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"Reading maketh a full man, conference a ready man and writing an exact man."

— *Francis Bacon*

Cooperative patronage dividends

The United States Claims Court recently issued an opinion in *Cotter and Company v. United States* (Case No. 493-82T, Aug. 30, 1984), concerning the deduction of patronage dividends made to patrons under Section 1382(b) of the Internal Revenue Code. The court considered three categories of income which had been returned to patrons: (1) interest income from the investment of surplus cash; (2) rental income from the leasing of excess warehouse space; and (3) rental incomes derived from other users of the cooperative's warehouse sprinkler system. The court also calculated the cooperative's charitable contribution deduction, using the maximum limit established for corporations of 5% of taxable income.

—*Terence J. Centner*

Reagan vetoes extension of Equal Access to Justice Act

Apparently acting at the behest of the Department of Justice, the Office of Management and Budget and various other federal agencies, President Reagan vetoed a unanimously passed bill extending the life of the three-year old Equal Access to Justice Act (EAJA), which expired under a sunset provision on Oct. 1, 1984. The President's November 9 veto message, however, expressed his hope that the new Congress will pass a somewhat different version of the bill, applicable retroactively to cases initiated on or after October 1.

The EAJA, which became effective Oct. 1, 1980, was enacted to deter government agencies from acting in an arbitrary fashion. Under the statute, citizens and small businesses may recover attorneys' fees when they successfully defend themselves against government action which a court finds not to be substantially justified. Although critics of the legislation feared a severe drain on the federal budget, fee awards under the EAJA over the past three years have totaled only about $3.5 million dollars, considerably less than the $350 million initially estimated.

In his veto message, Reagan reiterated his basic support for the EAJA, but noted his disapproval of a key provision in the reauthorization bill that would have altered the test used in determining whether the government's position was substantially justified. The federal courts, interpreting the original statute, have split on the question of whether the underlying governmental conduct or its position in court is to be examined in determining substantial justification. Compare *Tyler Bus. Serv. Inc. v. NLRB*, 695 F.2d 73 (4th Cir. 1982) (litigation position) with *Natural Res. Defense Council v. EPA*, 703 F.2d 700 (3d Cir. 1983) (underlying governmental position).

The reauthorization bill would have required that an agency's underlying action, not only its position in court, be substantially justified before a prevailing party can be denied attorneys' fees. Such an approach seems consistent with the purpose of the EAJA, which was designed to proscribe frivolous governmental action that requires a party to resort to the courts to vindicate his rights. The president's veto message, however, took the position that the revised bill "would result in needless and wasteful litigation over what is supposed to be a subsidiary issue and would further burden the courts. . ."

Despite his objection to this provision, as well as to new language that would require interest payments on fees not paid within 60 days, Reagan stated that he intends to make the permanent and retroactive reauthorization of the EAJA "a high legislative priority of the administration in the next Congress." Accompanying the veto message was a memorandum to agency heads, instructing them to en-

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Sales of secured property and dischargeability under the Bankruptcy Code

As more and more farmers experience financial distress, it is increasingly common for them to liquidate collateral subject to an Article 9 security interest in an attempt to provide for family living expenses and to generate operating capital. In such cases, secured parties are not likely to receive any part of the proceeds from the liquidation. A new line of cases appears to be developing involving challenges by the secured parties to the dischargeability of the underlying debt when these farmers file petitions under the Bankruptcy Code.

In Re Betzler, Bky, #5-83-39 (Bkrtcy. Minn., June 25, 1984) involved a farmer who had regularly sold hogs with the knowledge of the secured party. The farmer made periodic payments to the secured party and provided periodic reports on the value of the collateral. When it became obvious that the operation could no longer support itself, the farmer began to liquidate the hog herd with the knowledge and consent of the secured party.

However, the liquidation proceeds were used for operating, liquidation and family living expenses. The farmer subsequently filed a Chapter 7 bankruptcy petition. The secured party sought to bar the dischargeability of the underlying debt pursuant to 11 U.S.C. §523(a)(6), given the misuse of the sales proceeds.

The court held that the debtor had received no benefit from funds devoted to operating and liquidation expenses and that the lender would have incurred similar expenses had it liquidated the herd itself.

With regard to family living expenses, the court held that the use of collateral for personal subsistence does not, by itself, constitute the type of "willful and malicious" conversion required to bar a discharge of indebtedness under §523(a)(6). A similar result was reached in *In Re Simpson*, 29 B.R. 202 (Bkrtcy. N.D. Ia. 1983). See also *In Re Lloyd*, 11 B.C.D. 1297 (Bkrtcy. E.D. Tenn. 1984).

—Phillip L. Kunkel

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sure that their positions are "substantially justified" and to "accept and retain on file" applications for fee awards during the period prior to passage of new legislation.

Given Congress' unanimous passage of the reauthorization bill in the fading days of the last session, it has been speculated that an identical bill will be sent to the president shortly after the new Congress convenes, thus raising the possibility of an attempted override of any veto.

Although the EAJA has not frequently been used in Department of Agriculture cases, recent cases demonstrate its utility in that regard. For example, in *Gold Kist Inc. v. USDA*, 741 F.2d 344 (11th Cir. 1984), Gold Kist was assessed $70,600 in civil penalties for violating the Department's peanut marketing and handling regulations.

The company unsuccessfully argued in district court that the agency had no authority to issue regulations providing for such penalties, but the Eleventh Circuit Court agreed with Gold Kist and reversed. The appellate court also instructed the district judge to consider on remand Gold Kist's request for attorneys' fees under the EAJA, since the company had become a "prevailing party" on appeal.

—John Watkins
University of Arkansas

Supreme Court upholds FIFRA registration laws

The Supreme Court has upheld provisions governing the use and disclosure of pesticide registration data under the Federal Insecticide, Fungicide and Rodenticide Act (FIFRA). See *Ruckelshaus v. Monsanto Co.*, 104 S. Ct. 2862 (1984). FIFRA requires pesticide manufacturers to submit test data for new products and it authorizes the Environmental Protection Agency (EPA) to use data submitted by one applicant in evaluating the application of a subsequent applicant. The law also allows for public disclosure of health and safety data submitted by all applicants.

Monsanto asserted that disclosure of the data by the EPA and acquisition of this information by competitors constitutes a "taking" of its property under the Fifth Amendment. The Court agreed that Monsanto has a federal law property interest in its health and safety data, at least to the extent that the data is "cognizable as a trade secret property right" under state law. But the Court held that the use or disclosure of such data does not result in a taking unless FIFRA affirmatively provides a basis for a "reasonable, investment-backed expectation" of confidentiality and exclusive use.

Specifically, the Court held that federal laws did not provide such an expectation for data submitted to the EPA prior to Oct. 22, 1972, because FIFRA was silent with respect to the use of such data up to that time. Similarly, after the 1978 amendments to the law (effective Oct. 1, 1978), the Court

held that Monsanto was on notice of the manner in which the EPA was authorized to use and disclose any data turned over to it by an applicant for registration. The Court concluded that "if, despite the data consideration and data disclosure provisions in the statute, Monsanto chose to submit the requisite data in order to receive a registration, it can hardly argue that its reasonable, investment-backed expectations are disturbed when the EPA acts to use or disclose the data in a manner that was authorized by law at the time of submission."

During the interim period, however, the statutory scheme then in effect prohibited the EPA from publicly disclosing test data or considering such information in connection with the application of another if both the original applicant and the EPA determined the data constituted trade secrets.

Thus, the Court concluded that the federal government had "explicitly guaranteed to Monsanto and other registration applicants an extensive measure of confidentiality and exclusive use." Consequently, the Court held that if the EPA were now to use or disclose trade secret data in a manner not authorized by the version of FIFRA in effect between 1972 and 1978, that action might constitute a taking.

Monsanto had also argued that these FIFRA provisions effect a taking for a private use, rather than a public use, as required by the Fifth Amendment, because the statute forces original submitters to share their data with later applicants.

The Court rejected this claim by noting that even though the most direct beneficiaries of the law may be private companies, the statute furthers the important public purpose of eliminating costly duplication of research and streamlining the registration process, thereby making new end-use products available to consumers more quickly. So long as the taking has a conceivable public character, the Court concluded, the means by which that goal will be attained is for Congress to determine.

The Court also held that a Tucker Act remedy is available to provide just compensation for whatever takings may occur under the law. The Tucker Act, 28 U.S.C. § 1491, provides a cause of action for federal takings. Monsanto had argued, and the district court had agreed, that Congress intended the compensation scheme in FIFRA to be exclusive, thereby precluding any recovery under the Tucker Act. But the Supreme Court concluded that FIFRA merely requires a claimant to pursue the statutory remedy as a precondition to the Tucker Act claim. The Tucker Act remedy can therefore cover any shortfall between the statutory remedy and just compensation.

The *Monsanto* decision has apparently not resolved all legal questions concerning FIFRA registration laws, however. A federal district court in New York has declared unconstitutional the statute's binding arbitration procedures. See *Union Carbide Agricultural Products Co. v. Ruckelshaus,* 79 Civ. 2913 (S.D.N.Y. 1984), *prob, juris noted, Ruckelshaus v. Union Carbide Agricultural Products Co.,* 105 S.Ct. ______ (Nov. 26, 1984).

Section 3(c)(1)(D) of the Tucker Act requires a subsequent applicant for registration to offer reasonable compensation for the use of another applicant's test data. If the parties cannot agree on a sum, they must submit to binding arbitration. Awards made by arbitrators selected under the statute are subject to judicial review only on a showing of "fraud, misrepresentation or other misconduct." 7 U.S.C. §136a(c)(1) (D).

The federal district court has concluded that this procedure impermissibly intrudes on decision-making authority entrusted to the judiciary under Article III of the U.S. Constitution. The court is apparently adhering to its prior conclusion that FIFRA unlawfully deprives a federal court of its assigned role in ensuring the provision of fair compensation to data submitters. *Union Carbide Agricultural Products Co. v. Ruckelshaus,* 571 F. Supp. 117, 124 (S.D.N.Y. 1983).

This 1983 decision had been appealed to the Supreme Court, but the Court sent it back to the trial judge for reconsideration in light of the *Monsanto* opinion. The trial judge then reiterated his decision that the law is unconstitutional. On November 26, the Supreme Court noted probable jurisdiction to review the issue. The Court will probably schedule oral arguments sometime in Spring 1985.

— *David A. Myers*

Alabama: FmHA loans protected under 5th amendment

The 11th U.S. Circuit Court of Appeals directed the district court for the Southern District of Alabama to enter a preliminary injunction precluding the Farmers Home Administration (FmHA) from using Alabama's nonjudicial foreclosure procedure to foreclose on delinquent borrowers under the Rural Housing Loan Program of Section 502, Title V of the Housing Act of 1949. *Johnson* v. *United States Department of Agriculture*, 734 F.2d 774 (11th Cir. 1984). The 11th U.S. Circuit Court concluded that the FmHA loans were statutory entitlements and thereby qualified as property interests protected by the Fifth Amendment's Due Process Clause.

The issue of whether the nonjudicial foreclosure procedure deprived borrowers of notice and a meaningful opportunity to be heard prior to the forfeiture of their property interests was left for determination by the trial court.

— *Terence J. Centner*

North Dakota "Confiscatory Farm Price" statute

For the first time since it was enacted some 50 years ago during the Great Depression, the North Dakota "Confiscatory Farm Price" statute is being subjected to judicial interpretation. N.D. Cent. Code §§ 28-29-04 - 28-29-06.

The statute grants North Dakota courts special discretionary authority "until the price of farm products produced in this state. . . equal at least the cost of production," to extend time of foreclosure proceedings and to delay execution on judgments where strict legal proceedings would result in the confiscation of property by forcing sale of agricultural products upon a ruinous market, or the "depriving a debtor of his home and confiscating his property." The statute allows courts to take judicial notice of whether or not prices of farm products are confiscatory.

Recently, the North Dakota

(continued on page 7)

Curing defective special use valuation elections: An examination of Section 1025 of the Deficit Reduction Act of 1984 and its legislative history

*By Richard L. Dees**

Farm estate planning professionals throughout the country are aware that the Internal Revenue Service (IRS) has adopted a policy of denying an estate's special use valuation election under Section 2032A of the Internal Revenue Code solely because the notice of election or agreement to special use valuation filed with the federal estate tax return is not in exact compliance with the regulations.[1] Section 1025 of the Deficit Reduction Act of 1984 (DRA) was enacted to reverse this policy.

Section 1025 amends Section 2032A to instruct the Secretary of the Treasury to provide procedures permitting 90 days to perfect an election or agreement which substantially complies with the provisions of the regulations relating to the special use valuation election, but contains one or more technical defects. The effect of this amendment is not to permit more estates to qualify for the benefits under Section 2032A, but merely to insure that farm families which otherwise qualify are not precluded from qualifying solely because of technical defects in the election or agreement.

This amendment retroactively reverses the IRS policy and applies to the estates of decedents dying after Dec. 31, 1976. Estates whose Section 2032A elections were denied because of a technical defect which is curable under Section 1025, have until July 18, 1985 to file a claim for refund. Practitioners will want to review their files where a Section 2032A election has been denied on technical grounds to determine whether refund claims should be filed prior to this date.

In the waning hours of debate on the new tax bill, Illinois Senator Alan Dixon sponsored the amendment which was to become Section 1025 of the Act. In his floor speech,[2] Senator Dixon stated the purpose of the amendment:

Mr. President, this is a very simple and straightforward amendment. It attempts to deal with a policy of at least certain agents of the IRS that has the effect of undermining the actions Congress has taken to try to preserve family farms and other small family businesses.

• • •

The law and the report [to the Tax Reform Act of 1976] both state the public policy issue directly and forcefully. Congress wants to continue the family farm and small, family-owned enterprises. Congress does not want the death of the owner of a family farm or a small, family-operated business to force the sale of that farm or business if the family wants to stay in farming or the small business. The idea was to not permit the federal estate tax to destroy family farms or small businesses.

There seem to be people at the IRS, however, who are not interested in preserving family farms and small businesses, and who want to use the slightest technicality to prevent an estate from being valued under the provisions of Section 2032A. Let me give you two examples of steps the IRS seems willing to take in its effort to break up family farms and small businesses.

• • •

Mr. President, as I read subsection (D) [sic] of Section 2032A, the IRS already has sufficient discretion to permit parties to correct any good faith technical mistakes they make when filing applications for this special valuation treatment. However, the service seems to take the opposite view. Clarification of Congressional intent by amending the section is therefore necessary.

• • •

This may all sound very obscure and unimportant. But it is very important to family farmers and family-operated, small businesses. These families want a chance to be able to continue their family traditions through the generations. Congress has clearly decided to give them that opportunity and not to let the death of the head of a family force the sale of the family farm or business because of the need to pay federal estate taxes.

• • •

Farm estate planning professionals, however, should be aware that the conference report under Section 1025 does not reflect Senator Dixon's indictment of the IRS' narrow construction of Section 2032A. Instead, the Manager's Statement[3] adopts an extremely restrictive reading of the amendment. The Manager's Statement also endorses several of the more extreme positions taken by the IRS in the Final Regulations. Farm estate planning professionals should be aware of the more controversial aspects of the Statement in order to counter its potential use by the IRS.

The Manager's Statement contains none of Senator Dixon's eloquent criticism of the IRS' use of technical defects in an election to deny the benefits of special use valuation to the farm families which Congress intended to benefit. The failure to recite this important legislative history may mean that Congress has failed to send a message to the IRS that it should concentrate on the substantive aspects of Section 2032A elections rather than mere technical defects.

In fact, there are indications that the IRS has already hardened its position on strict compliance with the Final Regulations in response to the Manager's Statement. For example, the author has been told that in one IRS district, the IRS now sends an automatic notice citing the Manager's Statement and denying the Section 2032A election when an estate tax return is re-

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ceived, indicating that special use valuation is being elected, but without substantially all of the required information attached.

Prior to the amendment, the same IRS district would send a form agreement to the estate to be signed where the Section 2032A election box was checked and Schedule N was completed on the federal estate tax return. The experience of the author and others with IRS field agents bears out the hardening of the IRS position during the last few months.

This hardening of the IRS position increases the likelihood that the Manager's Statement will be cited by the IRS in taxpayer disputes. While Senator Dixon's statement from the Congressional Record can be cited in order to counter IRS use of the Manager's Statement, practitioners should be aware that the new IRS "hardline" position unfortunately finds *support* in the Statement.

First, although the Statement provides that the Senate amendment was adopted without change, the language requiring "substantial compliance" with the regulations was *not* in the original amendment offered by Senator Dixon as reported by the Congressional Record and as approved by the Joint Tax Committee staff. While this addition does not by itself support the IRS position, when coupled with the extremely narrow interpretations in the Statement the false conclusion might be reached (if Senator Dixon's comments are ignored) that little change in the law was intended. This latter notion was reinforced by the release, shortly after Senator Dixon's amendment was passed, of the first ruling permitting the correction of certain, very minor defects in a Section 2032A election.[4]

Secondly, the examples contained in the Manager's Statement are very restrictive. The Statement, of course, appropriately cites Senator Dixon's two examples where a parent, rather than a guardian, signed for a minor. However, the Statement goes further and states that perfection is *limited* to such extreme cases. These examples were selected to demonstrate the most egregious of the IRS' positions and cannot be viewed apart from Senator Dixon's broader statements of the purpose of the amendment.

In one example, the Statement is actually more restrictive than current law. This example provides that the amendment authorizes copies of written appraisals to be submitted later, but requires that the appraisals must have actually been completed before the election is filed. The IRS has ruled that where farmland was valued pursuant to the five-factor formula under Section 2032A, comparable cash rents can be filed later and the special use value method changed.[5] The Manager's Statement seems to indicate that the IRS' current position is not required.

Thirdly, the Manager's Statement sets forth a *de minimis* test based on actuarial values as to who must sign the agreement filed with the election in order to permit perfection thereafter. This test is not supported by any legislative history connected with the Dixon amendment. Based upon this new test, at least one IRS agent has taken the position that a guardian cannot be appointed to sign for minor grandchildren after the return is filed if the aggregate actuarial value of the grandchildren's interests exceeds 5% — despite the explicit language of the two examples. If the IRS adopts the actuarial value test, a substantial amount of litigation is likely to ensue as it is not supported by the literal language of the statute nor Senator Dixon's statement of purpose.

In arguing for a liberal interpretation of "substantial compliance," the practitioner can point to Senator Dixon's speech and the harm these extremely technical rules do to the farm families that Section 2032A was intended to benefit. Practitioners can also point to the lack of any tax policy objective which requires these extremely technical rules. The IRS does not need all of the information and signatures on the agreement required by the regulations at the time the election is made in order to administer the statute properly.

The Final Regulations and recent rulings permit a protective election to be filed which includes only a minimal amount of information and no agreement.[6] By using a protective election, the Section 2032A election can be perfected later, even though at the time the protective election was filed, the estate could have filed a complete election.

In addition to creating controversy over the meaning of "substantial compliance" in the amendment, footnote 1 of the Manager's Statement has created a separate controversy unrelated to Senator Dixon's amendment.[7] The first sentence of the footnote states that the conferees are aware that the IRS' current regulation on successive interests created in qualified real property is correct. In fact, the validity of the successive interest rule is a matter of much debate. Moreover, this statement should be considered irrelevant in the context of an amendment not dealing with qualification, but only with technical defects in the election.

The harshness of the successive interest rule is illustrated by a case currently awaiting decision in the Tax Court. The issue in the case is whether a devise of farmland to a trust can qualify for Section 2032A where the trust benefits descendants of the decedent, but also provides for a gift over to charity in the event all of the descendents die before the trust terminates.

The probability that the property would ever pass to charity is only 1½% and the probability that the property would pass to charity within the 15-year recapture period[8] is negligible. Yet, the Manager's Statement states that even this extreme unlikelihood that the property would actually pass to a non-family member (including a tax exempt entity) is sufficient to deny the benefits of Section 2032A to an otherwise qualifying farm family. It seems highly unlikely that Congress ever intended this result.

Nevertheless, the government in the Tax Court case has cited footnote 1 of the Manager's Statement in support of the successive interest rule, even though the arguments in the case were completed more than a year ago. This is not the first time that the government has cited legislative history associated with amendments to Section 2032A to support a questionable regulation which is unsupported by contemporaneous legislative history.

Worst of all, this unfavorable legislative history cited against farm families is generally connected with amendments which Congress intended to ben-

efit those same farm families. For example, the decision in *Schuneman v. United States*,[9] upholding the application to farming of the IRS' "qualified use" test in the Final Regulations, relied primarily on the legislative history associated with the 1981 tax act *retroactively* overruling the IRS' pre-death qualified use test.[10]

The successive interest rule was originally inserted into the Final Regulations without an opportunity for comment, contrary to the spirit of the administrative procedure rules.[11] This provision, virtually unsupported by any legislative history or statutory language, has been and continues to be challenged. In fact, the regulation has never been found valid and before the appearance of footnote 1, was unsupported by any authority.

Even the IRS is not completely convinced as to the reasonableness of its successive interest rule and is currently studying liberalization of the rule. Personnel from the IRS met with representatives of the Agriculture Committee of the Taxation Section of the American Bar Association (ABA) in May 1984 to consider comments regarding proposed regulations to modify the successive interest rule. Footnote 1 may eliminate the incentive for the IRS to work with tax professionals to develop a reasonable successive interest rule.

The Final Regulations also required that if the decedent owned an undivided interest in real property, the cotenants must also sign the agreement consenting to Section 2032A, even though they do not receive any interest in the decedent's estate. Footnote 1 of the Manager's Statement also provides that this questionable rule is correct.[12]

Footnote 1 is likely to be cited by the IRS in support of its position in the Final Regulations regarding the successive and concurrent interest rule. Farm estate planning professionals should be aware that footnote 1 is controversial and that the validity of these regulations is being litigated. The actual language of the official "Blue Book," published by the staff of the Joint Committee and due out later this year, should also be examined. It is possible that the controversial aspects of the Manager's Statement may be eliminated or modified.[13]

1. *See, e.g.*, Letter Ruling 8416077 (undated) (no corporate resolution authorizing corporate officer to sign agreement); Letter Ruling 8416002 (Dec. 14, 1983) (grandchildren with contingent interests did not sign); Letter Ruling 8412014 (Dec. 2, 1983) (tenant-in-common with decedent did not sign). No public ruling has yet been issued on this issue.
2. Congressional Record — Senate at 4318-19 (April 11, 1984).
3. Conf. Rep't H.R. 4170, Joint Explanatory Statement of the Committee of Conference, at 1240-41.
4. Letter Ruling 8422008 (Feb. 2, 1984) published CCH Letter Rulings Reports (June 6, 1984).
5. Letter Ruling 8227004 (March 17, 1982).
6. *See, e.g.*, Letter Ruling 8407005 (Nov. 8, 1983).
7. The footnote states:

   The conferees are aware that the current use valuation provision requires that, when successive interests or concurrent interests are created in specially-valued property, all parties with any interest in the property must be qualified heirs and all such parties must enter into the agreement to the election, regardless of the relative values of their interests. The de minimis rule established in this provision is intended to apply solely as a guideline in determining whether perfection of an agreement is to be permitted. The guideline is not intended to give rise to an inference that parties having an interest in specially-valued property, which has a relatively small value, are not required to enter into the agreement or that such persons need not be qualified heirs.

   Inexplicably, CCH Standard Federal Tax Reports, Extra Edition No. 31, ¶2302 (July 18, 1984) at 1134-35 omitted the footnote.
8. Now 10 years. *See* IRC §2032A(c)(1).
9. 570 F. Supp. 1327 (C.D. Ill. 1983).
10. Economic Recovery Tax Act of 1981 §421(b)(1).
11. *See* T.D. 7710 (July 28, 1980).
12. *See* J. Dennis — Strathmeyer, *The IRS Requires Co-Tenants to Consent to Section 2032A Special Use Valuation Elections: Overreaching or Confusion?* TAXES 549, 553 (August 1984):

    In any event, the IRS' position is unsupported by statutory history and produces bizarre inconsistencies. If the issue reaches the courts, there is little doubt about what will result. Indeed, unless the IRS attempts to modify its position, the most contested issue may involve the amount of the taxpayer's attorney fees.
13. The comments of practitioners concerning the Manager's Statement are being solicited. The Agricultural Committee of the ABA Section of Taxation has agreed to prepare comments critical of the more controversial aspects of the Statement discussed in this article.

Iowa: breach of implied warranties

Van Wyk v. Norden Laboratories Inc., 345 N.W.2d 81 (Iowa 1984). This case involved a claim by a cattleman against the producer of a cattle vaccine for damages stemming from the death of 50 cattle and the sickness of hundreds of other cattle, allegedly caused by the use of the producer's bovine virus diarrhea vaccine.

The district court had submitted only the theory of liability, based on implied warranty of fitness for a particular purpose and had entered a judgment for the cattle owners. The Iowa Supreme Court reversed the decision and ruled that fitness for a particular purpose was not a proper theory for recovery because a) the transaction did not show sufficient bargain-related aspects to demonstrate the required knowledge and reliance and b) even though the product involved has a very specialized use, it cannot be presumed that the buyer was relying on the producer and that the producer knew of this — where the product could be misused. In so doing, the court clarified the difference between warranties of fitness for a particular purpose and merchantability.

The Iowa Supreme Court remanded the case and ruled that it was an error of the district court to not submit the cattle owners' claims on the theories of liability for breach of warranty of merchantability and strict liability.

—Neil Hamilton

NORTH DAKOTA
CONTINUED FROM PAGE 3

Supreme Court held that any set of facts that can be pleaded as a defense or counterclaim in an *action to foreclose* may provide the basis for enjoining *foreclosure by advertisement. Folmer v. State,* 346 N.W.2d 731 (N.D. 1984). It is not necessary that a debtor prove that prices for farm products are confiscatory as a prerequisite to seeking the injunction.

A debtor need only allege by affidavit sufficient facts to appraise the court of a possible defense or counterclaim. The evidence pertinent to the counterclaim or defense will be heard in the subsequent *action to foreclose.*

A second issue is whether farm prices are in fact confiscatory. In recent months, two North Dakota district courts have ruled that current prices are not confiscatory. One decision sets forth a balance sheet test that requires a finding that prices of farm products are not confiscatory if a farmer's equity position (whether increasing or decreasing overall) will be greater if he plants, rather than forgoes a crop. *United Bank v. Martineson,* No. 34137 (South Central Dist., N.D., Aug. 29, 1984). A second court judicially noticed that current prices are not confiscatory. *Federal Land Bank v. Bagge,* No. 8403 (Dist. Court for Traill Co., N.D., Oct. 19, 1984).

Other issues are likely to arise, including: whether the statute is unconstitutionally vague; whether it has expired under its own terminology; and whether it applies to federal agencies.

— *David Saxowsky*

Iowa enacts supplier's lien law

In 1984, the Iowa legislature passed and the governor signed S.F. 510, to be codified as Chapter 570A, the Code of Iowa. The legislation, which became effective July 1, 1984, is commonly known as the supplier's lien law and was a response to concerns about losses experienced by agricultural suppliers as a result of their unsecured status on credit sales to farmers.

The legislation applies to dealers of agricultural chemicals, fertilizers, seed, feed and petroleum fuel. The legislation creates a lien in the favor of the agricultural supplier for the retail cost of the supplies sold which lien covers all crops grown on the land within 16 months and all animals consuming the feed. The lien can be perfected by filing a verified lien statement with the Secretary of State and enforced in procedures similar to usual Uniform Commercial Code methods. As to priority, the suppliers' lien is superior to liens perfected subsequently, except certain statutory liens, and is given an equal priority to existing liens of record, including perfected security interests of financial institutions.

The bill contains a provision requiring that a supplier communicate with the farmer's lender prior to or upon the sale and request a memorandum as to the financial ability of the farmer to pay for the supplies. If the bank states that the farmer has a sufficient net worth or a line of credit, the bank's memorandum becomes an irrevocable letter of credit covering the cost of the supplies. If the bank's answer is no, the bank is to transmit the records on the farmer's financial history to the supplier, as allowed by a signed waiver of confidentiality that was to accompany the supplier's inquiry.

Failure to respond or an incomplete response by the bank gives the supplier the right to perfect the lien. Failure on the part of the supplier to communicate with a lender prior to perfecting the lien is made an absolute defense to an attempt to jeopardize the financial institution's priority in an enforcement action.

Because the legislation contains a number of concepts and procedures that are drastic departures from traditional financing arrangements, it has resulted in a great deal of confusion among agricultural lenders and rural attorneys. In addition, the legislation contains a number of undefined terms and creates a number of serious, unanswered questions as to procedure and law which add to this situation. Any party possibly affected by this legislation should obtain a copy of the bill to review the specific language.

—*Neil Hamilton*

Iowa: liability and defects in leased agricultural property

A recent Iowa Supreme Court case, *Knapp v. Simmons,* 345 N.W.2d 118 (Iowa 1984) involved the duties a landlord owes to a tenant in an agricultural lease and illustrates the types of risks that can arise in farm leases.

The case involved the renewal of an oral lease between two farmers for the grazing of cornstalks after harvest. Shortly after the cattle were placed on the land, they became sick and a veterinarian's inspection indicated insecticide poisoning. A search of the premises revealed an open bag of Furadan, which the cattle had been eating. The district court dismissed the tenant's suit against the landlord, ruling that the landlord did not guarantee that the land was suitable for use in grazing or promise that the property was free of dangers.

On appeal, the Iowa Supreme Court ruled that a landlord does not impliedly warrant that agricultural land is suitable for the purposes for which it is leased. However, the Court returned the case to the district court to decide the factual question of whether the landlord was negligent in failing to warn the tenant of the possibility of insecticides on the premises or if under the terms of the lease, the landlord, who had joint control of the property, thus had a duty to maintain the premises in a safe condition.

The Iowa Supreme Court's ruling is different than what might be the result if the case had involved a defect with leased residential property. It indicates the unwillingness of the Court to charge agricultural landlords with an implied duty to guarantee the quality of the land they lease. Tenants should use independent methods to determine whether property can, in fact, be used for the desired purposes. This case will be the subject of a comment in a future issue of the Drake Law Review.

—*Neil Hamilton*

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