Agricultural Law Update

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That which is unjust can really profit no one; that which is just can really harm no one.

— Henry George

Fifth Circuit removes obstacle to farm reorganizations

A substantial obstacle to successful farm reorganizations under Chapter 11 of the Bankruptcy Code has been the requirement imposed by bankruptcy courts in some circuits that the debtor make periodic interest payments to undersecured creditors on the value of their collateral during the pendency of the proceedings.

The requirement is ostensibly based on sections 361 and 362(d)(1) of the Bankruptcy Code. Those sections authorize the dissolution of the automatic stay unless the undersecured creditor's interest receives "adequate protection."

While acknowledging the general rule that creditors are not allowed a claim for interest accruing on their debts during bankruptcy proceedings, undersecured creditors have argued that they are entitled to periodic payments from the debtor to compensate them for their lost "opportunity costs." In essence, opportunity costs are the sums the creditors would realize (if they were not restrained by the automatic stay) from foreclosing their liens, selling the collateral, and reinvesting the funds.

Debtors, unsecured creditors, as well as many commentators, have countered that undersecured creditors are adequately protected when they are protected against the depreciation of their collateral. Compensation for lost opportunity costs is also challenged on the grounds that the financial burden on the debtor cripples any chance for a successful reorganization and frequently results in the transfer of the unencumbered assets of the estate to the secured creditors prior to any time at which the unsecured creditors could obtain a share of those assets.

In the Ninth and Fourth Circuits, periodic postpetition interest payments on the value of an undersecured creditor's collateral have been held to be an element of adequate protection as a matter of law. *In re American Mariner Industries Inc.*, 734 F.2d 426 (9th Cir. 1984); *Grundy National Bank v. Tandem Mining Corp.*, 754 F.2d 1436 (4th Cir. 1985).

The Eighth Circuit, while declining to require such payments as a matter of law, has held that the circumstances of each case will dictate whether an undersecured creditor is entitled to periodic interest payments on the value of the collateral. *In re Briggs Transportation Co.*, 780 F.2d 1339 (8th Cir. 1985).

(continued on next page)

Supreme Court upholds FDA action levels

The Supreme Court has upheld the Food and Drug Administration's (FDA) use of informal "action levels" in regulating environmental contaminants (such as aflatoxins) in food. *Young v. Community Nutrition Institute*, 106 S. Ct. 2360 (1986).

The decision reversed the D.C. Circuit's holding that the Food, Drug and Cosmetic Act (FDCA) requires the FDA to use formal rulemaking procedures to fix tolerances — or permissible limits — for such unavoidable impurities.

The FDA's general practice is to set allowable levels of unavoidable environmental contaminants of food by internally establishing "action levels" which, if exceeded, render the food subject to regulatory action under the FDCA's basic adulteration provision.

For example, the FDA has set action levels for mercury in fish, lead in canned foods, various pesticides in agricultural products, as well as for aflatoxin (a potent carcinogen) in corn, peanut products and other foods. The FDA publishes these action levels once they are established, but does not give the public notice of their impending development or an opportunity for comment.

The action level for aflatoxin in corn is 20 parts per billion (ppb). In 1980, when the FDA permitted corn containing up to 100 ppb to be blended with untainted corn and used for animal feed, two consumer groups — the Community Nutrition Institute and the Ralph Nader-founded Public Citizen — as well as two individuals filed suit, contending the FDA had acted illegally.

(continued on next page)

OBSTACLE TO FARM REORGANIZATIONS

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In a thorough and well reasoned opinion, the Fifth Circuit recently declined to follow the lead of the Ninth, Fourth and Eighth Circuits, and held that section 361(3) of the Bankruptcy Code "...does not require periodic postpetition interest payments to an undersecured creditor to compensate it for the delay of the reorganization proceeding during the pendency of the automatic stay." *In re Timbers of Inwood Forest Associates Ltd.*, 793 F.2d 1380, 1416 (5th Cir. 1986).

Describing the issue as simply one of statutory interpretation, the court's opinion undertakes an exhaustive review of the legislative history, commentary and decisional authority addressing the issue.

Taking note of expressions of the "destructive effect" that the *American Mariner* decision will have on agricultural reorganizations, the court observed that the allowance of periodic postpetition interest payments to undersecured creditors was inconsistent with the congressional policy of favoring reorganizations because "...the reorganization proceeding could not continue after the unencumbered assets of the estate that were being used to fund the payments were exhausted, thereby requiring that the stay be lifted due to an inability to make further adequate protection payments." 793 F.2d at 1408, n. 48 (citing *In re Wolsky*, 53 B.R. 751 (Bankr. D.N.D. 1985).

Because many, if not most, secured creditors in farm reorganizations are undersecured, the import of the Fifth Circuit's decision may be significant — at least in that circuit and those that have not addressed the issue. However, because the court (on its own motion) has granted a rehearing *en banc*, speculation on the ultimate impact of the decision is premature.

— *Christopher R. Kelley*

FDA ACTION LEVELS

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The case turned on the proper interpretation of section 406 of the FDCA, 21 U.S.C. § 346. That section states:

> Any poisonous or deleterious substance added to any food, except where such substance is required in the production thereof or cannot be avoided by good manufacturing practice shall be deemed to be unsafe...; but when such substance is so required or cannot be so avoided, the Secretary shall promulgate regulations limiting the quantity therein or thereon *to such extent as he finds necessary* for the protection of public health...

The D.C. Circuit agreed with the consumer plaintiffs that this language *requires* the FDA to promulgate regulations (through the formal rulemaking process by which § 406 rulemaking must be carried out) for any such harmful substance unavoidably present in a food. The discretion-granting phrase "to such extent as ... necessary" referred, in the Court of Appeals' view, to the quantity limitation in the regulation.

By contrast, under the FDA's interpretation of the language, "to such extent as ... necessary" modifies "shall promulgate," and refers to whether a regulation need be issued at all. This interpretation legitimizes the FDA's standard practice of declining to undertake rulemaking proceedings altogether, and regulating instead through action levels that serve as guideposts for initiation of regulatory measures on a case-by-case basis.

Writing for the Supreme Court, Justice O'Connor stated that the wording of the statute was ambiguous and that the FDA's interpretation of the "free-floating phrase" was "sufficiently rational to preclude a court from substituting its judgment for that of the FDA." Justice Stevens, in lone dissent, charged the majority with "merely inventing an ambiguity and invoking administrative deference."

Food industry interests hailed the ruling, stating that a contrary decision would have threatened the legality of much of the nation's food supply for an indefinite period — until formal rulemaking could be completed for each unavoidable environmental contaminant. In general, administrative agencies should also find cause to rejoice, since the case bolsters their claims to wide discretion in interpreting the laws they enforce.

The FDA's regulatory process for environmental contaminants is not yet in the clear, however. The case is remanded to the Court of Appeals for consideration of the consumer plaintiffs' other major argument: that the setting of action levels is, in fact, "rulemaking" — requiring notice to the public and an opportunity for comment. Also at issue is whether the FDA can make exceptions to its action levels, as it did in 1980 with aflatoxins.

— *Robert B. Leflar*

USDA begins dairy indemnity payments

The first of a series of periodic dairy indemnity payments to dairy producers whose milk was removed from the market because their herds were contaminated by the pesticide heptachlor has begun, according to Secretary of Agriculture Richard E. Lyng.

The supplemental appropriations legislation signed into law by President Reagan on July 2, 1986 included $8 million earmarked for these indemnity payments.

Heptachlor-contaminated feed sold to some dairy producers in Arkansas, Oklahoma and Missouri resulted in the contamination of milk. This milk was removed from the market by public regulatory agencies. The maximum permitted level of heptachlor in milk is 0.1 parts per million. Some of the milk from the three affected states had over 10 parts per million.

In mid-March, Lyng dispatched an emergency dairy contamination task force to conduct an on-the-spot assessment of the situation in the affected area. Based on the task force's findings on milk production losses and the number of dairy cows under quarantine, a request was made to Congress for funds to cover indemnification payments for milk and other dairy products that had to be dumped.

Dairy herds were classified in three categories. Some producers were quarantined, and not allowed to market their milk for a brief period until it was determined that the milk from the herd was not contaminated. Some producers with low levels of contamination were quarantined for a longer period,

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Federal Land Bank stock and the federal securities acts

A federal district court has considered the issue of the application of the federal securities acts to the stock of a federal land bank. *Dau v. Federal Land Bank of Omaha*, 627 F.Supp. 346 (N.D. Iowa 1985).

The court found that the Section 3 exemption for securities of instrumentalities of the United States, 15 U.S.C. § 77c(a)(2) (1982), exempted the stock from the requirements at issue of the Securities Act of 1933. The district court also found that the Securities Act of 1934 did not apply to the land bank's stock.

Basically, the court concluded that the land bank's stock was not a security as defined by the 1934 Act, relying on the Supreme Court's holding in *United Housing Foundation v. Foreman*, 421 U.S. 837 (1975).

The court's determination that the stock was exempted from the Securities Act of 1933 raises a question of whether this case is consistent with other decisions. At least one court has found that a land bank is not a federal agency subject of the due process clause. *DeLaigle v. Federal Land Bank of Columbia*, 568 F.Supp. 1432 (S.D. Ga. 1983).

Another court declined to find a land bank a federal agency to support a basis of federal jurisdiction. *Federal Land Bank of St. Louis v. Keiser*, 628 F.Supp. 769 (C.D. Ill. 1986). *See also Birbeck v. Southern New England Production Credit Association*, 606 F.Supp. 1030 (D. Conn. 1985).

On the other hand, the Eleventh Circuit has concluded that a production credit association is a federally chartered instrumentality, and thereby was immune from punitive damages. *Smith v. Russellville Production Credit Association*, 777 F.2d 1544 (11th Cir. 1985). *See* 3 *Agricultural Law Update* 3 (July 1985).

— *Terence J. Centner*

EPA refines review procedures for open field experiments

The Environmental Protection Agency (EPA) has recently announced new review procedures for experiments involving genetically engineered microorganisms that are subject to the Federal Insecticide, Fungicide and Rodenticide Act (FIFRA). *See* 51 *Fed. Reg.* 23313-36 (1986).

Generally, before the EPA can register a pesticide, the EPA must conduct an evaluation of the product to determine that it will not cause an unreasonable adverse effect to humans or the environment. In order to generate sufficient data for this purpose, manufacturers may need to test their products under an experimental use permit (EUP). *See* 7 U.S.C. § 136(c) (1980).

The EPA has adopted a bi-level review system for field testing of genetically engineered microorganisms. This system is based on EPA predictions of potential risks posed by various types of microorganisms.

then were allowed to resume marketing milk after the contamination level was reduced to an acceptable amount.

Other producers whose herds were more seriously contaminated have still not been permitted to market their milk. Depending on the initial level of contamination, it can take anywhere from a few weeks to as long as a year or more before a dairy herd is removed from quarantine.

Payments to dairy producers cover losses for the amount of milk that is required to be dumped. Indemnity payments to dairy processors are for the market value of milk and milk products destroyed, minus any salvage value.

— *USDA News Release*

The EPA has concluded that microorganisms formed by deliberately combining genetic material from organisms of different genera (intergeneric combinations) pose a greater risk than microorganisms which combine source organisms from the same genus (intrageneric combinations).

This conclusion stems from an assessment that intergeneric combinations are more likely to exhibit new traits when released into the environment, and, therefore, that their behavior is less predictable. Similarly, the EPA has concluded that increased uncertainty concerning behavioral changes associated with genetically engineered pathogens (microorganisms having the ability to cause disease in humans, animals or plants) justifies a review of these microorganisms prior to any field testing.

Consequently, intergeneric combinations and genetically engineered microorganisms using pathogenic source organisms are subject to "level two reporting." This procedure includes review by a newly established Science Advisory Committee, which will consist of independent scientists and members of the lay public. The process also involves a risk assessment by the EPA, and, if necessary, review and comment from other federal agencies.

For intrageneric combinations, the EPA will simply make a preliminary determination of the need for an EUP. This process, referred to as "level one reporting," is designed to provide an expedited review for microbial pesticides posing fewer risks to humans or the environment. The same abbreviated review will be used for genetically engineered microorganisms which do not involve pathogenic source organisms.

Previously, under an interim policy adopted by the EPA, *any* field testing of genetically engineered microbial pesticides required EPA review and approval. *See* 49 *Fed. Reg.* 40659 (1984).

Microorganisms which are not genetically engineered, but which are "non-indigenous," also face the elevated scrutiny of "level two reporting." A microorganism is considered non-indigenous if it is isolated from outside any one of three specified areas — the continental United States, the Hawaiian Islands and the Caribbean Islands.

Thus, a microorganism from the continental United States, developed for use as a pesticide in the continental United States, will be considered to be non-indigenous to the Hawaiian Islands. The EPA would have to be notified before initiation of small-scale field testing of that pesticide in Hawaii.

Regulations for all microbial pesticides designed to be used in large-scale field tests (those which involve more than 10 acres of land) remain unchanged. The review for such tests are basically the same as those previously mentioned for "level two reporting."

These regulations are part of a general Coordinated Framework for the Regulation of Biotechnology. *See* 51 *Fed. Reg.* 23301 (1986). This coordinated framework includes separate descriptions of the regulatory policies of several governmental agencies authorized to review products of biotechnology.

The guidelines are designed to provide both consistent definitions as well as reviews of comparable rigor throughout the various agencies. Where there is an overlap in authority, the coordinated framework establishes a lead agency, with consolidated or coordinated reviews among other agencies.

The EPA, for example, is designated as the lead agency for pesticide microorganisms released into the environment. Significantly, these guidelines work within existing statutory structures — it is assumed that current statutes provide sufficient authority for regulating this developing technology.

— *David Myers*

IN DEPTH

A primer for the agricultural producer considering export

by Janet L. Wright and Christopher Perello

International sales of agricultural products have traditionally been an important segment of the U.S. agricultural economy. During the last decade, not only has there been a significant decrease in the volume of exported U.S. farm products, there has also been a significant increase in the volume of farm products imported to U.S. markets.

The combination of these two factors has had a devastating effect on the U.S. farm economy. Since the primary response to the dual phenomenon of decreased exports and increased imports has been the adoption of programs to increase agricultural exports by developing and facilitating access to agricultural export markets, there is now an even higher premium on participating in these markets.

Many agricultural producers who have previously relied exclusively on domestic markets are reluctant to access these markets because they are unfamiliar with international business transactions. Although in many respects participation in international markets is only an extension of domestic business activity, there are some mechanisms and procedures that are either unique to international marketing, or which are employed more frequently in international transactions.

The purpose of this article is to provide a brief summary of the most basic mechanisms and procedures in order that those agricultural producers (and their advisors) who are unfamiliar with the terminology and procedures of international trade will have a basis from which to approach the market. As such, this article is intended only as a starting point for the uninitiated, and not as a guide for international marketing.

Trade Instruments

One of the greatest problems in international trade is the fact that the parties involved are not generally subject to the other countries' laws. Consequently, if one party fails to uphold its side of the bargain, the other party is limited in the ways in which it can force compliance or receive recompense. Therefore, mechanisms for insuring both the payment for and the acceptance of goods are even more essential than in domestic transactions.

A. The Open Account

The basic problem faced by importers is ensuring that they receive the amount and quality of goods which were contracted. Ideally, importers would like to delay payment until they have received and inspected the goods to insure compliance with the contract. Transactions structured in this manner are referred to as open accounts.

Although such arrangements are not unknown (particularly between traders with established relationships in countries with cooperative governments and reasonable judicial systems), under this type of transaction, the exporter bears the full risk of initial noncompliance.

When the subject of the contract is perishable goods (such as fresh agricultural produce), the risk is especially acute because the exporter is not only running the risk that the importer will not pay for the goods, but also that the importer will reject the goods. Consequently, the exporter will be required to either find another buyer in the foreign location, or bring the produce back to the United States — neither of which may be viable alternatives with perishable produce.

B. Letters of Credit

The safest method of protecting both parties (and the preferred device of the experienced exporter) is the use of letters of credit. Basically, letters of credit are a process in which banks are employed as middlemen — restricting the transfer of funds until certain terms and conditions of the sale are met. The banks performing this service charge a fee. Following is a brief outline of the process involving the use of letters of credit:

1) The parties set the terms of the contract. As part of the contract, the parties agree on the documents which will be required to prove the goods were shipped, and that they were of requisite quality. The list of documents normally includes the invoice, bill of lading, export license, certificate of customs inspection, and proof of insurance. The required documents are listed on a letter of credit.

2) The importer instructs his bank (the issuing bank) to issue the letter of credit in the exporter's name, conforming to the terms of the contract.

3) The issuing bank sends the letter of credit to the exporter's bank (the advising bank).

4) The advising bank notifies the exporter that the letter of credit is available.

5) Thus, being assured of payment, the exporter ships the goods to the importer.

6) The exporter gathers the documents which are required by the letter of credit, and takes them to the advising bank, which compares them to the list on the letter of credit. (The exporter has transferred title to his goods on completion of this step).

7) If all necessary documents are present and correct, the advising bank sends the documents to the issuing bank.

8) The issuing bank makes another check of the documents, and if they are in order, sends the money to the advising bank. The importer's account is then debited in the proper amount.

9) The issuing bank then sends the money to the exporter.

A letter of credit can specify payment on presentation of the documents (sight letters of credit), or during a period of up to 180 days after presentation (usance letters of credit). Most export letters of credit specify a delay payment.

Precision is essential in the use of letters of credit. Banks deal in documents — not commodities. All of the shipping documents listed on the face of letters of credit provide specific information to all parties. For this reason, the documents are required to have the exact information listed, or the letter of credit will not be honored, i.e. the exporter will not be paid.

Consequently, if the terms of the agreement are changed after the letters of credit are issued, it is essential that the exporter obtain an amendment.

C. Variations in the Use of Letters of Credit

1. Revocable Letters of Credit

The usual letter of credit is irrevocable, meaning exactly that — once issued, it cannot be cancelled before the expiration date for any reason (including fraud) unless agreed to by all the parties. Revocable letters of credit can be modified or cancelled by any party at any time. Because the importer could cancel the letter of credit after the goods are shipped, this procedure provides the exporter with no more protection than the open account. Revocable letters of credit are seldom used, and should be avoided if offered.

2. Confirmed Irrevocable Letters of Credit

If the advising (exporter's) bank and the issuing (importer's) bank have a reliable working relationship, the advising bank may confirm the letter of credit. With this procedure, the advising bank pays the exporter directly (thus avoiding the payment delay — points 7-9 above) upon receipt of the requisite documents. The confirming bank is reimbursed by the issuing bank.

Although this procedure expedites payment to the exporter, it requires more than ordinary trust between the two banks, as well

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FmHA as second lienholder after an installment land sales contract

An interesting decision out of the Seventh Circuit preserves the Farmers Home Administration's (FmHA) right to a foreclosure remedy in a situation in which it took a second mortgage to secure an emergency loan to a vendee under an installment land sales contract.

The contract provided for the sale of 260 acres for $250,000, with a term of 20 years, and the interest rate set at 7%. A forfeiture clause was included.

Four years into the term, the vendees obtained an FmHA emergency loan for $183,000, and, with the consent of the vendors, gave the FmHA a second mortgage.

The vendees defaulted after having paid $123,280 to the vendors, but still owed $249,360 on the principal. The vendors sought (and were awarded) ejectment and forfeiture, despite the FmHA's motion for foreclosure.

In *Looney v. Farmers Home Administration*, 794 F.2d 310 (7th Cir. 1986), the Seventh Circuit reversed, and granted foreclosure. The trial court, it was observed, had "implicitly determined" that all the interest owed on the contract had to be paid first before the principal could be reduced. The effect of that implication was that the vendees were calculated to have paid only $639 against the principal from a total of $123,280 paid.

From this, the trial court concluded that at the time of default, the vendees had paid only a minimal amount on the contract — thus justifying the summary remedy.

This interpretation of Indiana law was rejected on appeal, and the Court concluded that payments should be allocated between principal and interest. It went further to hold that "... [e]ven when no principal is paid, a buyer's stake in the property may be sufficient to justify foreclosure."

— *John H. Davidson*

No security interest in federal milk diversion program

In many cases, an agricultural lender will look to various federal programs as an additional source of collateral. Numerous cases have dealt with the issue of whether a secured party may obtain a security interest in such federal benefits. *See e.g. In re Sunberg*, 729 F.2d 561 (8th Cir. 1984); *Osteroos v. Norwest Bank Minot, N.A.*, 604 F.Supp. 848 (D.C.N.D. 1984); and *In re Hollie*, 42 B.R. 111 (Bankr. M.D. Ga. 1984).

In general, most courts have held that it is possible for a lender to take an Article 9 security interest in such federal program benefits.

In *In re Bechtold*, 54 B.R. 318 (Bankr. Minn. 1985), however, a Minnesota Bankruptcy Judge ruled that federal law prohibited the granting of a security interest in benefits to be earned under the U.S. Department of Agriculture Milk Diversion Program.

Specifically, the court pointed to language found at 7 C.F.R. § 709.3(a), which provides that "no assignment may be made to secure or pay any pre-existing indebtedness of any nature whatsoever." According to the court, such a regulation clearly indicated that the Secretary of Agriculture intended that such milk diversion payments be free of claims by parties other than the farm participant.

— *Phillip L. Kunkel*

AG LAW CONFERENCE CALENDAR

Prevention of Groundwater Contamination.
Sept. 26-27, 1986, University of Kansas School of Law, Lawrence, KS.
Sponsored by the University of Kansas School of Law, Washburn University School of Law, and the University of Kansas Division of Continuing Legal Education.
For further information, contact Sharon Graham at 913/864-3284.

Pesticides and Groundwater Conference.
Oct. 16-17, 1986, St. Paul, MN.
Sponsored by 11 state departments of health in the Midwest.
For further information, contact The Health and Environment Network, 2500 Shadywood Road, Box 90, Navarre, MN 55392; 612/471-8407.

1986 Annual Meeting: American Agricultural Law Association.
Oct. 23-24, 1986, Worthington Hotel, Fort Worth, TX.
Sessions on the Current State of Agriculture, Agricultural Policy, the Role of the Bar, the Farmers Home Administration, the Farm Credit System, Innovative Financing, Creditor Responsibilities, Educational Directions, Farm Bankruptcies, The 1985 Farm Bill, Agricultural Labor, Tax "Reform," and U.C.C. § 9-307(1).

New Developments in Agricultural Lending and Regulation.
Nov. 12, 1986, Hyatt Regency, Atlanta, GA; Nov. 20, 1986, Chicago Marriott, Chicago, IL; Dec. 4, 1986, Sheraton Plaza La Reina, Los Angeles, CA.
Sponsored by The Bank Lending Institute.
For further information, call 800/831-8333 (within New York) or 800/223-0787 (outside New York).

Tax Planning for Agriculture.
Oct. 15-17, 1986, Fairmont Hotel, Denver, CO.
Sponsored by The American Law Institute and The American Bar Association.
For further information, contact Donald M. Maclay, Director, Courses of Study, ALI-ABA, 4025 Chestnut St., Philadelphia, PA 19104; 215/243-1630.

Tax consequences of hay donations

The recent drought in the Southeastern United States sparked donations of hay to farmers whose feed supplies dwindled with the absence of rainfall. The donations were organized by various groups, including state departments of agriculture and university extension services. When it comes time to file the 1986 tax return, some of the donors may wonder how their donations should be reported.

Section 170 of the Internal Revenue Code (IRC) allows a deduction for contributions to charities that have § 501(c)(3) status and to state governments and their subdivisions if the gift is made exclusively for public purposes. The contributions deduction is limited to 50% of adjusted gross income computed without any net operating loss carryback.

If the donors gave the hay to a church or other charitable organization, or to a subdivision of a state government, the contribution probably qualifies for the charitable deduction since it was made for the purpose of helping farmers in need.

STATE ROUNDUP

GEORGIA. *Beef Labeling*. Ga. Code Ann. § 26-2-30.1, effective July 1, 1986, authorizes the Commissioner of Agriculture to promulgate rules for labeling and certification of beef as having been produced without use of antibiotics or growth hormones. Act No. 1550.

— *Daniel M. Roper*

NORTH DAKOTA. *Confiscatory Price Defense*. In *PCA v. Lund*, Civ. No. 11, 135 (N.D. 1986), the district court denied a motion to reopen a default judgment foreclosure under Rule 60(b), N.D.R.Civ.P. or, in the alternative, for relief from judgment pursuant to the provisions of N.D.C.C. § 28-29-04, (the confiscatory price defense statute).

The lower court reasoned that N.D.C.C. § 28-29-04 had "self-terminated once the price of farm products equaled the cost of production." The North Dakota Supreme Court reversed, in part, and remanded for consideration of the request to reopen the judgment.

N.D.C.C. § 28-29-04 was enacted in 1933 in an attempt to deal with issues of foreclosure, farm debt, farm debtor relief, and low farm price during an agricultural and economic crisis. Although the first part of N.D.C.C. § 28-29-04 states "[u]ntil the price of farm products produced in this state shall rise to a point to equal at least the cost of production," the court construed the entire enactment (all three sections) together.

It determined that the language of all three sections (when read together) should be interpreted to mean that, " 'whenever' legal procedure will result in the confiscation of property 'by forcing the sale of agricultural products upon a ruinous market' the courts, within their discretion, may act as authorized under the provision 'until farm products... equal at least the cost of production.' "

The court noted that in the three sections, the words "whenever" and "when" are used elsewhere. Thus, a comprehensive reading of the three sections indicates the Legislature did not intend the provisions to self-terminate. Finally, the court noted that, unlike many other provisions passed during the Depression Era, the confiscatory price statute did not contain express repeal language.

It should be noted, however, that in an earlier decision, *Heidt v. State*, 372 N.W.2d 857 (N.D. 1985), the court said that, "[r]equiring the farmer to possess commodities in order to invoke the defense contained in N.D.C.C. § 28-29-04 flies in the face of the statute's intended purpose."

The farmer may have already sold the commodities he once had. *Lund* has cast a shadow on the *Heidt* language quoted above — by implying that a forced sale of an individual's agricultural products is required.

Although the constitutionality of the confiscatory price statutes was briefed in *Lund*, it was not discussed by the court. For an earlier discussion of the North Dakota confiscatory price statute, *see Agricultural Law Update*, December 1984, at p. 3. *See also FLB v. Thomas*, 386 N.W.2d 29 (N.D. 1986) (whether a farmer can use the confiscatory price defense is a question of fact preventing a summary judgment); *Lang v. Bank of North Dakota*, 377 N.W.2d 575 (N.D. 1985).

— *Allen C. Hoberg*

PENNSYLVANIA. *Easements by Necessity — Need for Easement Removed*. If the need for an easement by necessity is removed, the easement by necessity is extinguished. In this case, the owner of the dominant tenement purchased a tract that provided access to a public road.

As a result, the dominant tenement's easement by necessity was extinguished as it was no longer needed to provide access to the public road. *Dulaney v. Rohanna Iron and Metal Inc.*, 495 A.2d 1329 (Pa. Super. Ct. 1985).

— *John C. Becker*

Under I.R.C. § 170(e)(1)(A), the amount of the deduction is limited to the donor's basis in the hay. The donor's basis in the hay is the amount paid for the hay if it was purchased. If the hay was raised by the donor, the basis depends on whether the donor uses cash or accrual accounting.

If the donor uses accrual accounting, the basis is the amount included in inventory for the hay. If the donor uses cash accounting, however, the basis is any expense incurred to produce the hay that has not been deducted as a business expense.

Rev. Rul. 55-138, 1955-1 C.B. 223 denies the donor a business deduction for any expenses incurred to raise the hay in the year the hay is given away. Consequently, for taxpayers who use cash accounting, expenses incurred in years before the hay is given away should be left on the return for the year they were incurred, and should not be included in the basis of the donated hay.

Expenses incurred in the year the hay is given away should not be deducted on Schedule F, but should be included in the basis of the donated hay and deducted as a charitable contribution.

As a practical matter, most taxpayers are likely to report the 1986 expense of producing the hay on their 1986 Schedule F since it will be very burdensome to sort out the depreciation, fertilizer, pesticides, fuel, property taxes, insurance and other expenses that should be allocated to the donated hay.

The Internal Revenue Service (IRS) is not likely to challenge those deductions in 1986 since 100% of charitable contributions can be deducted even if the taxpayer does not itemize (I.R.C. § 170(i)). This means the IRS cannot increase taxable income by arguing that the expenses were improperly included on Schedule F unless the taxpayer has made other charitable contributions that use up the contributions deduction limit.

Rev. Rul. 55-138 also requires taxpayers who use accrual accounting to remove the hay that is donated from their beginning inventory for the year the hay is given away. That change in inventory will be offset by the charitable deduction of the basis in the hay which is equal to the inventory adjustment plus the expenses in the year of the donation that are not reported on Schedule F.

For many donors, there was probably no charitable organization or subdivision of a state government that took title to the hay. Therefore, the donation does not qualify for a charitable deduction.

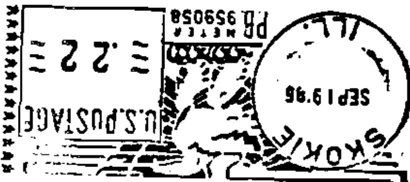
These donors may argue that the donation was made for business reasons, and, therefore, they should be allowed a trade or business deduction for the cost of raising the hay. That argument is difficult to support since it is hard to show that there is any direct or indirect benefit to the farmer's business.

Consequently, for many donors, there is no authority for deducting the costs that are incurred in the year the hay is given away. As with charitable deductions, donors can apparently deduct the expenses of raising hay that is given to another farmer if the donor uses cash accounting *and* gives the hay away in a year after the expenses of producing the hay are deducted. Rev. Rule 55-531, 1955-2 C.B. 520.

Late Developments — The Senate has added an amendment to the pending public debt limit increase bill that would allow a charitable deduction for some gifts of agricultural products amounting to their wholesale fair market value, reduced by any tax deductions the farmer has claimed for the cost of raising them. This new rule, if enacted, would apply to contributions made after June 30, 1986. The liberalized deduction would only be available for gifts by farmers of hay and other commodities to a state agency or subdivision thereof, for the benefit of individuals adversely affected by drought, flood or other major natural disaster.

— *Philip E. Harris*

Address Correction Requested



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American Agricultural Law Association News

1986 ANNUAL MEETING. The American Agricultural Law Association (AALA) will hold its seventh annual educational conference Oct. 23-24, 1986 at the Worthington Hotel, Fort Worth, TX. This year, the theme of the conference will be "Agriculture in a Time of Challenge." The program is co-sponsored by Texas Tech University College of Agricultural Sciences and the Agricultural Law Committee of the State Bar of Texas.

Professor Stephen F. Matthews will open the conference, addressing the topic "Current Status of Agriculture — How are the Farmer and Rancher Really Doing?" Other talks include: Dale S. Stansbury on "Government and Agriculture — An Analysis and Critique of Agricultural Policy and Factors Affecting It"; Martha Miller on "The Farmers Home Administration — Current Matters"; Marvin Duncan on "The Farm Credit System — Current Matters"; and John F. Schumann on "Financing Techniques and Business Structures for the Farm and Ranch."

In addition, Paul L. Wright will speak on "Fiduciary and Contractual Responsibilities of a Creditor"; Harry Dixon will address the issue of "Handling Farm Bankruptcy and Foreclosure — A Banker's View"; Mary Davies Scott will talk on "Handling Farm Bankruptcy and Foreclosure — A Debtor's View"; Ronald Knutson will speak on "The Farm Bill — A Review and Analysis"; Donald B. Pedersen will talk on "Agricultural Labor Laws"; Clark S. Willingham will speak on "'Tax Reform' on Agriculture"; and David W. Dewey will address the issue of "U.C.C. § 9-307."

Two panel discussions will be featured — one on the role of the bar in troubled agricultural times and the other on educational directions in agricultural law.

For more information, contact Martha Hise, Program Coordinator, Division of Continuing Education, Box 4110, Texas Tech University, Lubbock, TX 79409-4110; 806/742-2352.

JOB FAIR. The AALA is planning to hold its second Job Fair concurrent with the 1986 Annual Meeting. An announcement of the Job Fair is being mailed to firms and organizations known to be involved in agricultural law. Notices of available positions will be sent to law school placement offices for dissemination. Resumes received from job seekers will be forwarded to interested firms and organizations, and interviews will be scheduled during the conference whenever indicated. No employer or job seeker charges will be assessed for participation in the Job Fair.

Interview rooms in the Worthington Hotel will be provided for both days of the conference. In addition, highly visible space will be provided near meeting rooms so that job opportunities and messages can be posted. For more information concerning the Job Fair, contact Gail Peshel, Director of Career Services, Valparaiso University School of Law; 219/464-5498.