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INSIDE

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IN FUTURE ISSUES

Exhaustion of administrative remedies as jurisdictional requirement not mandated

In *Avocados Plus Incorporated v. Veneman*, 370 F.3d 1243 (D.C. Cir. 2004), the United States Court of Appeals for the District of Columbia held that provisions of the Hass Avocado Promotion, Research, and Information Act (Avocado Act), 7 U.S.C. §§ 7801-7813, did not require exhaustion of administrative remedies as a jurisdictional requirement.

The Avocado Act authorizes the Department of Agriculture to collect mandatory assessments from avocado growers and importers so that the assessments can be used to promote the domestic consumption of Hass avocados. *Avocados Plus*, 370 F.3d at 1245. Several importers of avocados and avocado products challenged the Avocado Act, arguing that it violated their First Amendment right to be free of compelled speech. *See id.* The Secretary of Agriculture filed a motion to dismiss, arguing that the plaintiff importers failed to exhaust their administrative remedies. *See id.* at 1247. The district court held that the plaintiffs were required to exhaust their administrative remedies and dismissed the action for lack of subject matter jurisdiction. *See id.* The plaintiffs appealed the district court's decision to the D.C. Circuit. *See id.*

The D.C. Circuit explained that under § 7806 of the Avocado Act "any 'person subject to an order' may file a petition with the Secretary 'stating that the order, any provision of the order, or any obligation imposed in connection with the order is not in accordance with the law; and ... requesting a modification of the order or an exemption from the order'" and that the Secretary must rule on the petition after a hearing. *Id.* at 1246 (citations omitted). It also explained that under the Avocado Act "the 'district courts of the United States ... shall have jurisdiction to review the ruling of the Secretary on the petition[,]' ... and must remand it if it 'is not in accordance with the law[.]'" *Id.*

The court explained that there are two types of exhaustion: "non-jurisdictional exhaustion" and "jurisdictional exhaustion." *Id.* The former is a judicially created doctrine that requires "parties who seek to challenge agency action to exhaust available administrative remedies before bringing their case to court"; the latter "arises when Congress requires resort to the administrative process as a predicate to judicial review." *Id.* at 1247 (citations omitted). *See also id.* (stating that "[w]hether a statute requires exhaustion is purely a question of statutory interpretation. If the statute does not mandate exhaustion, a court cannot excuse it.") (citations omitted). The court also explained that for a statute to mandate exhaustion, it must contain ""[s]weeping and direct' statutory language indicating that there is no federal jurisdiction prior to exhaustion, or the exhaustion requirement is treated as an element of the underlying claim.'" *Id.* at 1248 (citations omitted). It further explained that "[w]e presume exhaustion is non-jurisdictional unless 'Congress states in clear, unequivocal terms that the judiciary is barred from hearing an action until the administrative agency has come to a decision ....'" *Id.* (citation omitted).

The court stated that the Avocado Act "contains no ... 'sweeping and direct' language. It neither mentions exhaustion nor explicitly limits the jurisdiction of the courts. It merely creates an administrative procedure for challenging the Secretary's orders." *Id.* It added:

> Congress' failure to include in § 7806 of the Avocado Act the sort of 'sweeping and direct' language mandating exhaustion and thereby depriving the courts of jurisdiction tends to indicate that we are dealing here with non-jurisdictional exhaustion.... While the matter is not free from doubt, we therefore hold ... that the language of the Avocado Act does not make exhaustion jurisdictional.

Id. at 1249-50.

The court therefore reversed the district court's decision and remanded the matter for further consideration.

—Harrison M. Pittman, Staff Attorney, National AgLaw Center

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Eighth Circuit requires strict compliance with "direct notice" exception

In *Farm Credit Midsouth, PCA v. Farm Fresh Catfish Co.*, 371 F.3d 450 (8th Cir. 2004), the United States Court of Appeals for the Eighth Circuit held that a secured creditor was required to strictly comply with the direct notice requirement set forth in § 1631(e)(1) of the Food Security Act (FSA or Act) in order for a buyer in the ordinary course of business to take farm products subject to the secured creditor's security interest.

Farm Credit Midsouth, PCA (Farm Credit) loaned funds to Reece Contracting, Inc. (Reece) so that Reece could purchase and operate a catfish farm. *See id.* at 450. As collateral for the loan, Reece granted Farm Credit a first priority security interest in its catfish and catfish fingerlings. *See id.* Farm Credit filed a financing statement with the Arkansas Secretary of State and those counties in which Reece operated. *See id.* It also sent two letters to Farm Fresh Catfish Company (Farm Fresh), a company that purchased catfish from Reece, to inform Farm Fresh that Farm Credit provided financing to Reece and that it held a first priority lien in all of Reece's catfish. *See id.* Farm Fresh typically made its checks for catfish purchases payable to Farm Credit and Reece. *See id.* After Reece defaulted on its payment obligations, however, Farm Credit discovered that Farm Fresh only listed Reece as payee for the last forty-four payments it made prior to default, totaling approximately $700,000.00. *See id.* As a result, Farm Credit brought an action against Farm Fresh alleging that Farm Fresh converted Farm Credit's security interest. *See id.*

Section 1631(d) of the FSA provides that, except as provided in § 1631(e), "a buyer who in the ordinary course of business buys a farm product from a seller engaged in farming operations shall take free of a security interest created by the seller, even though the security interest is perfected; and the buyer knows of the existence of such interest." *Id.* Section § 1631(e) provides that

> a farm products purchaser "takes subject to a security interest created by the seller *if*" (1) the secured creditor provided, within a year before the sale, the farm products purchaser with direct written notice of the secured creditor's interest (direct notice exception) ... or (2) the secured creditor filed an effective financing statement covering the farm products if the state has established a central filing system that complies with the Act (central filing exception) ....

Id. (citations omitted).

The district court found in favor of Farm Fresh and concluded that the letters sent by Farm Credit did not strictly comply with the direct notice exception set forth in § 1631(e). *See id.* Farm Credit appealed the district court's judgment to the Eighth Circuit. *See id.*

Farm Credit argued that "it need only [to] substantially comply with the Act's direct notice exception, and [that] its letters to Farm Fresh substantially complied with the direct notice exception." *Id.* Thus, Farm Fresh purchased the catfish from Reece subject to Farm Credit's security interest and its failure to make payment to both Farm Credit and Reece constituted a conversion of Farm Credit's security interest. *See id.*

The court explained that Congress's use of the term "if" in § 1631(e) emphasizes that "the farm products purchaser takes the farm goods subject to the security interest *only* when the secured creditor complies with the direct notice exception or the central filing exception." *Id. See also id.* (noting that Arkansas did not have a central filing system and as a result the direct notice exception was applicable). The court explained that to comply with the direct notice exception:

> a secured creditor must send the farm products purchaser a written notice listing (1) the secured creditor's name and address, (2) the debtor's name and address, (3) the debtor's social security number or taxpayer identification number, (4) a description of the farm products covered by the security interest and a description of the property, and (5) any payment obligations conditioning the release of the security interest.

Id. (citations omitted).

The court stated that "[u]nlike the Act's definition of an effective financing statement in a central filing state, the Act's direct notice exception does not contain language indicating the required contents of the written notice are merely permissive or can be satisfied through substantial compliance." *Id.* It added that "[b]y including substantial compliance language in defining an effective financing statement for the central filing exception and excluding such language from the direct notice exception, Congress presumptively and logically intended that a secured creditor must strictly comply with the direct notice exception." *Id.* (citation and quotation omitted). The court recognized that "[f]orcing secured creditors to comply strictly with the direct notice exception does not run afoul of the Act's purpose" since "Congress adopted the Act to protect farm products purchasers from double payment[,]" and requiring the secured creditor to comply strictly with this exception "removes ambiguity regarding compliance, and protects farm products purchasers from double payment." *Id.* at 454. It added that "[e]xtending substantial compliance to the direct notice exception would have the opposite effect, requiring a farm products purchaser to guess whether the written notice substantially complied with the Act's direct notice exception." *Id.*

The court concluded that:

> Farm Credit's ... letters do not strictly comply with the Act's direct notice exception. Neither letter contains Reece's taxpayer identification number, Reece's address, or the counties in which the catfish subject to Farm Credit's security interest are produced or located. Because the ... letters fail to comply with the Act's direct notice exception, Farm Fresh purchased the catfish free of Farm Credit's security interest, even though Farm Fresh knew of the existence of such interest.

Id. (citation omitted).

—Gaby R. Jabbour, National AgLaw Center Research Assistant

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The meaning of "active business" for purposes of divisive reorganizations

The requirement of an "active business" is a key requirement for a successful, tax-free corporate reorganization.[1] A distribution in conjunction with a reorganization must be motivated, in whole or substantial part, by one or more corporate business purposes.[2] For farm and ranch reorganizations, the business purpose requirement is a central feature of a divisive reorganization.

The divisive reorganization has taken on greater importance since the Tax Reform Act of 1986 eliminated the possibilities for tax-free liquidation.[3]

The requirements for a divisive reorganization

A corporate division (or divisive reorganization) typically involves three major steps—(1) a new corporation, a subsidiary, is formed; (2) part of the parent corporation's assets are transferred, usually tax-free, to the subsidiary; and (3) the parent corporation transfers its stock ownership in the subsidiary to some of the parent corporation's shareholders in exchange for their stock in the parent corporation. The result is that part of the assets are spun off in corporate form to one or more former shareholders of the parent corporation.

For a divisive reorganization to be tax-free, five tests must be met—(1) a control test;[4] (2) an "active conduct of a business" test;[5] (3) the distribution must be of "solely stock or securities";[6] (4) the parent corporation must distribute all of the stock in the subsidiary or enough for control;[7] and (5) the transactions must not be used "principally as a device for the distribution of earnings and profits…."[8]

The "active business" requirement

Immediately after the distribution, in a divisive, type D reorganization,[9] both the parent corporation and the subsidiary must be engaged in the "active conduct of a trade or business," or immediately before the distribution, the distributing corporation had no assets other than stock or securities in the controlled corporations and each of the controlled corporations is engaged immediately after the distribution in the active conduct of a trade or business.[10] The trade or business must have been actively conducted for five or more years prior to the distribution by the parent.[11] A de minimis amount of assets held by the distributing corporation is disregarded for this purpose.[12]

What is not a business? A corporation that holds only investment assets is not considered to be in a trade or business.[13] In that setting, with no trade or business, a pro rata distribution would most likely be a dividend and a disproportionate distribution in exchange for some shareholders' stock in the distributing corporation would likely be a stock redemption.

In general, a corporation is treated as engaged in a trade or business if a specific group of activities is being carried on by the corporation for the purpose of earning income or profit.[14]

What is a business in context of leasing out assets? For farm or ranch corporations, a major question is whether land ownership alone is a trade or business. The regulations state that the leasing of land would be a business if the corporation performs "active and substantial management and operational functions."[15] In Rev. Rul. 73-234,[16] a livestock share lease with active involvement by the corporate representatives satisfied the active business requirement. The ruling states that the requirement that a trade or business be actively conducted connotes substantial management and operational activities directly carried on by the corporation itself, and not the activities of others outside the corporation, including independent contractors.[17] The 1973 ruling goes on to state that "…the fact that a portion of a corporation's business activities is performed by independent contractors will not preclude the corporation from being engaged in the active conduct of a trade or business if the corporation itself directly performs active and substantial management and operational functions."[18] In Rev. Rul. 73-236,[19] a trust conducting its real estate leasing business activities through independent contractors did not satisfy the requirement of active conduct of a trade or business.

Thus, the activities of an independent contractor or agent are not imputed to the principal (the property owner) even though, in general, activities of an agent are imputed to the principal except where a statute or regulation blocks imputation[20] as in the case where the activity is routed through Section 1402 of the Internal Revenue Code, which blocks imputation[21] or the activity comes under the passive activity rules of I.R.C. § 469.[22] Thus, it would appear that IRS, by ruling, is attempting to block imputation.

In Rev. Rul, 86-126,[23] the active business requirement was not met where a corporation cash rented farmland, with a sharing of expenses, to a tenant who planted, raised, harvested, and sold crops using the tenant's equipment. The activities of the corporate officers in leasing land, providing advice and reviewing accounts were not substantial enough to meet the active business requirement.[24]

In a 1992 ruling,[25] a corporation that was a general partner in a limited partnership was considered to be engaged in the active conduct of a trade or business if the corporate officers performed active and substantial management functions for the partnership.

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[1] I.R.C.§ 355(b). See generally 8 Harl, *Agricultural Law* § 59.07 (2004); Harl, *Agricultural Law Manual* § 7.02[6][c](2004).

[2] Treas. Reg. § 1.355-2(b)(1).

[3] See Pub. L. No. 99-514, Sec. 631, 100 Stat. 2269 (1986).

[4] I.R.C. § 355(a)(1)(A).

[5] I.R.C. § 355(a)(1)(A), (B).

[6] I.R.C. §355(a)(1).

[7] I.R.C. § 355(a)(1)(D).

[8] I.R.C. § 355(a)(1)(B).

[9] I.R.C. § 368(a)(1)(D).

[10] I.R.C. § 355(b)(1)(A), (B). See Treas. Reg. § 1.355-3(a)(1).

[11] I.R.C. § 355(b)(2)(B).

[12] Treas. Reg. § 1.355-3(a)(ii).

[13] Treas. Reg. § 1.355-3(b)(2)(iv)(A).

[14] Treas. Reg. § 1.355-3(b)(2)(iii).

[15] Treas. Reg. § 1.355-3(b)(2)(iii).

[16] 1973-2 C.B. 180.

[17] *Id*.

[18] *Id*.

[19] 1973-1 C.B. 183.

[20] See Harl, *Agricultural Law* § 41.06(2004)

[21] I.R.C. § 1402(a)(1). A 1974 amendment provides that material participation is to be achieved by the owner for S.E. tax purposes "without regard to any activities of an agent of such owner…in the production or the management of production of such agricultural or horticultural activities." *Id*.

[22] Temp. Treas. Reg. § 1.469-5T(b)(2)(ii).

[23] 1986-2 C.B. 58.

[24] *Id*.

[25] Rev. Rul. 92-17, 1992-1 C.B. 142.

Conservation Security Program Interim Final Rule: a truncated green payments program for FY04 needs future improvements

By Martha L. Noble

The Conservation Security Program (CSP) is a landmark new "green payments" program for working agricultural land authorized by the 2002 Farm Bill.[1] Green payments programs provide positive financial incentives for agricultural producers to take actions voluntarily for the conservation and improvement of natural resources and increase of environmental benefits associated with their agricultural operations. Green payments programs can be distinguished generally from "red ticket" programs, such as conservation compliance, which require that producers who receive non-conservation program benefits maintain mandatory minimal conservation standards on at least some of their operation.[2]

The CSP is supported by a wide array of agricultural and conservation organizations.[3] Many of these organizations praised the program's recognition of the past conservation performance of farmers and ranchers and the emphasis on the conservation and environmental benefits of a comprehensive package of conservation practices and systems for dealing with specific resource concerns, rather than a focus on providing financial assistance for individual practices.[4] But USDA's implementation of the CSP, which is currently under way, is not in keeping with the broad scope of the program envisioned in the 2002 Farm Bill. This article provides a brief description of the CSP legislation, the status of CSP funding in agricultural appropriations, and the Bush administration's current plan for implementation of a severely restricted CSP for this fiscal year.

CSP in the 2002 Farm Bill

The 2002 Farm Bill fashioned the CSP as a comprehensive, nationwide program to fund both existing and newly established conservation practices and promote sustainable production systems for all eligible farmers and ranchers. The legislation provides for a continuous enrollment process, with all producers with CSP conservation plans approved by the Natural Resources Conservation Service (NRCS) able to participate without competitive bidding or delay. The 2002 Farm Bill capped benefits per farm or ranch at a modest amount annually but supported ongoing payments for the life of the CSP conservation plan and contract, and provided for renewal of CSP contracts.

Additional significant features of the CSP legislation include a three-tiered payment system with increased base payments as program participants increase the amount of their acreage enrolled in the CSP and the resources of concern addressed in their conservation security plan. Under Tier I, producers must address at least one resource of concern on the portion of their agricultural operation enrolled in the program. Tier II requires that at least one resource of concern be dealt with on the entire agricultural operation, and Tier III requires that all resources of concern be addressed on the entire agricultural operation. The ultimate goal of CSP is to promote a whole farm and ranch planning approach, with a focus on cost-effective land management practices and systems and a payment structure that is intended to move federal farm bill conservation programs toward a performance, outcome-based reward structure. The CSP legislation also provides for special incentives to encourage diversified resource-conserving crop rotation systems, managed rotational grazing systems, conservation buffers, and other high payoff, multiple benefit conservation measures. Incentives for farmers and ranchers to participate in on-farm research and demonstration of new farming and ranching systems and practices are included, as well as incentives for CSP participants who also participate in on-farm and watershed level monitoring and evaluation of environmental and conservation outcomes and performance.

USDA administrative implementation of CSP

Although Congress directed USDA to promulgate CSP regulations within 270 days after the May 13, 2002 enactment of the 2002 Farm Bill, the agency took over two years to promulgate a regulation, with a process that included nationwide listening sessions on both an advanced notice of proposed rulemaking[5] and the proposed rule for the CSP.[6] On May 4, 2004, the NRCS issued a notice of CSP implementation criteria for FY04.[7] This was followed on June 21, 2004 by an interim final rule for CSP[8] and a notice of the CSP sign-up period for FY04,[9] which runs from July 6 to July 30, 2004.

The CSP proposed rule elicited over 14,000 public comments including 11,500 letters and emails and additional oral statements at listening sessions on the proposed rule, a record number of comments submitted to USDA on a conservation program. The vast majority of comments on the proposed rule objected to the NRCS proposal to severely curtail CSP participation in FY04 by limiting enrollment to a few selected watersheds, which the agency would announce shortly before designated CSP sign-up periods. In addition, thousands of comments objected to the NRCS proposal to create additional participant categories, not authorized by the CSP legislation, to further limit farmer and rancher participation within the selected watersheds. NRCS also proposed to provide only 10 percent of the statutorily authorized base payment for program participation, an amount set so low that even those farmers and ranchers eligible under the watershed and category restrictions would be hard put to find any financial incentive in CSP participation.[10]

In the preamble to the CSP proposed rule, NRCS based its severe restrictions on the CSP on a funding limitation of $41.4 million imposed on the program by congressional appropriators for FY04. Indeed, CSP funding has been a favorite target of the Bush administration and the House Agricultural Appropriations Subcommittee. The 2002 Farm Bill authorized the CSP with mandatory program funding and opened it to all farmers and ranchers who met program qualifications. The result was to put the CSP as a green payments program on the same footing as the agricultural commodity programs. In the FY03 appropriations process, however, the House restricted CSP to a single state (Iowa) while the Senate kept the farm bill funding intact. Though the Senate prevailed on that issue for FY03, the Administration then won a battle with Congress decreasing total outyear spending on CSP by $3.1 billion to offset emergency disaster aid. Then, in the FY04 appropriations process, the House zeroed out the CSP altogether while the Senate provided for program funding as authorized. The final compromise for FY04 appropriations was a $41.4 million funding limit in FY04, but in return an overall funding cap of $3.77 billion imposed on CSP in the FY03 disaster aid deal was removed.[11] This means that without further congressional action to restrict CSP funding from FY05 onwards, the CSP has returned to its original legislative status as an entitlement program with mandatory funding.

The Bush administration promised in the CSP proposed rule to issue a substantially revised CSP rule if Congress in the FY04 appropriations bill removed the funding cap for CSP from FY05 forward.[12] Even though Congress took that action, the NRCS issued an interim final rule for the CSP and a notice of CSP sign-up for FY04, with little change to the proposed rule and no revised rule in the offing as promised. Instead,

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NRCS indicated in the interim final rule that it plans to implement the CSP in future years in a truncated form, using periodic CSP sign-up notices to make adjustments for program funding increases.

This process has significant flaws. First, NRCS apparently perceives no legal or policy obligation to take public comments on the sign-up notices, even though major decisions on CSP implementation are covered in the notices. Second, this approach of setting a truncated CSP in the basic regulation, with yearly notices of tweaking to expand the program, works against the implementation of the CSP as a full-fledged green payments program, with the necessary predictability and stability for agricultural producers to view it as a lasting and significant component of U.S. agricultural policy.

A brief summary of the CSP interim final rule and the CSP notices issued in May and June for the FY04 signup details the method by which the NRCS has curtailed the CSP in FY04. On May 19, NRCS listed the 18 watersheds selected for the CSP in FY04, based on selection criteria announced in the May 4 public notice for choosing watersheds and for selecting particular categories of farmers within those watersheds who will get an opportunity to participate.[13] Significantly, California, the southwest, and the northeast were all but shut out of the CSP in FY04, due, according to the agency, to conflicting high demands on NRCS staff in those states. Only one watershed was selected in the entire region of New England plus the Mid-Atlantic states. NRCS estimates that the 18 watersheds selected for participation include about 27,000 farms and ranches, with a nationwide total of about 3,000 to 5,000 participants able to enroll given the $41.4 million cap on the CSP for FY04.

Despite a legal ban on using a ranking system to select farmers to participate in the CSP, the May 4 notice also revealed initial details of how NRCS will rank farmers and ranchers, with top ranked categories to be enrolled in the FY04 program first. This ranking will be done at the national level, which may result in some of the FY04 selected watersheds having few or no CSP participants. NRCS made its final determinations for the FY04 program in the June 21 interim final rule and notice of FY04 sign-up. NRCS is requiring all CSP participants to have already met its highest ranked conservation standards (known as resource management system quality criteria) for soil and water quality in order to be eligible to enroll. To simplify these eligibility requirements for FY04, the sign-up notice for this year requires that crop farmers attain a positive score (higher than 0.0) on the Soil Conditioning Index (SCI). Rather than requiring that all quality criteria be met for water quality, this has been limited to the quality criteria for nutrients, pesticides, salinity, and sediment for both surface and ground water. For pastureland and grassland, rather than these soil and water quality criteria, the producer must follow a management plan that provides a forage-animal balance, proper livestock distribution, and managing livestock access to water courses. For Tier 3 eligibility, all quality criteria for existing resource concerns must be met, except that for soil quality in which a positive SCI score will substitute for the quality criteria. For irrigation water management, a water use efficiency value of at least 50% will substitute for the quality criteria, and for wildlife a value of at least 0.5 on the Wildlife Habitat Index will substitute for quality criteria.

The interim final rule also makes some improvement in the CSP payment rates over the proposed rule. Rather than reducing the statutory base payments rates by 90 percent, as in the proposed rule, the interim final rule reduces the rates by 75 percent, 50 percent, and 25 percent for Tier I, II, and III participants respectively. At the same time, however, the interim final rule lowers CSP cost share payments from up to 75 percent, as required by law and included in the proposed rule, to not more than 50 percent.

One significant improvement in the interim final rule is the decision to value cropland that has been converted to pasture-based farming as higher valued cropland for CSP payment purposes. This change eliminates the earlier perverse incentive of giving a higher payment to annual cropping over grass-based, resource-conserving systems.

Most importantly, however, the interim final rule adds a new overarching payment constraint not found anywhere in the statute. This "contract limitation" would limit the total CSP payment, including the bonus or "enhanced" payments for outstanding environmental performance, to not more than 40 percent, 25 percent, and 15 percent of local land rental rates for Tier III, II, and I participants respectively. The brand new limitation will hit small acreage, high value crops and rangeland livestock operations particularly hard, even those offering some of the best conservation improvements or environmental benefits. The result may well be that few of these producers, if any, will enroll, including many farmers and ranchers who have been conservation leaders. In addition, the right of a farmer or rancher to renew a CSP contract and stay in the environmental program over the long-term, guaranteed in the legislation, is effectively voided by the interim final rule.

Overall, the interim final rule makes the CSP the most environmentally demanding program in the history of USDA conservation efforts, but then provides unreasonably low incentives for participation. USDA has adopted the rhetoric that the CSP is intended to "reward the best and motivate the rest."[14] The agency's approach to implementation, however, contradicts this motto. The selection of watersheds by national headquarters combined with a national ranking system and the low payments offered to individual program participants does not provide sufficient rewards for the best nor will it necessarily demonstrate the potential benefits of the program across a wide array of farming and ranching systems to motivate the rest. NRCS has opened a public comment period on the CSP interim final rule but also indicated in the preamble to the interim final rule that the agency plans to continue into future years with its process of limited selected watersheds and restrictive categories as a means of curtailing participation in the program.

CSP beyond FY04

Public support for full funding and implementation of the CSP remains strong. On May 11, the Senate Agriculture Committee's Subcommittee on Forestry, Conservation, and Rural Revitalization held a hearing on *Examining the Conservation Title of the 2002 Farm Bill.* Testimony on behalf of the Sustainable Agriculture Coalition from Francis Thicke, an Iowa dairy farmer and member of the Iowa NRCS State Technical Committee, focused on concerns with NRCS implementation of the Conservation Security Program (CSP), especially aspects such as the watershed-based approach that are not in keeping with the CSP statute. Other panelists at the Senate hearing testifying in support of a fully implemented CSP included Al Christopherson for the American Farm Bureau Federation; John Hansen representing the National Farmers Union; Gordon Gallup speaking on behalf of the National Association of Wheat Growers, the National Cotton Council, the National Corn Growers Association, the American Soybean Association and the USA Rice Federation; and Billy Wilson, President-Elect of the National Association of Conservation Districts.[15]

A similar hearing on Farm Bill conservation program implementation was held on June 15 before the Subcommittee on Conservation, Credit, Rural Development, and Research of the House Agriculture Committee. The opening statement of the subcommittee chairman Representative Frank Lucas was significant in that he addressed the issue of green payments at greater length than any House Agriculture Committee member has to date. Craig Cox, Executive Director of the Soil and Water Conservation Society, testified on behalf of the American Farmland Trust, Center for Science in the Public Interest, Defenders of Wildlife, Environmental Defense, Henry A. Wallace Institute for Agricultural and Environmental Policy at Winrock International, Mississippi River Basin Alliance, National Wild-

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support for full-scale implementation of the CSP. A highlight of this hearing was the response of panelists to a question from Subcommittee Chair Frank Lucas (R-OK) about the requirements of CSP for conservation planning, including the provisions of Tier III for a whole farm and ranch approach to conservation planning. Joe Logan, an Ohio farmer representing the National Farmers Union, responded that the CSP attention to planning and a comprehensive approach to conservation was just what a lot of farmers wanted in a conservation program. In addition, Bob Stallman, President of the American Farm Bureau Federation, responded to a question from Subcommittee Chairman Lucas about the challenges and cost of implementing CSP by saying that we need to look at the bigger picture including international trade and agriculture and World Trade Organization (WTO) rules. He stated that CSP is an opportunity to transition U.S. farm payments out of the WTO "amber box" of trade distorting payments to something else and that it was time to get onto the learning curve with the CSP, to get it out, get it going, and to implement this critically important green payments program.[16]

The 2002 Farm Bill provided record funding for conservation on agricultural working lands with the establishment of the CSP as a foundation green payments program on equal footing with the commodity support programs. Support for the CSP remains strong among individual farmers and ranchers and among a wide array of organizations. As indicated by the recent congressional hearings on conservation program implementation, agricultural conservation programs and the environmental performance of agricultural operations will continue as key issues when the farm bill comes up for reauthorization in 2007. Whether we enter that debate with an effective and fully implemented green payments program in place will depend on the response of Congress and the Administration in the coming year to the public call for a fully implemented CSP.

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[1] Farm Security and Rural Investment Act of 2002, Pub. Law No. 107-171, 116 Stat. 134, 223-233 (2002)(codified at 16 U.S.C. §§ 3838-3838c).

[2] For a detailed discussion of the evolution of green payment programs in federal farm bills, see J. Douglas Helms, Performance Based Conservation: The Journey toward Green Payments (USDA, NRCS, Historical Insights No. 3, Sept. 2003)(posted on the web at http://www.nrcs.usda.gov/about/history/articles/perfbasedconservation.pdf).

[3] See, e.g., Letter dated May 13, 2003 supporting full implementation of the CSP, sent to USDA Secretary Ann Veneman from the National Corn Growers Association, the American Farm Bureau Federation, the American Soybean Association, the National Association of Wheat Growers, the National Grain Sorghum Producers, the National Farmers Union, the National Cotton Council, the United Fresh Fruit & Vegetable Association, the USA Rice Federation, and the US Rice Producers Association (posted on the web at http://www.msawg.org/sac/csp/commodity_group_letter.shtml); Letter dated October 27, 2003 from the National Association of State Departments of Agriculture to House and Senate Appropriations and Agriculture Committees urging full funding and implementation of the CSP (posted on the web at http://www.nasda.org/joint/10-27-03-CSP-Letter.pdf); letter dated May 21, 2003 from conservation and environmental groups including American Farmland Trust, Defenders of Wildlife, Environmental Defense. Henry A. Wallace Center for Agricultural and Environmental Policy, Minnesota Project, National Association of Conservation Districts, National Audubon Society, National Campaign for Sustainable Agriculture, National Wildlife Federation, Natural Resources Defense Council, Sierra Club, Soil and Water Conservation Society and Sustainable Agriculture Coalition to USDA Secretary Ann Veneman in support of full funding and implementation of the CSP (posted on the web at http://www.msawg.org/sac/csp/conservation_group_letter.shtml).

[4] The CSP's focus on conservation planning, on promotion of sustainable farming and ranching, and on monitoring and evaluating conservation and environmental outcomes distinguish it from the farm bill's other program for conservation on agricultural working lands, the Environmental Quality Incentives Program (EQIP). The 2002 Farm Bill transformed EQIP by removing most statutory requirements for effective conservation planning, increasing the maximum contract payment from $50,000 to $450,000, and authorizing USDA to use the program to provide financial assistance for industrialized farming operations' infrastructure and equipment, which may be significant new sources of environmental pollution whose environmental harms outweigh environmental benefits.

[5] 68 Fed. Reg. 7720-7722 (Feb. 18, 2003).

[6] 69 Fed. Reg. 193-224 (Jan. 2, 2004).

[7] 69 Fed. Reg. 24560-24567 (May 4, 2004).

[8] 69 Fed. Reg. 34501-34532 (June 21, 2004)(Interim Final Rule to be codified at 7 C.F.R. pt. 1469).

[9] 69 Fed. Reg. 34533-34541 (June 21, 2004). The NRCS has established a website for the CSP at http://www.nrcs.usda.gov/programs/csp/ with links to the Federal Register material and other CSP information and documents.

[10] NRCS has posted CSP public comments on the web at http://www.nrcs.usda.gov/programs/csp/comments.html.

[11] Consolidated Appropriations Act of 2004,Title 7, § 752 (Pub. L. No. 108-199 (2004)). Note also that the FY05 agricultural appropriations process is underway. The Bush administration budget proposal included $209 million for the CSP, an amount $73 million lower than Congressional Budget Office's budget estimate of $282 million for the CSP as an uncapped mandatory entitlement program. The House Appropriations Committee, on June 23, 2004, approved an agricultural appropriations bill (H.R. 4766, House Report No. 108-584) with a CSP spending cap of $194 million. The Senate Agricultural Appropriations Subcommittee has not yet acted on FY05 appropriations.

[12] 69 Fed. Reg. 7720 (Jan. 2, 2004).

[13] A map and list of selected watersheds is available at http://www.nrcs.usda.gov/programs/csp/watersheds04.html. NRCS is adding to the watershed list links to NRCS State Conservation Office websites with detailed information about each watershed.

[14] See, e.g., USDA News Release No. 0425.03, Veneman Announces Proposed Rule for the Conservation Security Program (Dec. 17, 2003)(posted on the web at http://www.usda.gov/Newsroom/0425.03.html).

[15] The written testimony submitted for the hearing and a link to the audio-video transcript of the hearing are posted at http://agriculture.senate.gov/Hearings/hearings.cfm?hearingId=1163.

[16] The written testimony and links to the House Agriculture Committee hearing transcript are posted on the web at http://agriculture.house.gov/hearings/index.html.

Insurance companies fail to exhaust administrative remedies

In *Ace Property & Cas. Ins. Co. v. United States*, No. 03-470C, 2004 WL 626545 (Fed. Cl. Mar. 31, 2004), the United States Court of Federal of Claims held that it lacked jurisdiction because the plaintiffs failed to exhaust their administrative remedies pursuant to 7 U.S.C. § 6912(e).

Several private insurance companies (hereinafter plaintiffs) brought an action for breach of contract, breach of implied covenant of good faith and fair dealing, and unjust enrichment against the Federal Crop Insurance Corporation (FCIC) after the FCIC implemented policy changes pursuant to amendments to the Agricultural Research, Extension, and Education Reform Act of 1998 (AREERA), Pub. L. No. 105-185, 112 Stat. 523, and the Agricultural Risk Protection Act of 2000 (ARPA), Pub. L. No. 106-224, 114 Stat. 358. *Ace*, 2004 WL 626545, at *1, *1-4.

The FCIC filed a motion to dismiss, arguing that the court lacked subject matter jurisdiction because the plaintiffs failed to exhaust their mandatory administrative remedies. *See id.* at *4. The plaintiffs responded to the FCIC's motion to dismiss by arguing that "because they are suing the United States, not the FCIC, the requirements of administrative exhaustion ... are not controlling and thus do not deprive this Court of jurisdiction over their claims." *Id.* at *6. More specifically, the plaintiffs asserted that the alleged breaches derived from "FCIC's actions in implementing statutory changes introduced by Congress...; therefore, the United States is directly liable for those alleged breaches." *Id.* The plaintiffs further argued in the alternative that their claims "fall within judicial exceptions to the statutory and regulatory requirement of administrative exhaustion." *Id.* at *8.

The court explained that federal courts apply two types of exhaustion doctrines: statutory exhaustion and common law exhaustion. *See id.* at *6. It also explained that statutory exhaustion is mandatory and "courts are not free to dispense with them" and that common law exhaustion "recognizes judicial discretion to employ a broad array of exceptions that allow a plaintiff to bring his case in federal court despite his abandonment on the administrative review process." *Id. See McCarthy v. Madigan*, 503 U.S. 140, 144 (1992) (stating that "'[w]here Congress specifically mandates, exhaustion is required. But where Congress has not clearly required exhaustion, sound judicial discretion governs.'"). The court further explained that pursuant to 7 U.S.C. § 6912(e), "a person shall exhaust all administrative appeal procedures established by the Secretary or required by law before the person may bring an action in a court of competent jurisdiction against– (1) the Secretary; (2) the Department; or (3) an agency, office, officer, or employee of the Department." *Id.* (quoting 7 U.S.C. § 6912(e)).

The court rejected the plaintiffs' claim that they were actually suing the United States rather than the FCIC, noting that in their first amended complaint they expressly identified the FCIC as the defendant and alleged that a breach of contract resulted from the FCIC's actions in implementing the required policy changes. *See id.* at *7. The court concluded that the plaintiffs

> have neither specifically alleged nor ... shown, or provided evidence to suggest, that Congress mandated the way in which the FCIC should implement the relevant provisions of the AREERA or ARPA. Thus, they ... fail to satisfy their burden of showing that this Court has jurisdiction over the instant action.... Congress has expressly set out a statutory scheme that applies to suits, such as this one, that allege a breach ... resulting from the actions of the FCIC.

Id.

The court also rejected the plaintiffs' assertion that their claims fall within the common law exceptions to the statutory and regulatory exhaustion. *See id.* at *8. The court held that "because the various exceptions to exhaustion urged by the plaintiffs do not apply where, as here, a clear statutory exhaustion requirement exists, the plaintiffs' arguments relying on these exceptions are unavailing." *Id.* at *9. (citation omitted).

—Harrison M. Pittman, Staff Attorney, National AgLaw Center

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Call for nominations

The AALA Awards Committee invites and encourages nominations for three awards:

1. Distinguished Service Award
2. Professional Scholarship Award
3. Student Scholarship Award

For full consideration, a nomination should be submitted to uchtmann@uiuc.edu by August 21.

A nomination for the Distinguished Service Award should include a statement summarizing why the person is being nominated accompanied by appropriate supporting materials.

A nomination for either the Professional or Student Scholarship Award should include the complete citation to the published work, a brief statement summarizing why the work is being nominated, and the name of the person making the nomination (and contact information). The scholarship awards are intended to recognize and encourage written work demonstrating (a) excellence in quality of writing, (b) relevance to important legal issues in agriculture, (c) clarity of analysis, and (d) potential impact. A nominee for the student award must have been a student at the time the published work was accepted for publication; for example, student-authored Notes or Comments in law reviews would be eligible. A nominee for the professional award would have completed the J.D. or other highest degree when the writing was written and accepted for publication. As a general guideline, the work should have been published after March 31, 2003.

Information regarding previous award recipients is available at http://www.aglawassn.org/pagefile/whatisaalainfor/whatisaalaawards,html.

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The Public Mind Survey, Pennsylvania

In the results from Mansfield University's "The Public Mind Survey", 59 percent of Pennsylvania respondents considered themselves to be environmentalists. Compared to those who indicate they are "not environmentalists", these people are likely to recycle cans, refuse to buy environmentally harmful products, contribute money to environmental organizations, and be willing to spend more money for wind powered electricity. About one-sixth of these responding indicated they were members of an organized environmental group.

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AMERICAN AGRICULTURAL LAW ASSOCIATION NEWS

The 25th Annual Educational Symposium of the American Agricultural Law Association is quickly approaching on October 1 and 2, 2004 in Des Moines, Iowa. This year's conference has something for everyone. Session topics range from international trade to farm taxation, as well as a session on ethics that will discuss challenging ethical problems confronted by attorneys with agricultural interests. This year, the traditional Ag. Law Update presentations are expanded to 30 minutes each to provide greater review of the year's developments. Registration brochures will be mailed as soon as all presentations have been confirmed. Registration materials are available online at www.aglaw-assn.org. Click on the 2004 conference link on the home page. The registration form may be filled out on your computer if you have Adobe Acrobat Reader. A special dinner for students attending the conference has been planned for the evening of Oct. 1, 2004 sponsored by the Drake Ag. Law Student Ass'n.