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INSIDE

IN FUTURE ISSUES

I.R.C. section 197 — Amortization Opportunities Down on the Farm

The 1993 Revenue Reconciliation Act (Pub. L. No. 103-66, section 14261) resolved a long-simmering issue for farmers who purchase farm program allotments and milk base/quota with the adoption of I.R.C. section 197. The drive behind I.R.C. section 197 was a series of cases litigating the appropriate deductibility of "intangibles" purchased with a business, such as goodwill, going concern, customer list, and other cases where it was difficult to determine "a known useful life" for the asset (see Legislative History, H.R. 103-11, pp. 760-780 and *Newark Morning Ledger Co. v. U.S.*, ___ U.S. ___, 113 S. Ct. 1670, 123 L. Ed. 2d 288 (1993)). I.R.C. section 197 provides a single method and period for recovering the cost of most acquired intangibles.

Taxpayers may deduct the ratably amortized capital costs of "section 197 intangibles" over a fifteen-year period beginning in the month of acquisition. I.R.C. § 197(a). The fifteen-year amortization period applied regardless of the actual useful life of a "section 197" intangible asset. No other depreciation or amortization deduction may be claimed on a section 197 intangible that is amortizable under this provision. I.R.C. § 197(b). Generally, section 197 intangibles are eligible for the amortization deduction if acquired after August 10, 1993, and held in connection with a trade or business or in an activity engaged in for the production of income. I.R.C. § 197(c)(1).

"Section 197 intangible" is defined to include "any license, permit, or other right granted by a governmental unit or an agency or instrumentality thereof" (I.R.C. section 197(d)(1)(D)), but the term "section 197 intangible" does not include "land. — Any interest in land." I.R.C. § 197(e)(2). The issuance or renewal of a license, permit, and other right granted by the government is treated as an acquisition. The fact that the term of a license or permit is indefinite or renewable for an indefinite period does not affect its status as a section 197 intangible. H.R. 103-11, pp. 7647. Examples of amortizable governmental licenses, permits, and rights include taxical medallions, airport landing or takeoff rights, and television or radio broadcasting licenses. However, a government-granted right in an interest in land or an interest under a lease of tangible property is not a section 197 intangible (H.R. 103-11, pp. 767). Interests in land include fee interests, life estate, remainders, easements, mineral

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Food Securities Act Does Not Allow Commission Merchant/Secured Lender To Take Crops Free of Prior-Filed UCC Security Interest

On April 14, 1994, the Washington Supreme Court, sitting *en banc*, held in *Food Services of America v. Royal Heights, Inc.*, 123 Wash. 2d 779, 871 P.2d 590 (1994), that (a) the protection from conversion claims given to commission merchants and buyers of farm products under the federal Food Securities Act of 1985 (FSA), 7 U.S.C. section 1631(g)(1) does not at the same time give a commission merchant who also lends money to a grower, first priority over the prior-perfected security interest of another lender. The commission merchant, in its role as junior lien holder must look to state UCC Article 9 law to determine the priority of a commission merchant/junior lender's security interest.

Secured Lender 1 (Food Services of America, d.b.a. "Amerifresh") had a perfected security interest in a grower's crops and proceeds when Commission Merchant/Secured Lender 2 ("Zirkle") entered into a commission merchant relationship with the grower and loaned the grower $100,000 also secured by the grower's same crops and proceeds. The grower had delivered the crops in question to Zirkle for sale under a

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commission merchant agreement. A commission merchant is one who is in the business of receiving farm products for sale, on commission, or for or on behalf of another person without taking title to the farm products.

Zirkle sold the crops and retained all of the proceeds in satisfaction of the grower's loan with Zirkle. Amerifresh sued the grower and Zirkle for repayment of its loan to the grower, asserting its position as a prior perfected secured party under UCC Article 9.

Zirkle argued that it took the grower's crop free of Amerifresh's prior perfected security interest under FSA section 1631(g)(1). That section provides in part as follows:

> ...a commisison merchant... who sells, in the ordinary course of business, a farm product for others, shall not be subject to a security interest created by the seller in such farm product even though the security interest is perfected and even though the commission merchant ... knows of the existence of such interest.

The court rejected Zirkle's argument on the grounds that FSA section 1631(g)(1) applied only to Zirkle's sale of the grower's fruit in its capacity as a commission merchant. The court found that Zirkle had been acting in its capacity as a lender, not a commission merchant, when it retained the proceeds of the crop sale and applied them against the debt the grower owed Zirkle. The court concluded that the priority of Zirkle's security interest in the crop proceeds must be determined under Washington's UCC Article 9, since FSA section 1631(g)(1) does not mention lending, and since they concluded that the elimination of the farm products rule by the FSA was not meant to reorder the normal priority of liens in farm products as among competing lenders.

Therefore, at least in Washington, a commission merchant that acts in both that role and as lender to a grower can se farm products free of a security interes but may not retain the proceeds to satisfy its loan when a prior perfected security interest in those proceeds exists. Presumably, if Amerifresh had given Zirkle notice of its interest under the FSA, Zirkle would not even have been able to sell the crops free of the prior security interest.

—Gordon W. Tanner, Stoel Rives Boley Jones & Grey, Seattle, WA

"Just the Facts, Ma'am" — Seventh Circuit Upholds "Dragnet" Lien

In an opinion worthy of detective Jack Webb for its pointed prose, Judge Posner has refused to find that a "dragnet" clause in a security agreement between a farm couple and their operating capital lender "was meant to mean nothing." *In re Kazmierczak*, No. 93-3376, 1994 WL 200133 (7th Cir. May 23, 1994). A "dragnet" lien increases in reach with each subsequent advance of credit. In *Kazmierczak*, a farm couple borrowed and fully repaid annual operating capital from Terra International in 1990 and 1991. Each year's security agreement had a dragnet clause. In 1992, credit was again advanced, but before the usual security agreement was signed, the couple filed bankruptcy. In the bankruptcy proceedings, they conceded they would have signed a security agreement in 1992 had they not elected bankruptcy.

Terra International argued it had a security interest in the 1992 crops pursuant to the 1991 security agreement. The debtors and trustee objected. Applying Wisconsin law, Judge Posner settled the argument by finding the 1992 debt was sufficiently "related" to the 1991 debt to satify a "relatedness" requirement because they "were identical except for the date." Moreover, the debtors did not claim they did not understand the implications of the dragnet clause in the agreements they signed. Thus, in Judge Posner's words, "we would greatly doubt that tl debtors should be heard to argue that the future advances clause of the 1991 agreement, crystalline though it seems, was meant to mean nothing." The Seventh Circuit affirmed the district court's decision for Terra International.

—Christopher R. Kelley, Lindquist & Vennum, Minneapolis, MN

Sugar Marketing Allotments Upheld

A federal district court has rejected a challenge to the Secretary's imposition of marketing allotments on sugar beet and sugarcane processors. *Minn-Dak Farmers Cooperative v. Espy*, Civ. No. A3-93-116, 1994 WL 190035 (D.N.D. Apr. 21, 1994). Under the Agricultural Adjustment Act, the Secretary is authorized to impose marketing allotments on sugar beet and sugar cane processors if imports are estimated at less than a certain sum. An estimate of carryover stocks is used in the formula for estimating imports. In June, 1993, the Secretary imposed marketing allotments on sugar beet and sugar cane processors by estimating carryover stocks at an amount that triggered the allotments. The Secretary's intention was to avoid forfeitures under sugar's nonrecourse loan program by raising sugar prices. The plaintiffs claimed the Secretary had misinterpreted the allotment statute, 7 U.S.C. § 1359bb, by not relying on objective data in finding that the import "trigger" had been reached. The court, however, held that while the statutory language relevant to estimating carryover stocks was ambiguous, it granted the Secretary sufficient discretion to relieve him any obligation to act on an objective measurement of carryover stocks. The court also found that the Secretary had not abused his discretion or acted arbitrarily in imposing the allotments to avoid sugar forfeitures.

—Christopher R. Kelley, Lindquist & Vennum, Minneapolis, M

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rights, timber rights, grazing rights, riparian rights, air rights, zoning variances, and any other similar rights. H.R. 103-11, pp. 767.

Although allotments and quotas were originally tied to the land, this does not affect the ability of farmers to deduct purchased allotments and quotas. "...Quotas or allotments for such commodities as milk, tobacco, etc. ... are intangible property rights.... [They were not] subject to amortization or depreciation. However, beginning August 11, 1993 (beginning July 26, 1991, if an election is made), these intangible rights may qualify for an amortization deduction as section 197 property. The amortization deduction is figured ratably over a fifteen-year period. If you acquire a right to a quota with the purchase of land or a herd of dairy cows, allocate part of the purchase price to that right." I.R. Pub. 225, p. 55 (1993).

The Agricultural Adjustment Act of 1938 as amended has created quotas for tobacco (7 U.S.C.A. section 1314b), cotton (7 U.S.C.A. section 1344b), and peanuts (7 U.S.C.A. section 1358(a)). Although created as acreage allotments, these programs evolved to acreage/poundage quotas, and the law now allows the lease or sale of these "rights to produce" or the allotment right. In tobacco, cotton, and peanut programs, the original recipients of allotments were the farmers producing the commodity on their own land in 1938. *Id.* Likewise, milk base was awarded to producers at the time of the creation of the program. Milk base was originally created similar to Class I and Class II programs, paying a premium for fluid milk. Tobacco, cotton, and peanut federal farm programs evolved in the 1970's and 1980's into acreage poundage or poundage quotas due to increases in per acreage production. *Id.* Similarly, Virginia allows dairy farmers to purchase milk base (Tony Estes, Virginia Milk Commission, 7/25/94); California and Arizon have purchased milk quota programs (L.J. Butler, University of California at Davis and Jim Miller, ERS, USDA 7/25/94); North Carolina, South Carolina, and Florida, and Puget Sound, Washington, have had base purchase programs in the past. *Id.* and Maryland and other states are considering a milk base program now (W.E. Vinson, Dairy Science, Virginia Tech, 7/25/94). All of these programs, like the New York taxi cab medallion, provide the owner of the program license an opportunity to received enhanced income caused by the restriction of the right of others to produce the commodity or return a premium for commodities marketed under the program. The income is capitalized into the purchase price of the allotment base or right. The right is an intangible with an unknown life as the right is subject to renewal, non-renewal, reduction and other programmatic changes by state and federal legislators.

To qualify for a depreciation allowance, taxpayers must show that the useful life of such an asset can be estimated with reasonable accuracy. No depreciation is permitted if the asset's useful life is indefinite or unlimited. Treas. Reg. § 1.67(a)-3.

Previously, farm taxpayers have attempted to depreciate the farm program or milk base right based on an arbitrarily determined life of the intangible asset or the length of farm bill authorization (*Wenzel and Wenzel v. Comm'r*, 61 T.C.M. (CCH) 2396, T.C.M. (P-H) 91, 166, 1991 WL 50155 (U.S. Tax Ct.)(1991)). The IRS has routinely audited tobacco farmers in major production counties who purchased tobacco because many ill-advisably depreciated the purchased assets. In *Van De Steeg v. Commissioner* (60 T.C. 17 (1973) affd. 510 F.2d 961 (9th Cir. 1975); and Rev. Rul. 75-466, 1975-2 C.B. 74) the taxpayer was allowed a depreciation deduction for their Class I Milk base as an intangible income-producing asset because there was a "useful life for the asset" as it had an expressed expiration date. But most cases have held that depreciation was not allowed for similar intangibles where the right is customarily renewed or where legislation providing for a right to produce does not have an express termination date such as livestock grazing preference (*Uecker v. Commissioner*, 81 T.C. 983 (1973), affd. 766 F.2d 909 (5th Cir. 1985)(grazing preference); *Vander Hock v. Commissioner*, 51 T.C. 203 (1968)(right to deduct milk base denied); *Estate of Cordeiro v. Commissioner*, 51 T.C. 195 (1968)(right to milk base); *Shufflebarger v. Commissioner*, 24 T.C. 980 (1955)(grazing preference)). Thus, prior to the passage of I.R.C. section 197, the purchased milk base/quota and farm program allotments were to be capitalized and were not subject to amortization or depreciation.

By defining government license, permits, and other rights as "section 197 intangible" assets, a new opportunity to farm the tax code is available to farmers who purchase program allotment, quota, and milk base rights.

—L. Leon Geyer, Professor, Virginia Polytechnic Institute and State University

Federal Register *in brief*

The following matters were published in the *Federal Register* during the month of July, 1994.

1. EPA; Notification to Secretary of Agriculture of a proposed rule on plant-pesticides subject to the FIFRA. 59 Fed. Reg. 35662.

2. FCIC; Nursery crop regulations; final rule; effective date 6/30/94. 59 Fed. Reg. 35613.

3. Bureau of Land Management; Establishment of the Federal Livestock Grazing Fee Incentive Program Advisory Committee. 59 Fed. Reg. 35680.

4. Farm Credit Administration; Organization; General provisions; Disclosures to shareholders; Director and senior officer compensation; final rule. 59 Fed. Reg. 37406.

5. FCA; Organization; General provisions and disclosures to shareholders; miscellaneous admendments; final rule; effective date 12/31/94. 59 Fed. Reg. 37400.

—Linda Grim McCormick, Alvin, TX

Texas Institute for Applied Environmental Research Publications Available

Texas Institute for Applied Environmental Research [TIAER] at Tarleton State University is offering free of charge to American Agricultural Law Association members *Watershed Solutions*, TIAER's most recent publication examining a watershed-based approach to deal with the problems of nonpoint source pollution. It focuses extensively on the environmental issues associated with agriculture and concentrated animal feeding operations. In addition, copies of *Dimensions of Planned Intervention*, a publication emphasizing the need for a combination of voluntary and regulatory efforts to address the problem of agricultural pollution are also available at no cost.

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Federal Regulation of Activities on Wetland Areas

By Professor John C. Becker

One of the issues in the ongoing debate on reauthorization of the Clean Water Act and regulation of activities on wetland areas (S. 2093), is coordinating the many laws that already have an impact on wetland areas. In 1991, the General Accounting Office reported on more than sixteen federal laws and their regulations that have an impact on such areas. *Wetlands Overview: Policies, Legislation and Programs,* United States General Accounting Office Report, GAO/RCED-92-79-FAS, November, 1991. This article summarizes the requirements of the three major of federal laws that regulate activities on wetland areas and briefly addresses proposed changes. Understanding the requirements of current laws is an important step in understanding the thrust of proposals to amend them.

The Federal Water Pollution Control Act (The Clean Water Act)

The stated goal of the Clean Water Act (C.W.A.) (33 U.S.C. § 1251 *et seq.*) is the restoration and maintenance of chemical, physical and biological integrity of nation's waters. § 1251 (a). To achieve this objective the Act made it unlawful to discharge any pollutant, except under the terms and conditions of a permit issued by the responsible agency. § 1311. Under this regulatory scheme, point sources of pollution were directed to obtain permits under section 1342 of the C.W.A. (the Act) to gain needed authority to discharge pollutants without being in violation.

The principal permit-granting provision of the Act is section 1344. Under this section, the Secretary of the Army, acting through the Chief of Engineers, is granted authority to issue permits for the discharge of dredge or fill material into the navigable waters at specified disposal sites. The term "navigable waters" includes waters of the United States. §1362(7). In turn, the term "waters of the United States" are defined in 33 C.F.R. part 328, section 328.3, in a very broad and inclusive manner. From among a broad list, the regulations specifically include interstate wetlands (33 C.F.R. § 328.3(a)(2)); other waters, such as intrastate lakes, rivers, streams etc. the use, degradation or destruction of which could affect interstate commerce (§ 328.3(a)(3)), and wetlands that are adjacent to waters that are otherwise identified as waters of the United States (§ 328.3(a)(7)).

Current regulations (§ 328.3(b)) define the term "wetland" as areas that are inundated or saturated by surface or ground water at a frequency and duration sufficient to support, and that under normal circumstances do support, a prevalence of vegetation typically adapted for life in saturated soil conditions. Such areas generally include swamps, marshes, and similar areas. In *United States v. Riverside Bayview Homes, Inc.*, 474 U.S. 121 (1985), the Supreme Court reversed a Sixth Circuit opinion that held the definition of wetland should be narrowly construed to exclude areas that are not subject to flooding by adjacent navigable waters at a frequency sufficient to support the growth of aquatic vegetation. In so doing, the Supreme Court noted the regulation plainly states the definition of wetlands refers to land that is inundated or saturated by surface or ground water, without including the flooding requirement which the Sixth Circuit's holding found so compelling. 474 U.S. 121, 129.

Hoffman Homes, Inc. v. E.P.A., 999 F.2d 256 (7th Cir.1993) focused on the developer's attempt to fill in a tract less than an acre in area containing soil types and at least four kinds of wetland vegetation. The area drew its moisture by collecting rain and melting snows in the area. The nearest body of water which would fall within the general waters of the United States definition was a creek approximately 750 feet distant from the one acre tract. In this case, the isolated nature of the wetland in comparison to other bodies of water in the area eliminated EPA's ability to attach jurisdiction under sections (2) and (3) of the regulation. Section (7) requires showing a connection between destruction or degradation of the wetland and interstate or foreign commerce. Here, the tract had no surface or groundwater connection with Poplar Creek and served no purpose in performing flood control or sediment trapping functions associated with drainage into the creek or its possible flooding. 999 F.2d 256, 259. Noting that both EPA and the Corps of Engineers consider a wetland to affect interstate commerce if the wetland serves as a habitat for migratory birds (999 F.2d. 256, 259), the Seventh Circuit examined the testimony of experts before the agency administrative law judge. A review of that testimony revealed that the expert had not provided any evidence as to migratory bird use of the tract in question prior to the time the developer began to fill it in. Although the expert provided testimony of migratory bird use of other wetland areas, the substance of the expert's testimony was if migratory birds used a nearby area, it was logical to assume the birds would also use this relatively small area. In reaching its decision, the court held the agency failed to provide substantial evidence that the less than one acre tract was proven to be a suitable or potential habitat for migratory birds. 999 F.2d 256, 261. In a lighter comment, Senior Judge Harlington Wood noted that migratory birds are better judges of what is suitable for their welfare than the court or administrative law judges. Having avoided the small tract, the migratory birds spoke and submitted their own evidence. *Id.*

Pursuant to section 1344, the Secretary may issue permits, after notice and opportunity for public hearings, for the discharge of dredged or fill material into the navigable waters at specified disposal sites. Dredged material includes material that is excavated or dredged from waters of the United States. 33 C.F.R. § 323.2(c). Fill material includes any material used for the primary purpose of replacing an aquatic area with dry land or of changing the bottom elevation of a waterbody. § 323.2(e). The meaning of discharge of either of these materials into waters of the United States is also broadly defined in regulations (section 323.2(d)(F)), but exception is made for the discharge of material resulting from plowing, cultivating, seeding, and harvesting for the production of food, fiber, and forest products. § 323.4.

In the Act certain discharges are also treated as non-prohibited discharges. Subject to the provisions of section 1344(f)(2), these discharges of dredged or fill materials include those originating from normal farming, forestry, and ranching activities operations; maintenance and emergency reconstruction of dikes, dams and levees; construction or maintenance of farm or stock ponds or irrigation ditches; construction of temporary sedimentation basins; construction or maintenance of farm or forest roads or temporary roads for the movement of mining equipment which do not impair the flow and circulation patterns or impair the reach of navigable waters. 33 U.S.C. § 1344(f)(1)(A)-(F).

As mentioned above, the principal discharges that are allowed without a permit under the above list are subject to a

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further requirement set forth in section 1344(f)(2). Under this section, any discharge of dredged or fill material into navigable waters incidental to any activity that has as its purpose the bringing of an area of navigable waters into a use to which it was not previously subject, where the flow or circulation of navigable waters may be impaired or the reach of such waters reduced, will still be required to have a permit.

In *United States v. Akers*, 785 F.2d 814 (9th Cir. 1986), the property owner sought to take advantage of several of the non-prohibited discharges of fill or dredged material. The landowner acquired 9,600 acres that included 2,889 acres of wetland known locally as the "Big Swamp," a wildlife habitat that involves Ash Creek, a tributary of the Pit River. The government sued Akers based on construction activities that he undertook in the wetland area without ever having sought to obtain a permit.

In assessing the normal farming activities exception, the court noted that in order to fall under the exemption, the activities must be part of an established (i.e. on-going) farming, forestry, or ranching operation. In support of his claim, Akers presented testimony that the property had been farmed since 1897 and that discing and seeding activities were part of the activities traditionally undertaken on the land. In response, the court noted that Akers ignored the consequences that his current projects were going to have on the land in question. It noted that the record amply reflects that upland crop production had not occurred on the wetland areas on a regular basis and that such use represented a new operation in the wetland. 785 F.2d 814, 820. In regard to the irrigation non-prohibited discharge, the court compared a list of structures specifically described in the exemption (33 C.F.R. § 323.4(a)(3) (1993)) to the type of structures that the landowner was building. Since the structures described by the landowner were not found on the list of structures in the non-prohibited discharge list, the court concluded the landowner failed to satisfy his burden.

Noting that the list of non-prohibited discharges described in the statute and its regulation does not distinguish between minor and major changes, Akers argued that the effect of his proposed activities was simply a change in one form of agricultural activity to another. Recognizing the landowner's point, the court noted, however, that the intent of Congress in passing the Act was to prevent conversion of wetland areas to dry land areas. 785 F.2d 814,822. The emphasis of section 1344(f)(2) is on the substantiality of the impact on the wetland of the proposed non-prohibited activity. *Id.* The more substantial the impact, the greater the likelihood that section 1344(f)(2) will apply and require a permit to conduct the activity, despite the fact that the activity could otherwise be considered agricultural.

Wetland Area Regulations Under the Food Security Act of 1985(Pub. L. No. 99-198), As Amended By the Food, Agriculture, Conservation and Trade Act of 1990 (Pub. L. No. 101-624)

By most estimates, the Clean Water Act's wetlands regulation provisions apply to only about twenty percent of the activities that destroy wetland areas. *Wetlands Overview*, GAO Report, *op. cit.*, page 21. Activities not regulated under section 1344 include drainage, ditching, and channelization for agricultural production, which are major causes of past wetlands losses. To fill this gap in coverage, the Food Security Act of 1985 (Pub. L. No. 99-198) included two major wetlands-related provisions, Swampbuster and the Conservation Reserve Program (C.R.P.). The Food, Agriculture, Conservation and Trade Act of 1990 subsequently amended Swampbuster and the C.R.P. Both of these acts are codified in 16 U.S.C. sections 3801-3862.

Under these acts, several key terms help to define and describe the coverage provided and the protection afforded. For example, the term **highly erodible land** means land classed in categories IV, VI, VII, or VIII by the Soil Conservation Service, or that has an excessive average annual rate of soil erosion. Another example is the term **converted wetland**, which means wetland that has been drained, dredged, filled, leveled, or otherwise manipulated (including any activity that results in impairing or reducing the flow, circulation, or reach of water) for the purpose or to have the effect of making the production of an agricultural commodity possible if — (i) such production would not have been possible but for such action; and (ii) before such action — (I) such land was wetland; and (II) such land was neither highly erodible land nor highly erodible cropland. 16 U.S.C. § 3801(4)(A). Wetland is considered converted wetland if production of an agricultural commodity on such land during a crop year — (i) is possible as a result of a natural condition, such as a drought; and (ii) is not assisted by an act of the producer that destroys natural wetland characteristics. § 3801(4)(B).

A third key term is wetland itself. The term **wetland**, except when part of the term "converted wetland," means land that (A) has a predominance of hydric soils; (B) is inundated or saturated by surface or groundwater at a frequency and duration sufficient to support a prevalence of hydrophytic vegetation typically adapted for life in saturated soil conditions; and (C) under normal circumstances does support a prevalence of such vegetation. § 3801(a)(16). Hydric soils refer to those soils that in their undrained condition are saturated, flooded, or ponded long enough during a growing season to develop a condition that supports the growth and regeneration of hydrophytic vegetation that thrives in such saturated conditions.

Conservation Reserve Program

Unless exempted, any person who, in a crop year following December 23, 1985, produces an agricultural commodity on a field on which highly erodible land is predominant or on designated land on which highly erodible land predominates and is set aside or otherwise not cultivated under a USDA program will be ineligible in regard to such crop for price support; farm storage facility loans under the Commodity Credit Corporation; crop insurance; disaster payments; FmHA loans; loans made, insured, or guaranteed under the Consolidated Farm and Rural Development Act; and other Commodity Credit Corporation payments for storage of an agricultural commodity acquired by the Commodity Credit Corporation. 16 U.S.C. § 3811.

Producers who planted crops before December 23, 1985 or during a crop year that began before December 23, 1985 do not lose eligibility for any of the listed price support or loan program opportunities. § 3812.

Swampbuster Program

Following December 23, 1985, any person who in a crop year produces an agricultural commodity on converted wetland will be ineligible in regard to such crop for price supports; farm storage facility loans; crop insurance; disaster payments; FmHA loans; loans made, insured or guaranteed under the Consolidated Farm and Rural Development Act; and Commodity Credit Corporation payments during the crop year for storage of the commodity acquired by the Commodity Credit Corpo-

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ration. 16 U.S.C. § 3821. As a result of the 1990 amendments to this program, any person who in any crop year subsequent to November 28, 1990 converts a wetland shall be ineligible for the benefits listed above for the crop year in which the conversion takes place and all subsequent crop years.

Under certain situations a producer will not lose eligibility. § 3822(b). For example, if the conversion took place before December 23, 1985, no eligibility is lost. If the agricultural commodity is produced on an artificial lake, pond, or wetland created by diking or excavating nonwetland to collect and retain water for use in agricultural production, or on wet areas that are caused by water delivery or irrigation systems, the producer will not lose eligibility by reason of either the production or the conversion. If the wetland area becomes available for production through natural conditions which do not destroy the area's wetland characteristics, such as drought, and which do not involve action by the producer, the producer does not lose eligibility.

A second opportunity to avoid the ineligibility penalty is found in section 3822(f) which applies to converted wetlands and conversions of wetland areas. Under this section, eligibility will not be lost if (1) the action taken has minimal effect on the functional hydrological and biological value of the wetland, including value to waterfowl and wildlife; (2) the wetland has been frequently cropped prior to the date of the action and the wetland values. acreage, and functions are mitigated by the producer through the restoration of a converted wetland, the conversion of which occurred or was commenced prior to December 23, 1985. In addition, the following conditions must apply: (1) the restoration must be in accordance with a restoration plan; (2) the restoration must be in advance of, or concurrent with, such action; (3) the restoration is not at the expense of the federal government; (4) the restoration is on a one for one acreage basis unless more acreage is needed to provide equivalent functions and values; (5) the restoration takes place on land in the same general area of the local watershed as the converted wetland; and (6) the government is given a perpetual unpaid conservation easement for the wetland. *Id.*

An additional opportunity available to landowners is what has been labelled as the "good faith" exemption. § 3822(h). Under this exemption, a person who would otherwise be ineligible under section 3821 for farm programs and payments might instead be subject to a graduated sanction of not less than $750 nor more than $10,000, depending on the seriousness of the violation, if (1) the person is actively restoring the drained wetlands by agreement with the Secretary, and (2) the Secretary determines that the person has not violated section 3821 in the past ten years, and has converted the wetland "in good faith" and without the intent to violate the provisions of section 3821.

Environmental Conservation Acreage Program

This program has two principal parts. The first supplements the existing conservation reserve program by providing new opportunities for owners of eligible land (16 U.S.C. section 3831(b)) to enter into contracts with the federal government to conserve and improve the soil and water resources of the land. In return for the owner's agreement to take the land out of intensive agricultural production and convert it to a less intensive use as determined in a plan prepared with a local conservation district, the government agrees to pay the landowner an annual rental payment, provide financial assistance in meeting the cost of carrying out the conservation measures and provide technical assistance. §§ 3832, 3833. During the term of the agreement the landowner is limited to the conservation uses specified in the agreement, but retains the right to petition to change the use to some other conservation use or even restore the land to wetland conditions, if the land is a converted wetland.

The second part of this program is the wetlands reserve program. § 3837-3837f. In this program, owners of farmed wetland or converted wetland can offer to sell a wetland conservation easement to USDA and follow a wetland conservation plan that addresses future restoration and protection of the wetland area. section 3837a. During the easement period, the landowner agrees to permit access and inspection of the land and agrees to prohibit alteration of wildlife habitat and other natural features of the area. Compatible economic uses of the wetland area, including hunting, fishing, managed timber harvest, and periodic haying or grazing can be permitted if they are part of the wetland conservation plan and are consistent with the land's long-term protection and enhancement.

The term of the easement granted is to be permanent or thirty years or the maximum time provided by state law. In return, the landowner will be paid on an installment basis the value represented by the difference between the fair market value of the property without the easement and with the easement. In addition, U.S.D.A. agrees to share the cost of establishing the conservation measures and practices called for by the restoration and protection of the wetland.

President Clinton's 1993 Proposal

In August, 1993 President Clinton announced a new package of improvements to the federal wetland regulation program. Under the package, the following initiatives were of interest to agricultural producers: (1) to speed the issuance of Corps of Engineer permits and increas fairness in the process, the Army would be directed to establish an administrative appeal process; (2) the Soil Conservation Service would become the lead Federal agency responsible for identifying wetlands on agricultural lands under both the Clean Water Act and the Food Security Act; (3) all agencies, including the Corps of Engineers, EPA, SCS and the Fish and Wildlife Service would all be directed to use the same procedures to identify wetland areas; (4) final regulations would be issued to clarify that wetland areas converted to crop production prior to December 23, 1985 and which no longer exhibit wetland charcteristics will not be subject to wetland regulations, and (5) support was announced for increased funding of the wetland reserve program.

The Water Pollution Prevention and Control Act of 1994, Senate Bill 2093

Currently before Congress is Senate Bill 2093, a comprehensive bill dealing with reauthorization of the Clean Water Act. Title VII of the bill addresses wetlands management, conservation, and regulatory programs and incorporates provisions of Senate Bill 1304, the Wetlands Conservation and Improvement Act. Title VII addresses many aspects of the section 1344 permitting process but does not address several controversial issues contained in other legislative proposals. (Congressional Research Service Report on Senate Bill 2093, page 20, dated May 18, 1994) These other issues include implementing a wetlands classification system in which highly valuable wetlands would receive the greatest protection and less valuable wetlands are subject to less vigorous permit review and protection; and providing compensation to landowners when section 1344 permits are denied or restricted. The latter part is one of the important parts of the current controversy over regulatory "takings" of private property.

In addition to incorporating many of the proposals submitted by the President, the bill provides for the first statutory definition of "wetlands" in the Clean Water Act, authorizes the establishment of mitigation banks, which allow persons to to accrue wetland mtigation credits for restoration, creation, or enhancement of wetlands, credits which can be used to offset wetlands destruction, and integrates wetlands management with other water resource management activities under the Clean Water Act.

State Roundup

NORTH DAKOTA. *Constitutionality of workers compensation agricultural exemption.* In *Haney v. North Dakota Workers Compensation Bureau*, Civ. No. 930324, 1994 WL 259740 (N.D. June 15, 1994), the North Dakota Supreme Court considered the constitutionality of the state's workers' compensation agricultural exemption.

Haney, a farm worker, injured his back while cleaning grain storage facilities. Haney applied for, but was denied benefits by the Workers Compensation Bureau. In North Dakota, compensation coverage is provided for workers injured in hazardous employment. N.D. Cent. Code § 65-01-02(22)(). The district court affirmed the denial of benefits, and Haney appealed.

Haney claimed that the agricultural exclusion violates the equal protection clause of the North Dakota Constitution. N.D. Const. art. 1, section 21. Haney relied primarily on *Benson v. North Dakota Workmen's Compensation Bureau*, 283 N.W.2d 96 (N.D. 1979). In *Benson*, the supreme court, on a vote of 3-2, held that the agricultural exclusion violated the state constitution's equal protection guarantee. However, the agricultural exemption was not invalidated because the North Dakota constitution requires the concurrence of four justices to declare a statute unconstitutional. N.D. Const. art. VI, section 4.

The *Haney* court, also by a vote of 3-2, overruled *Benson* and affirmed the denial of benefits. The court first considered which of the three standards of judicial review for equal protection claims was appropriate; strict scrutiny, intermediate scrutiny, or rational basis test. In *Benson*, the court applied the intermediate scrutiny standard. Here, the court disagreed and found the rational basis test to be the correct standard of review. The court opined that the workers compensation exemption is economic legislation which "neither involves a suspect classification nor a fundamental or important substantive right which would require the strict scrutiny or intermediate standard of review." 1994 WL 259740, *5 (quoting *Kadrmas v. Dickinson Public Schools*, 402 N.W.2d 897, 902 (1987)).

Under this relaxed standard of review the court proceeded to consider the purpose underlying the agricultural exclusion. Justice Sandstrom acknowledged that "'It becomes apparent that farm laborers were excluded from the act not because farming is nonhazardous but because the Legislature chose not to extend the coverage of the act to that class for a possibly political or social reason.'" 1994 WL 259740, *7 (*quoting Otto v. Hahn*, 306 N.W.2d 587, 590 (Neb. 1981)). Although unarticulated by the legislature, the court noted many possible purposes for the exclusion. Concluding that the agricultural exemption satisfied the rational relationship test, the court cited cases from Indiana, Iowa, Michigan, Montana, Kentucky, Wyoming, Nebraska, and New Mexico that have upheld statutes against similar constitutional challenges. A dissenting opinion was written by Surrogate Judge Erickstad (retired chief justice), the only justice participating in *Haney* to have been on the supreme court when *Benson* was decided.

—Scott D. Wegner, Lakeville, MN

INDIANA. *Class action suit over grade of wheat and soybeans.* In *ConAgra, Inc. d.b.a. Graham Grain Company v. Farrington*, 84A01-9312-CV-386, 1994 WL 275710 (Ind. App. June 23, 1994), farmers claim that ConAgra fraudulently miscalculated the grade of wheat and soybeans by improperly measuring foreign material in the loads.

Richard and Robert Farrington sold wheat, corn, and soybeans to ConAgra at its Terre Haute grain elevator. Upon delivery ConAgra would remove a sample of the load for grading. Grading involved sifting the sample through two screens to separate the grain from the foreign material. The grade of the load was based in part on the foreign material content or dockage. ConAgra would deduct a percentage of the weight from the load if a load contained more than one percent foreign material. Accordingly, the higher the percentage of foreign material, the lower the number of bushels of grain in the load and the less money the farmers received.

The Farringtons filed suit alleging that ConAgra miscalculated the grade of soybeans at four Indiana elevators by using larger screens than those mandated by the USDA. The USDA required a 10/64 screen, while ConAgra used an 8/64 screen. The Farringtons allege violations of the Indiana Racketeer Influenced and Corrupt Organizations statute, breach of contract, negligence, unjust enrichment, and fraud. The Farringtons claim that the use of larger screens, with resulting higher foreign foreign material content and lower number of bushels sold, was a policy at the ConAgra elevators. The Farringtons also claim that ConAgra arbitrarily added an additional three percent foreign material to every load of wheat and soybeans. The trial court classified a class action represented by the Farringtons.

On interlocutory appeal, ConAgra argued that the certification order does not adequately define the class or the issues certified. The Indiana Court of Appeals for the First District disagreed, observing that the class consists of "persons and entities who sold soybeans and wheat to ConAGra during the period January 1, 1988 to January 1, 1992, at ConAgra's facilities in Indiana, who had a foreign material dockage greater than one percent." Further, the court found five common questions to have been certified:

> (a) Whether ConAgra has engaged in a common pattern and scheme of acts and omissions in connection with its business transactions with class members; (b) Whether ConAgra defrauded and deceived class members in its business transactions with class members; (c) Whether class members relied on the fraudulent and deceptive acts and omissions of ConAgra in accepting the price of grain set by ConAgra; (d) Whether the price of grains purchased by ConAgra from class members was artificially deflated due to other wrongful acts and omissions by ConAgra; (e) Whether the class members have sustained damages, and if so, the proper measure thereof.

The court of appeals also found without merit ConAgra's assertions that no common contractual arrangements unite the class, that each class member's damages differed, that the Farringtons are not typical of the class, that the Farringtons will not fairly and adequately represent the class interests, and that the Farringtons failed to establish that common questions will predominate over individual questions. Finding no abuse of discretion, the court of appeals allowed the suit to continue as a class action.

— Scott D. Wegner, Lakeville, MN

House GATT Panel Endorses DEIP Extension

The Committee on Agriculture of the House of Representatives unanimously approved inclusion of legislation to extend the Dairy Export Incentive Program (DEIP) in its package of recommendations for the GATT implementing legislation on July 28, 1994. The House Agricultural Committee proposal will extend DEIP to the year 2001, require use of the program at maximum authorized levels, and expand the list of countries eligible for the program.

DEIP facilitates export sales of dairy products by ensuring that U.S. dairy products can be competitive in world markets. About three billion pounds of U.S.-produced milk equivalent are sold overseas annuall under DEIP.

—Phil Fraas, McLeod, Watkinston & Miller, Washington, D.C.

AMERICAN AGRICULTURAL LAW ASSOCIATION NEWS

A Word From the President-Elect on the 15th Annual Meeting

American Agricultural Law Association
Friday-Saturday, October 21-22, 1994
Peabody Hotel, Memphis, Tennessee

The plans for the Memphis meeting are finalized and you will be receiving a brochure and registration form shortly. We look forward to going to Memphis for the first time. As with past meetings, I believe you will find this year's topics interesting and the speakers outstanding. We will, of course, request CLE accreditation in all mandatory states and expect credit hour approval similar to previous programs.

The meeting will be held in the PEABODY HOTEL MEMPHIS/149 Union Ave./Memphis, TN 38103. Rates: Deluxe $130 Single/$140 Double; Superior $120 Single/$130 Double; Traditional $105 Single/$115 Double (Oct. 19 through Oct. 23).

For your convenience, room registrations may be made directly with The Peabody by calling 1-800-PEABODY. A limited number of rooms are available and reservations must be made by September 21, 1994. After September 21, rooms will be booked on a space available basis only. When making reservations, please indicate that you are a registrant of the American Agricultural Law Association Conference.

I hope that many of you are able to attend and I look forward to seeing you there. You may receive more than one mailing of the finalized meeting brochure; please pass along any unneeded copies to an interested associate.

— J. Patrick Wheeler, President-Elect