

Major Legal Issues

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Notes for Power Point Presentation

Major Legal Issues:

There are a wide variety of legal issues that provide risk to an agricultural operation. It is not possible to cover all of these areas within this presentation but instead I will focus on several areas that tend to be of major importance to most agricultural operations. In this presentation we will talk a little bit about contracts and what is involved with contracts. We will not talk much about Hedge-to-Arrive contracts or Hybrid cash contracts or such things as off exchange options. Those type of contracts fall more into the marketing section of risk management and should be covered in those areas. However, we will talk about the different varieties of insurance that an agricultural operation should consider and some of the pitfalls to watch out for. I will then spend some time discussing environmental issues and environmental crimes. And then move into a discussion on contracts and damages related to broken contracts.

There are other major legal issues that one should not forget about. Such things as estate planning or structuring your operation to receive the best tax situation as possible. Deciding whether to have a corporation or a sole proprietorship or other types of legal structures to operate under are also major legal issues. Divorce can cause major upheavals in the best drafted plans for an operation. All of these, are legal issues that one must consider as a risk that needs to be managed and thought out for their agricultural operation.

Personal Insurance:

Medical Insurance:

There are several different types of insurance that an agricultural producer must be concerned about. For instance, medical insurance: One should make sure that the medical insurance coverage includes necessary prescription drugs under its coverage.

Disability Insurance:

Make sure you know the time frame required before the insurance kicks in. The disability insurance will probably do you little good if the waiting period is a year or two years before the insurance coverage actually kicks in. Also, make sure you know exactly what your coverage is with the disability insurance. Does the coverage provide enough to cover necessary bills in case you actually are disabled?

Make sure your long-term health care insurance includes home/health care.

Life Insurance: Make sure you actually understand why you are buying the life insurance policy you are. Is it to provide a minimum amount of coverage or is the purpose to pay off large amounts of debt at your death? The two most common mistakes related to life insurance is being over-insured and under-insured.

Make sure on all of your insurance policies that you have inflation protection coverage. It does little good to have insurance that at one time provided adequate coverage but when really needed provides only a small portion of what you actually need now. Inflation can erode the value of many insurance policies over a fairly quick period of time.

Liability Insurance:

Probably the most important part of liability insurance policy is to know what is excluded from that policy. Almost all, if not all, insurance policies written in the past few years specifically exclude environmental liability claims. That means if you have a spill from your lagoon, or an unexpected pesticide release, that your insurance will probably NOT cover the incident. The liability of such an event can be catastrophic. For instance, if an aquifer was damaged the clean-up cost could run up to ten, fifteen, twenty million dollars.

Other items that could be excluded from the policy are such things whether a tractor that you lease is covered under your insurance. What happens if you have an accident while transporting livestock? Would the animals be covered under your policy or would you have to swallow that loss?

Non farm business pursuits should also be a concern. Such things as a you-pick operation may not be covered under your policy.

The bottom line with insurance is to know what's in your policy and probably more importantly know what is NOT in your policy. Know what is excluded from coverage and what you would actually be liable for. By knowing this you can better plan for possible risk that your operation may encounter.

Property Insurance:

What's covered under your property insurance? Does your policy cover all the buildings at the same rate or is each building insured individually? For instance, if you have five or six buildings and one burns down do you get a prorated portion of the total of your policy rather than having that individual building covered? You may have a fifty thousand dollars insurance policy covering your buildings. But if one burns down the policy may be written such that each building gets one-fifth of the total policy value. That means each building only has ten thousand dollars of coverage on them.

Liability and Pollution Coverage:

Most, if not all, insurance policies have been written in recent years specifically exclude pollution coverage under their policy. It may be possible to buy riders for some types of pollution coverage but it is highly improbable that you would be able to get insurance coverage for all pollution liability. This is an area that would need to be discussed in great detail with your insurance provider.

There are two types of pollution sources, point and nonpoint. Point source is that type of pollution that comes out of the "end of the pipe." It is often related to industrial pollution. In other words, you can go to a plant and see the pollution coming out of the end of the pipe from the factory. The pollution has a very distinctive origin (the end of the pipe). Nonpoint sources have no distinct point of origin. Most of agriculture is considered nonpoint source pollution. It rains onto a field and the field has erosion. There is no specific point in that field that causes the pollution or releases the pollution. There is no single "point" of the pollution. Therefore it is considered nonpoint pollution.

Many of the environmental laws today specify between point and nonpoint sources of pollution. Insurance policies may do the same. It is important for the producer to know and recognize the difference between these two types of pollution.

Environmental Crimes

Even if you can get insurance coverage for pollution liability it will do little good if you are also convicted of a criminal penalty. How would you be able to pay back loans or support your family if you are in jail? Jail sentences are becoming much more common when environmental problems arise.

Environmental legislation has been written to require only "general intent" rather than "specific intent." Most all other criminal statutes require that the prosecution show "specific intent." As an example, to be guilty of murder the state must show that I had the specific intent to kill someone. In other words, they must show that I obtained a gun, loaded the gun, and shot the gun with the intent to kill someone. I may not have killed who I intended to kill but I still killed someone. If the state shows this then I would likely be convicted of murder. However, if "general intent" was only required then all the state would need to prove is that I had a gun and that someone was killed. The gun could've accidentally have fallen and was triggered and accidentally shot someone. However, under general intent, I would still be guilty. Under a general intent criteria what would need to be proved is that the event happened. In other words, I pollute, therefore I am guilty. The state does need to show that I intended to go out and violate that law or to do something that would result in a violation of that law. All they need to do is prove that the event happened.

Supplemental environmental projects are becoming more common as an alternative to jail time. I will discuss some specific examples later.

Environmental audits can help reduce the liability exposure that producers may face. If you get nothing else out of this discussion it should be that I strongly encourage you to do an environmental audit. Environmental audits allow you to look over your operation and see if any environmental problems exist. Then you can fix or clean up the environmental problem before it becomes a major problem. Or maybe you could prevent possible problems in the future. One of the best programs available to producers is a program offered by many land grant universities called FARM-A-SYST. This program is a self-audit that a producer can do on his own operation. I would however encourage producers to have a nonbiased third party assist them or do the actual audit. Often times it is easy to justify why we didn't do something environmentally and pass the risk off. Others may go through the checklist with you and help provide a better perspective.

Audit Privilege Statutes

Several states have enacted "audit privilege statutes." These statutes allow the producer to do an audit of his operation and to fix or repair many of the environmental problems that may exist. Most of these statutes will not allow a producer to be careless or reckless and then fall under the cover of protection of the statute. However, the statutes do allow an operator to do an audit without reporting the findings to the state or federal agency that oversees that regulation.

However EPA is adamantly opposed to statutes. They have indicated that they do not want states to have or implement these type statutes. EPA wants a producer to notify the appropriate agency if a problem is found during one of these audits. EPA has promised that they would likely impose softer penalties if one reported himself. However, in my mind, that offers little comfort to the person that is trying to run an environmentally sound operation. In fact, I would argue that EPA's position encourages what a call the three S's. Shoot. Shovel. Shut up. For instance, the Endangered Species Act says that if I find an endangered species on my property that I cannot disturb the habitat of that species. In the case of an animal like the bald eagle this area could be quite extensive. The habitat range could be upwards of two to three miles or more. That means I would not be allowed to make loud noises or do other things that may disturb the habitat of that eagle. It may be enforced that I would not be able to any intensive agricultural operations within several miles of the nest. So what is most likely to happen in this instance? Many people would, upon finding a bald eagle, would shoot it, bury it, and not tell anyone. This does little to promote a sound environmental program. I think it would be much better if a producer was allowed to, without fear of having penalties imposed upon him, make his operation more environmentally sound.

States With Environmental Audit Privilege Laws:

This page shows those states which have passed some sort of audit privilege statute. Again, EPA is adamantly opposed to these statutes, however, I would still encourage people in those states that do not have such an audit privilege to try to get one passed in their state.

7 Factors Which Make Environmental Law Punitive

There are several reasons why environmental laws tend to be much more punitive than other such laws.

Number 1) the laws tend to be extraordinarily broad. For instance, the Clean Water Act basically says that we should have clean water. It sounds very simple until it is enacted. Then the laws become extraordinarily complicated. The regulations surrounding the Clean Water Act cover several volumes. Few attorneys know all of the intricacies involved with the single law of the Clean Water Act. When you add upon them such things as the Clean Air Act, Super Fund, FIFRA, etc., you can easily see how one not well versed in these areas could easily violate these laws by a small technicality.

At the same time the regulations tend to expand through creative interpretations of the agencies. For instance, Congress enacted a law which gave EPA authority to regulate the navigable waters of the U.S. When I went to law school it was generally considered that to be a navigable water you had to at least be able to put a boat on in it. The argument was what size boat was required before it was considered navigable. Several years ago the agency decided that since groundwater moves through the ground and may eventually end up in rivers, lakes, streams, etc., that groundwater is also "navigable." Recently, EPA has issued a memo stating that soil is now considered a navigable water.

EPA has only been given authority over navigable waters of the U.S. however they wish to regulate the land application of manure from livestock operations. Since they have no direct authority to do this they have come to the conclusion that soil must be navigable because they do have authority over navigable waters. The reasoning goes like this; first you spread the manure out on to the fields. Then it may rain. The rain comes into contact with the manure on the field and goes into the groundwater. Once the rain has come into contact with the manure it has become polluted. It is well established that groundwater is navigable so therefore, the polluted water is now in the groundwater and is navigable. Therefore, the rain passing through the topsoil into manure must also be navigable. Therefore, soil must be navigable. This type of creative interpretation of the statutes is becoming increasingly common within the agencies. As we discussed earlier criminal sanctions under environmental laws require only a general knowledge rather than specific knowledge of violating the act to be guilty. This makes it much easier to prove criminal violations. At the same time you may find yourself facing both civil and criminal proceedings. The civil proceedings are to seek money damages while the criminal proceedings are to seek jail time. These are separate actions and you would have to defend both at the same time.

The government is quite serious about these type of "crimes." At the present time the FBI has over 550 investigations of environmental wrongdoing. In 1997 alone \$169 million dollars in criminal fines were issued. At the same time \$99 million dollars in civil fines were issued. At the same time 195 years of jail time was handed down to violators of environmental laws.

Emmett Runde

Mr. Runde was a fairly small farmer in Wisconsin. His operation allowed some animal waste to get into one of the streams in the state. The judge offered Mr. Runde, as an alternative to jail, to write and publish in the newspaper a confession of his "sins" and to apologize to the public for committing this crime. When offered with this opportunity Mr. Runde chose that alternative rather than sit in jail. This is an example of the supplemental environmental project that I spoke of earlier. It is not a judicial alternative that I necessarily agree with, however, it is becoming much more common in relation to environmental crimes.

Paul Tudor Jones

Paul Tudor Jones is a well-known and respected commodity futures trader. He has made millions trading the markets for himself and others. Mr. Jones said out to develop a major wetlands area. He hired who, at the time, was considered one of the national authorities in developing wetlands. This person worked closely with EPA over several years in developing a wetland project that covered hundreds of acres. However, towards the end of the project changed the definition of what a wetland was. As soon as the project was completed the director of the program was arrested. Paul Tudor Jones told his director to go ahead and implicate him in this case. He did not think it was fair that someone should go to jail for doing what he thought was right and for what he was hired to do. The court offered, in exchange for jail time, a fine of \$1 million dollars. This fine was not paid to the government but rather to the National Fish and Wildlife Foundation. It is becoming increasingly more common that environmental groups receive the monies collected from these type of enforcement activities and from lawsuits.

Taung Ming-Lin

Taung Ming-Lin was a small farmer in southern California. During this particular time southern California experienced vast fires which destroyed billions of dollars worth of houses and forestland. The fires lasted for weeks as the fire approached Taung Ming-Lin's house he got a tractor and a disc and drove around his house to develop a fire break. He saved his house from the fire. In fact, his act of using his tractor and disc to develop a fire break was on national TV.

The agency responsible for enforcing the act and within a few days they were on Taung Ming-Lin's farm. They said that Taung Ming-Lin had disturbed the habitat of an endangered species (a small mouse that lived in that type of area). The agency never did find any remains of dead mice but still said that Taung Ming-Lin had violated the act by disturbing the habitat of that mouse. The government demanded that Taung Ming-Lin give up 363 acres of his 720 acre farm as a preserve. In addition, he was asked to give \$172 thousand dollars to help fund the operation of that preserve.

Checklist of Some Environmental Laws

This page shows some of the environmental laws that a farming operation should at least review and be familiar with. This list is not all inclusive. I am not suggesting that you need to be an expert in every one of these topics, however, it may be prudent to at least be familiar with those laws and regulations that directly affect your operation.

Producer Contracts

This section of the discussion refers to those contracts where a producer contracts with another entity to provide a specific product. For instance high oil corn, high licing corn, or a pork or beef supply. In all of these instances the producer would contract with another person or company to provide those products. While all of these contracts are slightly different and specific to each individual producer, they all tend to share some common characteristics.

1. Independent Contractor: Most of these contracts state that the producer is an independent contractor. This has a great deal of legal significance. If you are found to be an independent contractor, rather than an employee of the operation, you are liable for your acts. If you were an employee the corporation could be held liable for your acts. As an independent contractor they cannot be held liable. To be determined to be an independent contractor the court will look at a number of different factors. My guess is that, because of the other clauses most of these contracts contain, that most courts would not consider the producer to be an independent contractor regardless of what the contract actually says. However, this does not get the producer off the hook.
2. Most of these contracts require the producer to follow specific practices outlined by the contractor. For instance, you must apply certain chemicals at certain times of the year, or not apply certain chemicals to the crop at any time; or to supply a particular breed of pig or a pig that meets certain specifications; or to feed a specific feed or a combination of feeds to the animals.
3. The majority of these contracts also specify that the producer will be responsible for the animal waste. That means any environmental problems associated with that waste would also be the responsibility of the producer.
4. The processor or contractor may inspect at any time. For instance, most, if not all, of the contracts related to the growing of roundup ready soybeans stated that the company had a right to inspect the farmer's fields to make sure he was in compliance with the contract. Other instances may be that the processor may inspect your poultry operation to make sure that proper procedures are being followed. Or the contractor may inspect your fields to make sure that the correct varieties have been planted or that proper separation distances have been followed.
5. The majority of these contracts contain a clause that says that the grower must indemnify the contractor for environmental liabilities. This clause most likely WILL be upheld by most courts. Therefore, the court may hold that you are not an independent contractor but you must still indemnify the company for any liabilities that arise. That means if the company is found to be liable you still have to pay the company's portion of that liability.
6. Mediation: Many of these contracts contain a mediation clause. That means you cannot take the company to court, at least in the beginning. Before going to court you must go through a mediation process whereby you present your case to a mediator who also listens to the other party's side. This mediator then tries to work out a solution. This is an added step that producers must be aware of that they must go through before taking someone to court.

Reasons For Breaking A Contract

There are numerous reasons for breaking a contract, however, the majority of contracts are broken for basically the same reasons.

1. The price has significantly increased (or decreased). For instance, I contract with an elevator to provide 50 thousand bushels of corn at \$2.50 per bushel. Afterwards the price climbed to \$5 per bushel. All of a sudden I don't have any corn to provide an elevator at \$2.50 per bushel. Or a packer contracts with a producer for a supply of hogs. The packer guarantees a minimum price of \$38 per hundredweight. The price falls to \$18 dollars per hundredweight. All of a sudden the producer's hogs do not meet the specifications that the packer has outlined.
2. Not enough was grown (or too much was grown). Reproducer contracts with an elevator to sell fifty thousand bushels of corn. The farmer experiences a drought and only raises ten thousand bushels of corn. The producer is unable to fulfill his portion of the contract. Note that in this instance it would be highly unlikely that a court would allow the producer to get out of this contract. The more likely scenario would be for the court to have the producer pay for any damages that the contractor incurred to fill that contract.
3. You may deliver part of the product you contracted with and the check that you were paid with bounced. This may be a very viable reason for breaking a contract.
4. Another likely reason for a contract to be broken is that one of the parties has a dispute over how the contract has been written and wants to cancel the contract. The person running out of the contract will probably need a very good reason to get out of that contract.

Damages

There are a variety of ways someone can recover the damages the claim to have experienced in the breach of contract situation.

1. You may be able to cancel the contract and recover what you have paid for in that contract.
2. You can "cover" and acquire the substitute goods and then get the difference in the cost. For example, a producer contracts with an elevator to sell his corn at \$2.50 a bushel. The price goes to \$5 a bushel and the farmer refuses to deliver. The elevator may be able to go onto the open market, buy the named amount of bushels at \$5 and sue the farmer for the difference. It cost the elevator to get that amount of corn.
3. They may be able to receive damages for any expenses incurred because the product was not delivered in accordance with contract terms. For instance, if nondelivery of the product resulted in the company losing business or having added expenses because the product was not delivered they may be able to recover these costs.
4. They may be able to recover goods that are identified. This is nearly impossible in a grain situation. Simply because grains are not identifiable. You cannot distinguish which kernels of corn are yours in a bin full of corn. However, with livestock this might be a viable alternative. There was one famous case out of Kansas where a cattle feeder drove his pick-up into the field each day to feed his cattle. When he did so he honked his horn to get his cattle's attention. The cattle learned that the sound of the horn meant food. The farmer sold these cattle to a market that soon after went bankrupt and the cattle disappeared. The farmer drove around the area in his pick-up honking his horn. When he went into one field and honked his horn a herd of cattle came to the truck. He was able to thereby identify his own cattle and to recover the cattle he had "lost."
5. If the goods contracted for are unique and cannot be supplied by others then the contractor can seek what is called Specific Performance. In other words, you will be required to provide those specific goods. If you still refuse to provide those goods then the amount of damages suffered by the contractor may be awarded.
6. Impracticality: It is important for producers to understand that just because it may be hard, or nearly impossible, to fulfill the terms of the contract that the courts will probably NOT let them out of the contract. The courts are reluctant to interfere with two people that have made a contract. Therefore unless the contract is unconscionable the court will probably uphold the provisions of the contract. For instance, just because you experience a drought does not mean you are likely to be let out of the contract. The court will rather direct you to go onto the open market to buy enough product to fill the terms of the contract. There are very few circumstances in which courts will let one person out of a contract just because the terms of that contract are hard to fulfill.

Basic Rules of Contracting

Before entering a contract there are several items that a producer should be aware of.

1. Read and understand the contract. While you may not understand every term or provision of the contracts you should be able to read a contract and get the general idea of what that contract says and means. If you are unable to understand the basic idea behind the contract then it would be very advisable for you to seek legal counsel before signing the contract. As stated previously, just because you did not understand the terms of the contract does not mean the courts will let you out of the contract later. If you have problems any portion of the contract then you should seek competent legal advice. Do not rely upon what the other party may tell you the contract means. The contract means what the contract says, not what others may say they think it means.
2. Make sure the contract, and any changes in the contract, are in writing. The statute of frauds requires that anything over \$500 dollars or that cannot be done within one year to be in writing. It is also important for producers to understand that any changes in a contract should be in writing. For instance, a representative of a company may tell a producer that they really don't need to do something as stated in the contract. Courts look at what is written in the contract for guidance. Most contracts state that only what is written can be considered. The courts will not look at what was stated orally if this is the case. Therefore, if an employee of the contractor states that you do not have to do something as stated in the contract be sure that is in writing and signed by a representative of the company.
3. A very important point in contracts is that the person who wrote the contract is probably protecting himself. While this may be obvious often times people sign contract without reading them which were prepared by others.
4. As was previously discussed you will probably not be excused for a failure to perform the contract.
5. An important part of any contract is negotiation. While many companies may not negotiate major portions of a contract many minor portions may very well be up for negotiations. For instance, one producer was given a contract that provided the company would pay them once per quarter. After running an economic analysis the farmer found out that this was an economically viable contract. The producer did find out however that if he was paid monthly that the contract was economically viable. The company was more than happy to change the provisions of the contract from being paid quarterly to monthly.
6. It is important to keep records of the transactions and conversations in relation to any contract. Good records can often settle disputes rapidly.
7. Stay in touch with the other party. If you are having problems following all of the provisions of the contract often times you may be able to change specific provisions within the contract to meet your present situation. Most companies, however, are very reluctant in changing the terms of contract at the end of the contract and not have any knowledge of any problems during the contract's time frame.
8. Know the other parties financial situation. Bankruptcy can completely change what you may get from a contract. It is often not a wise procedure to contract with someone that has a very precarious financial situation.