$$$

Ag Decision Maker

$$$

A Business Newsletter for Agriculture

Vol. 9, No. 3 www.extension.iastate.edu/agdm February 2005

Top ten agricultural law developments in 2004

by Roger McEowen, associate professor of agricultural law, (515) 294-4076, mceowen@iastate.edu

(first in a series)

1. Multi-billion dollar verdict rendered in cattle case.

On February 17, 2004, a federal jury in Alabama returned a $1.28 billion verdict against Tyson Fresh Meats, Inc. (Tyson) in a nation-wide class-action lawsuit alleging that Tyson manipulated the price for fed cattle that it purchased through the use of long-term contracts (known as captive supply cattle) in violation of the Packers and Stockyards Act (PSA). The PSA prohibits meat packers from engaging in any unfair, unjustly discriminatory or deceptive practice, or engaging in any course of business or doing any act for the purpose or with the effect of manipulating or controlling prices or creating a monopoly in the acquisition of, buying, selling, or dealing in, any article, or of restraining commerce. The plaintiff class of cattlemen claimed that Tyson's store of livestock (via captive supply) allowed Tyson to avoid reliance on auction-price purchases in the open market for most of its supply. Tyson then uses that leverage, the claim is, to depress the market prices for independent producers on the cash and forward markets in violation of the PSA. The trial court jury unanimously found that
1) there was a single national market for fed cattle;
2) Tyson's use of captive supply had an anticompetitive effect on the cash market for fed cattle;
3) Tyson had no legitimate business reason or competitive justification for using captive supply;
4) Tyson's use of captive supply proximately caused the cash market price for fed cattle to be lower than it otherwise would have been; and
5) Tyson's use of captive supply injured each member of the class. The jury then found that Tyson's use of captive supplies from February 1, 1994, through October 31, 2002, damaged the cash market for fed cattle in the amount of $1,281,690,000.

continued on page 2

Handbook updates

For those of you subscribing to the handbook, the following updates are included.

Crop Planning Prices– A1-10 (1 page)

Cash Corn and Soybean Prices– A2-11 (2 pages)

Lean Hog Basis – B2-41 (2 pages)

Live Cattle Basis – B2-42 (1 page)

Historic Farmland Values – C2-72 (10 pages)

Financial Terms – C3-05 (10 pages)

Please add these files to your handbook and remove

Inside . . .

IOWA STATE UNIVERSITY
University Extension

Ag Decision Maker is compiled by:
Don Hofstrand, ISU Extension farm management specialist, 641-423-0844, dhof@iastate.edu

Top ten agricultural developments in 2004, continued from page 1

In March, Tyson filed a motion for Judgment as a Matter of Law or for a New Trial, and on April 23, the trial court judge granted Tyson's motion, thereby invalidating the jury verdict. While the trial court judge did not disturb any of the jury's findings, particularly the finding that Tyson's use of captive supply cattle manipulated the cash market price for fed cattle, the judge ruled that Tyson was entitled to use captive supplies to "meet competition" and assure themselves of a reliable supply of cattle. The cattlemen appealed.

On December 17, oral arguments in the case were heard by the United States Court of Appeals for the Eleventh Circuit. During oral arguments, Tyson's counsel admitted that if the PSA prohibits the use of captive supplies, then the "meeting competition" defense was inapplicable. Tyson's counsel was also questioned as to Tyson's claim that the company could not control when captive cattle were delivered, but yet maintained that the use of captive supplies was necessary to achieve a consistent supply of cattle. Tyson's counsel also admitted that the jury was free to believe the cattlemen's expert economist and disbelieve Tyson's expert. In the end, however, the primary appellate issue is the appropriate legal standard for evaluating a claim of price manipulation under the PSA. The trial court judge adopted a Sherman Act "rule of reason" standard, thereby allowing Tyson to defend its actions by showing a legitimate business justification for using captive supplies (such as the assuring a reliable supply of cattle). The question is whether the Sherman Act's rule of reason is applicable under the PSA. An opinion is expected in 2005 by the appellate court. *Pickett. v. Tyson Fresh Meats, Inc.*, 315 F. Supp. 2d 1172 (M.D. Ala. 2004).

2. Developments in GMO patent infringement cases.

The patenting of seed technology has led to cases in which farmers have been sued for misappropriation of the technology. Generally, courts have held that the process by which the patented seed arrives on a farmer's land (whether by pollen drift or from passing grain trucks, for example) is irrelevant. But two cases decided in 2004 may indicate that the courts are re-evaluating the legal issues associated with the drift of genetically modified seed technology. On May 21, the Canadian Supreme Court rendered its opinion in *Monsanto Canada, Inc. v. Schmeiser*. Monsanto sued a Canadian canola farmer for the "theft" of the company's Roundup Ready canola technology when the traits showed up in Schmeiser's fields.

Schmeiser did not have a license to grow Roundup Ready canola, and claimed that the GMO canola was present in his fields either by cross-pollination from neighboring fields, blowing from passing grain trucks, or both. Schmeiser saved some of the resulting GMO canola and replanted it. While the Court ruled that plants are not patentable (in accordance with an earlier opinion of the Court holding that "higher life forms" are not patentable), the Court held that Monsanto's patent applied to the genes and cells of the plants and was, therefore, valid. The dissent (the opinion was 5-4) would have held that the cultivation of plants containing the patented gene and cell did not constitute infringement, and that to conclude otherwise would confer patent protection on the resulting plants – an unpatentable higher life form. Consequently, Schmeiser was found to have infringed the patent. However, the Court held that Monsanto was not entitled to damages because Schmeiser earned no profit from the technology – he never sprayed his crop with Roundup to reduce weeds. *Monsanto Canada, Inc. v. Schmeiser*, [2004] S.C.C. 34.

Earlier, in late April, the United States Court of Appeals for the Federal Circuit invalidated a patent on a self-reproducing antidepressant drug because previous clinical trials constituted a prior use that had placed the compound in the public domain. A concurring opinion reasoned that the patent was invalid not because of prior use of the subject matter, but because the subject matter was not patentable since it could reproduce itself in nature. The concurring judge compared the seeding and conversion

continued on page 3

Top ten agricultural developments in 2004, continued from page 2

process of the compound at issue to the spread of patented, biotech seed traits via cross-pollination, and concluded: "[T]he implication – that the patent owner would be entitled to collect royalties from every farmer whose cornfields contained even a few patented…stalks… - cannot possibly be correct." *Smithkline Beecham Corp. v. Apotex*, 365 F.3d 1306 (Fed. Cir. 2004).

While the Canadian Supreme Court opinion is not binding on U.S. courts, it will not go unnoticed. Likewise, the two cases provide a framework for the development of future cases and legislation supporting an equitable enforcement of patent laws respecting both the rights of patentees and the rights of innocent infringers.

3. WTO finds that U.S. cotton subsidies violate international trade rules.

On April 26, an interim panel of the World Trade Organization (WTO) issued a report finding that U.S. cotton subsidies violate international trade agreements and price developing countries out of markets. The WTO Agreement on Agriculture (AoA) requires that domestic subsidies that encourage production are not to exceed 1992 per-country levels. In 1992, cotton payments totaled $1.62 billion. However, cotton payments were pegged at $2.3 billion in 1999, $1.57 billion in 2000, and $2.06 billion in 2001. As a result the panel concluded that decoupled payments to U.S. cotton farmers (pursuant to the 1996 Farm Bill and continuing under the 2002 Farm Bill) provide an incentive for overproduction and distort trade by pricing developing nations' goods out of markets. The challenge was brought primarily by Brazilian cotton farmers, who also pointed out that the U.S. share of the global cotton market had increased during the same time frame. Challenged are direct payments to U.S. cotton farmers, as well as payments made under emergency supplemental appropriation bills. Involved are producer flexibility payments, market loss assistance payments and counter-cyclical payments.

The U.S. claims that direct payments are decoupled and are not trade distorting because they are not linked to current production and are, therefore, not "subsidies." Thus, the U.S. position is that direct payments to cotton producers should not be counted when compared to the 1992 levels because the payments are not encouraging production for the year in which the payments are made. However, from 1998 though 2001, U.S. cotton production increased almost 50 percent, and the U.S. share of world cotton exports increased from 24 percent in 1996 to 37 percent in 2001 (anticipated to be 42 percent in 2004). In 2002, cotton was exported from the U.S. at 61 percent below the cost of production. Under the Agreement on Subsidies and Countervailing Measures, agricultural subsidies are deemed to be harmful to international trade if the subsidizing member increases its share of the world market when compared to its average share over the prior 3-year period.

The interim panel's ruling was later affirmed by a panel of trade experts. On October 18, the U.S. formally appealed the ruling to the appeals body of the WTO. The appeals body has until Jan. 18, 2005, to produce a final ruling in the matter.

The WTO ruling provides an opportunity for the U.S. Congress to debate seriously the future of agricultural policy. The core issue is whether the policy that emerges will support independent family farmers or continue the subsidization of multinational agribusiness cartels in world markets. In theory, the WTO dispute could lead to a dramatic reduction in U.S. agricultural subsidies.

4. Rabobank's attempted takeover of a Farm Credit System lender.

On July 30, Rabobank, a Dutch banking conglomerate that is the fifteenth largest banking institution in the world, announced that it had agreed to purchase Farm Credit Services of America (FCSAmerica) for $600 million – at the time FCSAmerica represented

continued on page 4

Top ten agricultural developments in 2004, continued from page 3

6.5 percent of the Farm Credit System's total assets and 6.9 percent of System's combined capital. That same day, AgStar Financial Services, a Farm Credit Sytsem (FCS) association headquartered in Minnesota, confirmed that it had made a formal merger offer to the FCSAmerica Board of Directors to merge the two FCS lenders. FCSAmerica later began the regulatory process for terminating its status as a System institution by submitting to the Farm Credit Administration, its board of director's resolution to terminate its System status and then merge the association into a subsidiary of Rabobank. The proposed acquisition of a unit of the FCS by a private (albeit foreign) lender was unique, and raised significant tax and legal issues as well as the concern of whether the Congress ever intended that current stockholders of a unit of the FCS should be permitted to benefit from a sale of the entity to a non-System buyer.

On October 20, 2004, FCSAmerica announced that its board voted to terminate its agreement with Rabobank and remain a System institution. FCSAmerica also announced that it had rejected the merger offer from AgStar. Throughout the late summer and early fall of 2004 it became clear that the FCSAmerica board had not fully analyzed the legal, tax and policy ramifications of the proposal or anticipated the widespread opposition to the deal among family farmers.

From a policy perspective, it is highly unlikely that the Congress ever intended that an FCS unit could be sold to a private entity. Also, the Congress has given the FCS a privileged position in agricultural lending that has contributed to the value of FCSAmerica. This "agency status" allows the FCS to access funds from the money markets at a slightly higher cost than the U.S. Treasury can borrow in the same markets. Had the deal gone through, the four remaining districts would most certainly have taken note that they could become targets from other large lenders looking to enhance their position in agricultural lending. Consequently, the buyout could have initiated the demise of the FCS. Likewise, Rabobank would likely have been more attuned to serving relatively larger borrowers because of their share of the purchase price. However, small and mid-size borrowers in the four states at issue (IA, NE, SD and WY) would likely have seen the picture differently, at least until a new holder of the FCS charter had established a truly competitive presence (and that could have taken several years). The buyout would also have contributed to a dramatic increase in the input-supply side of agriculture, raising further questions about competition in agricultural lending. Also, questions would have abounded concerning Rabobank's willingness to work with borrowers in financial distress compared to local lenders or a lender whose mandate is to assist farm borrowers.

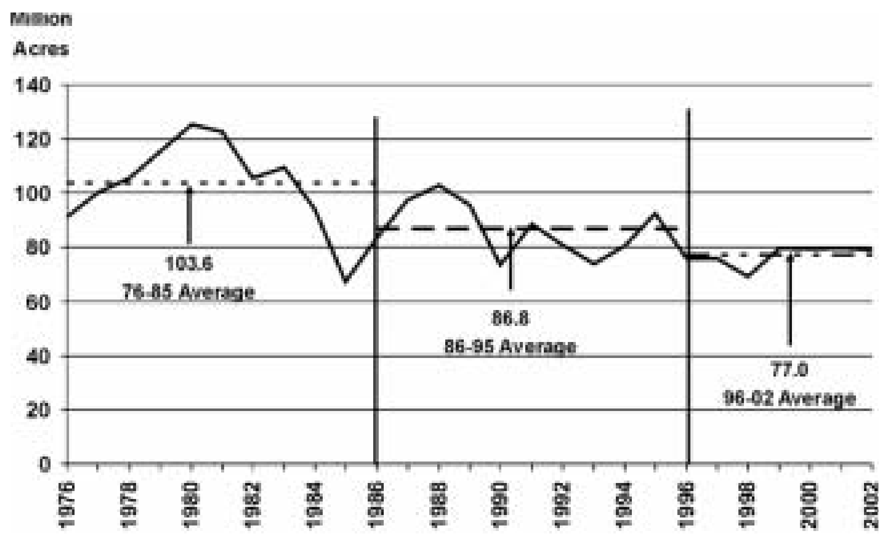
continued on page 5

Acreage devoted to export production shrinks over last 25 years

by Darryl Ray, Blasingame Chair, Excellence in Agricultural Policy, Institute of Agriculture, University of Tennessee, and Director, UT Agricultural Policy Analysis Center (APAC). (865)974-7407; dray@utk.edu; http://www.agpolicy.org

In recent statements like one she made on December 11 announcing that the United States and Chile had concluded a free-trade agreement, U.S. Secretary of Agriculture Ann Veneman emphasized the importance of this agreement for U.S farmers and ranchers. She said, "The agreement will give America's farmers and ranchers and the businesses they support improved, and in many cases, new access to a market of 15 million consumers."

Figure 1. Net U.S. export acreage for eight major crops (corn, soybeans, wheat, grain sorghum, rice, cotton, oats and barley), 1976-2002. Data source: USDA.

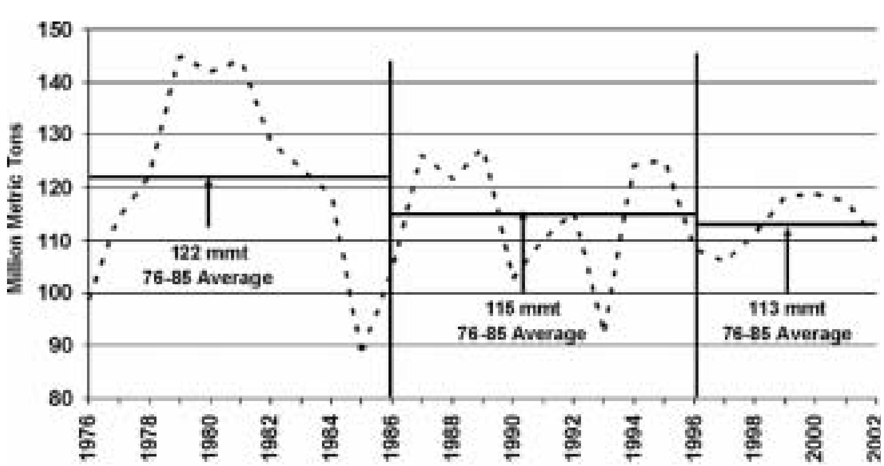


For more than one hundred years, agricultural exports have been important to America's farmers and ranchers providing a market that has allowed them to produce more food than can be consumed domestically. Without exports, the ag sector would be considerably smaller than it is today. That being said, we need to remember another lesson that this history has taught us. Exports do not guarantee prosperity. They are not an assured solution to the chronic price and income problems faced by U.S. producers.

When we talk about exports of agricultural crops we need to make sure that we don't overplay the potential and foster unrealistic expectations on the part of producers. Time and time again we have hung our hat on the star of growing exports only to be disappointed.

Let's examine the data with an eye toward what they might mean for the future. In figure 1 we can see that, on average, during the ten years before the 1985 Farm Bill 103.6 million acres were needed to supply the net exports of the 8 major crops that were sold in the international marketplace. The 1985 low of 67 million acres and the decline in exports that those reduced acres represent, were surely one set of the factors that led Congress to adopt export oriented legislation that year.

Figure 2. Net U.S. export volume for eight major crops (corn, soybeans, wheat, grain sorghum, rice, cotton, oats and barley), 1976-2002. Data source: USDA.



continued on page 6

Acreage devoted to export production shrinks over last 25 years, continued from page 5

In the 1996 Farm Bill, Congress again took another shot at making U.S. crops more competitive in the export market by eliminating the price floor under crops instituting the use of Loan Deficiency Payments/Marketing Loan Gains. By using these devices, farmers increed the amount of acres needed to produce for exports, the acreage dropped again,averaging 77.0 million acres in the 1996-2001 period.

But what about the straight volume of exports? Figure 2 shows that volume of exports dropped as well. In the ten years before the adoption of the 1985 Farm Bill, the U.S. exported, net of imports, an average of 122 million metric tons of the 8 major crops (corn, wheat, soybeans, grain sorghum, cotton, rice, oats and barley). In the most recent period the average dropped to 113 million metric tons.

Exports definitely absorb a significant portion of U.S. crop production. But, despite the upbeat statements by USDA officials and some general farm and commodity organizations, major crop exports have shown no real growth for decades, even though we have spent hundreds of billions of dollars since 1985 in policies designed to expand exports.

It is apparent that non-price factors have dominated the markets suggesting that we could have spent significantly less, allowed farmers to receive more of their income from the marketplace, and still exported nearly the same volume of grains and seeds.

the out-of-date material.

Internet updates

In addition to those listed on Page 1, the following updates have been added to www.extension.iastate.edu/agdm.

Adding Value – C5-01 (2 pages)

Issued in furtherance of Cooperative Extension work, Acts of May 8 and June 30, 1914, in cooperation with the U.S. Department of Agriculture. Stanley R. Johnson, director, Cooperative Extension Service, Iowa State University of Science and Technology, Ames, Iowa.