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From the AALA Executive Director

In order to help us catch up with the dates of issues, this is a special expanded double issue.

Call for articles. For many members, the main benefit of membership in the AALA is the Update, making the newsletter a major means of reaching and learning from our colleagues in agricultural law. As you can see by the date of this issue, we are very much behind in publishing the Update. Although the traditional articles have been longer, with substantial footnotes, it needs to be emphasized that articles of all lengths are accepted. Articles do not need to be definitive scholarship and can be exposition of current developments. Many members will also appreciate practice tips, forms or approaches to handling client interactions with government agencies. If you feel uncertain about the appropriateness of your article, it can be reviewed by members of the Update Editorial Board before publication.

The AALA board is seeking new members, including student members, for the Update Editorial Board, responsible for overseeing and writing for the *Agricultural Law Update*. Please contact Jesse Richardson, jessj@vt.edu.

2010 Membership Renewals Please send yours in as soon as possible if you have not already.

2010 Annual Conference. President-elect Pat Jensen is seeking topics and speaker suggestions for the 2010 Annual Agricultural Law Symposium, October 8-9, 2010 at the Hilton Hotel in Omaha, NE. Contact her at wcolemanpjensen@aol.com.

Robert P. Achenbach, AALA Executive Director

JURY VERDICT AGAINST BAYER FOR LIBERTY LINK RICE

BREAKS NEW GROUND IN BIOTECH LIABILITY

by Thomas P. Redick* and A. Bryan Endres**

The close of 2009 brought ground-breaking litigation in agricultural biotechnology that raises potential liability concerns for those crops that secure federal approval, but do not have approval in overseas markets. On December 4, 2009, a federal jury in St. Louis, Missouri in the case *In re Genetically Modified Rice Litigation*, Case No. 06-md-01811 (E.D. Missouri) awarded two “test plaintiff” growers approximately \$2 million in compensatory damages for “economic loss” from the commingling (“contamination”) of their rice crops with an experimental biotech rice variety—Liberty Link 601 (LL601) rice. This article discusses the jury verdict and the court’s ruling on the preceding summary judgment motions (*In re Genetically Modified Rice Litigation*, 2009 U.S. DIST. LEXIS 98302 (October 9, 2009)).

The facts behind this case first came to light in June 2006; Riceland Foods, the nation’s largest rice cooperative, alerted Bayer CropScience (Bayer) of its discovery of genetically engineered rice in the 2005 rice harvest. Shortly thereafter, Bayer confirmed this finding and reported the results to USDA. At the time of Riceland’s discovery, USDA had approved two varieties of genetically engineered rice for commercial release—LLRice06 and LLRice62. Bayer chose not to market these genetically engineered varieties, however, because growers had no interest in producing rice not yet approved for sale in major importing nations such as Japan and the European Union. The variety discovered in the 2005 harvest, however, LLRice601, was not yet approved by USDA for commercial release or import to the E.U. USDA announced Riceland’s discovery on August 19, 2006, precipitating an immediate decline in rice futures, the pulling of U.S. rice from European grocery shelves, and, not surprisingly, the filing of multiple lawsuits.¹ Building upon the standard from *In re Starlink* of “physical injury” from pollen flow² or post-harvest commingling, the court’s ruling on summary judgment motions extended the theory to allow compensable “damage” where the crop’s only flaw was its lack of approval for export to major markets overseas

– and was carelessly commingled broadly in the foundation seed sold to many states in the “rice belt” of the Southern Midwest. Although the jury denied plaintiffs’ request for over \$80 million in punitive damages, it nevertheless broke new ground in U.S. common law when it awarded nearly \$2 million in compensatory damages to two plaintiffs for their economic losses arising from lost overseas markets for rice.

A. Another Billion-Dollar Debacle? Going for “Ten Figures”

This decision at trial of two farmer test plaintiffs was only the first of more than 1,000 similar cases filed against Bayer in the southern United States since the USDA’s announcement.³ The second bellwether trial of three Arkansas and Mississippi farmer plaintiffs commenced in January 2010. The second trial resulted in a jury verdict of just over \$1.5 million in compensatory damages, distributed to the three plaintiffs based on the number of planted acres. A third test trial involving a non-farmer plaintiff (Riviana Foods, Inc.) will begin on April 19, 2010.

Bayer was held liable based on evidence of negligence involving its alleged lack of oversight of the LL601 field trials nearly ten years ago. Field trial records indicate that the “cooperating” researcher at Louisiana State University elected, out of an abundance of caution, to grow the LL601 at a planting distance ten times greater than the USDA recommendation, and three times what Bayer recommended. Although rice can pollinate openly to other rice in a stiff breeze, it generally is not a wide pollinator like corn or canola, and the exact path taken by the rice to commingle with foundation seed supplies is not known.⁴ Under the circumstances, the researcher who chose to grow this rice in the same general vicinity did not appear to have reason to fear pollen drift to foundation seed.

With plaintiffs’ counsel estimating that another six thousand farmers will have claims, and at least 1,000 still awaiting trial,⁵ and plaintiffs’ counsel adding Bayer A.G. (foreign parent of Bayer CropSciences (BCS)) as a defendant, the Bayer defendants may be inclined to settle the remaining consolidated cases using these “test plaintiff” verdicts, and the absence of punitive damages, as a

sign to settle before a future jury awards punitive damages. This court, in an earlier ruling on cross-motions for summary judgment, allowed the jury to give grower plaintiffs damages for their “economic loss” from the “physical injury” that occurs from commingling a biotech crop (or other crop, like treated seed), which is one step beyond what occurred in the Starlink Corn litigation, discussed next. If the case is settled, and thus eliminates the chance that the district court’s groundbreaking decision is reversed on appeal, the biotech rice litigation could influence other courts (and international negotiations over biotech liability), as is discussed below at Section D. While an appeal of a test plaintiff jury verdict is possible, appeals face a high bar for appellate standard of review (“against the manifest weight of the evidence”).

C. The Summary Judgment Motion

This verdict without a published opinion followed an October 9, 2009 judgment entered on summary judgment motions with an accompanying detailed opinion by Judge Catherine D. Perry. The judgment dismissed most of the claims against defendants, but allowed claims for negligence and private nuisance from “negligent contamination of the nationwide rice supply” leading to “market losses and damage to other property, including equipment, land, and rice” to proceed to trial. In its summary judgment ruling, the court rejected Bayer’s argument that low level presence (LLP) in the US rice supply was federally permitted and provided a defense – since the USDA is in the process of proposing new LLP regulations.⁶ Rather, plaintiffs were correct in stating that the current regulations would not allow LLP.⁷ Bayer had a duty to ensure that the GM trait did not “escape and contaminate other non-GM rice” because this was a “known and foreseeable risk” of conducting field trials (since federal law required strict containment, a common law duty arose).⁸

This regulatory breach (i.e., LLP), however, did not support a claim of negligence *per se*, as the performance standards outlined in the APHIS regulations did not provide a standard of care.⁹ Moreover, the court held that both industry practices and the regulatory scheme

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are relevant to the standard of care, but the parties cannot rely on compliance or non-compliance with regulations as evidence for or against liability.¹⁰

The court also found the common-law tort claims for negligence and private nuisance were not barred by the economic loss doctrine. The court distinguished two prior cases involving “the negligent spread of GM food” where contracting farmers – who had purchased contaminated seed directly from the seed company – had claims that were barred, at least in part, by the economic loss doctrine. One case, *Sample v. Monsanto*, arose in the same court (E.D. MO), where the court granted summary judgment on a poorly documented nuisance claim involving unapproved-in-EU corn and soybeans, which was tacked onto an antitrust claim as an apparent afterthought.¹¹ The other case involved Bayer – *In re Starlink* – and applied Wisconsin and Illinois law to bar claims from a grower who bought contaminated seed while allowing those whose corn was commingled via pollen drift or other means.¹² While the LL601 plaintiffs bought contaminated seed, they did not buy it from Bayer and their harvested crop was “injured by Bayer’s negligent contamination of the nationwide rice supply,” which made the economic loss doctrine inapplicable to their claims.¹³

One of the arcane issues of agricultural law that may surface in an eventual appeal involved Bayer’s dispute of plaintiffs’ claims for any amounts that plaintiffs owed to their “share-rent landlords” on the ground that the landlords had not filed suit to recover their shares.¹⁴ The court found the law in Missouri widely divergent in defining share-rent farming as a leasehold interest or a tenancy in common. A tenant under a lease has legal possession of the crop until it is harvested and divided, with the right to sue a third party for damage to the crops. If it is a tenancy in common, both landlord and tenant must sue to collect their share of the damages. To the extent that plaintiffs seek lost profits, however, they must prove an adequate basis for estimating the lost profits with reasonable certainty. *Citing Ameristar Jet Charter, Inc. v. Dodson Int’l Parts, Inc.*, 155 S.W.3d 50, 54-55 (Mo. 2005).

E. Punitive Damages and the Starlink Corn Legacy

While no punitive damages were awarded in this verdict, Bayer probably cannot use issue preclusion (collateral estoppel) to prevent hundreds of other plaintiffs from having their day in court on punitive damages.¹⁵ In consolidated cases, each test plaintiff seeking punitive damages requires an “individualized hearing,”¹⁶ presumably to provide Defendant with due process and to give each plaintiff their day in court on the subject of defense misconduct.

Bayer’s past experience with failures of “identity preservation” in Starlink corn (sold by Bayer’s predecessor) was admitted as evidence of a pattern of negligence at the trial just concluded in St. Louis. At the turn of the millennium, the US corn production complex had to survive a nationwide food recall in the 2000 EPA-FDA recall of Starlink corn. In a 2000 memorandum cited by the court in denying Bayer’s summary judgment motion, Bayer managers noted that if their rice was found to have spread to conventional varieties, “We could make any national newscast ... and the rice industry would be quite affected.”¹⁷ Around that time, the Starlink corn variety sold by Bayer’s predecessor company, Aventis Crop Sciences USA (“Aventis”), was making the national news. This corn was approved only for feed or fuel use (not food) in the United States.¹⁸ When testing by the activist group Friends of the Earth found this biotech corn had commingled with food in the United States, the biotech seed company, Aventis Crop Sciences USA (“Aventis”), worked diligently to assure that all corn containing Starlink corn was directed to lawful non-food uses¹⁹ but the corn continued to be found (and removed from food supply chains as illegal) for at least eight years after its discovery in the US food supply.²⁰

Aventis paid a number of claims for damages. The cost of the resulting recall, the ensuing litigation settlements and lost shareholder value all tallied up to several billion dollars. An estimated two billion dollars in shareholder value was lost – and some economists suggested Starlink cost over \$1 billion in comparative value at sale of the US corn crop.²¹ Aventis shareholders lost nearly \$2 billion, while growers

received several hundred million dollars in settlements.²²

In the pending rice litigation, the plaintiffs alleged that Bayer (the successor to Aventis CropScience) and its subsidiaries were responsible for both Starlink corn and LL601 rice, thereby justifying an award of punitive damages. In denying Bayer’s motion for summary judgment on the claim for punitive damages, Judge Perry cited disputed issues of Bayer conduct. For example, did Bayer: 1) ascertain whether the LL601 field trials were planted too close to foundation seed, 2) monitor for unauthorized releases of LL601 outside areas in which it was planted, and 3) verify whether the LSU “cooperators” were taking necessary steps, such as cleaning their equipment and boots, properly storing the rice, or adequately documenting compliance? These and other questions regarding punitive damages will be heard in future trials.²³

G. Intervening Tortfeasors and Transboundary Grain Handler Liability

The transboundary liability negotiations under Article 27 of the Cartagena Protocol on Biosafety (“Biosafety Protocol”) will establish international rules and procedures for biotech crop liability as regulated “living modified organisms” (“LMOs”), including protection of indigenous Mexican corn. In May 2008, at the fourth meeting of the parties to the Protocol, the parties considered a working draft of options regarding liability and redress from damage caused by the international shipment of LMOs. Article 27 of the Protocol, subtitled ‘liability and redress’ should not include food products that contain no viable organism.

One contentious question in these negotiations is the “channeling” of liability to the grain shipper, as a person who can exercise some modicum of physical control. This approach would assess the entire amount of liability against that person, who would either insure for this loss or seek reimbursement from others who could be blamed – e.g., the grower cooperative that sold a variety of biotech crop lacking overseas approval, or *the seed company that negligently allowed the* (cont. on page 4)

commingling to occur.

The LL601 litigation has consolidated the claim of the German rice importing company (Rickmers), which is suing for breach of contract. Rickmers, by suing a grower cooperative, hopes to recover its losses by suing for trace-back through the chain of commerce. Grain shippers may find their remedies limited against seed companies, who are adept at use of liability disclaimers in adhesion contracts signed by growers. In the LL601 litigation, Riceland can sue Bayer to recover amounts paid due to the commingling that Bayer caused. This may prove difficult, however, if the grower cooperative (Riceland) has growers who purchased seed with disclaimers of liability from Bayer (and those disclaimers or limitations of liability are enforced to deny recovery by Riceland of amounts paid to Rickmers). Seed contracts typically have boilerplate disclaimers of liability for traces of genetic “off-types,” which might include biotech crops that were never submitted for regulatory approval in the U.S., much less the overseas markets at issue in the LL601 rice case.

In the LL601 summary judgment ruling, however, the court found little reason to hold the handlers like Riceland liable for any degree of comparative fault, as a matter of law suitable for decision on summary judgment. Bayer asserted that it could not have caused the harm in question “due to the intervening and/or superseding acts or omissions of parties or non-parties to this action for whose acts or omissions the BCS Defendants and Bayer Corporation are not liable.”²⁴ Generally, the actions of an intervening wrongdoer break the chain of causation – e.g., a joyriding car thief who sees a baby strapped into a car seat in his rearview mirror just as a drunk truck driver broadsides them.²⁵

The court, however, held that “[a]lthough plaintiffs still have to prove proximate cause, Bayer may not argue that others may have caused the losses.... the negligence, if there was any, was in Bayer’s handling of the GM rice that it controlled.... The risk that the GM trait might escape and contaminate other non-GM rice or other plants is precisely the known and foreseeable risk that Bayer undertook when it undertook to introduce the rice. Bayer’s duty included the duty to assure

that those it chose to test the rice followed proper procedures.”²⁶

Grain shippers, for their own part, have noted that intervening causes abound in developing countries, where hungry bystanders may take a few buckets worth of a grain shipment from railcars that are not well-guarded. These swarms of hungry intervenors are called “hormigas” (“ants”) in Spanish. To industry insiders, they are a foreseeable consequence of doing business when shipping corn to Mexico. If these U.S. biotech corn events end up circulating in the Mexico highlands, causing “contamination”, should the seed company, grain shipper or the U.S. be held responsible for this foreseeable harm to biodiversity? This is the legal issue being negotiated under the Biosafety Protocol.

Developing countries have sought a liability standard that would allow them to recover for economic loss from “contamination” of their non-GMO crops. The LL601 verdict will be a shot heard around the world and discussed in international liability negotiations taking place in June 2010 in Montreal. Developing nations have also expressed concern that the “channeling” approach to liability, which holds the importers liable and forces them to conduct transnational litigation or arbitration to collect under breach of contract, may actually serve to insulate manufacturers of dangerous goods from having to pay full compensation. For example, if the biotech seed companies have defenses to enforcement of a foreign judgment in their home jurisdiction (e.g., as in the Bhopal litigation, where the subsidiary of Union Carbide’s assets were the only ones exposed) or there is not complete tracing back to the biotech seed company, then channeling may not be an effective approach to compensation for economic harm.²⁷

A similar issue of “economic impact” lies at the core of other pending litigation enjoining biotech beets and alfalfa. Two U.S. federal district courts in California have enjoined further planting of biotech alfalfa and beets under the National Environmental Policy Act. The economic interests protected in the beets and alfalfa cases, in light of the duty of care established in the LL601 litigation, may give rise to a potential duty of seed companies to prevent

commingling before approvals for major export markets.

Faced with accusations from developing nations of an intent to dump “GMOs” on their environments, causing harm, and retreating behind legal walls, the biotech seed industry took a historic step into voluntary self-insurance for harm to biodiversity. The six largest global biotech seed companies, led by Monsanto, submitted the draft text of a voluntary arbitration system at a meeting of the parties drafting the supplemental liability protocol to the Biosafety Protocol. The voluntary “Compact” from the industry coalition led by Monsanto is a historic step forward for any industry in international liability law. But as the LL610 verdict illustrates, there are economic damages that do not relate to biodiversity and hence fall outside the intended scope of the Compact. Moreover, a grain trader facing “channel” liability may not have the same success against a biotech seed company as the LL601 plaintiffs. The direct contractual chain of commerce that exists with the sale of a biotech crop that lacks regulatory approval in an overseas market (e.g., the biotech corn lacking E.U. approval that has disrupted E.U. exports for several years) is a legally distinguishable fact pattern. Growers are told of the lack of approval, buy the corn with knowledge of that fact (actual or constructive), and have domestic markets that may absorb enough of this corn to mute any price impacts.

I. Would Other Conduct Disrupting Exports Constitute A Potential “Nuisance”

The facts of this case may present a relatively singular set of circumstances, given that the release involved an unauthorized release from a field trial of a variety of biotech crop that never reached the market. Bayer was deemed to have breached a duty that began with its field trial’s necessary containment under federal law. The summary judgment did not allow a defense for USDA’s approval that came after the commingling had occurred and disrupted export markets.

Under other facts involving trade disruption that occurs despite full US approval (e.g., the recent disruption of soybean meal exports to the EU due to commingling of foreign material corn)²⁸ courts may find the duty

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of care met by US approval despite similar economic losses (lost export markets). Other cases involving similar facts have resulted in defense verdicts on pretrial motions in the US²⁹ and Canada.³⁰

One emerging threat of liability, which will merit further discussion in industry dialogues, is the potential for “generic” biotech crops that are “off-patent” to become sources of trade disruption. Using a short hypothetical to illustrate, assume that another seed company (not Monsanto) seeks to market the Roundup Ready Soybean in 2015 when the patents have all expired. Further assume that this generic provider does not seek to renew regulatory approval in the E.U. and China through several renewals (e.g., 2016 for the E.U. and every 3 to 5 years for China). This failure to maintain Monsanto’s established standard of care for seeking overseas approvals could be deemed to be a breach of a duty of care – as set by the industry-wide standard of care for managing export-related impacts in soybeans. Could a court find a standard of care to have been violated outside the regulatory setting? This is a question that remains to be answered, but if the trade disruption is avoided, it need never be answered.

K. Conclusion

In conclusion, the verdict in this LL601 case is bad news for Bayer, but may not create a broad remedy at common law for the loss of an export market in a commodity crop. It should, however, direct new attention to stewardship initiatives for export-related economic impact. Bayer’s unauthorized release of LL601 was unlawful when it occurred, even if the subsequent regulatory review by USDA removed any duty to conduct a recall of rice in the U.S. In contrast, a seed company that is fully compliant with U.S. regulations, and also undertakes disclosure of the regulatory approval (or lack thereof) of the seed being sold, has *less* evidence of negligence than Bayer (with its alleged lack of oversight of its LL601 field trial), even if it fails to meet an industry standard for overseas approval. The Bayer rice order and accompanying jury verdict arising from the loss of an export market will likely redouble existing efforts at stewardship for overseas markets. Failure to take this seriously could lead to future claims that seek to push the boundary of biotech crop liability even farther than it was extended thus far in the LL601

rice litigation.

ENDNOTES

¹ A. Bryan Endres & Justin G. Gardner, *Genetically Engineered Rice: A Summary of the LL Rice 601 Incident*, Agric. L. & Tax Brief No. 06-04 (Dec. 2006).

² *In re Starlink Corn Prods. Liab. Litig.*, 212 F. Supp. 2d 828 at 841-42 (N.D. Ill. 2002).

³ The panel on multi-district litigation consolidated most of these lawsuits in the U.S. District Court for the Eastern District of Missouri. There are a few state court cases pending, as well.

⁴ USDA Workshop Presentation, *Hybrid Rice Production*, available at www.aphis.usda.gov/brs/confine_workshop/nelson_present.pdf.

⁵ CBG Coordination gegen BAYER-Gefahren/Coalition against BAYER-Dangers (Tr. Susanne Schuster), *GMO Rice: BAYER ordered to pay damages* (Dec 9, 2009) (3,000 claims expected after the \$2 million verdict) www.tlaxcala.es/pp.asp?lg=en&reference=9538. Yet another source indicates there are 6,000 rice producer claims filed against Bayer. See *Verdict Lands Farmers Money*, STUTTGART DAILY LEADER, (Fed. 8, 2010) at www.stuttgarterdailyleader.com/features/x644563964/Verdict-lands-farmers-money.

⁶ *In re Genetically Modified Rice Litigation*, 2009 U.S. DIST. LEXIS 98302, *62-63 (October 9, 2009) (hereinafter “LL601 MSJ”)

⁷ *Id.*

⁸ *Id.*

⁹ *Id.* at *64-65. See also RESTATEMENT 2D TORTS § 288B(2) (noting that where a statute “is found not to provide any standard of conduct applicable to the negligence action, violation is ordinarily not even considered to be relevant evidence” regarding the standard of care for negligence, but in some cases, the “fact of the violation may still be accepted as relevant evidence bearing upon the conduct of a reasonable man in the actor’s position”).

¹⁰ LL601 MSJ, *supra* note 7, at *68.

¹¹ *Sample v. Monsanto Co.*, 283 F. Supp. 2d 1088, 1092-94 (E.D. Mo. 2003).

¹² *In re Starlink Corn Prods. Liab. Litig.*, 212 F. Supp. 2d 828 at 841-42 (N.D. Ill. 2002).

¹³ LL601 MSJ at *47-48.

¹⁴ *Id.* at *83-87 (discussing share-rent landlord damages and denying Defendants’ motion for summary judgment).

¹⁵ See e.g., *In re Vioxx Products Liability Litigation*, MDL 1657 (U.S.D.C E.D. La.) (awarding punitive damages in “bellwether” test trial to one of thousands of plaintiffs) <http://vioxx.laed.uscourts.gov/Orders/Barnett.o&r.pdf>; *In re Vioxx Products Liability Litigation*, 448 F.Supp.2d 737 (E.D.La.,2006); *In re Vioxx Products Liability Litigation*, 448 F.Supp.2d 737, 738-39 (E.D. La. 2006).

¹⁶ *Philip Morris USA v. Williams*, 549 U.S. 346 at 356-57 (2007) (constitutionally protected defenses include individualized inquiries such as a plaintiff’s knowledge); Cf. *Dukes v. Wal-Mart, Inc.*, 474 F.3d 1214 at 1242 (9th Cir. 2007) (statistical formulas are employed to fashion the appropriate remedy).

¹⁷ LL601 MSJ at 26.

¹⁸ D. L. Uchtman, *StarLink™: Farmer and Elevator Claims for Economic Losses* (2001), available at http://www.farmdoc.uiuc.edu/legal/pdfs/StarLink_claim.pdf; see also, D. L. Uchtman, *StarLink – A Case Study of Agricultural Biotechnology Regulation*, 7 DRAKE J. AGRIC. L. 160-208 (2002).

¹⁹ *Biotech Firm Executive Says Genetically Engineered Corn Is Here to Stay*. Knight-Ridder, Available at www.organicconsumers.org/ge/starlinkforever.cfm (“The company has spent tens of millions of dollars to fix the problem, ... rerouted 28,135 trucks, 15,005 rail cars and 285 barges”).

²⁰ EPA White Paper Regarding StarLink[reg] Corn Dietary Exposure and Risk; Availability, 73 Fed. Reg. 22715-22716 (April 25, 2008) <http://www.epa.gov/fedrgstr/EPA-PEST/2008/April/Day-25/p9003.htm> (White Paper concludes that the Cry9C protein has been sufficiently removed from the human food supply to render the level of risk low enough that continued testing for the protein in yellow corn at dry mills and masa production facilities provides no added public health protection.)

²¹ Troy G. Schmitz, Andrew Schmitz & Charles B. Moss, Two Approaches to Measuring the Economic Impact of Starlink Corn on U.S. Producers, *Selected Paper*

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prepared for presentation at the American Agricultural Economics Association, Annual Meeting, Denver, Colorado, August 1-4, 2004) at 13, (2004), available at <http://ageconsearch.umn.edu/bitstream/20306/1/sp04sc04.pdf> (“But for StarLink-contaminated corn, U.S. corn producers would have received an additional U.S. \$1.3 billion in revenue”).

²² Uchtmann, *Starlink*, *supra*.

²³ LL601 MSJ at *91.

²⁴ *In re Genetically Modified Rice Litigation*, 2009 U.S. DIST. LEXIS 98302 (October 9, 2009).

²⁵ DOUGLAS HODGSON, *THE LAW OF INTERVENING CAUSATION* (Ashgate Publishing, 2008) (available on <http://books.google.com>).

com).
²⁶ *Id.* at 68-71 (discussing Bayer’s affirmative defense for intervening causation).

²⁷ International Institute for Sustainable Development, *Biosafety Policy Brief*, (February 7, 2007) available at <http://www.iisd.ca/africa/brief/briefing0501e.pdf> (“keep efficiency considerations in mind, such as how to channel liability to firms operating from abroad”); *see also*, Meridian Institute, *Dialogue on Liability and Redress Under the Cartagena Protocol on Biosafety*, (September 11 – 13, 2001) available at [www.merid.org/pdf/Liability_Meeting_Summary_\(Short\)_010920.pdf](http://www.merid.org/pdf/Liability_Meeting_Summary_(Short)_010920.pdf) (“some developing countries are

concerned about the difficulties associated with identifying a liable party”) (last visited January 17, 2010).

²⁸ Marybelle Ang, *A Slow Motion Tennis Match – GMO Debate Continues*, 14 ABA SEER Agricultural Management Newsletter 8 (January 2010) available at http://www.abanet.org/environ/committees/agricult/newsletter/jan10/AgMgmt_Jan10.pdf.

²⁹ *Sample v. Monsanto Co.*, 283 F. Supp. 2d 1088, 1092–94 (E.D. Mo. 2003).

³⁰ *Hoffman v. Monsanto Canada Inc. et al.* 2007 SKCA 47 (May 2, 2007) available at <http://www.saskorganic.com/oapf/pdf/2007SKCA047.pdf>.

THE MEANING OF “EXCESS FARM LOSSES”

by Neil E. Harl*

In an effort to curb the offsetting of farm losses against non-farm income, Congress in 2008 passed a provision as part of the 2008 “Farm Bill,” the Food, Conservation, and Energy Act of 2008.¹ Aside from the fact that it is unusual for a tax provision to be included in a farm bill, the legislation is also notable because of the uncertainty over the meaning of “aggregate gross income or gain” in the legislation.² The issue is important (1) because the definition of that term can affect a taxpayer’s handling of losses and (2) the Internal Revenue Code has similar language in different Code sections and the interpretations have not been the same in the resulting regulations.

The statutory provision

As enacted by Congress and signed into law, the 2008 provision specifies that, for taxpayers other than C corporations receiving an “applicable subsidy,” excess farm losses are disallowed as a deduction against non-farm income.³ The provision was effective for taxable years beginning after December 31, 2009.⁴

Meaning of “excess farm losses.” The term “excess farm losses” is defined as the greater of \$300,000 (\$150,000 for married taxpayers filing separately) or the net farm income for the previous five years.⁵

Disallowed losses can be carried forward to the next taxable year and subsequent years.⁶

Definition of “applicable subsidy.” The term “applicable subsidy” means any direct payments or counter-cyclic payments (or any payment in lieu of such payments) or any Commodity Credit Corporation (CCC) loan.⁷

What is a “farming business?” The legislation defines “farming business” as defined in I.R.C. Sec. 263A(e)(4) but *includes* income from processing activities.⁸

Losses disregarded. The provision specifies that casualty losses (fire, storm or other casualty)⁹ or losses by reason of disease or drought are to be disregarded in the calculations.¹⁰

Relationship to passive losses. The legislation states that the provision¹¹ is to be applied *before* the passive loss rules are invoked.¹²

Treatment of pass-through entities. For partnerships and S corporations, and presumably for other pass-through entities, the limitation is applied at the partner or shareholder level.¹³

A proportionate part of the income, gain or deduction as well as applicable subsidies are to be taken into account.¹⁴

If the taxpayer is a member of a cooperative to which Subchapter T applies, any trade or business of the cooperative is treated as a trade or business of the taxpayer.¹⁵

Meaning of “aggregate gross income”

The meaning of the term “aggregate gross income” is unclear.¹⁶ The term is not yet defined in regulations and is not discussed in the committee reports.¹⁷ However, similar although not identical language appears elsewhere in the Internal Revenue Code.

Soil and Water Conservation Expenditures. The Soil and Water Conservation Expenditure provision¹⁸ which was enacted in 1954 and which has been viewed widely as the most influential of the definitions, uses the term “gross income derived from farming.”¹⁹ However, that language was modified in the final regulations to include gains from the disposition of livestock held for draft, dairy, breeding or sporting purposes but gains from the sale or other disposition of farm machinery and land were not included.²⁰

Income averaging for farmers and fishermen. Income averaging for farmers and fishermen, in using the term “elected farm income,”²¹ in the statute and in the regulations refers to gain or loss from the sale or other disposition of property that is regularly used in the individual’s farming business for a substantial period of time except for land.²² The regulations make it clear that elected farm income includes the fixtures affixed to the land, however.²³

Estimated gross income from farming. The Internal Revenue Code, in the rules applicable

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for determining penalties for failure to pay estimated tax and providing the special treatment for farm taxpayers, refers to “gross income from farming or fishing.”²⁴ The regulations under the prior provision (I.R.C. Sec. 6073) have not been reissued under I.R.C. Sec. 6654(i) but rulings indicate that the term includes the gains from the sale of livestock used in the trade or business of farming and held for draft, dairy or breeding purposes but it does not include gains from the sale of “farm land” or farm equipment subject to an allowance for depreciation.²⁵ In this respect, the estimated tax provision parallels the soil and water conservation expenditure provision,²⁶ and indeed the key ruling issued in 1963²⁷ refers specifically to the soil and water conservation provisions and patterns the estimated tax rules after that provision’s guidance.

It should be noted that the entire gain including that from sales of farm land and equipment was part of total gross income against which the required two-thirds (from

farming) was measured.²⁸

It is likely, until regulations are issued (if they are) or other guidance is published, that it will not be clear what meaning is to be given to “aggregate gross income.”²⁹ However, the history of development of farm tax suggests that the Section 175 regulations have an edge in becoming the guidance for the “excess farm loss” provision.³⁰

ENDNOTES

¹ Pub. L. No. 110-246, § 15351(a), 122 Stat. 2285 (2008), adding I.R.C. § 461(j).
² I.R.C. § 461(j)(4). See Harl, “Food, Conservation, and Energy Act of 2008, Pub. L. No. 110-246 (the 2008 Farm Bill)” 19 *Agric. L. Dig.* 12 (2008).
³ I.R.C. § 461(j)(1).
⁴ Pub. L. No. 110-246, § 15351(b), 122 Stat. 2285 (2008).
⁵ I.R.C. § 461(j)(4)(B)(i).
⁶ I.R.C. § 461(j)(2).
⁷ I.R.C. § 461(j)(3).
⁸ I.R.C. § 461(j)(4)(D).
⁹ I.R.C. § 1033.

¹⁰ I.R.C. § 461(j)(4)(D).
¹¹ I.R.C. § 461(j).
¹² I.R.C. § 461(j) (7).
¹³ I.R.C. § 461(j)(5), (5)(A).
¹⁴ I.R.C. § 461(j)(5)(B).
¹⁵ I.R.C. § 461(j)(4)(C)(ii)(II).
¹⁶ See I.R.C. § 461(j)(4).
¹⁷ H.R. Conf. Rep. No. 110-627 to Pub. L. No. 110-246, *supra*.
¹⁸ I.R.C. § 175.
¹⁹ I.R.C. § 175(b).
²⁰ Treas. Reg. § 1.175-5(a)(2).
²¹ I.R.C. § 1301(a), (b)(1).
²² I.R.C. § 1301(b)(1)(B); Treas. Reg. § 1.1301-1(e)(1)(ii)(A).
²³ Treas. Reg. § 1.1301-1(e)(ii)(A).
²⁴ I.R.C. § 6654(i)(2)(A).
²⁵ Rev. Rul. 63-26, 1963-1 C.B. 295.
²⁶ I.R.C. § 175.
²⁷ Rev. Rul. 63-26, 1963-1 C.B. 295.
²⁸ Rev. Rul. 63-26, 1963-1 C.B. 295.
²⁹ I.R.C. § 461(j)(4).
³⁰ I.R.C. § 461(j).
* * * * *

THE LACEY ACT — ITS IMPACT ON AQUACULTURE

by Elizabeth R. Springsteen *

Aquaculture includes the cultivation of aquatic species for human consumption as well as for recreational or ornamental purposes. The practice has a long history, tracing back through ancient Chinese records indicating that carp was raised more than 4,000 years ago and hieroglyphics in the tombs of the Pharaohs describing tilapia farming in ancient Egypt. However, aquaculture in the U.S. has a much more limited history, beginning in the mid 1800s when federal and state hatcheries were built to raise various sport fish species for stocking public and private waters. Attempts to commercialize aquaculture for food purposes did not begin until the 1950s, with channel catfish farming in the Mississippi Delta region. From those small beginnings it has become an extensive industry, bringing in \$1.5 billion a year nationwide, with \$12.5 million of that revenue in the state of Minnesota, according to the 2007 Census of Agriculture.

The practice of aquaculture is regulated at several levels of government, with state and local authorities generally regulating

activities and issuing permits dealing with zoning, building, water use, waste discharge, and species certification related to wildlife management, marketing or processing. Due mainly to environmental concerns, requirements for each type of operation are varied, with states administering permits based on its own specific rules. As a result, regulations can vary considerably between geographic locations. At the federal level, agencies responsible for different areas of regulation include the FDA, USDA, EPA and Fish and Wildlife Service, or FWS.

One major statute with the potential to severely affect aquaculture is the Lacey Act, 18 U.S.C. §§ 41-48, a federal statute passed in 1900 to protect wildlife. It was originally intended to combat hunting to supply commercial markets, the interstate shipment of unlawfully killed game, the killing of birds for the feather trade and the introduction of harmful invasive species. The Lacey Act applies to all “wild” animals, specifically including fish and amphibians, even when those animals have been “bred, hatched, or born in captivity.” It is unlawful

to “import, export, transport, sell, receive, acquire or purchase” any fish or wildlife “taken, possessed, transported, or sold” in violation of laws or regulations (state, federal or foreign) that are fish- or wildlife-related. In 2008, plants were added to the scope of the Act.

Penalties for violating the Lacey Act are severe. If an individual “knew” or “was generally aware of” the illegal nature of the wildlife and the value of the wildlife was over \$350, he may be prosecuted and convicted under the Act’s felony provisions. If that happens, the penalty is up to 5 years in prison and/or a \$250,000 fine (\$500,000 in the case of an “organization,” including a business). Misdemeanor prosecution may occur in two situations. The first is if the defendant takes/possesses/transport/sells the prohibited wildlife “without exercising due care,” or negligently. The second is if the defendant knew about the illegal nature but the value of the wildlife was less than \$350. It is important to note, however that

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prosecutors may aggregate violations for charging purposes, potentially causing the offense to be elevated from misdemeanor to felony status. Misdemeanor penalties are up to a year in prison and/or \$100,000 fine (\$200,000 for organizations). Further, false labeling of wildlife transported in interstate commerce is also criminalized, regardless of intent. If the products have a market value of less than \$350, false labeling is a 1 year/\$100,000 misdemeanor, but if the value is greater than \$350, the offender may be charged with another 5 year/\$250,000 felony.

Federal enforcement of the Lacey Act is triggered when a state law regarding fish or wildlife is violated. This is important, especially considering the disparity between the state and Lacey Act penalties. For example, in Minnesota it is illegal to transport “prohibited invasive species” on a public road, and violation subjects the offender to a \$250 civil penalty or a misdemeanor (up to 90 days and/or \$1,000).

Each state has its own prohibited invasive species list, typically established by the state Department of Natural Resources (DNR), and the creatures on the list can vary widely from one state to the next.

How does this affect aquaculture? Imagine that a single fish (or even fish egg)- legal to possess in Wisconsin- is inadvertently loaded with a 2,000 lb truckload of other fish that had been sold to an aquaculture producer in Minnesota. This single fish is on the Minnesota prohibited list. Once the truck crosses the state line, it is stopped by the DNR, searched, and the prohibited fish is found. Both the seller and the buyer may be prosecuted under the Lacey Act, and what would have been a maximum penalty of 90 days and/or \$1,000 from the state of Minnesota has now turned into a potential year in federal prison and up to a \$100,000 fine. Moreover, the seller may also be charged with false labeling (for failing to include the prohibited fish in the list of the shipment’s contents), adding up to another

5 years and/or \$250,000 to the sentence.

The risks associated with the Lacey Act can, of course, be minimized by only shipping products in-state. However, this is not a reasonable or feasible option for many producers. For those producers involved in interstate shipment of aquacultural products, the only advice that may be helpful is to check, double-check and document every step taken to ensure that prohibited species are not transported, because their freedom and livelihood might depend on convincing a judge or jury that they exercised due care in trying to prevent it.

For more information on the legal aspects involved in aquaculture operations, please visit the National Agricultural Law Center’s “Aquaculture” reading room, located at <http://www.nationalaglawcenter.org/readingrooms/aquaculture/>

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EMERGING TRENDS IN CLASS ACTION LAWSUITS AGAINST FOOD MANUFACTURERS

by Judy Okenfuss & Julianna Plawecki*

Food manufacturers have been repeatedly hit with class actions in recent years. These cases are time-consuming and costly, diverting valuable resources from a company's mission. Fortunately, food manufacturers have recently had some success obtaining early dismissal of class actions. The manufacturers, who are seeking to avoid protracted litigation and costly discovery, have sought dismissal of the lawsuits through a motion to dismiss filed early in the case or by challenging class certification.

A motion to dismiss challenges the sufficiency of the complaint itself and generally does not consider facts outside the complaint. If a defendant is successful in having the complaint dismissed, and the plaintiff cannot fix the problems by amending the complaint, the litigation ends.

In a recent case, *Wright v. General Mills, Inc.*, a consumer challenged General Mills' marketing of its Nature Valley granola bars and other products as "100 percent natural" because the products contained high fructose corn syrup (HFCS). The consumer argued that HFCS is a man-made sweetener that does not occur in nature, and the advertising was therefore false, misleading and deceptive. The consumer sought economic damages for herself and all class members because the "100 percent natural" advertising led them to "purchase, purchase more of, or pay more for, these Nature Valley products."

However, the court found that "[t]his sparse allegation of injury" did not meet the pleading requirements set forth by the United States

Supreme Court. The court also found that other allegations claiming that members of the public were likely to have been deceived by the advertising and to have made their purchases based on a belief that "100 percent natural" would not include a highly processed ingredient such as HFCS were inadequate. The court dismissed the complaint but gave the consumer an opportunity to file an amended complaint. The plaintiff elected not to do so and withdrew the claim.

Manufacturers have also sought to end cases at class certification stage because the claims asserted in class actions are generally not cost-effective to pursue on behalf of a single individual. Thus, if a defendant can show that a case is not appropriate for treatment as a class action, the plaintiffs (and their lawyers) typically lose interest in the case.

On January 6, 2010, the Ninth Circuit Court of Appeals handed down a victory for defendants. In *Kennedy v. Natural Balance Pet Foods*, the plaintiff sought to represent a nation-wide class of all individuals who purchased Natural Balance pet food that was labeled as having been made in the United States but contained an ingredient made in China. The Ninth Circuit affirmed the district court's denial of class certification, holding that the plaintiff had failed to satisfy the predominance requirement of Federal Rule of Civil Procedure 23(b)(3). The plaintiff had included claims under multiple states' consumer fraud statutes, arguing that the statutes were "substantially similar." However, the Ninth Circuit held

that where different states' laws would apply to the claims, the class plaintiff must provide a thorough analysis of the applicable laws in order to show that common issues predominate, which the plaintiff failed to do.

The Ninth Circuit also rejected the plaintiff's argument that the district court should have certified a nationwide class for his claim under California's Unfair Competition Law. The Ninth Circuit held that the district court was not required to certify only a subclass or a class with respect to particular issues.

These cases bode well for food manufacturers seeking early dismissal of class actions, but one or two cases do not make a trend. There are several other cases currently pending involving food manufacturers which will address these same issues and, hopefully, further develop this emerging trend.

* * * * *

"Discourage litigation. Persuade your neighbors to compromise whenever you can. As a peacemaker the lawyer has superior opportunity of being a good man. There will still be business enough."
-Abraham Lincoln

* IceMiller, LLP

NO ESTATE TAX CERTAINTY (YET)

by Kevin Alerding*

Last minute Congressional efforts to extend the federal estate tax into 2010 were side-lined by the focus on health care reform. Consequently, the estate tax has been repealed effective January 1, 2010.

What are the new rules?

The law now provides that there is no federal estate tax for those who die this year. Instead, complicated carry-over basis

rules apply for property inherited in 2010. Also, there currently is no federal generation skipping transfer tax. The gift tax remains, however, along with the \$1,000,000 lifetime gift tax exemption and \$13,000 annual exclusion. The gift tax rate has dropped to 35 percent.

Lawmakers say they will address the estate tax later this year, and a variety of proposals

have been discussed. If a new estate tax law is passed in 2010, some senators and representatives have expressed an intention to make its application retroactive to January 1, 2010.

If lawmakers do not pass new estate tax legislation in 2010, then the estate tax would reappear for persons dying in 2011 and later, with a \$1,000,000 exemption.

ESTATE TAX		
2009	2010	2011
\$3,500,000 federal estate tax exemption	No federal estate tax	\$1,000,000 federal estate tax exemption
Step-up in basis on all assets included in decedent's estate	\$1,300,000 of basis step-up available for all decedents, plus \$3,000,000 of basis step-up for assets passing to a surviving spouse	Step-up in basis on all assets included in decedent's estate

The generation skipping transfer tax would come back, too, along with a projected \$1,100,000 exemption.

GENERATION SKIPPING TRANSFER TAX		
2009	2010	2011
\$3,500,000 federal generation skipping transfer tax exemption	No federal generation skipping transfer tax	\$1,100,000 (projected) federal generation skipping transfer tax exemption

The gift tax would remain in place through 2010, and it too would be subject to a \$1,000,000 exemption.

GIFT TAX		
2009	2010	2011
\$1,000,000 federal gift tax exemption	\$1,000,000 federal gift tax exemption	\$1,000,000 federal gift tax exemption
Exclusion from gift tax for gifts of \$13,000 per year / per donor / per donee	Exclusion from gift tax for gifts of \$13,000 per year / per donor / per donee	Exclusion from gift tax for gifts of \$13,000 (projected) per year / per donor / per donee

The top marginal estate, gift, and generation skipping tax rate would be 55 percent.

TAX RATES		
2009	2010	2011
45 percent top marginal tax rate for gift, estate, and generation skipping transfer taxes	35 percent top marginal tax rate on lifetime taxable gifts	55 percent top marginal tax rate for gift, estate, and generation skipping transfer taxes

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Alerding—NO ESTATE TAX CERTAINTY (YET) cont. from p. 11)

Keep in mind that these rules for 2010 and 2011 could well change if Congress does, in fact, pass a new tax law this year.

Is there anything to do about 2009?

If you made taxable gifts in 2009 be sure to report them on a gift tax return, due on April 15, 2010. If you made large reportable gifts to your grandchildren in 2009 or earlier and have not yet allocated generation skipping transfer tax exemption to them, you should consider making that allocation when you file your 2009 gift tax return.

What to do in 2010?

Since the generation skipping transfer tax is not in effect now, you might choose to make additional gifts to grandchildren and great-grandchildren in 2010. But in doing so you could risk triggering a now uncertain tax if Congress enacts a new generation skipping transfer tax in 2010 and makes it retroactive to January 1.

Also, 2010 might be a good year to make gifts that would result in the payment of gift tax, because the tax rate is lower (35 percent) than it was in 2009 (45 percent), and lower than it is scheduled to be in 2011 (55 percent)... subject to possible retroactive application of a new tax law.

You also should consider updating your personal financial statement to include a record of your tax basis in each asset. This information might become important if carry-over basis stays in effect for 2010 or beyond.

What about my estate planning documents?

Many estate plans include provisions that were used to minimize federal estate and generation skipping taxes. If individuals with such provisions die this year, it may be difficult to implement some of those provisions during this period, when the estate and generation skipping taxes are temporarily not applicable. And in some cases, if a person dies during this period of tax repeal, her or his plan could result in serious unintended consequences, such as the disinheritance of beneficiaries whose bequests were dependent on a tax structure that now has been repealed. Prudence dictates that those estate plans be updated to take into account that there is no estate tax currently in effect.

As uncertain as the estate tax is now, it is a useful reminder that it is essential that estate plans be kept up-to-date.

**“Farming looks
mighty easy when your
plow is a pencil, and
you’re a thousand miles
from the corn field.”
—Dwight D. Eisenhower**