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Character is much easier kept than recovered.

— Thomas Paine

Imputed interest rules changed again

On Oct. 11, 1985, President Reagan signed P.L. 99-121, which was H.R. 2475, Simplification of Imputed Interest Rules (Simplification Act). This revision of the imputed interest lives up to its name — at least with respect to eliminating many of the complexities introduced in the 1984 Tax Reform Act.

The 1984 Tax Reform Act created new § 1274 of the Internal Revenue Code (IRC). (See September 1984 *Agricultural Law Update*). This section required parties to an installment sale to charge a specified "testing" interest rate (which changed every six months, and was different for short-, mid- and long-term loans), or be treated, for income tax purposes, as if the sale called for an even higher "imputed rate."

There were several exceptions to § 1274. For example, if a transaction fell within one of the exceptions, it was subject to the rules of § 483, which was also revised by the 1984 Tax Reform Act.

The 1984 Tax Reform Act revisions of the imputed interest rules were to have been effective Jan. 1, 1985, but were postponed on Oct. 12, 1984 by stopgap legislation. (See November 1984 *Agricultural Law Update*). This stopgap legislation limited the test rate to 9% (compounded semiannually) for transactions under $2 million.

The stopgap legislation expired on June 30, 1985, which meant that the 1984 Tax Reform Act provisions were once again in effect. However, the most recent changes are effective retroactively to July 1, 1985. Therefore, no installment sale transactions are subject to the imputed interest provisions of the 1984 Tax Reform Act.

The Simplification Act makes the imputed interest rules less convoluted in several respects:

1) The bifurcated testing and imputed rates are eliminated. Transactions are now subject to a single rate. If the parties do not set the interest rate equal to (or in excess of) the required rate, the required rate will be imputed.

2) The rate for transactions under $2.8 million (other than the sale of new investment credit property) is the lesser of 9% (compounded semiannually) or the applicable federal rate (AFR).

This means that for such transactions, taxpayers can specify a 9% rate, thereby avoiding the imputed interest rules — even if the current AFR is higher.

3) For transactions under $2 million, if the lender is neither a dealer of the property sold, nor an accrual basis taxpayer, the parties can elect to account for the interest on the transaction by using the cash-basis method. I.R.C. § 1274A.

(continued on next page)

Conservation issues: The 1985 farm bill debate

As part of the 1985 farm bill debate, the House and Senate are considering three conservation measures — the so-called sodbusting, swampbusting and conservation reserve provisions.

On Oct. 8, the House agreed on a final version of the 1985 farm bill, but at this writing, the Senate is still debating the bill that emerged from the Senate Agriculture Committee. It is not anticipated, however, that any changes in the conservation provisions of the Senate bill will be made on the floor of the Senate.

The sodbuster program is designed to discourage farmers from converting highly erodible land to cropland in the future by denying price supports and other farm benefits for their crops. Similarly, the swampbuster program would deny farm benefits to producers who, in the future, convert wetlands to croplands.

The conservation reserve program, in contrast, would attempt to encourage the removal of fragile land from *current* use as farmland by reimbursing farmers who shift fragile cropland to less intensive uses.

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IMPUTED INTEREST RULES

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This means the interest is reported as a deduction by the buyer, and as income by the seller at the time it is paid (or deemed paid under the imputed interest rules), rather than when it is accrued. Consequently, the seller can postpone recognition of income by delaying interest payments — if the buyer is willing to delay the interest deduction.

The Simplification Act also revises the rules for setting the AFR. Temporary regulations issued by the Internal Revenue Service (IRS) in February 1985 set new applicable federal rates each month. These alternative rates could be used by the taxpayer if they were lower than the rates set for a six-month period by the 1984 Tax Reform Act.

The Simplification Act eliminates the six-month rates as an alternative. Therefore, taxpayers are now required to apply the rates set each month. However, taxpayers are allowed to use the lesser of the AFR for the month the transaction is entered into, or the AFR for the previous two months.

Prior to the Simplification Act, a taxpayer who sold land to a family member could charge as little as 6% interest on the first $500,000 of the sale per year and still not be subject to the imputed interest rules. If such a taxpayer charged *less* than 6%, a 7% rate was imputed. The Simplification Act continues the special treatment of these sales, but eliminates the difference betwee the testing and the imputed rate. Therefore, for sales of land to a family member after June 30, 1985 — if the contract rate is less than 6% (compounded semiannually) — a 6% rate (compounded semiannually) will be imputed.

The Simplification Act does not change an exemption for the sale of farms for less than $1 million from the rules of § 1274, which makes them subject to the rules of § 483. Since the required rate under § 483 is the same as § 1274, the only advantage of this exception is that the cash accounting rules apply — even if the requirements for cash accounting under § 1274A are not met.

— Philip E. Harris

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CONSERVATION ISSUES

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The Sodbusting Program

The House and Senate bills provide that any person who produces an agricultural commodity on highly erodible land during any crop year shall be ineligible, as to *any* commodity produced by such person during that crop year, for price support payments, Commodity Credit Corp. (CCC) farm storage facility loans, federal crop insurance, federal disaster payments, and certain Farmers Home Administration (FmHA) loans — if the Secretary of Agriculture determines that the proceeds will be used for a purpose that will contribute to excessive erosion of highly erodible lands, and leasing of storage space to CCC.

The Senate bill would ban federal farm program assistance to any farmer who continues to cultivate highly erodible land after 1988 without a government-approved conservation plan. Generally, the House provision requires that, by 1990, all highly erodible land must be farmed according to an approved conservation plan in order to qualify for U.S. Department of Agriculture (USDA) benefits.

The other significant difference between the Senate and House bills is that the House's sodbuster program would not include land capability class IIIe. As a result, the Senate bill would cover approximately 750 million acres of land, of which about 70 million acres have a high or medium potential of being converted to cropland. The House bill would reach about 650 million acres of land, of which approximately 30 million acres have a high or medium potential of being converted to cropland.

The Conservation Reserve Program

Over 50% of all soil erosion occurs on just 12% of the nation's cropland. The Conservation Reserve Program would pay an annual fee for a number of years to farmers who shift highly erodible cropland to less erosive — but still profitable — uses. In contrast to the sodbuster provisions, The Conservation Reserve Program is aimed at taking fragile land out of crop production.

There are striking differences between the House and Senate conservation reserve programs. In terms of acreage limits, the Senate bill establishes a conservation reserve program of 25 to 30 million acres.

It requires that not less than 10 millio acres be set aside in each of the 1986 and 1987 crop years, while stating that not less than five million acres, nor more than 10 million acres, be set aside during the 1988 and 1989 crop years. The House bill establishes a reserve of only 25 million acres, with no per-year minimum or maximum number of acres specified.

The bills also differ as to the length of contracts, with the Senate version stating seven to 15 years as the contract term, and the House bill generally stating a period of not less than 10 years.

Under the House and Senate provisions, the conservation reserve contract must require the Secretary of Agriculture to provide technical assistance, share the cost of carrying out certain conservation measures and practices when such cost sharing is in the public interest, pay an annual fee, and to retire any cropland base and allotment history that the owner or operator agrees to permanently retire.

The fee would be paid for a period of years, but not in excess of the duration of the contract. Under both bills, no producer is to annually receive more than $50,000 in contract payments, and all such payments must be in cash, in kind, or in some combination thereof.

"Erosion-prone cropland" is defined i both the House and Senate bills. "Eligible erosion-prone land," for the conservation reserve, is defined only under the Senate version. It is land that has been (or has been

FmHA delinquent borrower regulations promulgated

On Nov. 1, 1985, the Farmers Home Administration (FmHA) published a final rule on special supervision of delinquent and problem cases of FmHA farm borrowers. 50 Fed. Reg. 45740-45803 (1985) (to be codified in various parts of 7 C.F.R.). The Supplementary Information, *Id.* at 45740-45750, states that the FmHA intends that this final rule implements a procedure for deferring payments for farmer program borrowers to conform with 7 U.S.C. § 1981a and various court orders.

The rule establishes a method of informing farmer/borrowers of servicing alternatives, including deferral. *Id.* at 45740. The final rule was effective Nov. 1, 1985.

Beginning Dec. 31, 1985, it is provided that all borrowers (except those under the jurisdiction of a bankruptcy court) that are more than $100 behind schedule on their FmHA loan payments on this date will immediately be sent Form FmHA 1924-25 (Notice — Farmer Program Servicing Options Including Deferrals and Borrower Responsibilities), Form FmHA 1924-14 (Notice of Intent to Take Adverse Action), and Form FmHA 1924-26 (Borrower Acknowledgement of Notice of Intent to Take Adverse Action).

This mailing could be the beginning of a process leading to the involuntary liquidation of many FmHA farmer/borrowers.

The regulations contemplate that the farmer must respond, using Form 1924-26, within 30 days of receipt of the above packet of forms. The forms must indicate whether the farmer/borrower elects to apply for servicing, to go directly to administrative appeal, to cure the default, or to proceed to liquidation.

It is anticipated that many farmer/borrowers will elect to ask for servicing. Form 1924-25 sets out available servicing actions, including rescheduling, reamortization, consolidation, deferral, subordination, or limited resource loans, as well as the restructuring of the debt and business by selling a portion of the assets.

If the borrower elects to ask for one or more of these servicing actions, a conference with the county supervisor will be scheduled. The borrower must attend this conference, and will bear the burden of presenting a great deal of information that could form the basis for granting the requested servicing action(s).

The FmHA must send a letter to the borrower within seven days after the conference, either granting or denying the servicing request. If the request is denied, the reasons for the denial and all facts supporting these reasons must be set forth in writing.

For example, if the request for servicing is denied, the next step for the borrower will be to file an administrative appeal within the agency. FmHA administrative appeal procedures appear at 7 C.F.R. § 1900.51 et *seq.*, as amended at 50 Fed. Reg. 45755-45758 (1985).

If the farmer/borrower does not succeed with the administrative appeal, an administrative review will be requested to exhaust administrative remedies. If the result is still adverse to the farmer/borrower after the review, the regulations contemplate that the FmHA will have satisfied all statutory and due process requirements, and that a Notice of Acceleration can then be issued. The next step, of course, is foreclosure.

While there will be requests for the full array of servicing actions, it is anticipated that requests for deferral and for transfer to limited resource status will be particularly popular.

The Nov. 1, 1985 regulations set forth standards under which the FmHA will assess requests for deferral. 50 Fed. Reg. 45774-45777 (1985) (to be codified at 7 C.F.R. § 1951.44). The regulations state that the borrower must meet *all* of the following five conditions:

1) The reasons for needing deferral must be due to circumstances beyond the borrower's control. Several circumstances are listed, including loss of critical, non-farm employment, illness, injury, death, natural disasters, and certain unplanned expenses. In addition, the following is an acceptable reason:

> Economic factors that are widespread (and not limited to an individual case), such as high interest rates or low market prices for agricultural commodities — as compared to production costs — that reduce the repayment ability of the borrowers so that the scheduled payments cannot be made. *Id.* at 45775 (to be codified at 7 C.F.R. § 1951.44(b)(1)(D)).

2) The farmer/borrower must demonstrate that the need for deferral is "temporary," and that at the end of the deferral period, the borrower either will be able to pay in full, or will be able to resume regular payments — eventually leading to retirement of the debt.

3) The borrower must demonstrate that without deferral, there will be undue impairment of the borrower's standard of living.

4) The borrower must attend the conference with the county supervisor, and provide sufficient information (financial records, production records and cash flow projections) to allow a decision to be made on the deferral request.

5) The farmer/borrower must have attempted certain voluntary adjustments and/or rescheduling with non-FmHA creditors.

The deferral regulations indicate that the FmHA official must make a number of determinations about the borrower, including the borrower's good faith effort to meet agreements with the FmHA, the borrower's "honest" efforts to pay, and whether the borrower has the appropriately documented request for deferral.

In addition, it is the FmHA's responsibility to determine whether the borrower has made the payments of taxes, etc. on time prior to the "hardship," whether the borrower has the ability to make payments after the deferral, whether the borrower plans to continue personal operation of the farm, whether the borrower uses "recommended and recognized successful production and financial management practices,"

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considered to have been) devoted to the production of an agricultural commodity during at least two of the three crop years prior to Jan. 1, 1986, thus ensuring that land actually in use as cropland is put into The Conservation Reserve Program.

The Swampbusting Program

Wetlands provide wildlife habitat, nesting areas, groundwater recharge and flood control, yet nationwide, fewer than half of our original wetlands still exist. Four out of every five acres of wetlands lost are converted to agricultural uses.

The House and Senate bills provide that any person who produces an agricultural commodity on converted wetlands during any crop year shall be ineligible — as to *any* commodity produced by such person during that crop year — for price support payments, CCC farm storage facility loans, federal crop insurance, federal disaster payments, as well as certain FmHA loans if the Secretary of Agriculture determines that the proceeds will be used for a purpose that will contribute to the conversion of wetlands.

The proposed legislation would not apply to any person who, during a crop year, produces an agricultural commodity on wetlands that become available as a result of natural conditions (such as a drought), so long as the producer does not destroy natural wetland characteristics.

The same is true if the land becomes available as a result of the conversion of artificial wetlands that were created for such purposes as stock water, fish production, irrigation, subsurface irrigation, settling basins, cooling, rice growing, flood control, or irrigation systems. Finally, the Secretary of Agriculture may exempt actions by producers, which either cumulatively or individually, have a diminutive impact on hydrological and biological values.

— *Linda A. Malone*

FmHA DELINQUENT BORROWER
CONTINUED FROM PAGE 3

whether the borrower maintains and accounts for security, whether the borrower intends to dispose of non-essential assets, as well as if the borrower demonstrates a "realistic" farm plan of operation.

The last point contemplates:

> [C]ash flow or other financial projections acceptable to the FmHA that, during the deferral period, the borrowers can, at least, pay essential family living and/or farm operating expenses (for partnerships, corporations and cooperatives, living expenses are included), repay any loans made during the deferral period for operating and family living expenses, meet all installment payments owed to other creditors, and any FmHA loans not deferred. *Id.* at 45775 (to be codified at 7 C.F.R. § 1951.44(c)(8)).

If deferral is granted, the borrower will not be considered delinquent during the deferral period. During that period, payments of principal and interest on loans deferred will not be collected.

However, interest will continue to accrue, but interest will not be charged on deferred interest. Of course, the deferred obligations are not forgiven, and must eventually be repaid. Deferral, according to the regulations, can be granted for up to five years, but it is doubtful that we will see the granting of many deferrals of anywhere near that duration.

Presumably, farmer/borrowers who receive deferrals will have positive action on their requests for operating loans.

Some borrowers will discover that they will qualify for limited resource status, and that the lower interest rate charged to such borrowers will be an integral part of their survival plan.

As a general rule, the regulations prevent the FmHA from taking adverse action against a farmer/borrower until the entire procedure outlined above is carried out, servicing is denied, and denial is upheld on administrative appeal and review.

Adverse actions include pressing for involuntary liquidation, cutting off planned releases under the Farm and Home Plan, as well as such steps as acceleration, exercise of rights under Part 5 of Article 9 of the Uniform Commercial Code (UCC), and commencement of real estate foreclosures.

Caveat. The above summary does not begin to deal with all of the provisions in the regulations promulgated on Nov. 1, 1985. Also, at this writing, no information is available as to whether the various courts that have issued injunctions preventing the FmHA from taking adverse actions against farmer/borrowers will lift those injunctions as a result of the final rule.

However, if the injunctions are lifted quickly, the schedule set forth in the final rule will undoubtedly be observed by the FmHA, and many FmHA farmer/borrowers will begin 1986 by opening their mail boxes and withdrawing an envelope containing the three FmHA forms described hereinbefore.

Request to readers. If you have observations about the final rules, have information about court hearings involving FmHA requests to lift injunctions, or become aware of other developments in this critical area, please contact either: John H. Davidson Jr., University of South Dakota School of Law, (605/677-5361), or Donald B. Pedersen, University of Arkansas School of Law, (501/575-6109). We want to report further developments promptly in upcoming issues of *Agricultural Law Update.*

— *Donald B. Pedersen*

Next year's crop is not enough

Under Section 363 of the Bankruptcy Code, a farmer who has filed a Chapter 11 bankruptcy petition may use the proceeds of prepetition milk or crops to finance the continued operation of his farming business — only if the secured creditor consents to such use, or is provided adequate protection.

In *In Re Martin*, 761 F.2d 472 (8th Cir. 1985), a farmer sought to use the cash proceeds from the sale of commodities secured to the Commodity Credit Corp. (CCC). As adequate protection, the farmer offered a replacement lien on crops contemplated to be grown in 1984, plus an assignment of federal crop insurance proceeds.

The Bankruptcy Court allowed the debtor to sell the grain and use the "cash collateral." The District Court reversed the Bankruptcy Court's ruling, and held that the debtor's offer of a first lien on the 1984 crop (plus an assignment of federal crop insurance proceeds) was not adequate protection of the CCC's security interest within the meaning of § 363.

The Eighth Circuit Court of Appeals held that the Bankruptcy Court had applied an incorrect legal standard in making its "adequate protection" determination, and did not properly consider relevant factors affecting the CCC's security interest.

The Eighth Circuit Court of Appeals held that, in any given case, the Bankruptcy Court must necessarily: 1) Establish the value of the secured creditor's interest; 2) Identify the risk to the secured creditor's value resulting from the debtor's request for use of cash collateral; and 3) Determine whether the debtor's adequate protection proposal protects the value (as nearly as possible) against risks to that value. The Court, by virtue of its opinion, clearly adopts a very narrow view of the concept of adequate protection.

— *Phillip L. Kunkel*

Federal Deposit Insurance Corp.

The Family Farm Organizing Resource Center has compiled a manual of Federal Deposit Insurance Corp. (FDIC) procedures for liquidating the assets of failed banks. The manual contains selected portions of the FDIC field manuals, as well as internal agency memorandums. It can be obtained by contacting: The Family Farm Organizing Resource Center, 2395 University Ave., St. Paul, MN 55114; 612/645-1231.

— *Annette Higby*

Debt is incurred when goods are shipped under forward contract

In *In re Gold Coast Seed Co.*, 751 F.2d 1118 (9th Cir. 1985), a trustee in bankruptcy sought to avoid the debtor's payment under a forward contract to purchase seed from a third party seed supplier. Under the Bankruptcy Code, preferential transfers by a debtor within 90 days before filing of the petition in bankruptcy may be avoided by the trustee. Transfers made in payment of a debt incurred in the ordinary course of business, however, are not subject to avoidance if the payment was made within 45 days after creation of the debt. 11 U.S.C. § 547.

Here, payment was made within 45 days of shipment of the seed, but more than 45 days from the date of the contract. The trustee contended that the debt was incurred on the date the contract was made. The Court of Appeals, relying on U.C.C. §§ 2-503, 2-504 and 2-507, held that in absence of a contrary agreement, the buyer's debt incurred when the goods are shipped — not when the contract is signed. As a result, the trustee's attempt to avoid the payment was denied.

— *Kenneth J. Fransen*

Farmer allowed meals and lodging exclusion

In *J. Grant Farms Inc. v. Commissioner*, T.C. Memo 1985-174, the taxpayer had an employment contract with his farm corporation that required him to manage and operate the corporation's farm properties and which provided living accommodations to the taxpayer and his family. Because the corporation's swine and grain-drying operations needed around-the-clock monitoring, the court allowed the taxpayer to exclude the value of the living accommodations from his income under Internal Revenue Code § 119. The court further held that the corporation was allowed to deduct the expenses related to providing the living accommodations. The court reached a similar result in *Denny L. Johnson v. Commissioner*, T.C. Memo 1985-175.

— *Philip E. Harris*

PCA must litigate damage claims

In *Yankton Production Credit Association (PCA) v. Larsen*, 219 Neb. 610, 365 N.W.2d 430 (1985), the PCA filed a replevin action against a farmer in an effort to realize on collateral. The farmer stipulated that judgment be entered for the PCA, but the farmer reserved the right to file a counterclaim. The counterclaim sounded in breach of contract. It was alleged that the PCA breached a duty of good faith to advance the balance of three separate loans and that the PCA expressly and impliedly represented it that it would provide a continuing line of credit to finance the expansion of the farmer's operation, livestock inventory and operating expenses.

The lower court granted the PCA's motion for summary judgment, but the Nebraska Supreme Court reversed and remanded for further proceedings. The Nebraska Supreme Court saw a factual issue as to whether the PCA had made a promise to the farmer to finance the expansion, and whether the farmer relied on such promise to his detriment.

The farmer alleged promissory estoppel and represented that he did rely, and as a result of the failure of the PCA to continue to advance funds, could not expand sufficiently to fully utilize his operation and generate the necessary profits to pay the debt.

The Nebraska Supreme Court also saw a factual issue as to whether the PCA acted in good faith when it refused further advances. If the PCA did not base its decision on a good faith business judgment, the court indicated that the PCA would be liable to the farmer for money damages.

— *Donald B. Pedersen*

Recovery of litigation costs

A cooperative plaintiff has been successful with its motion for reasonable litigation costs against the government in connection with a civil proceeding concerning an income tax deduction. *Columbus Fruit and Vegetable Cooperative v. United States*, No. 599-83T (U.S. Cl.Ct. July 9, 1985).

The Internal Revenue Service (IRS) had issued a statutory notice of deficiency against the cooperative, contending that the plaintiff did not operate on a cooperative basis within the meaning of section 1381(a)(2) of the Internal Revenue Code (IRC), and thus, was not entitled to a deduction under section 1382(b)(1) for patronage dividends paid to members. The plaintiff paid the deficiency, filed a claim for refund for the taxable years in issue, and was successful in *Columbus Fruit and Vegetable Cooperative v. United States*, 7 Ct. Cl. 561, 85-1 U.S. Tax Cas. (CCH) ¶ 9314.

Plaintiff then sought an award of reasonable litigation costs pursuant to section 7430, IRC. The court excused the cooperative from the statutory requirement that the prevailing party exhaust administrative remedies because the IRS had failed to send a preliminary notice of proposed disallowance prior to the issuance of a statutory notice of disallowance.

The government's position in disallowing the deduction was found to be unreasonable because it was predicated upon authority unsuccessfully asserted by the government in the Eighth Circuit in *Conway County Farmers Association v. United States*, 588 F.2d 592 (8th Cir. 1978).

— *Terence J. Centner*

Purchase money security interest terminated by rewriting of loan

Under 11 U.S.C. Sec. 522(f)(2), certain types of non-possessory, non-purchase money security interests may be avoided by a debtor — to the extent that such security interests impair an exemption to which the debtor is otherwise entitled under the Bankruptcy Code.

In the case of a farming operation, it sometimes may be difficult to ascertain whether the security interest claimed by a creditor is subject to this "lien avoidance" provision since the creditor very well may have advanced funds to the debtor to allow the debtor to acquire assets, but the outstanding balance later may have been "rolled over" into a larger promissory note.

In *In Re Slechta*, Bkry. No. 3-84-1456 (Bkry., Minn., June 26, 1985), a production credit association (PCA) argued that it had advanced purchase money to the debtors to enable them to acquire certain farm machinery (later claimed exempt by the debtors in their Chapter 7 bankruptcy).

In so arguing, the PCA pointed out that it began to finance the debtors in 1974, and had maintained a consistent lending relationship with them since that time. In 1980, however, a new basic loan agreement was executed by the debtors and the PCA. This new loan agreement provided that it amended and replaced any and all earlier loan agreements outstanding between the parties. At the same time, the debtors executed a new security agreement and financing statement.

Upon learning of the debtors' bankruptcy filing, the PCA filed its claim with the bankruptcy court based upon the 1980 basic loan agreement.

The court held that the execution by the parties of the basic loan agreement and security agreement in April 1980 constituted a novation of earlier notes and security interests in favor of the PCA.

It further held that this novation resulted in a new non-purchase money security interest in the debtors' farm machinery and equipment. Accordingly, the lien of the PCA in the debtors' farm machinery could be avoided by the debtors.

— *Phillip L. Kunkel*

§ 2032A Qualified use but hunting is not farming

In Ltr. Rul. 8516012, the Internal Revenue Service states that a ranch leased for 30% of the gross income from livestock operations and 50% of the gross income from hunting activities meets the qualified use requirements of Internal Revenue Code (IRC) § 2032A(b). However, hunting activities do not qualify the land as being used for farming purposes. Therefore, the land must be valued under IRC § 2032A(e)(8) rather than IRC § 2032A(e)(7).

— *Philip E. Harris*

Foreign investment in U.S. agricultural land

by J. Peter DeBraal

Data Findings

The U.S. Department of Agriculture (USDA) reported that foreign persons owned 14 million acres of U.S. agricultural land as of Oct. 8, 1984, DeBraal, J.P., & Majchrowicz, T.A., "Foreign Ownership of U.S. Agricultural Land Through Dec. 31, 1984," Econ. Res. Serv. Staff Report No. AGES850320, 1985.

This 14-million-acre figure is slightly more than 1% of the 1.29 billion acres of privately owned U.S. agricultural land, and approximately 0.6% of the total 2.27 billion acres comprising the United States.

Information received at the time of reporting shows that forest land accounts for 57% of all foreign-owned acreage, cropland accounts for 14%, pasture and other agricultural land for 24%, while non-agricultural and unreported uses account for 5%.

Corporations own 83% of the acreage; partnerships own 9%; and individuals own 7%. The remaining 1% is held by estates, trusts, associations, institutions and others.

U.S. corporations (in which 5% or more of the ownership is foreign) reported owning 62% of all the foreign-held acreage. The remaining 38% was reported as being held or acquired by foreign persons not affiliated with a U.S. corporation.

The largest number of acres owned by foreign persons was reported in Maine. Foreign holdings in Maine account for 21% of the total reported holdings and 15.5% of the total privately owned agricultural land in Maine. Four large timber companies own 95% of the foreign-held acres in Maine. One company has one parcel, another company has only partial interest in 32% of the acreage, while the other two companies are U.S. companies which are partially foreign owned.

Except for Maine, foreign holdings are concentrated in the South and West — 36% of the holdings are in the South and 27% in the West. Rhode Island is the only state with no reported foreign-owned agricultural land (see Table 1).

Foreign persons from Canada, the United Kingdom, Hong Kong, West Germany and the Netherlands Antilles account for 73% of the foreign-held acreage (see Table 2).

Foreigners do not appear to be taking their agricultural land out of production. No change in intended use at the time of filing was reported for 92% of the acreage. No change in tenure was reported for 41% of the acres, while some change was reported for 31% of the acres. No responses regarding tenure change were received for the remaining 28% of the acres.

The foregoing findings are based on an analysis of reports submitted to the USDA under the Agricultural Foreign Investment Disclosure Act of 1978 (AFIDA), 7 U.S.C. §§ 3501-3508 (1982), and the regulations thereunder, 7 C.F.R. §§ 781.1-.5 (1984), which were effective through Oct. 8, 1984. New regulations became effective Oct. 9, 1984, 29 Fed. Reg. 35,072 (1984).

The new regulations incorporate most of the old regulations, but make some changes, including requiring that foreign investors making transactions in U.S. agricultural land after Oct. 8, 1984 provide some additional information.

Summary of the Reporting Requirements and Definitions

AFIDA, as implemented by the regulations, requires all foreign persons holding agricultural land as of Feb. 1, 1979 to file a report of such holdings with the Secretary of Agriculture by Aug. 1, 1979. All foreign persons who acquire or dispose of agricultural land on or after Feb. 2, 1979 are required to report such transactions within 90 days of the transaction.

In addition, any foreign person who holds land which subsequently becomes agricultural land, or any person who holds agricultural land who subsequently becomes a foreign person, must also file a report within 90 days of such change. 7 U.S.C. § 3501(a)-(b) (1982); 7 C.F.R. § 781.3 (b)-(e) (1984).

AFIDA specifies (in detail) the information to be supplied by the foreign person, and provides that necessary additional information may be obtained by the Secretary. The information required to be reported consists of the legal name and address of the foreign person; citizenship, if an individual; if not an individual or a government, the nature of the legal entity, including the entity's country of creation and principal place of business; types of interest; legal description; acreage; purchase price, or any other consideration given; and the land's intended use.

In the case of a disposition, the party disposing of the interest is also required to give the legal name and address of the purchaser; citizenship, if the purchaser is an individual; and if the purchaser is not an individual or government, the nature of the entity, country of creation and principal place of business. 7 U.S.C. § 3501(a)-(b) (1982); 7 C.F.R. § 781.3(b)-(c) (1984).

Failure to comply with AFIDA subjects the foreign owner to a possible civil penalty of up to 25% of the fair market value of the interest held in the land in question. 7 U.S.C. § 3502 (1982); 7 C.F.R. § 781.4 (1984).

"Agricultural land" is defined in AFIDA as all land used for agricultural, forestry, or timber production purposes. 7 U.S.C. § 3508(1) (1982). The regulations further refine this definition by including idle land, if its last use within the past five years was for agricultural, forestry, or timber production purposes. 7 C.F.R. § 781.2(b) (1984). The old regulations exempted all land that was held in parcels of not more than one acre (in the aggregate) from which agricultural, forestry, or timber products were less than $1,000 in annual gross sales, and if such products were for the use of the person holding an interest in the land. *Id.*

AFIDA requires reporting "any interes in land other than a security interest (a mortgage or other debt-securing instrument). 7 U.S.C. § 3501(a) (1982). The regulations exempt leaseholds of less than 10 years duration, contingent future interests, and those non-contingent future interests that do not become possessory upon termination of the present estate. Non-agricultural easements, rights-of-way, and interests solely in mineral rights are also exempt. 7 C.F.R. § 781.2(c) (1984).

A "foreign person" includes any individual who:

1) Is not a U.S. citizen or national;

2) Is not a citizen of the Northern Mariana Islands or the Trust Territories of the Pacific Islands; or

3) Is not lawfully admitted into the United States for permanent residence.

Any person who holds an Immigration and Naturalization Service Form I-151, I-155 or I-551 (green card) is considered lawfully admitted for permanent residence, and is exempt from the requirements of the act. Foreign governments, entities which are created under the laws of, or have their principal place of business in a foreign country, or U.S. entities in which there is a significant foreign interest or substantial control, are also defined as foreign persor 7 U.S.C. § 3508(2)-(3) (1982); 7 C.F.R. 781.2 (g) (1984).

The act is designed to impute foreign person status to certain U.S. entities holding direct and indirect interest in U.S. agricul-

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tural land. This entity need not actually be foreign, but under the act, it is deemed a foreign person because another foreign person holds a significant interest or substantial control in it. 7 U.S.C. § 3508(3) (1982).

The old regulations defined "significant interest or substantial control" to mean a 5% or more interest in the U.S. entity. 7 C.F.R. § 781.2(d) (1984). In some instances, the second and third tiers also may not actually be foreign, but may be deemed foreign under the act for the same reason.

Under the old regulations, the reporting entity (other than an individual or government), whether U.S. or foreign, was required to provide information (names, addresses, citizenship, and the nature of the entity) on each foreign person holding a 5% or greater interest in the entity. Similar information could also have been requested of second-tier entities in which foreign persons each held a 5% or greater interest in that entity. 7 C.F.R. § 781.3(f)-(g) (1984).

This 5% standard differed from the standard for determining whether or not an entity was required to file at all. In the latter instance, if several foreign persons cumulatively owned 5% or more of the entity, and if no single foreign person owned a 5% interest, the entity was defined as a foreign person, and was required to file a report. However, such an entity was not required to list the names, addresses and other related information about the foreign persons each holding less than 5% of the entity.

New Regulations

The new AFIDA regulations raise the threshold reporting level for U.S. entities in which there are foreign interest holders by changing the definition of "significant interest or substantial control" in a U.S. entity from 5% to 10%, if held by a single foreign person (or a group of foreign persons acting in concert), and to 50%, if held by a group of foreign persons (not acting in concert), none of whom individually holds a 10% or greater interest in the U.S. landholding entity. 7 C.F.R. § 781.2(g),(k) (1985).

This new definition of "significant interest or substantial control" also applies to the reporting requirements for second- and third-tier interests. Thus, the reporting entity (other than an individual or government), whether U.S. or foreign, is required to provide information, as under the old regulations, on each foreign person holding a significant interest or substantial control in the reporting entity. *Id.* § 781.3(f).

Similar information may also be required about the owners of second-tier entities in which foreign persons each have a significant interest or substantial control. *Id.* § 781.3(g).

The new regulations also:

1) Increased the minimum reportable acreage from one acre to more than 10 acres in the aggregate, but retained the $1,000 gross receipts limitation, *Id.* § 781.2(b);

2) Require reports on changes in status from agricultural to non-agricultural and from foreign to non-foreign, as well as changes of name and address, *Id.* § 781.3(i)-(k);

3) Require additional information about the representative of the foreign investor (where applicable), how the interest in the land was transferred, the relationship of the foreign owner to the operator, type of rental agreement, if any, and the date the interest in the land was transferred, *Id.* § 781.3(a)(g)-(11); and

4) Refined the definition of agricultural land, which now means land used for "farming, ranching, forestry, or timber production. . .", *Id.* § 781.2(b).

The USDA is realigning the existing data base to reflect the change made by the new regulations, and purging the files of reports under the old regulations which are no longer required under the new regulations. Because this process has not yet been completed, it is not currently possible to determine the extent to which these changes have altered the data base.

(continued on next page)

Table 1
U.S. Agricultural Landholdings of Foreign Owners by State, Oct. 8, 1984

State	Foreign-owned agricultural land	State	Foreign-owned agricultural land
Alabama	598,375	Nebraska	78,463
Alaska	753	Nevada	51,386
Arizona	289,376	New Hampshire	111,732
Arkansas	131,968	New Jersey	26,419
California	906,106	New Mexico	465,154
Colorado	504,372	New York	381,264
Connecticut	1,057	North Carolina	277,225
Delaware	8,310	North Dakota	20,004
Florida	610,615	Ohio	50,206
Georgia	1,117,949	Oklahoma	28,224
Guam	336	Oregon	418,131
Hawaii	59,812	Pennsylvania	176,656
Idaho	165,804	Puerto Rico	1,398
Illinois	156,387	Rhode Island	0
Indiana	94,501	South Carolina	524,800
Iowa	32,438	South Dakota	42,014
Kansas	68,386	Tennessee	358,846
Kentucky	44,664	Texas	971,800
Louisiana	148,856	Utah	72,144
Maine	2,926,559	Vermont	100,816
Maryland	47,313	Virginia	133,816
Massachusetts	442	Washington	403,029
Michigan	196,578	West Virginia	61,145
Minnesota	240,424	Wisconsin	19,110
Mississippi	347,783	Wyoming	128,866
Missouri	62,833		
Montana	373,091	**Total**	**14,037,736**

FOREIGN INVESTMENT

CONTINUED FROM PAGE 6

Table 2
U.S. Agricultural Landholdings by Country of Foreign Owner, Oct. 8, 1984

(Interests excluding U.S. corporations with foreign shareholders)

Country	Acres
Andorra	3,742
Argentina	14,913
Australia	3,117
Austria	36,678
Bahamas	31,322
Belgium	66,467
Belize	1,405
Bermuda	17,923
Bolivia	11
Brazil	3,156
British Virgin Islands	37,518
Canada	1,731,293
Cayman Islands	14,420
Chile	521
China	1,217
Colombia	16,069
Costa Rica	16,844
Cuba	20
Czechoslovakia	485
Denmark	19,859
Dominican Republic	2,147
Ecuador	1,040
Egypt	519
El Salvador	194
France	75,041
Germany (West)	726,865
Greece	56,349
Guatemala	486
Guyana	35
Honduras	892
Hong Kong	16,789
Hungary	110
India	983
Indonesia	673
Iran	3,880
Iraq	550
Ireland	9,624
Israel	3,962
Italy	11,251
Ivory Coast	119
Jamaica	313
Japan	113,090
Jordan	1,549
Kenya	32
Korea (South)	402
Kuwait	1,578
Lebanon	13,674
Liberia	33,560
Libyan Arab Republic	302
Liechtenstein	108,309
Luxembourg	5,949
Malaysia	139
Mexico	215,129
Morocco	675
Namibia	146
Netherlands	147,225
Netherlands Antilles	544,179
New Zealand	367
Nicaragua	1,348
Nigeria	14
Norway	7,143
Oman	449
Pakistan	2,171
Panama	181,551
Peru	487
Philippines	2,733
Poland	147
Portugal	801
St. Vincent	2,637
Saudi Arabia	16,925
Singapore	1,909
South Africa	249
Spain	2,542
Sweden	7,568
Switzerland	260,584
Syria	4,004
Taiwan	2,811
Tanzania	20,421
Thailand	131
Trinidad & Tobago	1,667
Turkey	558
Turks Islands	1,580
United Arab Emirates	2,801
United Kingdom	391,114
Uruguay	12,459
U.S.S.R.	835
Venezuela	26,505
Vietnam	152
Yugoslavia	161
Multiple [fn. 1]	21,562
Multiple less than 5%	510
Third tier [fn. 2]	185,800
Subtotal [fn. 3]	**5,277,436**

(Interests of U.S. corporations with foreign shareholders)

Country	Acres
US/Argentina	3,560
US/Australia	1,119
US/Austria	14,967
US/Bahamas	37,473
US/Belgium	63,523
US/Bermuda	34,972
US/Brazil	3,102
US/British Virgin Islands	12,029
US/Canada	2,863,435
US/Cayman Islands	26,225
US/China	870
US/Colombia	2,390
US/Denmark	1,844
US/Ecuador	1,559
US/Egypt	160
US/El Salvador	12
US/Finland	3,047
US/France	328,289
US/Germany (West)	482,989
US/Greece	6,769
US/Guatemala	412
US/Guyana	334
US/Hong Kong	1,691,629
US/Iran	4,308
US/Iraq	960
US/Ireland	188
US/Italy	78,021
US/Japan	28,289
US/Korea (South)	75
US/Kuwait	766
US/Lebanon	703
US/Liberia	31,327
US/Libyan Arab Republic	28[illegible]
US/Liechtenstein	62,93[illegible]
US/Luxembourg	119,078
US/Malaysia	300
US/Mexico	39,890
US/Netherlands	337,279
US/Netherlands Antilles	244,612
US/New Hebrides	2,991
US/Nicaragua	282
US/Norway	352
US/Panama	58,290
US/Philippines	1,224
US/Saudi Arabia	12,567
US/South Africa	3,309
US/Spain	5,953
US/Sweden	3,322
US/Switzerland	203,478
US/Taiwan	4,077
US/Thailand	252
US/Trinidad & Tobago	30
US/Turkey	443
US/United Kingdom	1,539,126
US/Uruguay	581
US/Venezuela	47,470
US/Multiple	175,434
US/Multiple less than 5%	601
US/Third tier	170,797
Subtotal [fn. 4]	**8,760,300**
Total of all landholdings	**14,037,736**

[1] A report is processed as "multiple" when no single country predominates — for example, an equal partnership between a Canadian and a West German.

[2] A report is processed as "third tier" if three or more levels of ownership are reported with no foreign interests indicated.

[3] Total interests (excluding U.S. corporations with foreign shareholders).

[4] Total interest of U.S. corporations with foreign shareholders.

STATE ROUNDUP

MONTANA. *Irrigation Ditch Drowning.* The construction and maintenance of an irrigation ditch is not an abnormally dangerous activity that subjects the owner of the ditch to strict liability. However, Montana's recreational use statute did not preclude the doctrine of attractive nuisance in a case in which a 5-year-old child drowned in the irrigation ditch.

Additionally, under a liability theory based on willful and wanton negligence, a record that supports an inference that a water user association acted with indifference toward the danger of children drowning is sufficient to preclude the granting of summary judgment in favor of the association. *Harmon v. Billings Bench Water Users Association*, 765 F.2d 1464 (9th Cir. 1985).

— *Donald D. MacIntyre*

PENNSYLVANIA. *Zoning — Non-Conforming Use by Equitable Estoppel.* Where a prospective buyer of an eight-acre tract in an area zoned for residential use was given approval by the municipal planning commission to raise farm animals and grow crops on the tract, the buyer was entitled to continue his farm use based on the non-conforming use by equitable estoppel. The tract had previously been used in agriculture, but evidence showed that such use stopped *before* the land was re-zoned, and agriculture would not be a non-conforming use under the terms of the ordinance. *Caporali v. Ward*, 493 A.2d 791 (Pa. Commonwealth Ct. 1985).

— *John C. Becker*

SOUTH CAROLINA. *Entrustment of Crop to Co-tenant.* The Fourth Circuit Court of Appeals upheld the District Court of South Carolina in ruling that a purchaser of fruit from orchards owned by co-tenants was not liable to one co-tenant when the other co-tenant failed to divide payments received. *Robinson v. Gerber Products Co.*, 734 F.2d 774 (4th Cir. 1975).

Plaintiff had established a 10-year course of dealing, whereby she had entrusted control over her portion of the crop to her co-owner husband's corporation, and had acquiesced in the sale of her portion to defendant Gerber. The court cited the entrustment provision of South Carolina's commercial code (S.C. Code 1976, Section 36-2-403), which states, "Any entrusting of possession of goods to a merchant who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in the ordinary course of business."

Additionally, the court held that defendant Gerber was not under a duty to be informed of plaintiff's domestic difficulties, and was, therefore, a buyer in the ordinary course of business.

— *Charles H. Cook*

SOUTH DAKOTA. *Drainage of Sloughs.* Suit by landowner for abatement of nuisance resulting from drainage of sloughs onto his land not barred by res judicata upon showing of excessive damage due to flooding. In a former suit between the same parties, no evidence was offered to show that water would collect on plaintiffs' land and trial court had held water would drain from plaintiffs' land, following the natural watercourse. *Lee v. Schultz*, No. 14564 (S.Ct. S.D. Sept. 1985).

— *Annette Higby*

SOUTH DAKOTA. *Feedlot Runoff Causes Contamination.* The Supreme Court of South Dakota upheld trial court determination that a feedlot owner, a lessee/operator and a creditor holding sheriff's certificate to property during redemption period, were jointly and severally liable for damages resulting from the discharge of irrigation pond water onto property owned by plaintiffs.

The water which was discharged was contaminated with feedlot waste, sediment and debris. Plaintiffs were awarded damages for injury to land and contamination of their domestic well. A permanent injunction was denied because there was no evidence offered to show impending danger of further flooding. *Gross v. Conn. Mut. Life Ins. Co.*, 361 N.W.2d 259 (S.D. 1985).

— *Annette Higby*

TEXAS. *Overweight Vehicles.* Under a state law banning overweight vehicles, an exception exists for the loading of an agricultural or a forestry commodity prior to the first processing of the commodity. Tex. Stat. Ann. Art. 6701d-11(b)(6) (Vernon Supp. 1985).

However, the exception does not apply to the owner or operator of a woodyard who overloads a vehicle transporting logs for milling, since the timber has already undergone processing in the woodyard. "By the time logs and pulpwood leave a woodyard, they are products that have been prepared for market, or converted into marketable form by trimming of branches, by sorting, by reloading, or by cutting into appropriate lengths, and may already have entered into channels of commerce." Op. Tex. Atty. Gen. No. JM354 (Oct. 1985).

— *Marvin Martin*

WASHINGTON. *Agricultural Producers Lien.* In April 1985, the Washington Legislature gave agricultural producers a first priority statutory lien from the date the agricultural products are delivered to a processor until 21 days after payment for the product is due. This lien attaches to the processor's inventory and accounts receivable, as well as to the agricultural products delivered.

Further, if the lien is filed in writing within 20 days of being unpaid, it continues its priority. The processor lien terminates six months after the date of attachment or filing — unless a suit to foreclose the lien has been filed. The prevailing party in the foreclosure suit is allowed reasonable attorney fees. Ch. 412 of Washington Laws, 1985, to be codified in Title 60, Revised Code of Washington.

— *Linda Grim McCormick*

Cooperative taxation — Section 521 quantitative requirement not required by Section 1381(a)(2)

The Court of Claims has ruled that an organization operating on a cooperative basis in which members accounted for approximately 24% of the association's total sales for the tax year in question qualified for a deduction of patronage dividends under Section 1382(b)(1) of the Internal Revenue Code (IRC). *Columbus Fruit and Vegetable Co-op. v. United States*, 7 Ct. Cl. 561 (1985). In agreeing that the cooperative qualified for the income tax deduction, the court carefully drew a distinction between Section 521 cooperatives and other associations organized on a cooperative basis which may qualify under Part I, subchapter T, IRC (Sections 1381-1383). Any corporation operating on a cooperative basis may qualify under Section 1381(a)(2) for a tax deduction of patronage dividends without meeting the Section 521(b)(4) requirement that the cooperative conduct more than 50% of its business with members. Thus, the court followed *Conway County Farmers Association v. United States*, 588 F.2d 592 (8th Cir. 1978), and declined to read into Section 1381(a)(2) a quantitative requirement.

— *Terence J. Centner*

Address Correction Requested

5520-G Touhy Avenue
Skokie, IL 60077

AMERICAN AGRICULTURAL LAW ASSOCIATION NEWS

CALL FOR PAPERS: EURO-AMERICAN AGRICULTURAL LAW SYMPOSIUM. The American Agricultural Law Association (AALA) and the Comite European de Droit Rural (European Agricultural Law Committee) are co-sponsoring a symposium to be held in Plymouth, England, Sept. 8-12, 1986. Selected participants from North America and Europe will present papers on "Agriculture and Forestry as Creators and as Victims of Pollution" and "Legal Implications: Limiting Agricultural Production." Persons interested in presenting a paper on either topic should contact the appropriate coordinator **prior to Dec. 15, 1985**, to express such interest and to seek further instructions for submitting a formal proposal.

Contact either: Donald L. Uchtmann, 151 Bevier Hall, 905 S. Goodwin, Urbana, IL 61801 (Environmental topic); or Neil E. Harl, 478 Heady Hall, Iowa State University, Ames, IA 50011 (Limiting agricultural production topic).

The conference will be the first of its kind, and promises to be an exciting new development for agricultural law. Participants, including those presenting papers, will be expected to arrange for their own financial support. Selection of speakers will occur in early 1986, so don't delay if you have an interest in presenting a paper.

CALL FOR PAPERS: NATIONAL SYMPOSIUM ON WATER RESOURCES LAW. The American Agricultural Law Association (AALA) is cooperating with the American Society of Agricultural Engineers in calling for proposals for papers to be presented at the National Symposium on Water Resources Law, Dec. 15-16, 1986, Hyatt Regency Chicago, Illinois Center, Chicago.

The focus is on litigation and other ajudicatory proceedings that may serve as benchmarks for the future. Proposals must be received no later than Dec. 1, 1985. A proposal form and additional information can be obtained from Swayne F. Scott, program chairman, Soil Conservation Service, P.O. Box 2890, Washington, D.C. 20013; 202/447-8723.

STATE REPORTERS: *Agricultural Law Update* is pleased to announce the appointment of additional state reporters: COLORADO: Bruce McMillen; HAWAII: Kemp P. Burpeau; MONTANA: Donald D. MacIntyre; NEW MEXICO: John D. Copeland; NEW YORK: Joseph B. Bugliari, Dale Arrison Grossman; WYOMING: Ann Stevens.

MEMBERSHIP DIRECTORY. All members who need to update their listing for the 1986 issue of the Membership Directory should immediately send the necessary information to Terence J. Centner, AALA Secretary-Treasurer, University of Georgia, College of Agriculture, 301 Conner Hall, Athens, GA 30602.