right away. You just need to gather some intelligence. Intelligence is a valuable tool.”

Stern pointed out the importance of documenting the conversation either in a letter or



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—DALE STERN OF STERN, VAN VLECK & MCCARRON LLP

e-mail to the winery confirming what was discussed. This letter or e-mail can be very important if action needs to be taken to collect payment, either through the services of an attorney or through a complaint filed with the **Market Enforcement Branch of the California Department of Food and Agriculture (CDFA)**.

For example, if a few months go by and a grower still hasn't been paid, and he is still making the same phone calls and getting the same excuses, he can refer back to earlier e-mails and letters that document the winery's promises to pay. Another valuable reason to document everything is that if a grower needs to file a complaint with Market Enforcement, this history of communications will help Market Enforcement understand where the delinquency has come from, and where it is going. Finally if a grower needs to hire an attorney, this documentation will give the attorney extra tools if forced to go to court to seek an injunction to keep the winery from selling the wine without paying the grower first.

TERMS OF THE INITIAL CONTRACT

Stern emphasized the importance of not waiving the terms of the initial purchase contract. Don't replace your existing contract just to give the winery a new payment date. "Some wineries have said, 'We talked about this back on January 20th and I told you what my payment plan was and you agreed to a new verbal contract. The old winegrape purchase contract is no longer in effect because we substituted this new verbal agreement with a new payment plan.' Growers should not go along with this; it can undermine collection efforts under the original grape purchase agreement. Growers who choose to help their winery by waiting for payment should say something like, 'I'm not waiving the terms of our contract, but I understand you are in a little bit of a hard position and I am willing to go along with you for a couple weeks,'" he said.

DOCUMENT YOUR COMMUNICATION

As part of the communications with the non-paying winery, it is recommended that a grower should also remind the winery that the producer's lien is in effect. Summarizing, the points to include in the documentation letter

to the winery are:

- The winery is past due on payment.
- The grower is not waiving the terms of the contract.
- The producer's lien has attached and the winery may not sell or transfer the wine made from the grower's grapes. If the winery has any question about the law and penalties for violations, contact the CDFA Market Enforcement Branch at (916) 341-6276.
- A request to inform the grower where the wine made from his grapes is currently located and provide him with the winery's assurance that it won't leave possession or control of the winery until the grower is paid in full.
- Ask the winery to please reply in writing.

Growers who have not been paid for their grapes have nine months from the final payment due date to file a complaint with the CDFA Market Enforcement Branch. They have two years to file suit if the contract was verbal and four years if it was written.

FOOD AND AGRICULTURAL CODE

There is a valuable section in the state Food and Agricultural Code, 55609, which provides:

Not later than 5 days after demand, the processor shall give to every such producer so requesting a full and complete statement of such producer's account which shows all of the following:

- *The entire quantity of the product that has been delivered by the producer.*
- *The grades of the product which have been delivered by the producer.*
- *The amount owed for every lot and for the total amount of the product that has been delivered by the producer.*

Failure to comply is grounds for a complaint to the CDFA Market Enforcement Branch.

“Once you receive the winery’s statement of account, you have a much clearer picture of whether the winery thinks there were any quality problems with the grapes that were delivered; whether it has downgraded the grapes because of sugars, mold, mildew or some other reason. This will tell you right up front whether there were any problems in the winery’s mind as to the quality and tonnage of the grapes. You will find out a lot about them,” he said.

CDFA MARKET ENFORCEMENT BRANCH

CDFA issues licenses to entities that purchase, negotiate, or solicit winegrapes for the purpose of putting them into wine. They handle all commodities grown in California with the exception of milk and timber. CDFA Market Enforcement Branch Chief, **Aggie d’Esterhazy** brings 32 years of experience to the job and there isn’t much relating to agricultural contract disputes that she hasn’t seen.

MARKET ENFORCEMENT WEBSITE

D’Esterhazy’s first piece of advice to winegrape growers who are preparing to enter into a contract with a winery is that they know whom they are dealing with. “Check our website (www.cdfa.ca.gov/mkt/meb) for information that will identify all of our licensees. If you are wondering about complaint history, give us a call at (916) 341-6276 and we can tell you over the phone whether there



“MARKET ENFORCEMENT HAS THE ABILITY TO TAKE ADMINISTRATIVE ACTION, CIVIL ACTION, AND CRIMINAL ACTION. SO IF A WINERY COMMITS A VIOLATION AND IF THEY ARE LICENSED AND IT IS REPEATED AND FLAGRANT, WE CAN TAKE THEIR LICENSE AWAY.”

—AGGIE D’ESTERHAZY, CDFA MARKET ENFORCEMENT BRANCH

is some prior history of complaints.”

The Market Enforcement website provides additional information as well. For example, if an entity is required to post a surety bond because of previous financial problems, that information is available. The same holds true for an employment bond, which is required when an entity hires an employee who will be involved in contract talks if that employee has had previous financial problems. Market Enforcement can also identify the principal officers and owners of a company. Whatever is listed on the license is public information and can be provided when a request is made.

FILING A COMPLAINT

“Market Enforcement has the ability to take administrative action, civil action, and criminal action. So if a winery commits a violation and if they are licensed and it is repeated and flagrant, we can take their license away,” D’Esterhazy said.

Any grower can file a complaint with Market Enforcement if the default is within the previous nine months. Market Enforcement takes complaints for such things as failure to pay, failure to harvest, breach of contract, rejections, failure to provide bins or boxes, failure to provide weight tags. In addition to filling out the complaint form, D’Esterhazy said a grower should include a letter explaining the situation from his or her perspective, “I suggest that you tell me a story, write something down to give some insight to us. Once we receive the complaint, we notify the winery that the complaint has been filed. They have 30 days to respond to our agency to explain their position and whether they agree or disagree,” she said.

If Market Enforcement thinks the dispute may be resolved through an informal mediation, they will attempt to do that. “The success rate is about 80 percent, but if we cannot get it resolved, we then write what we call a verified complaint summary. All the details are prepared and a summary is sent to both sides—the complainant and respondent—along with our opinion.”

EXPEDITED ARBITRATION

Two years ago, Market Enforcement created expedited arbitration. For \$600, Market Enforcement takes all of the paperwork from complainant and respondent, along with CDFA's paperwork and faxes it to an arbitrator. Within 30 days, a decision is rendered that is binding on everyone. If it is against the winery, the winery has to honor it. If the winery doesn't pay, CDFA can take away the winery's license to buy California grapes.

If the winery requests a hearing, Market Enforcement will conduct a pre-hearing conference at which time the winery has to come up with a payment plan that is realistic.

"I don't like hypothetical statements such as 'we are planning to come up with some funding.' That isn't going to cut it. If they bring a plan to the table that is somewhat doable, the department is willing to do a stipulated decision and order. That means we are going to put that winery's license on probation for whatever time it takes. It may be a year; it may be up to four years. They have to honor certain conditions, such as making payment according to the judgment, and getting a review every three months. If they violate any of the conditions, we will take their license," D'Esterhazy said.

GENERAL CONTRACT TERMS

It is important that growers deliver their grapes to a licensed California processor that is the same person with whom they have a contract. It is not uncommon to see a winery use several different business names or brand names for their grower contracts, some of which are different than the correct business name under which the winery holds its processor's license.

"Be sure that the name on your contract is the same as the one on the winery's license. The tools available to a grower may not be as many if you're in a dispute with an unlicensed buyer. A grower's lien rights may not apply to most custom crush arrangements; nor if you are selling to a broker, your neighbor, or anyone else who isn't a licensed processor," advised Stern.

RIGHTS TO PAYMENT

Growers should be aware of their rights to payment. State law provides that payments are due 30 days after delivery of the grapes to a winery, unless a contract sets a later payment date.

Stern noted that contracts should clearly spell out payment terms. For example, typical language might include: "Buyer's payment for the grapes purchased under this agreement shall be 50 percent of the purchase price on or before December 1st of the same year as harvest; 25 percent on or before January 15th of the year immediately following harvest; and the balance due on or before February 15th of the year immediately following harvest."

To confirm provenance of grapes and protect both the grower and winery, it is important that the grower provides a field tag with their crop upon delivery. "While large vineyards and management companies do this routinely, smaller growers are often unaware of this important paperwork trail," said Stern.

"A field tag does not need to be complicated, but should be a statement signed by both grower and driver that includes: date, time of harvest, the variety, block location, picked by hand or machine, number of bins and weights, and the truck or trailer's license plate. One copy is provided to the driver for delivery to the winery, a second copy is kept by the grower, and other copies are often kept by the trucking company."

It is important that a contract clearly states when grape ownership transfers take place. Contracts often refer to this as the time of "acceptance" of the grapes, which typically occurs at the grade stand or crusher. We are seeing more contracts lately that give a winery the right to evaluate flavors and color, and reject a grower's grapes after the winemaking process has begun. Growers should carefully consider what they'd do with a lot of partially made wine under such a contract clause before they sign it.

It is important that growers confirm the names of the winery and winery agents or representatives with whom

they have a contract. To confirm that a buyer and their agents are licensed in California, Stern advised growers to contact the CDFA Market Enforcement Branch, or visit the website at www.cdfa.ca.gov/mkt/meb. Think of it as part of your due diligence similar to a credit check on the buyer before delivering your grapes to them in return for payments over time,” said Stern.

INTEREST CHARGES

Stern noted that in many of the contracts he is now writing, he’s recommending that the growers no longer include interest charges for past due accounts. Instead, he is including statutory late charges as spelled out in Section 55881 of the state Food and Agricultural Code. That section provides: “Under a contract for the purchase of any farm product, any delinquent payment of money under this chapter shall also include a late charge of 5 percent per month of the unpaid balance calculated on a daily basis for the period of the delinquency for the first month and an additional 1 percent per month on the unpaid balance calculated on a daily basis for the remaining period of the delinquency. Any such late charge shall be payable to the person from whom the farm product was purchased, unless the person waives, in writing, his right to such payment. Such waiver shall be valid and effective only when given after a delinquency has occurred.” The rate is better for the grower than most interest clauses, and the CDFA Market Enforcement Branch will actively help growers collect these charges whereas they can’t help with collection of contractual interest.

MEDIATION AND ARBITRATION

Stern also addressed the issue of mediation and arbitration. If there is a large amount of money to be paid under a contract, he encourages growers to consider including a mediation/arbitration clause in the contract. If it is a smaller contract, less than \$50,000, it may be preferable to omit this clause. He noted that if a grower files a complaint with Market Enforcement and there is an arbitration clause in the contract, the winery could inform CDFA that it intends to arbitrate, which effectively puts Market Enforcement on the sidelines until the arbitration process is completed.

Along those lines, Stern advises that if a grower does file a complaint with Market Enforcement, the Complaint form contains a large number of boxes representing the various types of alleged violations. “Check as many boxes as you can reasonably say are true. Don’t just say the winery didn’t pay you. If they didn’t give you the statement of account in five days as you asked for, then you should check that box. The more boxes you check, the more tools that Market Enforcement has to help you,” he said.

PRODUCER’S LIEN

One form of protection for growers that goes into effect automatically upon delivery of grapes to a winery is the producer’s lien. One aspect of this statutory lien is that a winery cannot lawfully sell the wine without first paying or making arrangements to pay the grower out of the proceeds of the sale of that wine. There are a number of ways the winery can make arrangements to pay so the wine can be sold legally if they need to do that to get the money to make a grower payment.

“I never advise signing a contract that would waive a producer’s lien. Contracts typically include language along the lines of ‘Grower warrants that all grapes are grower’s sole property and are not subject to any other sale or contract to sell, or to any lien or other encumbrance except (blank).’ I recommend inserting into the blank, the words ‘producer’s lien’ he said.

A remedy available to a grower if he is not paid is to file a complaint seeking foreclosure on the lien. This is similar to foreclosing on many other types of liens. “It is a pretty straightforward procedure, but can take time. A court order is obtained that gives the grower the authority to take physical possession of the wine, often with the assistance of a sheriff. A broker or other authorized person may be retained to then market and sell the wine, with the proceeds going to the grower to cover what is owed, with the winery getting whatever is left,” he said.

While foreclosing under a producer’s lien, a grower may also have to get a prejudgment writ of attachment or preliminary injunction in order to protect the value of the wine until it can be foreclosed upon and sold in the

best possible condition. Even if the grower's grapes are blended with grapes delivered by others, the whole lot of wine can be foreclosed upon, up to the value of what is owed to the grower. If the grower holds winery licenses issued by ABC and TTBB he should be able to take possession of, and sell bulk or bottled wine. If the grower isn't licensed, he may need to seek assistance from a licensee or broker to sell that wine to a third party. There are a lot of variables, Stern said.

If the winery files bankruptcy and the grower is seeking payment in bankruptcy court, the Producer's lien is generally superior to all of the secured and unsecured creditors. The only claims the Producer's lien is typically junior to are liens for wages and liens for the warehousemen, Stern advised.

DELAYED HARVEST

In the fall of every year, there are big decisions to be made throughout California's winegrape country. When should the grapes be picked for maximum production and highest quality? The answer isn't an easy one and occasionally results in conflicts between growers and wineries.

Delayed harvest, or extended hang time has become an issue of conflict between growers and wineries in recent years as more subjective measurements are being applied when determinations are made regarding the right time to harvest the grapes. As noted by Stern, many contracts contain a clause saying that wineries will determine the harvest date after consultation with the grower.

When objective criteria—such as the grapes reaching a certain Brix level—are used to determine the harvest date, there are relatively few points of conflict between grower and winery. But in recent years, more and more wineries began using other determinations to signal when the grapes were ready to harvest. Stern said when a winery wants to leave the grapes hanging longer than the grower thinks reasonable, then the grower needs to look at other aspects of the contract, such as quality standards, projected tonnage, and which party bears the risk of loss while the grapes are still on the vine.

“GROWERS NEED TO MAINTAIN A RELATIONSHIP IN WHICH THEY ARE COMFORTABLE TALKING WITH THE WINERY REPRESENTATIVES THROUGH CONTINUOUS OPEN COMMUNICATIONS. THIS ‘WIN-WIN’ PARTNERSHIP RELATIONSHIP IS ABSOLUTELY CRITICAL.”

—DALE STERN WITH STERN, VAN VLECK & MCCARRON, LLC

Some of the delayed harvest issues outlined by Stern include:

- Exposure to crop losses from weather, pests, and diseases
- Lost weight from dehydration means lost income on a tonnage contract
- Exposure to potential rejection and/or deductions because grapes fail to meet stringent quality requirements at the winery.

“The bottom line is that someone has to make the decision on when the grapes are ready to be harvested. If harvest is delayed, there are going to be tonnage losses. It also may be late enough in the year that you are worried about frost, mold or mildew, pest infestations, or any number of other problems that may come about because the grapes are more vulnerable when harvest is delayed. Also there are some wineries that may reject the grapes after the extended hang time. They hold up the contract and say it is their call and the grapes don't meet the quality standards,” he said.

Stern emphasized that there are solutions available to the grower. A sample provision that he recommends be considered in these contracts is one that establishes the maximum Brix. If a winery requires the grower to delay harvest beyond that Brix level, the winery is in breach. Another option is a provision that states that the winery waives the ability to reject the grapes if the decision to hang past maximum Brix is the winery's call.

“Another option that can be added to contracts gives the grower financial incentives—for example, paying the grower \$100 per ton for each tenth of a degree of Brix over the maximum on a load-by-load basis. That way, the grower receives an incentive for the extended hang time. All three of these sample provisions ought to be consid-

ered if a grower is concerned about delayed harvest,” he said.

Stern said the “extended hang time” conflict serves to illustrate the importance of open communications between growers and the wineries that buy their grapes. “Growers need to maintain a relationship in which they are comfortable talking with the winery representatives through continuous open communications. This ‘win-win’ partnership relationship is absolutely critical.”

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Agatha (Aggie) d’Esterhazy, Market Enforcement Branch Chief of the CDEA can be reached at: (916) 341-6276 or mktenforce@lcdfa.ca.gov. d’Esterhazy is located in Sacramento at 560 J Street, Suite 170A.

FOR ADDITIONAL INFORMATION AND RESOURCES FROM PAST SMART MARKETER WORKSHOPS AND PUBLICATIONS, PLEASE VISIT THE “MEMBERS ONLY” SECTION OF THE CAWG WEBSITE, WWW.CAWG.ORG.

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