INSIDE

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IN FUTURE ISSUES

Congress extends Chapter 12 bankruptcy

On December 19, 2002, President Bush signed into law H.R. 5472, a bill extending Chapter 12 Bankruptcy for six months, from January 1, 2003 to July 1, 2003. Pub. L. 107-377, 116 Stat. 3115 (2002). Without this extension, Chapter 12 would have expired on December 31, 2002. Chapter 12 thus continues as a temporary chapter of the Bankruptcy Code. This temporary status, combined with the short term extensions and frequent lapses in authorization, have made bankruptcy planning difficult for farmers and their attorneys.

Chapter 12, *Adjustment of Debts of a Family Farmer with Regular Annual Income*, was first enacted in October 1986 with a sunset provision for repeal on October 1, 1993. *Bankruptcy Judges, United States Trustees and Family Farmer Bankruptcy Act of 1986*, Pub. L. No. 99-554, tit. II, § 255, 100 Stat. 3088, 3105-3113 (1986) (codified at 11 U.S.C. §§ 1201 - 1231). Shortly before it sunset, Chapter 12 was extended for another five years, to October 1, 1998. *Farm Bankruptcies, Extension*, Pub. L. No. 103-65, 107 Stat. 311 (1993).

During this extension, Congress began its debate of overall bankruptcy reform. The National Bankruptcy Review Commission was formed to study bankruptcy law and to suggest necessary reform. *Bankruptcy Reform Act of 1994*, Pub. L. No. 103-394, 108 Stat. 4106 (1994). Its final report issued in 1997 included the recommendation that Chapter 12 be made permanent. National Bankruptcy Review Commission Final Report, http://govinfo.library.unt.edu/nbrc/default.html. The Chapter 12 recommendation did not generate controversy, although other aspects of bankruptcy reform did. The National Bankruptcy Review Commission Report was not adopted by Congress, and Chapter 12 officially sunset at the end of its extension, on October 1, 1998.

Chapter 12 was resurrected with a six month retroactive extension as part of an omnibus appropriations bill passed later in October 1998. *Omnibus Consolidated and Emergency Supplemental Appropriations Act*, Pub. L. 105-277, div. C, tit. 1, § 149, 112 Stat. 2681, 2681-610-11 (1999). On March 30, 1999, one day before sunset, another short term extension was enacted. *Bankruptcy: Extension of Reenactment of Chapter 12, Family Farmers Indebtedness*, Pub. L. No. 106-5, 113 Stat. 9 (1999). This extension provided a six month extension to October 1, 1999. Meanwhile, comprehensive bankruptcy reform legislation containing Chapter 12 permanency provisions continued to be debated.

Chapter 12 sunset on October 1, 1999, but was resurrected shortly thereafter for another nine months. *Bankruptcy - Extension of Family Farmer Debt Adjustment*, Pub.L. 106-70, S 1, 113 Stat. 1031 (1999). However, Congress did not take action to stop the July

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Debt excepted from bankruptcy for farmer making false financial statements

The United States Bankruptcy Court for the District of Kansas has held that $8,409.65 of a farmer's debt was excepted from discharge in bankruptcy under Bankruptcy Code § 523(a)(2) because the farmer made false financial statements with respect to a debt owed to the farmer's bank. *In re Diel*, 277 B.R. 778, 780 (Bankr. D. Kan. 2002). The court also determined that the farmer's sale of hay for $4,797.12 would have constituted "willful and malicious injury" to the bank in violation of Bankruptcy Code § 523(a)(6) if the land on which the hay was grown had been sufficiently described in the bank's security agreement pursuant to Kan. Stat. Ann. § 84-9-203(1)(a). *See id.* The court also ruled that it would not except from discharge the proceeds of the farmer's sale of other crops under § 523(a)(2) or (a)(6) because the bank failed to demonstrate that the farmer had damaged the bank's property interests. *See id.* Finally, the court ruled that the sale of an anhydrous applicator was not in violation of § 523(a)(2) or (a)(6) because the bank did not prove that the farmer profited from the sale or was personally involved in the sale. *See id.*

In 1992, Lanny Diel ("Diel") started a farming operation independent of his father, Virgil Eugene Diel, that was comprised entirely of land that he leased from his father and several other individuals. *See id.* In addition to running his farm operation, Diel "also

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1, 2000 sunset. Chapter 12 was repealed as of that date and was not resurrected for almost a year.

On May 11, 2001, Congress revived Chapter 12 with an eleven month extension. *Bankruptcy, Chapter 12- Reenactment*, Pub.L. 107-8, S 1, 115 Stat. 10 (2001). However, because the effective date applied retroactively back to the previous sunset, the bill only extended Chapter 12 from May 11 to June 1, 2001.

Chapter 12 again sunset as of June 1, 2001. On June 26, 2001, it was reenacted for six months until October 1, 2001. *Bankruptcy, Chapter 12- Reenactment*, Pub.L. 107-17, 115 Stat. 151 (2001). It again sunset as of October, 2001, and it was not reenacted until May, 2002. *Bankruptcy, Chapter 12-Reenactment*, Pub.L. 107-170, S. 1, 116 Stat. 133 (2002). Again, because of a retroactive provision, the reenactment, only provided authorization for a few days, until June 1, 2002. The 2002 Farm Bill, enacted May 8, 2002, provided additional authority, extending Chapter 12 until January 1, 2003. Pub. L. No. 107-171, tit. X, § 10814(a), 116 Stat. 532 (2002).

Last October, as Congress continued its debate of the overall bankruptcy reform bill, the House passed the bill that authorized the current six month extension of Chapter 12. *Protection of Family Farmers Act of 2002,* H.R. 5472. Representative Holden (D-Pa.) spoke on behalf of the reenactment, but expressed the following concerns.

> I rise to reluctantly offer my support for H.R. 5472, the Family Farmer Protection Act of 2002. I say "reluctantly" because the legislation before us today is an incomplete solution to a problem that has existed for more than 5 years.... The bill we are considering today marks the sixth time we are ignoring the 1997 recommendation and are instead extending chapter 12 on a temporary basis. It does not make sense. Chapter 12 is by no means a controversial issue.... For 5 years now, family farmers have been held hostage by the contentious debate surrounding the larger bankruptcy issue. For years they have been made to sit on pins and needles waiting to see if Congress will extend these protections for another few months until we reach the next legislative hurdle on the larger bankruptcy issue.

148 Cong. Rec. H6849 (daily ed. Oct. 1, 2002) (statement of Rep. Holden).

The *Protection of Family Farmers Act of 2002* that was passed by the House was not immediately considered by the Senate. In late October, it appeared that overall bankruptcy reform legislation was on the verge of passage. On November 15, 2002, however, the Conference Committee Report on that legislation was defeated in the House. *Bankruptcy Abuse Prevention and Consumer Protection Act of 2001,* H.R. 333, House vote on Nov. 15, 2002. In light of this defeat, on November 20, 2002, the Senate considered the legislation to temporarily extend Chapter 12. Before that vote, Senator Leahy also expressed his frustration with the process. He stated, "[u]nfortunately, too many family farmers have been left in legal limbo in bankruptcy courts across the country because Chapter 12 of the Bankruptcy Code is still a temporary measure.... Our family farmers do not deserve these lapses in bankruptcy law that could mean the difference between foreclosure and farming." 148 Cong. Rec. S11792 (Nov. 20, 2002)(statement of Sen. Leahy).

The Senate passed the temporary reauthorization of Chapter 12 by unanimous consent, and President Bush signed it on December 19, 2002. Pub.L. 107-377, 116 Stat. 3115 (2002).

Bi-partisan legislation that would make Chapter 12 a permanent part of the Code was introduced on November 19, 2002. *Protection of Family Farmers and Family Fisherman Act of 2002*, S. 3174 (107th Cong. (2d Sess. 2002). It was referred to the Committee on the Judiciary. Whether this bill will proceed forward or be stalled by those favoring a complete overhaul of bankruptcy law remains to be seen.

—Susan A. Schneider, Director and Associate Professor, Graduate Program in Agricultural Law, University of Arkansas School of Law, Fayetteville, AR

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AALA Editor.....Linda Grim McCormick
2816 C.R. 163, Alvin, TX 77511
Phone: (281) 388-0155
E-mail: lgmccormick@teacher.esc4.com

Contributing Editors: Susan A. Schneider, University of Arkansas School of Law, Fayetteville, AR; Jay Kiiha, University of Arkansas School of Law, Fayetteville, AR; Brandy L. Brown, University of Arkansas School of Law, Fayetteville, AR; Anne Hazlett, Washington, D.C.

For AALA membership information, contact Donna French Dunn, Executive Director, 4115 South Duff Avenue, Suite C, Ames, IA 50010-6600. Phone: (515) 956-4255.

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engaged in custom bailing work, custom cattle work, and he worked for wages in the farming operation of Mike Yazel." *Id.*

In 1997, Diel entered a period of financial difficulty. *See id.* At that time, Farmers State Bank of Hardtner ("FSB") had two security agreements, one dated June 30, 1992, and the other dated January 20, 1995. *See id.* The 1992 agreement was executed only by Diel's father "and purport[ed] to hypothecate to Farmer's State Bank an interest in [Virgil Diel's] anhydrous ammonia applicator and a New Holland Swather." *Id.* This agreement was executed to secure Diel's notes. *See id.* The 1995 agreement granted FSB "a security interest in all of ... Lanny Diel's livestock, machinery, equipment, crops and general intangibles." *Id.* The 1995 agreement did not reference any accounts and did not give a description of the land on which Diel's crops were grown. *See id.*

Diel and his former loan officer, who no longer worked for FSB, testified that "the course of dealing between them was that when Diel sold collateral of any kind, he was to bring the proceeds to the bank for application on his notes." *Id.* at 781. They also testified that Diel was occasionally allowed to use some of the proceeds to pay farming bills. *See id.* As Diel's financial situation worsened, however, the Bank often did not allow Diel to use the proceeds to pay bills. *See id.*

In 1999, Diel and his wife, Christine, opened a checking account at the Alva State Bank and Trust Company in Alva, Oklahoma. *See id.* Diel stated "that he opened [the] account after [FSB] refused to either advance him funds for his operation or allow him to use any collateral proceeds." *Id*. Diel also stated that "he used the account to avoid the Bank taking all of his deposits." *Id*.

After Diel harvested his wheat crop in June 1999, he knew that he would no longer be able to farm and that he would soon have to file for bankruptcy. *See id.* Diel's father took over his leased ground soon thereaf-

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ter, and Diel began working entirely as a cattleman, a custom bailer, and as an employee of Mark Yazel. *See id.*

On April 2, 2002, FSB filed a complaint with the bankruptcy court to determine whether Diel's debts were dischargeable. *See id.* at 780. FSB argued that Diel's debt should be "excepted from discharge under 11 U.S.C. § 523(a)(2) for making false financial statements and under § 523(a)(6) for willful and malicious injury to the Bank's property." *Id.* FSB also asserted that Diel's discharge should be denied because "Diel defrauded the bank under § 727(a)(2), concealed and falsified recorded information from which his financial condition or business transactions might be ascertained under § 727(a)(3), and [because he] knowingly and fraudulently made a false oath or account in connection with his case under § 727(a)(4)." *Id.*

FSB based these allegations on "several specific transactions which it contends demonstrate either Diel's fraudulent conduct or his willful and malicious damage to [its] security interest." *Id.* FSB first complained that in July, 1998, Diel sold hay to Cody Boevers for $8,409.65. *See id.* Boevers paid for the hay with two checks, one written for $4,048.20 and the other for $4,361.45. *See id.* The checks were returned for insufficient funds. *See id.* FSB advised Diel to initiate a collection action on the checks and to file bad check charges against Boevers. *See id.* Although Diel advised the bank that he would do so, he instead collected cash in the amount of the bad checks from Boevers. *See id.* Diel originally testified at the evidentiary hearing that "he had made no sales of hay for cash," but later admitted at trial that "he had not accounted to the Bank for the cash because he did not want the Bank to know he had spent the money." *Id.*

FSB further complained of transactions that arose from Diel's employment relationship with Mark Yazel. *See id.* As part of his employment, Diel cared for Yazel's cattle by allowing them to graze "on his leased land while it was planted in wheat." *Id.* The wheat that the cattle did not consume was cut and converted into "wheatlage" so that it could be saved for cattle feed. *See id.* In addition, on December 10, 1999, a check was deposited in the Diels' bank account at the Alva State Bank for $4,797.12. *See id.* Diel testified that the deposit represented the proceeds of the sale of hay to Mark Yazel. *See id.* As with the wheat and wheatlage, FSB claimed a security interest in the hay through the crops provision of the 1995 security agreement. *See id.* FSB asserted that because it had a security interest in Diel's crops via the 1995 security agreement, it therefore had an interest in the wheat that Diel fed to Yazel's cattle, the wheatlage that he saved, and the proceeds from the sale of hay to Yazel. *See id.*

Finally, FSB complained that "Diel should be held accountable for the proceeds of the anhydrous applicator his father sold at a farm auction." *Id.* at 782. The applicator had been pledged by Diel's father as security for Diel's debt at FSB. *See id.*

Because FSB subsequently withdrew its § 727 objections, the bankruptcy court stated that it was only necessary to consider the issue of "whether Farmer State Bank's debt should be discharged under §§ 523 (a)(2)(A) and (a)(6)." *Id.* The bankruptcy court concluded that "Diel's debt to Farmers State Bank is excepted in the amount of $8,409.65, the sum of the Boevers checks as funds obtained by actual fraud." *Id.*

The court first considered the checks for the sale of the hay in the amounts of $4,048.20 and $4,361.45 under the discharge provisions of § 523(a)(2). The court stated that:

[t]o prevail on a nondischargeability claim under 11 U.S.C. § 523(a)(2)(A), a creditor must prove by a preponderance of the evidence that (1) the debtor made a false representation; (2) the debtor had the intent to deceive the creditor; (3) the creditor relied on the debtor's conduct; (4) the creditor's reliance was justifiable; and (5) the creditor was damaged as a proximate result.

Id.

Applying § 523(a)(2), the court held that "Diel committed actual fraud by retaining [the] checks and seeking payment in cash which was not turned over to the bank." *Id.* at 783. The court noted that Diel contradicted his earlier testimony at the evidentiary hearing when he stated at trial that "he did not want the Bank to know he spent the funds on something other than debt service." *Id.* Thus, the court ruled that the full amount of $8,409.65 was excepted from discharge. *See id.*

Next, the court considered the December 10, 1999, sale of hay to Mark Yazel for $4,797.12. Bankruptcy Code § 523(a)(6) excepts from discharge "any debt for willful and malicious injury by the debtor to another entity or to the property of another entity." *Id.* (citing 11 U.S.C. § 523(a)(6)). The court noted that "[u]nless the creditor can prove not only that the debtor knew of the security interest, but also that the debtor knew that a transfer of the property was wrongful and certain to cause financial harm to the creditor, the debt should not be found nondischargeable." *Id.* (citing *Collier's on Bankruptcy* § 523.12[1] (15th ed. rev. 2001)).

Applying § 523(a)(6) the court concluded that, as a result of Diel's failure to inform FSB of the proceeds of the sale of the hay to Yazel, "Diel's depositing of Mark Yazel's check for hay at Alva State Bank [constituted] malicious damage, provided the Bank's security interest was valid." *Id.* The court concluded, however, that FSB did not have a valid security interest in Diel's crops because the security agreement failed to include a description of the land concerned in violation of Kan. Stat. Ann. § 84-9-203(1)(a). *Id.* at 784. As such, the court ruled FSB's interest in the check from Yazel for $4,797.12 was unenforceable. *Id.*

Addressing FSB's argument that it had an interest in Diel's wheat and wheatlage, the court stated that "the details of the Yazel cattle care transactions are not sufficiently fleshed out in the evidence to support judgments under either §§532(a)(2) or (a)(6)." *Id.* The court noted that FSB did not provide definitive evidence on the total amount of Diel's wheat that was fed to Yazel's cattle. *See id.* The court concluded that FSB, "at least where the Yazel transactions [were] concerned," failed to demonstrate that "its property interests [were] damaged at all." *Id.*

The court also rejected FSB's claim that it suffered a "willful and malicious" injury when Diel's father sold the anhydrous applicator. *See id.* The court stated that because "Diel did not participate in the sale or share in the proceeds[,] Lanny Diel cannot be said to have 'injured' the bank." *Id.* The court explained that Virgil Eugene Diel's failure to account was not a willful and malicious injury for which Lanny Diel could be held responsible. *See id.* The court added that "[i]f the Bank has a claim or cause of action concerning the applicator, it would appear to be against [Virgil Eugene] Diel and not the debtor." *Id.*

—Jay Kiiha, Graduate Fellow, Universty of Arkansas School of Law, Fayetteville, AR

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Supreme Court tie upholds fines against farmer for plowing wetlands

By Anne Hazlett

In late 1999, Angelo Tsakopoulos ("Tsakopoulos"), a California farmer, was fined $500,000 for converting 900 acres of grazing land to vineyards and orchards without a permit under §404 of the Clean Water Act. *Borden Ranch P'ship v. United States Army Corps of Eng'rs*, 1999 U.S. Dist. Lexis 21389 (E.D. Cal. 1999). When that judgment was affirmed by the Ninth Circuit Court of Appeals last year, Tsakopoulos took his case to the United States Supreme Court on the issue of whether his use of a "deep ripping" plow, a tool that penetrates restrictive layers of soil in preparing land for grape and fruit production, required a permit from the Army Corps of Engineers ("the Corps"). On December 16th, the Supreme Court issued a one line, 4-4, per curiam opinion in the case.[1] *Borden Ranch P'ship v. United States Army Corps of Eng'rs*, 2002 U.S. Lexis 9430 (Dec. 16, 2002). In effect, this tie allows the Ninth Circuit decision affirming the government's ability to regulate Tsakopoulos' plowing activity to stand.

The purpose of this article is to review the Ninth Circuit decision and possible implications for future farming practices.

Background

In 1993, Tsakopoulos, who was then a Sacramento real estate developer, purchased the Borden Ranch, an 8400 acre property in the Central Valley of California. *Borden Ranch P'ship v. United States Army Corp of Eng'rs*, 261 F.3d 810, 812 (9th Cir. 2001). Prior to this purchase, the portions of the ranch at issue in this case had been used for grazing cattle. *Id.* This acreage contained significant hydrological characteristics including vernal pools, swales, and intermittent drainages.[2] *Id.* The existence of these features depends on a dense layer of soil, called a "restrictive layer" or "clay pan," that prevents surface water from penetrating more deeply into the soil. *Id.*

After purchasing the Borden Ranch, Tsakopoulos decided to convert the property from rangeland to vineyards and orchards while subdividing it into smaller parcels for sale. *Id.* To accommodate the much deeper root systems needed for vineyard and orchard cultivation, Tsakopoulos used a procedure known as deep ripping in order to penetrate the restrictive layer of soil supporting the hydrological features of the area. *Id.* Deep ripping involves dragging four to seven-foot long metal prongs through the soil behind a tractor or bulldozer. *Id.* When the prongs puncture the restrictive soil layer, the displaced soil is then dragged behind the ripper. *Id.*

Tsakopoulos initiated this process without a permit in the fall of 1993. *Id.* After agreeing to several mitigation measures, he obtained a retrospective permit from the Corps in the spring of 1994. *Id.* That fall, the Corps of Engineers and the Environmental Protection Agency ("EPA") told Tsakopoulos he could deep rip in upland areas and drive over swales with the deep ripper in its uppermost position, *id.*, but that he could not conduct deep ripping activity in any vernal pools. *Id.* at 812-13. The next spring, the Corps learned that Tsakopoulos had performed deep ripping in protected wetlands and issued a cease and desist order. *Id.* at 813. The agency subsequently issued another cease and desist order in 1995 when Tsakopoulos continued to rip wetland areas in spite of the first order. *Id.*

In May of 1996, Tsakopoulos settled his violations with the Corps and EPA in an administrative order. *Id.* There, he agreed to set aside a 1368-acre preserve and to refrain from further violations. *Id.* Nevertheless, in 1997, the Corps concluded that Tsakopoulos had continued to deep rip in wetland areas without permission. *Id.* EPA then issued an administrative order against Tsakopoulos. *Id.*

Tsakopoulos responded to that action by filing a suit to challenge the authority of the Corps of Engineers and the EPA to regulate deep ripping. *Id.* The government filed a counterclaim, seeking injunctive relief and civil penalties for Tsakopoulos' alleged violations of the Clean Water Act. *Id.* Both parties filed motions for summary judgment. *Id.*

The district court granted the government's motion on the question of whether the Corps had jurisdiction over deep ripping in jurisdictional waters. *Id.* However, a bench trial was held on the issue of whether deep ripping had in fact occurred. *Id.* From that trial, the district court found 348 separate violations of deep ripping in twenty-nine drainages and ten violations in a single vernal pool. *Id.* Tsakopoulos was given the option of paying $1.5 million in penalties or paying $500,000 and restoring four acres of wetlands. *Id.* He chose the latter option and filed an appeal. *Id.*

On appeal, the Ninth Circuit affirmed the district court's order and reasoning, with the exception of reversing its finding that violations had occurred in a vernal pool.3 *Id.* at 819.

Analysis

In its review of the district court decision, the Ninth Circuit began with the question of whether the Corps of Engineers has the authority to regulate deep ripping. *Borden*, 261 F.3d at 813. It then looked at the lower court's calculation of the penalty to be imposed. *Id.* at 816.

Corps jurisdiction over deep ripping

In addressing the Corps' authority to regulate deep ripping, the Court first considered the requirements of the statute. The Clean Water Act prohibits the "discharge of any pollutant" into the nation's waters. *Id.* at 813-14 (quoting 33 U.S.C. §1311(a)). A discharge is defined as "any addition of any pollutant to navigable waters from any point source." *Id.* at 814 (quoting 33 U.S.C. §1362(12)). A point source is "any discernible, confined and discrete conveyance ... from which pollutants are or may be discharged." *Id.* (quoting 33 U.S.C. §1362(14)). A pollutant is defined, inter alia, as "dredged spoil, ... biological materials, ... rock, sand [and] cellar dirt." *Id.* (quoting 33 U.S.C. §1362(6)). It is unlawful to discharge pollutants into wetlands without a permit from the Army Corps of Engineers. *Id.* (citing 33 U.S.C. §§1344(a), (d)). An exception to this prohibition is made for any discharge resulting from certain farming and ranching activities. *Id.* at 815 (citing 33 U.S.C. §§1344(f)(1)(A), (f)(2)).

Discharge of a pollutant. Looking initially at the question of whether deep ripping constitutes the discharge of a pollutant, the Court rejected Tsakopoulos' position that such activity cannot cause an addition of pollutant because it simply turns up soil that is already there. Id. at 814. In so doing, the Court reasoned that this argument is inconsistent with case law squarely holding that redeposits of materials can constitute "an addition of pollutant" under the Clean Water Act. Id. Citing *Rybacheck v. United States Envt'l Prot. Agency*, 904 F.2d 1276 (9th Cir. 1990), and *United States v. Deaton*, 209 F.3d 331 (4th Cir. 2000), the Court stated that previous cases have found activities that destroy the ecology of a wetland are not immune from regulation under the statute merely because they do not involve the introduction of material brought in from somewhere else. Id. at 814-15.

In *Rybacheck*, the Court considered a claim that placer mining activities were exempt from the Clean Water Act. *Id.* at 814. The Court held that removing material from a stream bed, sifting out the gold and returning the material to the stream was an addition of a pollutant. *Id.* The pollutant in that case was the material segregated from the gold during the mining process. *Id.*

In *Deaton*, the Fourth Circuit held that the Corps could regulate "sidecasting," a process in which dredged or excavated material from a wetland is deposited back into

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Anne Hazlett is an associate counsel with the House Agriculture Committee in Washington, D.C.

that same wetland. *Id.* The Court reasoned that once any matter was removed from the wetland, it became dredged spoil, which is a statutory pollutant and a type of material that up until then was not present on the Deaton property. *Id.* The Court stated that it was of no consequence that what became dredged spoil was previously present on the same property. *Id.* Of significance was the fact that once the material was excavated from the wetland, its redeposit in that same wetland added a pollutant where none had been before. *Id.* Finally, the Court instructed that Congress had determined that "plain dirt, once excavated from the waters of the United States, could not be redeposited into those waters without causing harm to the environment." *Id.* (quoting *Deaton*, 209 F.3d at 336).

Reviewing these cases, the *Borden* Court concluded that there was no "meaningful distinction" between those activities and deep ripping with a plow. *Id.* at 815. In the situation at hand, the Corps alleged that Tsakopoulos essentially punctured the bottom of protected wetlands. *Id.* Prior to the deep ripping activity, the protective layer of soil was intact and held the wetland in place. *Id.* After that procedure, the soil was wrenched up, moved around, and redeposited somewhere else. *Id.* While it is true that no new material was added, a pollutant was added in violation of the Clean Water Act. *Id.*

In a dissenting opinion, Circuit Judge Ronald Gould disagreed with the majority on this point. While he believed that Congress could regulate the deep ripping activity being challenged, Judge Gould concluded that Congress has not exercised its power in this regard. *Id.* at 819. Following the D.C. Circuit's reasoning in *National Mining Assn. v. U.S. Army Corps of Engineers*, 145 F.3d 1399 (D.C. 1998), Judge Gould held that deep ripping does not constitute the discharge of a pollutant because it does not involve any significant removal or addition of material to the site. *Id.* at 820.

In *National Mining*, the D.C. Circuit held that the Corps had exceeded its authority by regulating the redeposit of dredged material that incidentally falls back in the course of a dredging operation. *Id.* at 819. The Court explained that the statutory term "addition" could not be reasonably interpreted to encompass the situation in which material is removed from waters of the United States and a small portion just happens to fall back. *Id*. Rejecting the government's primary argument that the incidental fallback was an "addition" because once dredged the material becomes a pollutant under the statute, the Court wrote: "Although the Act includes 'dredged spoil' in its list of pollutants, Congress could not have contemplated that the attempted removal of 100 tons of that substance could constitute an addition simply because only 99 tons of it were actually taken away." *Id.* at 819-20 (quoting *National Mining*, 145 F.3d at 1404).

Finding this logic persuasive, Judge Gould determined that deep ripping is not a regulable activity. *Id.* at 820. While this form of plowing modifies the hydrological characteristics of the soil, the Clean Water Act speaks of discharge or addition of pollutants, not of changing the hydrological nature of the soil. *Id.* Judge Gould contended that if Congress intends to prohibit "so natural a farm activity as plowing," it can and should be more explicit. *Id.* It was an undue stretch for the majority to reach and prohibit the plowing done by Tsakopoulos, which seems to be a traditional form of farming activity. *Id.* The policy decision involved here should be made by Congress, who has the ability to study and the power to make such a fine distinction. *Id.* at 821.

Exception for normal farming activities. Having determined that Tsakopoulos' deep plowing caused a discharge of pollutants, the Court turned to the issue of whether his activity was nonetheless exempt from regulation under the statute's farming exception. *Id.* at 815. There, "normal" farming and ranching activities such as plowing are not subject to a permit unless they fall under the so-called "recapture" provision. *Id.* Under that limitation, any discharge of dredged or fill material requires a permit where: (1) the discharge is incidental to an activity which is bringing an area into a new use, (2) the flow or circulation of waters may be impaired, or (3) the reach of such waters may be reduced. *Id.* (quoting 33 U.S.C. §1344(f)(2)).

Applying these prongs, the Court concluded that Tsakopoulos' deep ripping was governed by the recapture provision. *Id.* Specifically, it held that converting pasture into orchards and vineyards constituted bringing the land into a new use. *Id.* Further, there was a clear basis in the record for concluding that the destruction of the protective layer in the soil created an impairment of the flow of nearby waters. *Id.* While the Corps cannot require a farmer who is merely changing from one wetland crop to another to obtain a permit, it can regulate activities that require substantial hydrological alterations. *Id.* Because Tsakopoulos' plowing radically altered the hydrological characteristics of protected wetlands, the Court held that the Corps and EPA properly exercised jurisdiction over his activities. *Id.* at 816.

Once again, the dissent parted ways with the majority to hold the farming exception covered deep ripping with a plow. *Id.* at 820. Judge Gould conceded that the recapture provision defeated the exception for any deep ripping that had the purpose of transforming land. *Id.* However, in his view, it did not defeat the exemption for any unintended impairment. *Id.* at 820-21. While many of the violations found by the district court involved a purposeful attempt to change the land, some of the transgressions were unintentional and, therefore, within the bounds of the exemption. *Id.* at 821.

Penalty calculation

Moving from the substance of the case to a review of the penalty calculated, the district court counted each pass of the deep ripper through a protected wetland as a separate violation. *Id.* The statute provides for a maximum penalty of $25,000 per day for each violation. *Id.* (citing 33 U.S.C. §1319). Although the final penalty was set at $1.5 million[4], the district court could have assessed a penalty of $8.95 million. *Id.* at 817.

Nevertheless, Tsakopoulos challenged the district court's calculation on the basis that the penalty should have been assessed on the number of days in which illegal activity occurred, not on the number of individual passes with the deep ripping plow. *Id.* He maintained that the statutory language "per day for each violation" meant that he could only be assessed $25,000 for any day in which ripping violations occurred, regardless of the total number of rippings in that day. *Id.* He also argued that a contrary reading would lead to nonsensical results where a polluter who emitted 25,000 gallons of a pollutant continuously over the course of a day would be subject to a $25,000 maximum penalty, whereas a polluter who made three separate discharges of one gallon each would be subject to a $75,000 maximum penalty. *Id.* at 818.

The Ninth Circuit rejected this argument, reasoning that the statutory language clearly focuses on the maximum penalty per day for each violation. *Id.* at 817. Further, the Court expressed concern for the irrational results that would follow from Tsakopoulos' position. *Id.* at 818. Citing the Fourth Circuit's decision in *United States v. Smithfield Foods, Inc.*, 191 F.3d 516 (4th Cir. 1999), the Court noted that under Tsakopoulos' reading a landowner could incur one violation and then rip away the rest of a protected area with impunity because no additional penalty would be imposed. *Id.* Lastly, the Court stated that Tsakopoulos' concern about the disparate treatment of a polluter who emits several small amounts and a serial polluter is not without remedy in the district courts as

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judges have substantial discretion in imposing penalties. *Id.*

Implications

Notwithstanding the brevity of the Supreme Court's opinion in this case, the *Borden Ranch* decision has garnered significant attention from government regulators as well as members of the agricultural, development, mining and environmental communities. Unlike previous lawsuits, which have targeted activities designed to create land that can be used for food or fiber production such as filling wetlands with imported soil, this action has been labeled as one of "landmark potential" because it is focused solely on plowing, a common farming practice. *See* Denny Walsh, *Trial Plowing New Legal Ground: Tsakopoulos Battles Punishments Sought Over Wetlands*, The Sacramento Bee, Aug. 30, 1999, http://www.sacbee.com/news. Beyond its potential implications for future farming activities, *Borden Ranch* is also noteworthy to the extent that it has created unlikely bedfellows in environmental advocates and the Bush Administration who find themselves on the same side defending the government's perception of its jurisdiction.

In effect, the Supreme Court's tie ruling affirms the lower court decision but is not binding as precedent for other cases outside the Ninth Circuit. With that outcome, many in the environmental community appear to view the Court's decision as something less than a victory. In an interview with *The Sacramento Bee*, Tim Searchinger, a lawyer with Environmental Defense, said: "We're calling it a reprieve. Don't dance late into the night." Whitney, *Tsakopoulos Loses Battle in a Tie Vote*. Similarly, Julie Sibbing of the National Wildlife Federation told the *Los Angeles Times*: "This is good news for today, but I'm sure industry will try to bring this up again." David Savage, *Justices Uphold Wetlands Ruling*, Los Angeles Times, Dec. 17, 2002, http://www.seattletimes.nwsource.com.

Proponents of the Ninth Circuit's decision maintain this position is necessary to protect millions of acres of valuable wetland resources. *Id.* In particular, some supporters believe that the ruling is critical where the Bush Administration is under pressure from development, logging and mining interests to relax wetland protections around small and medium-sized streams. Whitney, *Tsakopoulos Loses Battle in a Tie Vote*. In denouncing Tsakopoulos' challenge, proponents of the Ninth Circuit's ruling argue that industry, including agriculture, already has wide latitude to alter marshes and streams without penalty. Stuart Leavenworth, *Tsakopoulos Wetlands Case Goes to the Top*, The Sacramento Bee, Dec. 6, 2002, http://www.sacbee.com/content/news. Pointing to California which has allegedly lost 90 percent of its wetlands, they acknowledge that development is a significant contributor to wetland degradation. *Id.* However, they maintain that Congress also intended the Clean Water Act to protect wetlands from degradation as a result of unusual farming activities, like deep ripping. *Id.* Further, they warn that a ruling against the Ninth Circuit in favor of Tsakopoulos would open a loophole in the statute permitting the drainage of wetlands by developers contending that they were engaged in a farming operation. Whitney, *Tsakopoulos Loses Battle in a Tie Vote*.

By contrast, agricultural interests have expressed substantial concern about the Ninth Circuit's decision. First and foremost, agriculture is concerned that EPA and the Corps will continue to ignore the plain language of the Clean Water Act. Leavenworth, *Tsakopoulos Wetlands Case Goes to the Top*. Rather than follow the text, the agencies will make their own law by regulating based on what they perceive the environmental effects of an activity to be. *Id.* If the Clean Water Act is insufficient to safeguard wetlands or other ecological resources, critics of the Ninth Circuit contend the answer is to amend the statute, not rewrite its language through "judicial acquiescence to administrative fiat." Jonathan Adler, *Plowed Under: The Supremes Consider a Landowner's Challenge to Federal Wetlands Regulation*, National Review Online, Dec. 11, 2002, http://www.nationalreview.com.

Where agencies continue to interpret the statute without Congressional clarification, Bill Thomas, a rancher and lawyer representing the California Cattlemen's Association, told *The Sacramento Bee*: "Our concern is that the 9th [Circuit decision] will be interpreted by the regulating agencies to give rise to extremely aggressive enforcement to folks doing rather routine agricultural practices." Whitney, *Tsakopoulos Loses Battle in a Tie Vote*. Similarly, Don Parrish, Senior Director of Regulatory Relations for the American Farm Bureau Federation, has stated: "Hopefully, we don't see a big erosion of agricultural practices in wetlands or a limit on what farmers and ranchers can do in terms of planting crops on their farms as a result of this case. But, we could see some of that." Tom Steever, "Court Case Threatens the Plow," American Farm Bureau Federation, Dec. 23, 2002, http://www.fb.org. And, Bill Stokes, president of the Lodi District Grape Growers Association, has predicted: "We are going to be overwhelmed with environmental restrictions, which we already are." *High Court Weighs in on Wetlands*, MSNBC News, Dec. 18, 2002, http://www.msnbc.com/news.

Putting their differences aside, advocates for both positions seem to agree on one thing—that the Court's commitment to wetlands protection is fragile. In announcing its tie ruling, the Court did not indicate how each justice decided this case. Nevertheless, counsel to the parties presume, based on the Court's decision in the *Cook County* case which limited federal regulation of isolated wetlands, that Chief Justice Rehnquist and Justices Scalia, Thomas, and O'Connor favored Tsakopoulos while Justices Souter, Breyer, Ginsburg and Stevens supported the government's position. Whitney, *Tsakopoulos Loses Battle in a Tie Vote*. Looking at Justice Kennedy's vote with the majority in that matter, many speculate that his decision not to participate in this case was dispositive of the ruling. *Id.* Looking to a future case presenting these questions, Timothy Bishop, a Chicago attorney representing Tsakopoulos, told the *Los Angeles Times*: "Obviously, the court is very divided. They will be looking for another case to decide this issue, and the environmentalists have to be worried. We think Justice Kennedy would have been on our side." Savage, *Justices Uphold Wetlands Ruling*.

Beyond the absence of Justice Kennedy, a subsequent regulatory challenge to farming activities may also be shaped by the profile of the regulated plaintiff. In this case, Tsakopoulos was a real estate developer turned farmer. In his dissent, Judge Gould criticized the majority for focusing on the development aspects of his business enterprise. *See Borden*, 261 F.3d at 819. Gould maintained that his rights as a citizen were the same whether he was viewed as a farmer, rancher, or developer. *Id.* Nevertheless, that bias, coupled with the environmental community's concern that developers will use the farming exception as a protective shield, presents some likelihood for a different outcome where the regulated party is a full-time producer without outside business interests.

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[1] Justice Kennedy did not participate in the decision because he is an acquaintance of Tsakopoulos. David Whitney, *Tsakopoulos Loses Battle in a Tie Vote*, The Sacramento Bee, Dec. 17, 2002, http://www.sacbee.com.

[2] Vernal pools are pools that form during the wet season, but are generally dry during the summer. *Borden Ranch P'ship v. United States Army Corps of Eng'rs*, 261 F.3d 810, 812 (9th Cir. 2001). Swales are sloped wetlands that transport aquatic plant and animal life, filter water flows, and minimize erosion. *Id.* Intermittent drainages are streams that transport water before and after a rain. *Id.*

[3] The district court found Clean Water Act violations in one isolated vernal pool. *Id.* at 816. Following the Supreme Court's

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Insurance policy application ruled not part of policy.

The United States District Court for the Western District of Arkansas has granted an insurer's motion for summary judgment and denied the insureds' motion for summary judgment in an action brought by the insureds seeking recovery for losses they suffered when one of their poultry houses was destroyed by fire. *Forrest v. Northland Cas. Co.*, 213 F.Supp.2d 1023, 1023-24 (W.D. Ark. 2002). The court ruled that the plaintiffs' insurance policy application, including all of the property valuations contained in that application, did not become a part of the insurance policy, and therefore the Arkansas valued policy law, Ark. Code Ann. § 23-88-101, did not apply. *Id.* at 1024-25.

On June 1, 2001, the plaintiffs purchased an insurance policy from the defendant covering three poultry houses and certain equipment. *See id.* at 1024. The application that the plaintiffs submitted for the policy contained the separate values of each of the plaintiffs' poultry houses and equipment. *See id.* The policy that was issued, however, did not include these individual property valuations, it only established an overall policy limit of $370,000.00 for "'blanket buildings and equipment.'" *See id.* (quoting Doc. 12 Ex. C "Commercial Property Coverage Part Declarations").

The policy provided that "the replacement cost for any loss of damage is not recoverable unless the property is actually repaired or replaced as soon as reasonably possible after the loss or damage." *Id.* The policy also provided that "[i]f this is not done, then only the actual cash value, which takes depreciation into account, is recoverable." *Id.*

On July 1, 2001, one of the plaintiffs' poultry houses was completely destroyed by fire. *See id.* The plaintiffs filed a loss claim with the insurer pursuant to the terms of their insurance policy. *See id.* The plaintiffs calculated their loss amount by first "determining the replacement cost of the poultry house and its equipment at the time of the loss, which it estimated to be $171,000," and then deducting a depreciation amount because they had not rebuilt the poultry house. *Id.* The actual cash value of the poultry house was later determined to be $97,256.00. *See id.* The insurer "added $7,000 for debris removal, which was also covered under the policy, subtracted the $1,000 deductible, and made a total payment of $103,256 to the Plaintiffs." *Id.*

The plaintiffs brought an action against the insurer contending that they were entitled to an additional $58,744.00 because the insurance policy application they submitted listed the destroyed poultry house as having a value of $162,000.00. *See id.* The plaintiffs argued that their policy application should become part of the policy and that "under Arkansas' valued policy law, they are entitled to the full $162,000.00 because the poultry house was totally destroyed." *Id.*

The court stated that "[a] 'valued policy' is one where the value of the insured property is agreed to by the parties in the contract in advance." *Id.* (citing *St. Paul Fire & Marine Ins. Co. v. Griffin Constr. Co.*, 993 S.W.2d 485, 487 (Ark. 1999)). The court explained that "Arkansas' valued policy law requires insurers to pay the full amount stated in the policy or the full amount for which the company collects premiums in cases 'of a total loss by fire or natural disaster of the property insured.'" *Id.* (quoting Ark.Code Ann. § 23-88-101). The court also explained that Arkansas' valued policy law "is intended to relieve the insured of the burden of having to prove the value of the property after its total destruction and to prevent insurance companies from receiving premiums on overvaluations and then applying policy limitations concerning valuation when the property is destroyed. *See id.* (citing *Underwriters at Lloyd's v. Pike*, 812 F.Supp. 146, 148 (1993)).

The plaintiffs also asserted that Ark. Code Ann. § 23-79-118(a) required that the policy application become part of the insurance policy, thereby making the $162,000.00 amount the amount agreed to by the parties. *See id.* at 1024-25. Section 23-79-118(a) provides that "an insurance contract is to be construed 'according to the entirety of its terms and conditions as set forth in the policy and as amplified, extended, or modified by any rider, endorsement, or application *made a part of* the policy.'" *Id.* at 1025 (quoting § 23-79-118(a) (emphasis supplied)).

The court rejected the plaintiffs' argument, ruling that the plaintiffs' application did not become a part of the policy, and, therefore, Arkansas' valued policy law was not applicable. *See id.* The court stated that "the application is not attached to the policy, nor is there any language in the policy incorporating the application. Accordingly, the application is not '*a part of*' the policy and there is no agreed-to value for the destroyed property." *Id.* (citing *American Pioneer Life Insurance Co. v. Allender*, 713 S.W.2d 249, 251 (1986) (*en banc*) (emphasis supplied)).

The plaintiffs argued in the alternative that "even if the application is not part of the insurance contract and there is no agreed-to value in the contract, Defendant should be 'estopped as a matter of law from ascertaining any value of the building other than' the $162,000 figure reflected in the application since the application was completed only a month prior to the fire and the parties agreed on that value then." *Id.*

The court rejected this argument, stating that "the policy states that only the actual cash value, not the replacement value which the $162,000 figure represents is payable if the insured property is not rebuilt." *Id.* The court stated that "[u]nder the terms of the policy ...[P]laintiffs were not entitled to the replacement cost because they did not rebuild. The policy specifically states that in such circumstances, only the actual cash value, which takes depreciation into account is payable. The court also stated that the plaintiffs' belief that they would receive the $162,000.00 amount contained in the application "is contrary to the plain language of the policy." *Id.* at 1025-26 (citing *Elam v. First Unum Life Ins. Co.*, 57 S.W.3d 165, 169 (2001) (ruling that if a policy's language is not ambiguous, then a court is required to give plain effect to the policy's plain language)).

The court noted that there was no evidence presented that warranted a reformation of the parties' policy. *See id.* The court stated that "[a] contract may be reformed to comport with a party's understanding of it only if there was a mistake on that party's part accompanied by fraud or other inequitable conduct of the other party." *Id.* at 1026 (citing *Mikus v. Mikus*, 981 S.W.2d 535, 538-39 (Ark. Ct. App. 1998)).

—Brandy L. Brown, Graduate Fellow, University of Arkansas Masters in Agricultural Law Program

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decision in *Solid Waste Agency of N. Cook County v. United States Army Corps of Eng'rs*, 531 U.S. 159 (2001), the government conceded that ruling precluded the Corps' authority over that wetland. *Id.* Accordingly, the Ninth Circuit reversed the district court's findings with respect to this violation. *Id.*

[4] The district court allowed Tsakopoulos to suspend $1 million of the penalty in exchange for performing various restoration measures. *Id.* at 817.