Top Ag Law and Tax Developments of 2022 – Numbers 2 and 1

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Overview

Today's article concludes my look at the top ag law and tax developments of 2022 with what I view as the top two developments. I began this series by looking at those developments that were significant, but not quite big enough to make the "Top Ten." Then I started through the "Top Ten."

The top two ag law and tax developments in 2022 – it's the topic of today's post.

Recap

Here's a bullet-point recap of the top developments of 2022 that I have written about:

- Nuisance law (the continued developments in Iowa) - *Garrison v. New Fashion Pork LLP*, *977 N.W.2d 67 (Iowa Sup. Ct. 2022).*
- Minnesota farmer protection law - *Pitman Farms v. Kuehl Poultry, LLC, et al., 48 F.4th 866 (8th Cir. 2022).*
- Regulation of ag activities on wildlife refuges - *Tulelake Irrigation Dist. v. United States Fish & Wildlife Serv., 40 F.4th 930 (9th Cir. 2022).*
- Corps of Engineers jurisdiction over "wetland" - *Hoosier Environmental Council, et al. v. Natural Prairie Indiana Farmland Holdings, LLC, et al., 564 F. Supp. 3d 683 (N.D. Ind. 2021).*
- U. S. Tax Court's jurisdiction to review collection due process determination - *Boechler, P.C. v. Commissioner, 142 S. Ct. 1493 (2022).*
- IRS Failure to Comply with the Administrative Procedure Act - *Mann Construction, Inc. v. United States, 27 F.4th 1138 (6th Cir. 2022); Green Valley Investors, LLC v. Commissioner, 159 T.C. No. 5 (2022).*
- State law allowing unconstitutional searches unconstitutional - *Rainwaters, et al. v. Tennessee Wildlife Resources Agency, No. 20-CV-6 (Benton Co. Ten. Dist. Ct. Mar. 22, 2022).*
- No. 10 – USDA's Emergency Relief Program and the definition of "farm income."
- No. 9 - USDA decision not to review wetland determination upheld - *Foster v. United States Department of Agriculture, No. 4:21-CV-04081-RAL, 2022 U.S. Dist. LEXIS 117676 (D. S.D. Jul. 1, 2022).*
- No. 8 - Dicamba drift damage litigation - *Hahn v. Monsanto Corp., 39 F.4th 954 (8th Cir. 2022), reh'g. den., 2022 U.S. App. LEXIS 25662 (8th Cir. Sept. 2, 2022).*
- No. 7 – The misnamed "Inflation Reduction Act."
- No. 6 – Caselaw and legislative developments concerning "ag gag" provisions.
- No. 5 - WOTUS final rule.
- No. 4 – Economic issues
- No. 3 – Endangered Species Act regulations

No. 2 – California Proposition 12

National Pork Producers Council, et al. v. Ross, 6 F.4th 1021 (9th Cir. Jul. 28, 2021), cert. granted, 142 S. Ct. 1413 (2022)

In a huge blow to pork producers (and consumers of pork products) nationwide, the U.S. Court of Appeals for the Ninth Circuit has upheld California's Proposition 12 in 2021. Proposition 12 requires any pork sold in California to be raised in accordance with California's housing requirements for hogs. This means that any U.S. hog producer, by January 1, 2022, was required to upgrade existing facilities to satisfy California's requirements if desiring to market pork products in California. In early 2022, the U.S. Supreme Court announced that it would review the Ninth Circuit's opinion.

While each state sets its own rules concerning the regulation of agricultural production activities, the legal question presented in this case is whether one state can override other states' rules. The answer to that question involves an analysis of the Commerce Clause and the "Dormant" Commerce Clause.

The Commerce Clause. Article I Section 8 of the U.S. Constitution provides in part, "the Congress shall have Power...To regulate Commerce with foreign Nations and among the several states, and with the Indian Tribes." The Commerce Clause, on its face, does not impose any restrictions on states in the absence of congressional action. However, the U.S. Supreme Court has interpreted the Commerce Clause as implicitly preempting state laws that regulate commerce in a manner that disrupts the national economy. This is the judicially-created doctrine known as the "dormant" Commerce Clause.

The "Dormant" Commerce Clause. The dormant Commerce Clause is a constitutional law doctrine that says Congress's power to "regulate Commerce ... among the several States" implicitly restricts state power over the same area. In general, the Commerce Clause places two main restrictions on state power – (1) Congress can preempt state law merely by exercising its Commerce Clause power by means of the Supremacy Clause of Article VI, Clause 2 of the Constitution; and (2) the Commerce Clause itself--absent action by Congress--restricts state power. In other words, the grant of federal power implies a corresponding restriction of state power. This second limitation has come to be known as the "Dormant" Commerce Clause because it restricts state power even though Congress's commerce power lies dormant. *Willson v. Black Bird Creek Marsh Co., 27 U.S. 245 (1829).* The label of "Dormant Commerce Clause" is really not accurate – the doctrine applies when the Congress is dormant, not the Commerce Clause itself.

Rationale. The rationale behind the Commerce Clause is to protect the national economic market from opportunistic behavior by the states - to identify protectionist actions by state governments that are hostile to other states. Generally, the dormant Commerce Clause doctrine prohibits states from unduly interfering with interstate commerce. State regulations cannot discriminate against interstate commerce. If they do, the regulations are per se invalid*. See, e.g., City of Philadelphia v. New Jersey, 437 U.S. 617 (1978).* Also, state regulations cannot impose undue burdens on interstate commerce. *See, e.g., Kassel v. Consolidated Freightways Corp., 450 U.S. 662 (1981).* Under the "undue burden" test, state laws that regulate evenhandedly to effectuate a local public interest are upheld unless the burden imposed on commerce is clearly excessive in relation to the local benefits.

The Court has never held that discrimination between in-state and out-of-state commerce, without more, violates the dormant Commerce Clause. Instead, the Court has explained that the dormant Commerce Clause is concerned with state laws that both discriminate between in-state and out-of-state actors that compete with one another, *and* harm the welfare of the national economy. Thus, a discriminatory state law that harms the national economy is permissible if in-state and out-of-state commerce do not compete. *See, e.g., General Motors Corp. v. Tracy, 117 S. Ct. 811, 824-26 (1997).* Conversely, a state law that discriminates between in-state and out-of-state competitors is permissible if it does not harm the national economy. *Hood & Sons, Inc. v. Du Mond, 336 U.S. 525 (1949).*

California Proposition 12 Litigation

In 2018, California voters passed Proposition 12. Proposition 12 bans the sale of whole pork meat (no matter where produced) from animals confined in a manner inconsistent with California's regulatory standards. Proposition 12 established minimum requirements on farmers to provide more space for egg-laying hens, breeding pigs, and calves raised for veal. Specifically, the law requires that covered animals be housed in confinement systems that comply with specific standards for freedom of movement, cage-free design and minimum floor space. The law identifies covered animals to include veal calves, breeding pigs and egg-laying hens. The implementing regulations prohibit a farm owner or operator from knowingly causing any covered animal to be confined in a cruel manner, as specified, and prohibits a business owner or operator from knowingly engaging in the sale within the state of shell eggs, liquid eggs, whole pork meat or whole veal meat, as defined, from animals housed in a "cruel manner." In addition to general requirements that prohibit animals from being confined in a manner that prevents lying down, standing up, fully extending limbs or turning around freely, the measure added detailed confinement space standards for farms subject to the law. The alleged reason for the law was to protect the health and safety of California consumers and decrease the risk of foodborne illness and the negative fiscal impact on California.

In late 2019, several national farm organizations challenged Proposition 12 and sought a declaratory judgment that the law was unconstitutional under the dormant Commerce Clause. The plaintiffs also sought a permanent injunction preventing Proposition 12 from taking effect. The plaintiffs claimed that Proposition 12 impermissibly regulated out-of-state conduct by compelling non-California producers to change their operations to meet California's standards. The plaintiffs also alleged that Proposition 12 imposed excessive burdens on interstate commerce without advancing any legitimate local interest by significantly increasing operation costs without any connection to human health or foodborne illness. The trial court dismissed the plaintiffs' complaint. *National Pork Producers Council, et al. v. Ross, No. 3:19-cv-02324-W-AHG (S.D. Cal. Apr. 27, 2020).*

On appeal, the plaintiffs focused their argument on the allegation that Proposition 12 has an impermissible extraterritorial effect of regulating prices in other states and, as such, is per se unconstitutional. This was a tactical mistake for the plaintiffs. The appellate court noted that existing Supreme Court precedent on the extraterritorial principle applied only to state laws that are "price control or price affirmation statutes." *National Pork Producers Council, et al. v. Ross, No. 20-55631, 2021 U.S. App. LEXIS 22337 (9th Cir. Jul. 28, 2021).* Thus, the extraterritorial principle does not apply to a state law that does not dictate the price of a product and does not tie the price of its in-state products to

out-of-state prices. Because Proposition 12 was neither a price control nor a price-affirmation statute (it didn't dictate the price of pork products or tie the price of pork products sold in California to out-of-state prices) the law didn't have the extraterritorial effect of regulating prices in other states.

The appellate court likewise rejected the plaintiffs' claim that Proposition 12 has an impermissible indirect "practical effect" on how pork is produced and sold outside California. *Id.* Upstream effects (e.g., higher production costs in other states) the appellate court concluded, do not violate the dormant Commerce Clause. The appellate court pointed out that a state law is not impermissibly extraterritorial unless it regulates conduct that is wholly out of state. *Id.* Because Proposition 12 applied to California and non-California pork production the higher cost of production was not an impermissible effect on interstate commerce.

The appellate court also concluded that inconsistent regulation from state-to-state was permissible because the plaintiffs had failed to show a compelling need for national uniformity in regulation at the state level. *Id.* In addition, the appellate court noted that the plaintiffs had not alleged that Proposition 12 had a discriminatory effect on interstate commerce.

Simply put, the appellate court rejected the plaintiffs' challenge to Proposition 12 because a law that increases compliance costs (projected at a 9.2 percent increase in production costs that would e passed on to consumers) is not a substantial burden on interstate commerce in violation of the dormant Commerce Clause.

As noted above, the U.S. Supreme court decided to review the Ninth Circuit's opinion. Unfortunately, the Supreme Court has been careless in applying the anti-discrimination test, and in many cases, neither of the two requirements--interstate competition or harm to the national economy--is ever mentioned. *See, e.g., Hughes v. Oklahoma, 441 U.S. 322 (1979).* The reason interstate competition goes unstated is obvious – in most cases the in-state and out-of-state actors compete in the same market. But, the reason that the second requirement, harm to the national economy, goes unstated is because the Court simply assumes the issue away. The Supreme Court's decision in 2023 is a highly anticipated one for agriculture and the dormant Commerce Clause analysis and application in general.

No. 1 – The "Major Questions" Doctrine

West Virginia, et al. v. Environmental Protection Agency, et al., 142 S. Ct. 2587 (2022)

Clearly, the biggest development of 2022 that has the potential to significantly impact agriculture and the economy in general is the Supreme Court's opinion involving the Environmental Protection Agency's (EPA's) regulatory authority under the Clean Air Act (CAA). The Court invoked the "major question" doctrine to pair back unelected bureaucratic agency authority and return policy-making power to citizens through their elected representatives. The future impact of the Court's decision is clear. When federal regulations amount to setting nationwide policy and when state regulations do the same at the state level, the regulatory bodies may be successfully challenged in court.

The case involved the U.S. Supreme Court's review of the EPA's authority to regulate greenhouse gas emissions from existing power plants under the CAA. The case arose from the EPA's regulatory development of the Clean Power Plan (CPP) in 2015 which, in turn, stemmed from then-President

Obama's 2008 promise to establish policy that would bankrupt the coal industry. The EPA claimed it had authority to regulate CO2 emissions from coal and natural-gas-fired power plants under Section 111 of the CAA. Under that provision, the EPA determines emission limits. But EPA took the position that Section 111 empowered it to shift energy generation at the plants to "renewable" energy sources such as wind and solar. Under the CPP, existing power plants could meet the emission limits by either reducing electricity production or by shifting to "cleaner" sources of electricity generation. The EPA admitted that no existing coal plant could satisfy the new emission standards without a wholesale movement away from coal, and that the CPP would impose billions in compliance costs, raise retail electricity prices, require the retirement of dozens of coal plants and eliminate tens of thousands of jobs. In other words, the CPP would keep President Obama's 2008 promise by bypassing the Congress through the utilization of regulatory rules set by unelected, unaccountable bureaucrats.

The U.S. Supreme Court stayed the CPP in 2016 preventing it from taking effect. The EPA under the Trump Administration repealed the CPP on the basis that the Congress had not clearly delegated regulatory authority "of this breadth to regulate a fundamental sector of the economy." The EPA then replaced the CPP with the Affordable Clean Energy (ACE) rule. Under the ACE rule, the focus was on regulating power plant equipment to require upgrades when necessary to improve operating practices. Numerous states and private parties challenged the EPA's replacement of the CPP with the ACE. The D.C. Circuit Court vacated the EPA's repeal of the CPP, finding that the CPP was within the EPA's purview under Section 7411 of the CAA – the part of the CAA that sets standards of performance for new sources of air pollution. *American Lung Association v. Environmental Protection Agency, 985 F.3d 914 (D.C. Cir. 2021).* The Circuit Court also vacated the ACE and purported to resurrect the CPP. In the fall of 2021, the U.S. Supreme Court agreed to hear the case.

The Supreme Court reversed, framing the issue as whether the EPA had the regulatory authority under Section 111 of the CAA to restructure the mix of electricity generation in the U.S. to transition from 38 percent coal to 27 percent coal by 2030. The Supreme Court said EPA did not, noting that the case presented one of those "major questions" because under the CPP the EPA would tremendously expand its regulatory authority by enacting a regulatory program that the Congress had declined to enact. While the EPA could establish emission limits, the Supreme Court held that the EPA could not force a shift in the power grid from one type of energy source to another. The Supreme Court noted that the EPA admitted that did not have technical expertise in electricity transmission, distribution or storage. Simply put, the Supreme Court said that devising the "best system of emission reduction" was not within EPA's regulatory power.

Clearly, the Congress did not delegate administrative agencies the authority to establish energy policy for the entire country. While the Supreme Court has never precisely defined the boundaries and scope of the major question doctrine, when the regulation is more in line with what should be legislative policymaking, it will be struck down. The Supreme Court's decision is also broad enough to have long-lasting consequences for rulemaking by *all* federal agencies including the USDA/FSA. The decision could also impact the Treasury Department's promulgation of tax regulations.

The Supreme Court's decision returns power to the Congress that it has ceded over the years to administrative agencies and the Executive branch concerning matters of "vast economic and political

significance." But it's also likely that the Executive branch and the unelected bureaucrats of the administrative state will likely attempt to push the envelope and force the courts to push back. It's rare that the Executive branch and administrative agencies voluntarily return power to elected representatives as was done in numerous instances from 2017 through 2020.

Conclusion

Agricultural law and tax issues were many and varied in 2022. In 2023, the U.S. Supreme Court will issue opinions in the California Proposition 12 case and the *Sackett* case involving the scope of the federal government's jurisdiction over wetlands. Also, there has been a major development in the Tax Court involving tax issues associated with deferred grain contracts that has resulted in a settlement with IRS, the terms of which cannot be disclosed at this time. If 2022 showed a trend with USDA it is that the USDA will continue several "hardline" positions against farmers – a narrow definition of farm income; broad regulatory control over wet areas in fields; and ceding regulatory authority to the EPA and the COE. The U.S. Supreme Court is also anticipated to issue on opinion with potentially significant implications for Medicaid planning.

Of course, the expanding war against Russia being fought in Ukraine will continue to dominate ag markets throughout 2023. At home, the general economic data is not good and that will have implications in 2023 for farmers and ranchers. On January 26, the U.S Bureau of Economic Analysis issued a report (https://www.bea.gov/) showing that the U.S. economy grew by 2.9 percent in the fourth quarter of 2022 and 2.1 percent for all of 2022. But, the report also showed that economic growth in the economy is slowing. Business investment grew by a mere 1.4 percent in the fourth quarter of 2022, consisting almost entirely of inventory growth. That will mean that businesses will be forced to sell off inventories at discounts, which will lower business profits and be a drag on economic growth in 2023. Nonresidential investment was down 26.7 percent due to the increase in home prices, increased interest rates and a drop in real income. On that last point, real disposable income dropped $1 trillion in 2022, the largest drop since 1932 - the low point of the Great Depression. Personal savings also dropped by $1.6 trillion in 2022. This is a "ticking timebomb" that is not sustainable because it means that consumers are depleting cash reserves. This indicates that spending will continue to slow in 2023 and further stymie economic growth - about two-thirds of GDP is based on consumer spending. Relatedly, the Dow was down 8.8 percent for 2022, the worst year since 2008.   2022 also saw a reduction in the pace of international trade. Imports dropped more than exports which increases GDP, giving the illusion that the economy is better off.

Certainly, 2023 will be another very busy year for rural practitioners and those dealing with legal and tax issues for farmers and ranchers.

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