

**REPORT OF THE JUDICIAL COUNCIL
AGRICULTURAL CORPORATIONS ADVISORY COMMITTEE**

During the 2013 Legislative Session, identical bills were introduced that would have made extensive amendments to the Agricultural Corporations Act, K.S.A. 17-5902 *et seq.* Hearings were held on HB 2404 in the House Committee on Agricultural and Natural Resources and on SB 191 in the Senate Committee on Natural Resources, but neither bill made it out of committee. In May 2013, the chairpersons of the Committees – Representative Sharon Schwartz and Senator Larry Powell, requested that the Judicial Council review the Kansas Agricultural Corporations statutes to determine if there are potential constitutional issues with the laws as currently written. The written request included a number of potential questions for the Judicial Council to pursue.

The Judicial Council considered the Legislators' request in June 2013. The Council agreed to form a new advisory committee to undertake a study to review K.S.A. 17-5902 *et seq.* for potential constitutional issues. If the advisory committee were to determine that provisions of the law have questionable constitutional footing, the committee would suggest changes to the law that would strengthen its constitutionality. In conducting its work, the Agricultural Corporations Advisory Committee directed its attention to existing language and did not consider alternative statutory schemes.

COMMITTEE MEMBERSHIP

The members of the Judicial Council Agricultural Corporations Advisory Committee are:

Rep. Lance Y. Kinzer, Co-Chair, Member of Kansas House of Representatives, member of the Kansas Judicial Council, and attorney in private practice; Olathe

Sarah Bootes Shattuck, Co-Chair, Member of the Kansas Judicial Council and attorney in private practice; Ashland

Prof. Jeffrey D. Jackson, Professor at Washburn University School of Law; Topeka

Jim Kaup, Attorney in private practice, Topeka

Prof. Richard E. Levy, Professor at Kansas University School of Law; Lawrence

Erick E. Nordling, Attorney in private practice; Hugoton

Dale G. Schedler, Attorney in private practice; Kansas City

Rep. Sharon Schwartz, Member of Kansas House of Representatives and Business Manager of a family farm; Washington

BACKGROUND

A thorough summary of the background of current Kansas law relating to agricultural corporations is contained in a memorandum drafted by the Kansas Legislative Research Department and attached hereto at page 7. A request for an opinion on the constitutionality of the Kansas Agricultural Corporations Act was also presented to the Office of the Attorney General. The Attorney General's response is attached at page 19.

Questions about the constitutionality of the Kansas Agricultural Corporations Act have been a source of concern for several years as a result of three cases decided in the Eighth Circuit which struck down statutory provisions and state Constitutional provisions of South Dakota, Iowa, and Nebraska as unconstitutional under the Dormant Commerce Clause. See *Smithfield Foods, Inc. v. Miller*, 241 F. Supp. 2d 978 (2003), *South Dakota Farm Bureau, Inc. v. Hazeltine*, 340 F.3d 583 (2003), and *Jones v. Gale*, 470 F.3d 1261 (2006). The concern has been raised that portions of the Kansas statutes are similar to those that have been deemed unconstitutional. The Kansas statutes have not been challenged to date, and such a challenge would be a case of first impression for the Tenth Circuit Court of Appeals, which has jurisdiction over cases heard in the federal district courts in Kansas.

COMMITTEE STUDY

The Committee met in person on August 30, September 27, and October 25, and via telephone conference on November 22, 2013 to discuss constitutional issues surrounding the Agricultural Corporation statutes. The Committee was not charged to consider the underlying policy of the law or address its wisdom, but rather focused only on whether the law is vulnerable to a constitutional challenge and, if so, how the law might be changed to avoid constitutional difficulties.

After an initial discussion, the Committee agreed that the only serious constitutional issues appear to arise under the so-called "Dormant" Commerce Clause. Under the applicable constitutional precedents, the critical issue is whether the agricultural corporations law discriminates against interstate commerce or nonresidents.

If a law is discriminatory, then it is "virtually per se invalid" and will survive only if it "advances a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives." *Department of Revenue of Ky. v. Davis*, 553 U.S. 328, 338 (2008). This test is very difficult to meet and a law would be unlikely to survive under this test because it is possible to accomplish the state's legitimate objectives in nondiscriminatory ways.

If, on the other hand, a law is not discriminatory, then the law "will be upheld unless the burden imposed on [interstate] commerce is clearly excessive in relation to the putative local benefits." *Id.* at 338-39. If this test applies, then a law is more likely to be upheld as constitutional.

A. The Committee identified some provisions that explicitly discriminate against interstate commerce by preferring Kansas residents or business:

- K.S.A. 17-5903(k) requires an "authorized farm corporation" to be formed under the laws of Kansas.

- K.S.A. 17-5903(d)(2) and (u)(2) define “limited agricultural partnerships” and “limited liability agricultural companies” by reference to ownership by “general partnerships other than corporate partnerships formed under the laws of Kansas.”

These provisions explicitly discriminate on the basis of whether the entity was formed under Kansas law (as opposed to the laws of another state), so the provisions would have to meet the stringent test for discriminatory laws. Because the provisions are unlikely to survive this test, the Committee recommends revising the provisions to eliminate the reference to formation under the laws of Kansas, as follows:

17-5903. Definitions. As used in this act:

...

(d) "Limited agricultural partnership" means a limited partnership founded for the purpose of farming and ownership of agricultural land in which:

- (1) The partners do not exceed 10 in number;
- (2) the partners are all natural persons, persons acting in a fiduciary capacity for the benefit of natural persons or nonprofit corporations, or general partnerships other than corporate partnerships formed under the laws of the state of Kansas; and
- (3) at least one of the general partners is a person residing on the farm or actively engaged in the labor or management of the farming operation. If only one partner is meeting the requirement of this provision and such partner dies, the requirement of this provision does not apply for the period of time that the partner's estate is being administered in any district court in Kansas.

...

(k) "Authorized farm corporation" means a ~~Kansas~~ corporation authorized to do business in Kansas, other than a family farm corporation, all of the incorporators of which are ~~Kansas residents~~ natural persons, family farm corporations or family farm limited liability agricultural companies or any combination thereof, and which is founded for the purpose of farming and the ownership of agricultural land in which:

- (1) The stockholders do not exceed 15 in number; and
- (2) the stockholders are all natural persons, family farm corporations, family farm limited liability agricultural companies or persons acting in a fiduciary capacity for the benefit of natural persons, family farm corporations, family farm limited liability agricultural companies or nonprofit corporations; and
- (3) if all of the stockholders are natural persons, at least one stockholder must be a person residing on the farm or actively engaged in labor or management of the farming operation. If only one stockholder is meeting the requirement of this provision and such stockholder dies, the requirement of this provision does not apply for the period of time that the stockholder's estate is being administered in any district court in Kansas.

...

(u) "Limited liability agricultural company" means a limited liability company founded for the purpose of farming and ownership of agricultural land in which:

- (1) The members do not exceed 10 in number; and
- (2) the members are all natural persons, family farm corporations, family farm limited liability agriculture companies, persons acting in a fiduciary capacity for the benefit of natural persons, family farm corporations, family farm limited liability agricultural companies or nonprofit corporations, or general partnerships other than corporate partnerships ~~formed under the laws of the state of Kansas~~; and
- (3) if all of the members are natural persons, at least one member must be a person residing on the farm or actively engaged in labor or management of the farming operation. If only one member is meeting the requirement of this provision and such member dies, the requirement of this provision does not apply for the period of time that the member's estate is being administered in any district court in Kansas.

B. The Committee also identified several identical provisions that might be considered discriminatory. All of these provisions define acceptable business entities that may conduct farming operations by requiring that “at least one” of the partners, stockholders or members of the company “is a person residing on the farm or actively engaged in the labor or management of the farming operation.” See K.S.A. 17-5903(d)(3), (j)(3), (u)(3), and (w)(3).

This language is not explicitly discriminatory, but it could arguably be discriminatory in practice if the language of the statute is interpreted in a way that requires a person to live on the farm or nearby because it would then discriminate against nonresidents. In *South Dakota Farm Bureau, Inc. v. Hazeltine*, 340 F.3d 583 (8th Cir. 2003) and *Jones v. Gale*, 470 U.S. 1261 (8th Cir. 2006), the court invalidated state corporate farming laws that required a person to “reside on or be actively engaged in the *day-to-day* labor *and* management” of a farm. The court concluded that these laws were discriminatory in effect because being actively involved in the day-to-day labor and management of the farm required the person to live on the farm. In addition, there was evidence in the history of these provisions suggesting that their purpose was to exclude nonresidents. Thus, the court in those cases concluded that the laws were discriminatory.

There are important differences between the Kansas statutes and those invalidated in the cases discussed above. First, the Kansas statutes do not require that active engagement relate to “day-to-day” operations. Second, the invalid statutes require engagement in both labor “and” management, while the Kansas statute refers to labor “or” management. This difference is important because labor would require physical presence, while management would not. Thus, a person could be actively involved in the management of a farm without living there, especially with the advent of computers, cell phones, and other forms of telecommunications. Third, the Committee did not find any evidence of a discriminatory purpose in legislative history of the Kansas statute. The Committee therefore concluded that these provisions would probably not be considered discriminatory.

Nonetheless, the Committee also concluded that the provisions are still potentially vulnerable and it cannot be stated with certainty that they would be upheld as nondiscriminatory. One step that might be taken to improve the chances that these provisions would be upheld would be to clarify that physical presence on the farm is not required to satisfy the active engagement requirement. This step might be accomplished by adding a definition for the phrase “actively engaged in the labor or management.” That definition might be phrased as follows:

“Person actively engaged in the labor or management of the farming operation” includes a person who is directly involved in farming operations through activities such as physical labor, supervision of employees, financial planning, purchases and sales, or other aspects of the business. Physical presence at the farm is not required.

A simpler alternative might be to simply state that “Being actively engaged in the labor or management of the farming operation does not require physical presence at the farm.”

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MEMORANDUM

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KANSAS CORPORATE FARMING LAW

Background

The following summarizes former and current corporate farming statutes in Kansas.

The original law prohibiting certain types of corporate farming in Kansas was passed in 1931. It prohibited corporate farming for the purpose of growing wheat, corn, barley, oats, rye, or potatoes and the milking of cows. Following the enactment of the corporate farming law of 1931, several amendments were made, among which was an amendment to allow a domestic or foreign corporation, organized for coal mining purposes, to engage in agricultural production on any tract of land owned by the corporation which had been strip mined for coal.

In 1965, major amendments were made to the law. Grain sorghums were added to the list of crops that were restricted. In addition, the 1965 amendments made it possible for certain types of corporations, which met detailed specifications, to engage in agricultural production of those restricted crops and also the milking of cows. However, problems with the statute continued to exist. As a result, the Legislature had special interim committees study the problems with the Kansas Corporate Farming Law in 1972, 1975, and 1978. As a result of the 1972 interim study, the 1973 Kansas Legislature passed additional reporting requirements of corporations which held agricultural land in the state. The purpose of this legislation was to determine the extent of corporate ownership of agricultural land. Neither the 1975 nor the 1978 study resulted in legislation being adopted. Additionally, discussions of the problems with the corporate farming statute were held throughout this time period.

Among the problems discussed with the law between 1972 and 1981 were the following:

- The fact that the former corporate farming statute permitted corporations to be engaged in certain types of crop endeavors, while having no restrictions on crops such as alfalfa and soybeans. Also, the former statute was unclear as to whether pasture land was to be included in the acreage restrictions contained in the statute (5,000 acres).
- The fact that the former corporate farming statute lacked an enforcement provision, which was said to have made it difficult for the Attorney General or other officials to enforce.

- The fact that the 5,000-acre limitation imposed on corporations permitted to engage in certain agricultural activities was too restrictive, especially given the various types of farming enterprises in the state, and particularly if pasture land was to be included in the 5,000-acre limitation. This acreage limitation was of particular concern to farming interests in western Kansas, where acreages generally are much larger.
- The restriction of ten stockholders was too limiting; and the restriction of owning stock in more than one agricultural corporation is encountered often through marriage and inheritance.
- The fact that nonagricultural corporations often owned agricultural land as a buffer zone or for expansion purposes. Because the former statute placed restrictions on the characteristics of corporations permitted to be engaged in certain farming activities, some of them may have been in violation when they leased or rented the land back to farmers. This issue was addressed in the Attorney General's case against the DuPont Corporation in 1980 and 1981.
- The fact that some of the universities and colleges in the state acquired agricultural land and were somewhat dependent upon the land's revenue-raising capabilities.
- The fact that some legislators were concerned that large pension and benefit funds operating as trusts could acquire significant amounts of agricultural land for investment purposes.

As a result of these concerns and others expressed to the Senate Agriculture and Small Business Committee early in the 1981 Legislative Session, the Committee introduced SB 298. Extensive hearings as to the problems inherent in the current law were held before the decision was made to introduce a bill. Additional hearings were conducted after the bill had been introduced. This bill eventually became the basis for the state's current Corporate Farming Law, being signed by the Governor on April 28, 1981.

Since 1981, this law has undergone slight modifications. However, these modifications, for the most part, have not impacted significantly on the intent or policy of the legislation.

The law prohibits corporations, trusts, limited liability companies, limited partnerships, or corporate partnerships other than family farm corporations, authorized farm corporations, limited liability agricultural companies, limited agricultural partnerships, family trusts, authorized trusts, or testamentary trusts from either directly or indirectly owning, acquiring, or otherwise obtaining or leasing any agricultural land in Kansas.

Legislators in 1981 recognized certain circumstances or entities which may at one time or another have a legitimate need or situation which requires the acquisition of agricultural land. As a result, 13 exemptions from the restrictions outlined above were included in the original legislation. The restrictions on owning, acquiring, obtaining, or leasing do not apply to:

- a bona fide encumbrance taken for purposes of security;
- agricultural land when acquired as a gift, either by grant or devise, by a bona fide educational, religious, or charitable nonprofit corporation (this addresses the problems that some state colleges have when agricultural land is left to them by grant or devise, and is used as a source of revenue);
- agricultural land acquired by a corporation or a limited liability company as is necessary for the operation of a nonfarming business, provided the corporation does not engage or receive any financial benefit, other than rent, from the farming operation (this exemption was to solve problems with nonfarming businesses, such as DuPont, which need land for buffer zones, industrial expansion, or other similar needs);
- agricultural land acquired by a corporation or a limited liability company by process of law in the collection of debts or pursuant to a contract for deed executed prior to the effective date of the act, or by any procedure for the enforcement of a lien or claim, if the corporation divests itself of any agricultural land within ten years (except that the provisions of K.S.A. 9-1102 are to apply when a bank acquires agricultural land);
- a municipal corporation;
- agricultural land which is acquired by a trust company or bank in a fiduciary capacity or as a trustee for a nonprofit corporation;
- agricultural land owned or leased by a corporation, corporate partnership, limited corporate partnership, or trust either: (a) prior to July 1, 1965; or (b) which was not in compliance with K.S.A. 17-5901 prior to its repeal, provided that under both (a) and (b) these entities do not own or lease any greater acreage of agricultural land than they owned or leased prior to this Act; or (c) which was not in compliance with K.S.A. 17-5901 prior to its repeal, but is in compliance by July 1, 1991 (this exemption is the "grandfather clause," which clarifies the status of corporations, corporate partnerships, limited corporate partnerships, or trusts previously engaged in agricultural activities in the state or which own or lease agricultural land prior to the enactment of the 1981 law);
- agricultural land held or leased by a corporation or a limited liability company for use as a feedlot, a poultry confinement facility, or rabbit confinement facility;
- agricultural land held or leased by a corporation for the purpose of the production of timber, forest products, nursery products, or sod;
- agricultural land used for educational research or scientific or experimental farming;
- agricultural land used for the growing of crops for seed purposes or alfalfa by an alfalfa processing plant within 30 miles of the plant site;

- agricultural land owned or leased by a corporate partnership or limited corporate partnership in which either natural persons, family farm corporations, authorized farm corporations, limited liability agricultural companies, family trusts, authorized trusts or testamentary trusts, are associated; and
- any corporation, either domestic or foreign, or limited liability company organized for coal-mining purposes, which engages in farming on any tract of land owned by it which has been strip mined for coal.

A fourteenth exception was enacted in 1986 (SB 308). The exception stated: agricultural land owned or leased by a limited partnership prior to the effective date of the act would be exempted from the general prohibition of acquiring agricultural land.

An amendment in 1987 made it clear that when a bank acquires ownership of real estate through the satisfaction of debt that the bank statute, K.S.A. 9-1102, is the statute that governs (HB 2076). This statute permits the ten-year ownership by banks, but also grants the State Bank Commissioner the authority to grant an extension for an additional four years, or any portion of four years.

The 1981 enactment made corporations, trusts, limited corporate partnerships, or corporate partnerships which violated the provisions of the bill subject to a civil penalty of not more than \$50,000 and the divestiture of any land acquired in violation within one year after judgment is entered. The bill permitted district courts to prevent and restrain violations through injunction, and authorized the Attorney General or county attorney to institute suits on behalf of the state to enforce the provisions of the bill. Civil penalties sued for and recovered by the Attorney General are paid into the State General Fund. Civil penalties sued for and recovered by the county attorney or district attorney are paid into the general fund of the county where the proceedings were instigated. The additional entities covered by the law through subsequent amendments are covered by the penalties.

Other bills that attempted to make amendments to the Kansas Corporate Farming Law before 1987 included 1985 SB 288 and 1986 SB 543.

Background on the Issue of Permitting Corporate Hog Operations

The issue of permitting corporate hog operations (or sometimes referred to as swine confinement facilities) to expand their acreages was first brought to the Legislature by former State Senator Charlie Angell of Plains in 1984. He requested legislation be introduced that would permit Dekalb Swine Breeders to expand its operation in the Plains area in a partnership with the Seaboard Corporation and Pauls & Whites International. The legislation was introduced by the Senate Agriculture and Small Business Committee and received eventual approval by that Committee. The bill, SB 519, added an additional exemption to the provisions of the Corporate Farming Law. The exemption was for "swine confinement facilities" owned or leased by a corporation. "Swine confinement facility" was defined to mean the structures and related equipment used for housing, breeding, farrowing, or feeding of swine in an enclosed environment. The term included within its meaning agricultural land in such acreage as is necessary for isolation of the facility to reasonably protect the confined animals from exposure to disease and minimize environmental impact. Eventually, the bill received approval by both the Committee and by the Senate Committee of the Whole. In the House, the bill was referred to the Judiciary Committee, which passed the bill without recommendation. The House

Committee of the Whole referred the bill to the House Agriculture and Livestock Committee, where it eventually died. In its final form, SB 519 would have permitted corporations to own or lease agricultural land for use as a swine confinement facility, but only as much agricultural land as would be necessary for proper disposal of liquid and solid wastes and for isolation of the facility to reasonably protect the confined animals from exposure to disease.

During this time, the Attorney General was asked by then Secretary of Economic Development, Jamie Schwartz, to respond to specific questions regarding the types of activities that are permitted under the state's Corporate Farming Law. Specifically, Secretary Schwartz asked whether a corporation, desiring to operate a feedlot for hogs, is precluded from the ownership of agricultural land because of its desire to incorporate an incidental breeding operation on its feedlot premises. The Attorney General was responding to the premise that the hogs would be bred, fed, and slaughtered on the feedlot premises.

1987, 1988, and 1989 Legislative Actions and Amendments

The next time the issue of corporate hog operations came before the Legislature was in 1987, as a result of a recommendation made by the Legislative Commission on Kansas Economic Development and by the Economic Development Task Force on Agriculture. The Task Force heard from a spokesperson from the Dekalb Swine Breeders, Inc. He indicated that the firm had intentions, at that time, of expanding its facilities and would like to do so in Kansas, but said that the Corporate Farming Law prevented its expansion in Kansas. As a result, the Agriculture Task Force recommended that legislation be introduced to expand the Kansas Corporate Farming Law by permitting a corporation to own or lease agricultural land for the purpose of operating a swine confinement facility.

In making this recommendation, the Task Force had learned that since 1980 hog numbers in Kansas had declined by 32 percent and the number of hog operations had declined by 42 percent. Also, the Task Force heard testimony that Kansas is ideally located for pork production, the result of which should be the fostering of hog processing facilities. The Task Force also recommended that the expansion of the law should apply to the poultry industry as well.

The recommendation of the Task Force also was made by the Commission. This recommendation resulted in 1987 HB 2076, which was first referred to the House Economic Development Committee. The House Economic Development Committee amended the bill to permit corporations to purchase agricultural land for the purpose of operating poultry confinement facilities. The bill at this point also prohibited any city or county from granting any exemption from ad valorem property taxation under Section 13 of Article 11 of the Kansas Constitution to a poultry confinement facility located on agricultural land and owned or operated by a corporation. The bill also prohibited any exemption from ad valorem property taxation for property purchased, equipped, constructed, repaired, or enlarged with all or part of the proceeds of revenue bonds used for any poultry confinement facility which is located on agricultural land and owned, acquired, or leased by a corporation. The Committee had eliminated the provision granting any exemption to swine confinement facilities. When it was referred to the Senate Agriculture Committee, rabbit confinement facilities were added to the exemption list. In the Senate Committee of the Whole, an amendment was added to exempt swine confinement facilities. During Conference Committee, the swine confinement facility exemption was deleted. The Governor signed the version exempting poultry and rabbit confinement facilities, and prohibiting them from taking advantage of the tax exemptions described above.

Other bills were introduced during the 1987 Session designed to address, either directly or indirectly, the swine confinement facility issue. These bills included SB 497, HB 2845, HB 2846, HB 2827, and HB 2990 in its amended form.

During the interim of 1987, the Special Committee on Agriculture and Livestock was assigned to study the topic of corporate farming and its impact on Kansas swine producers. During this time period, a consultant was hired to do an analysis of the swine industry in Kansas. The Special Committee reviewed the consultant's report and concluded that a select committee should be formed during the 1988 Legislative Session to consider further the consultant's report, and to receive input from around the state.

The Select Committee again reviewed the consultant's report and received testimony from concerned citizens. The Select Committee recommended legislation, which the Senate Ways and Means Committee introduced, and on which the Senate Agriculture Committee held hearings. This bill, SB 727, did not receive approval by the Senate Agriculture Committee.

The 1988 Legislature, however, did approve HB 3018, which contained amendments to the Kansas Corporate Farming Law. The bill amended the Kansas Corporate Farming Law by defining the terms "processor" and "swine confinement facility"; making it unlawful for processors of pork to contract for the production of hogs of which the processor is the owner or own hogs except for 30 days before the hogs are processed; making pork processors violating the ownership of hogs restriction subject to a \$50,000 fine; clarifying that, except for the pork processors' limitation, agricultural production contracts entered into by corporations, trusts, limited partnerships or corporate partnerships, and farmers are not to be construed to mean the ownership, acquisition, obtainment, or lease of agricultural land. The bill also prohibits any "swine confinement facility" from being granted any exemption from ad valorem taxes by a city or county, the use of proceeds of revenue bonds, the benefits of being in an enterprise zone, or the benefits of the Job Expansion and Investment Credit Act of 1976. Further, the bill establishes a swine technology center at Kansas State University, but provides no appropriations for its establishment. No moneys were appropriated for the swine technology center by the 1988 Legislature, or by any subsequent Legislature.

Three bills were introduced during the 1989 Legislative Session that proposed amendments or related to the corporate farming issue. These bills included HB 2257, HB 2368, and HB 2369. None of these bills were enacted.

Limited Liability Companies—1991 and 1992 Proposals

The 1991 Legislature approved and the Governor signed HB 2535, which made amendments to the Kansas Corporate Farming Law. The bill was assigned to the Judiciary committees in both the House and the Senate. Numerous amendments to various sections of the Corporation Code were made by the bill regarding limited liability companies. Among those were the amendments to the Corporate Farming Law.

In regard to the amendments made to the Kansas Corporate Farming Law, "limited liability companies" were added to the list of entities that are generally prohibited from indirectly or directly owning, acquiring, or otherwise obtaining or leasing any agricultural land in this state. To review the earlier explanation of the Kansas Corporate Farming Law, other entities that are generally prohibited from owning or acquiring agricultural land in Kansas are: corporations, trusts, limited partnerships, or corporate partnerships. The term "limited liability company" is

defined in K.S.A. 1991 Supp. 17-7602 to mean a company that is organized under the Kansas Limited Liability Company Act.

As was related earlier in this memorandum, the 1981 and subsequent amendments did establish a list of exemptions to the general prohibition established in the law. The 1991 bill amended the exemptions to the general prohibitions in K.S.A.17-5904. As a result of the legislation, limited liability companies are now able to own and acquire agricultural land:

- in such acreage as is necessary for the operation of a nonfarming business;
- by process of law in the collection of debts, or pursuant to a contract for deed executed prior to the effective date of the Act, or by any procedure for the enforcement of a lien or claim;
- for use as a feedlot, a poultry confinement facility, or rabbit confinement facility;
- if the "limited liability companies" are partners in corporate partnerships or limited corporate partnerships; and
- if they are organized for coal mining purposes and engage in farming on any tract of land owned by them which has been strip mined for coal.

The Kansas Limited Liability Company Act specifically states that a limited liability company formed under the Act is to be considered a separate legal entity and is not to be construed as a corporation.

The Kansas Corporate Farming Law also was amended to permit limited liability agricultural companies to own and acquire agricultural land in Kansas. Again to review, prior law had permitted only family farm corporations, authorized farm corporations, limited agricultural partnerships, family trusts, authorized trusts, and testamentary trusts to own and acquire agricultural land. (Of course, this law never prohibited or attempted to prohibit any individual from owning any amount of agricultural land in Kansas.)

The term "limited liability agricultural company" was defined by the 1991 legislation. By law this term means a limited liability company founded for the purpose of farming and ownership of agricultural land in which:

- the members do not exceed ten in number;
- the members are all natural persons, persons acting in a fiduciary capacity for the benefit of natural persons, or nonprofit corporations, or general partnerships other than corporate partnerships formed under the laws of the State of Kansas; and
- at least one of the members is a person residing on the farm or actively engaged in the labor or management of the farming operation. If only one member is meeting the requirement of this provision and such member dies, the requirement of this provision does not apply for the period of time that the member's estate is being administered in any district court in Kansas.

The legislation also modified the term "processor" to include limited liability companies. This would mean that any limited liability company that directly or indirectly controls the manufacturing, processing, or preparation for sale of pork products having a total annual wholesale value of \$10,000,000 or more would be considered a "processor." This is significant since it is unlawful under K.S.A. 17-5904 for processors of pork to contract for the production of hogs of which the processor is the owner or to own hogs except for 30 days before the hogs are processed. Also including the term "processor" would be any person, firm, corporation, member, or limited partner with a 10 percent or greater interest in another person, firm, corporation, limited liability company, or limited partnership involved in the manufacturing, processing, or preparation for sale of pork products having a total annual wholesale value of \$10,000,000 or more.

The 1992 Legislature considered HB 3082, which would have eliminated the permission for limited liability agricultural companies to own, acquire, obtain, or lease, either directly or indirectly, any agricultural land in this state. The bill died in House Agriculture Committee.

Legislative Actions and Amendments—1994

Two bills received legislative and gubernatorial approval during 1994. These bills made changes to the Kansas Corporate Farming law by permitting the acquisition of agricultural land by corporation for the purposes of developing either swine production facilities or dairy production facilities. The two bills which were adopted are described below.

Kansas Corporate Farming Law— Swine. SB 554, as amended by HB 3096, amended the Kansas Corporate Farming Law to permit the establishment of swine production facilities owned or leased by a corporation or limited liability company within a county through one of two methods. The first method allows a board of county commissioners to adopt a resolution, subject to notification and protest petition, permitting the establishment of a swine production facility within the county. The second method allows qualified voters to submit a petition to a board of county commissioners requesting establishment of such a facility within the county. The question of whether the swine production facility should be permitted, either through the protest petition (the first method) or the petition requesting the facility (the second method), is to be triggered by the signatures of not less than 5 percent of the county electors who voted in the election of the Secretary of State in the last preceding general election.

In addition, the bill amended the Kansas Corporate Farming Law to: define "swine marketing pool"; changed the existing definition of "swine confinement facility" to "swine production facility"; and permitted a corporation or a limited liability company, included in the definition of "swine production facility," to hold or lease agricultural land. Several statutes which previously prohibited "swine confinement facilities" from being granted economic development incentives were amended in the bill to apply those prohibitions to "swine production facilities." Two sections of the law were repealed: the restriction on processors of pork from owning hogs (K.S.A. 17-5905), and the penalty imposed for violations of the provision dealing with ownership of hogs by processors (K.S.A. 17-5906).

Furthermore, the bill amended the provisions of the Kansas Basic Enterprises Loan Program, administered by the Kansas Development Finance Authority, to give preference among agricultural business enterprise applicants for program loans to certain swine production facilities and swine marketing pools.

The bill also authorized the registration of swine marketing pools by the Kansas State Board of Agriculture. The intent of such registration is to foster the orderly marketing of swine in Kansas, facilitate the capture of markets by swine producers, and improve the quality of the state's swine herd. The bill outlines the powers assigned to registered swine marketing pools.

Provisions of the bill impose certain requirements on contractors who establish swine production facilities in Kansas, or who contract for the production or raising of hogs, with respect to the treatment of registered swine marketing pools. Despite the requirements enumerated in the bill, no contractor will be prohibited from purchasing hogs from any other business entity, nor will such contractor be prohibited from refusing to purchase or from discounting hogs (or both) if the hogs fail to meet the contractor's quality specifications, or if the shipment of hogs fails to meet the contractor's delivery terms. In addition, no marketing pool will be prevented from selling hogs to any other business entity. The bill also requires any swine purchasing contract, swine marketing contract, or swine production contract between a contractor and a swine production facility owner or swine marketing pool or swine producer to contain language providing for a resolution of contract disputes, either by mediation or arbitration.

Additional provisions address contractual arrangements between "contractors" and "producers" of hogs in Kansas. These provisions concern the procedures to be followed for failure by either party to pay or perform according to the provisions of the contract.

The Kansas State Board of Agriculture is authorized to promulgate rules and regulations to implement provisions of the bill concerning the registration of, and contractual arrangements pertaining to, swine marketing pools.

Kansas Corporate Farming Law—Dairy. HB 2584, as amended by HB 3096, permits dairy production facilities to be established in a county where a board of county commissioners has adopted a resolution to permit such facilities to be established, subject to certain conditions. If a resolution is passed permitting the establishment of dairy production facilities by a board of county commissioners, the bill requires that the resolution be published in the official county newspaper. The resolution will have to be published twice, and 60 days after the final publication the resolution will be effective.

Further, the bill permits the filing of a valid protest petition in opposition to the resolution adopted by the board of county commissioners, if it is filed within the 60-day time period. The protest petition will have to be signed by at least 5 percent of the number of qualified electors who voted in the last general election for Secretary of State. If the protest petition is found to be valid, the issue of whether dairy production facilities are to be permitted in the county will be placed on the ballot of the next countywide election.

In addition, the bill permits the electors of a county to file a petition allowing the issue of whether to permit dairy production facilities in the county to be placed on the ballot. Specifically, the bill permits the qualified voters of a county to file a petition with the county election officer asking that the issue of whether dairy production facilities should be permitted on the ballot. The petition will have to be signed by not less than 5 percent of the number of electors who voted for the office of Secretary of State at the last preceding general election.

The bill also defines a "dairy production facility" to mean the land, structures, and related equipment used for housing, breeding, raising, feeding, or milking of dairy cows. The term includes within its meaning only such agricultural land as is necessary for proper disposal of liquid and solid wastes and for isolation of the facility to reasonably protect the confined cows from exposure to disease.

The bill further establishes the language that will be used when circulating a petition for signatures and also for the question presented on the ballot when this issue is to be voted upon by the electorate of a county. This language lists the entities which will be permitted to establish a dairy production facility.

Further Legislative Modifications 1996 and 1998

1996 Amendments. In 1996, the Kansas Legislature considered and approved additional amendments to the Kansas Corporate Farming Law. HB 2745 added "family farm limited liability agricultural companies" to the list of entities which are permitted to own, acquire, or otherwise obtain or lease agricultural land in Kansas.

The bill established a definition for the term "family farm limited liability agricultural company." The term means a limited liability company founded for the purpose of farming and ownership of agricultural land in which:

- The majority of the members are persons related to each other, all of whom have a common ancestor within the third degree of relationship, by blood or by adoption, or the spouse or the stepchildren of any of these persons, or persons acting in a fiduciary capacity for these related persons;
- The members are natural persons or persons acting in a fiduciary capacity for the benefit of the natural persons; and
- At least one of the members is a person residing on the farm or actively engaged in the labor or management of the farming operation.

In addition, the bill modified the definition of the term "authorized farm corporation," which is one of the recognized entities permitted to own and acquire agricultural land in Kansas. Under the bill, the incorporators of an "authorized farm corporation" now can include "family farm corporations" and "family farm limited liability agricultural companies" as well as Kansas residents. Likewise, under the bill, the stockholders of "authorized farm corporations" could include "family farm corporations" and "family farm limited liability agricultural companies" as well as natural persons. The bill restricted the requirement that at least 30 percent of the stockholders be persons residing on the farm or actively engaged in the day-to-day labor or management of the farming operation in order to meet the definition of an "authorized farm corporation" to the situation where all of the stockholders are natural persons.

The bill also deleted the portion of the definition of "authorized farm corporation" which stated that if more than one person receives stock from a deceased stockholder that they collectively were to be considered one stockholder, and a husband and wife and their estates were considered to be one stockholder.

In addition, the bill modified the definition of the term "limited liability agricultural company," which is one of the recognized entities permitted to own and acquire agricultural land in Kansas. Under the bill, the members of a "limited liability agricultural company" could include "family farm corporations" and "family farm limited liability agricultural companies" as well as natural persons. The bill also restricted the requirement in this definition that at least one of the members of the "limited liability agricultural company" be a person residing on the farm or

actively engaged in the labor or management of the farming operation to the situation where all of the members are natural persons.

The bill added an additional exception to the general prohibition of corporations, trusts, limited liability companies, limited partnerships, or corporate partnerships from owning, acquiring, or otherwise obtaining or leasing agricultural land in Kansas. The bill permitted corporations and limited liability companies to hold or lease agricultural land used in a hydroponic setting. The bill defined "hydroponics" to mean the growing of vegetables, flowers, herbs, or plants used for medicinal purposes, in a growing medium other than soil.

1998 Amendments. In 1998, among numerous other provisions dealing with swine production, the Legislature further modified the Kansas Corporate Farming Law. These modifications were contained in Sub. for HB 2950 and dealt with the issue of the authority of the board of county commissioners.

Specifically, New Sec. 38 of the bill allows the board of county commissioners, in any county which has conducted an advisory election on the question of rescinding a resolution allowing swine production facilities under the Kansas Corporate Farming Law, to adopt a resolution rescinding a resolution adopted under the Corporate Farming Law as it existed before the effective date of the bill. The resolution would be submitted to the qualified electors of the county at the next state or county-wide regular or special election which occurs more than 60 days after the adoption of the resolution. If the majority of the voters vote in favor of the resolution, the county election officer would be required to send a copy of the results to the Secretary of State. The bill required the Secretary of State to publish the results in the *Kansas Register* and swine production facilities would not be allowed to be established in that county. The bill allowed a petition to put the issue on the ballot with respect to rescinding the resolution. The bill sunsets this section on December 31, 1998. In addition, Sec. 39 amends a section of the county home rule law to prohibit counties from exercising their home-rule powers to exempt themselves from the other provisions of the bill. Sec. 45 amends the Kansas Corporate Farming Law to provide that, in the future, swine production facilities may be established in a county only after approval by the voters. The bill deleted the protest petition provision because the issue would be automatically submitted to the voters. Sec. 44 of the bill added an additional exception to the general prohibitions under the Kansas Corporate Farming Law. This exception allowed corporations and limited liability companies to acquire agricultural land for swine production facilities in those counties where voters have approved their establishment under the county option provision of the Kansas Corporate Farming Law as amended by the bill.

Swine and Dairy Production Facilities – 2012

2012 Amendments. HB 2502 made amendments to the provisions of law which permit certain dairy production facilities and swine production facilities to be established in counties under the Kansas Corporate Farming Law. The bill aligned the approval process for the establishment of a swine production facility with that of a dairy production facility by giving the decision-making power to county commissioners and under certain conditions to qualified electors.

Provisions relating to dairy production facilities were amended to clarify that if an election is needed, it is held during the next state, county, or special election. In addition, these provisions were amended to allow a board of county commissioners to either permit (continuing law) or deny by resolution the establishment of a dairy production facility in its county. Commissioners will decide or place on the ballot whether to permit the establishment of a dairy

production facility by only "a corporation, trust, limited liability company, limited partnership or corporate partnership."

With respect to the establishment of swine production facilities in counties, the prior provisions of law which required a vote by the electors of a county were repealed. Under the new provisions, a board of county commissioners is authorized by resolution to permit or deny a swine production facility within its county. The permission or denial is subject to a petition protesting the decision within 60 days of the resolution signed by five percent of the county voters in the last election for Secretary of State. Under the bill, provisions relating to the petition and ballot language questions regarding swine production facilities become identical to those of dairy production facilities regarding whether a corporation, trust, limited liability company, limited partnership, or corporate partnership, either directly or indirectly, own, acquire, or otherwise obtain or lease agricultural land in the county. The bill does not impact the authority of a family farm corporation, authorized farm corporation, limited liability agricultural company, limited agricultural partnership, family trust, authorized trust, or testamentary trust to own, acquire, or otherwise obtain or lease, either directly or indirectly, agricultural land for either dairy or swine production facilities.

The bill added that denial by the county commissioners of such a production facility, which had been an absolute rejection, also is subject to a petition protesting said denial following the guidelines of a petition protesting the establishment of such a facility.



STATE OF KANSAS
OFFICE OF THE ATTORNEY GENERAL

OFFICE OF THE SECRETARY

JAN 02 2013

KS DEPT OF AGRICULTURE

DEREK SCHMIDT
ATTORNEY GENERAL

January 2, 2013

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Dale A. Rodman, Secretary
Kansas Department of Agriculture
109 SW 9th Street, 4th Floor
Topeka, KS 66612-1280

Re: Request for Attorney General Opinion on the constitutionality of Kansas corporate farming restrictions and limitations in K.S.A. 17-5903 *et seq.*

Dear Secretary Rodman:

As Secretary of the Kansas Department of Agriculture, you ask for our opinion on the constitutionality of Kansas corporate farming restrictions and limitations in K.S.A. 17-5903 *et seq.*, known as the Kansas Agricultural Corporations Act (Act), under the Dormant Commerce Clause or any other theory. I would note that your request is quite broad and essentially invites this Office to the unusual task of seeking legal theories under which a Kansas statute might be successfully challenged as unconstitutional.

My staff spent a great deal of time researching the issues involved in your request. Based on our review, we believe the exception to the law for an "authorized farm corporation" is likely unconstitutional under the Dormant Commerce Clause, as this term is defined to include only Kansas corporations and is therefore facially discriminatory. See K.S.A. 17-5903(k). Laws that are found to be discriminatory are subject to an almost *per se* rule of invalidity.¹ We cannot conceive a circumstance under which a court would find this provision to pass constitutional muster.

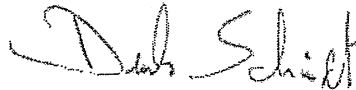
Regarding the remainder of the Act, we believe there are reasonable arguments to be made, on both sides, regarding whether these provisions violate the Dormant Commerce Clause, and that those arguments have not been resolved by any Court whose decision would be dispositive in the matter. While the 8th Circuit Court of Appeals has found similar statutes in other states to be unconstitutional, those decisions are not binding on the 10th Circuit Court of Appeals, which includes Kansas. In the event a legal challenge to the constitutionality of this Act were brought by a party aggrieved by its enforcement, that case would be one of first impression. In such a situation, the precise facts and circumstances of which are necessarily speculative until such time as a lawsuit is actually filed, it is likely that this Office would have a role to

¹ See *Maine v. Taylor*, 477 U.S. 131, 148 (1986); *Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978).

play, possibly as an advocate, in any such litigation.² For that reason, we decline to issue a formal opinion on this matter except in regard to the provision of K.S.A. 17-5903(k) that we believe is clearly unconstitutional.

The Legislature, through enactment of law, establishes policy for the State of Kansas. One of the roles of this office is, in most cases, to defend the decisions of the Legislature if Kansas laws are challenged in court.³ While we do not defend laws that are clearly unconstitutional under binding court rulings or other law, such is not the case with this Act, except as described above. Therefore, we encourage you to approach the Legislature should you believe changes to the Act are necessary or desirable as a matter of public policy.

Sincerely,



Derek Schmidt
Attorney General

² See, e.g., K.S.A. 75-702 on the duty of the Attorney General to appear for the state when the constitutionality of any law of this state is at issue. See, also, 28 U.S.C. 2403(b) and FRAP 44(b), requiring notice to the state attorney general when the constitutionality of a state statute is challenged in federal court.

³ This approach is consistent with the well-established fundamental rule of statutory construction, adopted by Kansas courts, to which all other rules are subordinate – that the intent of the legislature controls if it can be ascertained. See, e.g., *Bergstrom v. Spears Manufacturing Co.*, 289 Kan. 605, 607 (2009).