KANSAS LEGISLATIVE RESEARCH DEPARTMENT

68-West–Statehouse, 300 SW 10th Ave.
Topeka, Kansas 66612-1504
(785) 296-3181 • FAX (785) 296-3824
kslegres@klrd.ks.gov http://www.kslegislature.org/klrd

February 20, 2012

To: Raney Gilliland

From: Abigail Boudewyns, Legislative Fellow

Re: Corporate Farming

CORPORATE FARMING LAWS

Throughout the Midwest and in Kansas, corporate farming laws exist which restrict corporations and other corporate forms, excepting family farm operations, from owning, acquiring, or leasing any agricultural land in the state for farming activities.[1] The purpose behind corporate farming laws was and is to protect local family farms from corporations coming in and creating competition that would have negative economic impacts on smaller family farms.[2]

Since their inception, corporate farming laws have been challenged in the courts under the Equal Protection Clause, Due Process Clause, Privileges and Immunities Clause, and finally the Contract Clause of the United States Constitution.[3] They have been consistently upheld as constitutional until recently when Nebraska's and South Dakota's corporate farming laws were struck down by the Eighth Circuit for violating the Dormant Commerce Clause of the Constitution. This memorandum will summarize the Eighth Circuit's decisions regarding Dormant Commerce Clause challenges to corporate farming laws as well as compare and contrast Kansas' corporate farming law to the laws that have been found to be unconstitutional.

Constitutional Challenges to Corporate Farming Laws

Corporate farming laws have been brought before the Eighth Circuit three times in recent years under the Dormant Commerce Clause. First in South Dakota where the Court struck down a constitutional amendment which had passed, second in Iowa where the Iowa Legislature amended the statute during the trial, and most recently in Nebraska where the Court struck down a corporate farming constitutional provision. The following is a summary of the Dormant Commerce Clause and the decisions made by the Eighth Circuit.

---

1 *See* K.S.A. 17-5904 (2011).

2 Pittman, Harrison M., *The Constitutionality of Corporate Farming Laws in the Eighth Circuit*, The National Agricultural Law Center,1 (2004).

3 *See id.*

Dormant Commerce Clause

The Commerce Clause of the *U.S. Constitution* grants Congress the power to regulate interstate commerce and any state law that conflicts with a federal law enacted under the Commerce Clause will be held to be unconstitutional.[4] The Dormant Commerce Clause comes from this authority in that even if Congress has not expressly acted pursuant to its power under the Commerce Clause, states may still not enact laws that discriminate against or unduly burden interstate commerce.

In examining whether a state has violated the Dormant Commerce Clause, a court will look first to whether the enacted law discriminates against interstate commerce by examining whether in-state and out-of-state interests are treated differently, with the in-state interests benefiting at the cost of burdening out-of-state interests.[5] A court will find a law to be discriminatory if it was enacted with a discriminatory purpose or has a discriminatory effect.[6] If a law is found to be discriminatory on its face - either through purpose or effect, then it will be held to be unconstitutional unless the state can demonstrate that it has no other means of advancing a legitimate local interest.[7]

If a law is not found to be facially discriminatory through its purpose or effect, then it may still be held unconstitutional under a second analysis. Under the second analysis, a challenged law will be struck down if the burden it imposes on interstate commerce is clearly excessive when compared to its supposed local benefits.[8]

South Dakota

In 1998, South Dakota amended its state constitution to prohibit corporations and syndicates from acquiring or obtaining any interest in real estate used for farming and to engage in farming.[9] An exemption was created for a "family farm corporation or syndicate," which was defined as a corporation or syndicate engaged in farming or the ownership of agricultural land, in which a majority of the partnership interests, shares, stock, or other ownership interests were held by members of a family, or a trust created for the benefit of a member of that family.[10] Additionally, family members in a family farm corporation had to reside on or be actively engaged in the day-to-day labor and management of the farm; day-to-day labor and management requiring daily or routine substantial physical exertion and administration.[11] The Eighth Circuit ultimately found the amendment to be unconstitutional as a violation of the Dormant Commerce Clause.

---

4 *Id* at 3.

5 *Jones v. Gale*, 470 F.3d 1261, 1267 (8th Cir. 2006).

6 *See id.*

7 *See id* at 1270.

8 Pittman at 4.

9 *South Dakota Farm Bureau, Inc. v. Hazeltine*, 340 F.3d 583, 587 (8th Cir. 2003).

10 *Id.*

11 *Id* at 588.

The Eighth Circuit, in striking down the corporate farming amendment, looked to direct evidence that the drafters of the constitutional amendment, or the South Dakota populace who voted for the constitutional amendment, had the intent to discriminate against out-of-state businesses.[12] The court noted that there was a substantial amount of direct evidence, with the most compelling being a "pro-con" statement created by the drafters of the amendment, the South Dakota Secretary of State, which was disseminated to the public. The "pro-con" statement listed as a "con" that without passage of the amendment, "desperately needed profits [would] be skimmed out of local economies and into the pockets of distant corporations."[13] Additionally, the statement explained that the amendment would give South Dakota the opportunity to decide whether control of the state's agriculture should remain, "in the hands of family farmers and ranchers or fall into the grasp of a few large corporations."[14] Additionally, notes from drafting and planning meetings also provided direct evidence of the drafters' intent to discriminate against out-of-state businesses.[15]

Based on the evidence, the Eighth Circuit concluded that the constitutional amendment was motivated by a discriminatory purpose, thus making it unconstitutional unless the state could demonstrate that there were no other reasonable alternatives by which the state could achieve its legitimate local interest of promoting family farms and protecting the environment.[16] The Court agreed that promoting family farms and protecting the environment was a legitimate local interest; however, the state provided no evidence that there were no reasonable alternatives to achieving those legitimate interests, and the Court, while not proposing alternatives, believed that several could be found.[17] Due to the discriminatory intent and the availability of reasonable alternatives to achieve the legitimate local interests, the Court found that the corporate farming constitutional amendment was unconstitutional under the Dormant Commerce Clause.

Nebraska

In 1982 Nebraska passed a constitutional amendment which prohibited ownership of Nebraska farm or ranch land by any corporation, domestic or foreign, which was not a Nebraska family farm corporation.[18] The prohibition did not apply to family farm corporations or limited partnerships in which at least one family member resided on or engaged in the daily labor and management of the farm.[19] The Eighth Circuit found that because the prohibition on farming by corporations did not apply to the family farm corporations in which a family member resided, or engaged in the daily labor and management of the farm, that the law essentially required a

---

12 *Id* at 593.

13 *Id* at 594.

14 *Id.*

15 *Id.*

16 *Id* at 597.

17 *Id.*

18 *Jones v. Gale*, 470 F.3d 1261, 1264 (8th Cir. 2006).

19 *Id* at 1265.

person to be within a physically and economically feasible commute of Nebraska farms and therefore favored Nebraska residents.[20]

In reaching its decision, the Court looked at the plain language of the constitutional amendment and asserted that its reasonable interpretation required a family member or major shareholder to reside on, or engage in the daily labor and management of, a farm or ranch in Nebraska.[21] The Court found that the constitutional amendment essentially prohibited absentee ownership and operation of a farm and ranch land by a corporate entity.[22] The Court found the constitutional amendment to be discriminatory on its face because it afforded differential treatment of in-state and out-of-state economic interests that benefited the in-state interests and burdened the out-of-state interests.[23] After determining that the amendment was facially discriminatory, the Court also noted that the amendment would be discriminatory based on intent or purpose.[24] Again, in looking at direct and indirect evidence, the Court, as it did in South Dakota, found that the text of the amendment and ballot title, as well as advertisements in support of the constitutional amendment, all had a discriminatory intent.[25]

After finding the constitutional amendment to be discriminatory, the Court then looked for whether the state could show that it had no other way to advance a legitimate local interest. Nebraska argued that the amendment was necessary to deal with absentee owners of land and negative effects on the social and economic culture of rural Nebraska.[26] Unlike in South Dakota, the Eighth Circuit in the Nebraska case found that a desire to maintain the *status quo* was not in itself a legitimate local interest, but rather was the kind of "xenophobia" that the Dormant Commerce Clause was meant to protect individuals from.[27]

In 2009, the Nebraska Legislature attempted to pass a statute which found it to be in the public interest of the state to encourage ownership and control of agricultural production and agricultural assets by individuals and families engaged in day-to-day labor and management of farming or ranching operations.[28] The proposed legislation would have loosened up the prohibitions to allow qualified owner-operator controlled entities, non-profit corporations, farms for research purposes, farming or ranching operations conducted for the purpose of raising poultry, as well as various other exceptions.[29] However, the bill failed to receive enough support

---

20 *Id* at 1268.

21 *Id.*

22 *Id* at 1269.

23 *Id* at 1269.

24 *Id.*

25 *Id* at 1269-1270.

26 *Id* at 1270

27 *Id.*

28 Anthony B. Schutz, *Corporate-Farming Measures in a Post-Jones World*, 14 Drake J. Agric. L. 97, 143 (2009).

29 *Id.*

in the legislature, and since the finding of unconstitutionality of the constitutional amendment, Nebraska has been without a corporate farming law or constitutional provision.[30]

In Comparison: Kansas' Corporate Farming Law

KSA 17-5904 states that "no corporation, trust, limited liability company, limited partnership or corporate partnership [. . .] shall, either directly or indirectly, own, acquire or otherwise obtain or lease any agricultural land in this state." The statute exempts family farm corporations and authorized farm corporations, as well as other forms of limited liability family farm companies and partnerships.[31] Much like the corporate farming laws described above, Kansas' law requires family farm corporations, authorized farm corporations, and limited agricultural partnerships to have at least one stockholder or partner residing on the farm or actively engaged in the labor or management of the farming operations.[32] Farming is then defined to mean the "cultivation of land for the production of agricultural crops," among other things, but does not include contracting for spraying, harvesting, or other farm services.[33] Additionally, all incorporators of "authorized farm corporations" must be Kansas residents.[34]

Kansas is in the Tenth Circuit, which has not yet addressed the constitutionality of corporate farming laws under the Dormant Commerce Clause. While the Tenth Circuit is not required to follow the Eighth Circuit's analysis, circuit courts often will look to the analysis of other circuits when considering an issue for the first time. Under the Eighth Circuit's analysis, Kansas could face potential problems with its statute because it requires at least one of the stockholders or partners to physically reside on the farm or be actively engaged in the labor or management of the farming operations. The statute could also run into problems with its requirement that all incorporators be Kansas residents in order to qualify as an authorized farm corporation. Any language that explicitly or implicitly favors in-state residents runs the risk of being found discriminatory by a court under the Dormant Commerce Clause.

However, there is some flexibility in the Kansas corporate farming law in that it requires either physical residence on the farm or active engagement. Active engagement can be achieved through either physical labor or management. Nebraska's constitutional amendment was much harsher in that it required both daily labor and management - with the requirement for daily labor having the impact of requiring someone to live fairly close to the farm, thus favoring Nebraska residents. Much of the analysis on the Kansas statute would depend on how the Tenth Circuit would choose to interpret the phrases "farming operations," the "farm," and the requirement of "active engagement."[35] If the Tenth Circuit construes the terms narrowly to mean that you have to be physically present on the farm in order to manage it, or to be actively engaged in the farming operations, then the statute would likely be found to be discriminatory under a rationale similar to that used in Nebraska. Additionally, it is likely that any requirement

30 *Id.*

31 *Id.*

32 K.S.A. 17-5903(j).

33 K.S.A. 17-5903(h).

34 K.S.A. 17-5903(k).

35 *See* Anthony B. Schutz, *Corporate-Farming Measures in a Post-Jones World*, 14 Drake J. Agric. L. 97, 130 (2009).

to live on the farm would be found to be discriminatory by a court as the language would benefit Kansas residents to the detriment of out-of-state individuals.[36] Finally, the explicit requirement that a person must be a Kansas resident in order to qualify under some of the exemptions, such as for the authorized farm corporation, would likely be found to be discriminatory because out-of-state individuals would not be able to qualify for such an exemption. While out-of-state individuals may be able to qualify under the family farm corporation exemption, it still presents them with a significant hurdle that in-state residents do not face.[37]

While the initial question in determining whether the Kansas statute is discriminatory would focus on the differential treatment of in-state and out-of-state individuals, the second part of the analysis, if the court were to find discrimination, would be to look at whether the state has no reasonable alternative to achieve its legitimate local interest. So far, states have been unable to meet this burden as they have not provided any evidence that there are no reasonable alternatives to the corporate farming laws. Additionally, the State would need to provide a legitimate local interest that was acceptable in the Tenth Circuit. The Eighth Circuit found promoting family farms and protecting the environment to be an acceptable local interest, but maintaining the *status quo* in rural communities not to be.[38] It is unclear what the Tenth Circuit would consider to be acceptable, as the issue has yet to be considered in that circuit.

---

36 *See id* at 131.

37 *Id.*

38 *South Dakota Farm Bureau, Inc. v. Hazeltine* at 597; *Jones v. Gale* at 1270.