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At the Heart of Agriculture

by Dean Zimmerli

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Southern Minnesota has long been a leading region in the agriculture industry. The area boasts incredibly productive farmland, making Minnesota a leading producer of corn, soybeans, sugar beets, sweet corn, and peas. A robust group of pork, beef, dairy, and poultry producers helps place Minnesota among the top ag-producing states in the county. Along with this, there is an extensive collection of related industries supporting production and processing of these agricultural products, including meat, poultry, egg, and vegetable processors, ethanol plants, feed producers, financial institutions, and hundreds of other manufacturers and service providers focused on agriculture.

Mankato, Minnesota and the surrounding region has become a major hub of agribusiness. The Greenseam initiative, based in Mankato, continues to help attract and grow ag-related business, helping to turn the region into a food and agribusiness epicenter. Leaders in the pork industry will gather in Mankato for the 2022 Pork Congress. Numerous other trade shows and industry meetings will continue to occur throughout the year.

Gislason & Hunter LLP is proud to have its offices in New Ulm and Mankato at the center of this agribusiness hub, where we can focus on addressing the legal needs of this diverse group of businesses and producers. With the challenging and ever-evolving legal and regulatory climate affecting agribusinesses throughout the supply chain, it is important to partner with professionals who understand and focus on agribusiness. Our DIRT magazine continues to be a timely source of information addressing some of these changes. With the Pork Congress meeting in Mankato in February 2022, this issue has a particular emphasis on legal challenges facing the pork industry from several of Gislason's attorneys.

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An Employer's Obligation to Reasonably Accommodate Sincerely Held Religious Beliefs

by Brittany R. King-Asamoa

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Publication of the Occupational Safety and Health Administration's COVID-19 vaccination and testing emergency temporary standard had many employers asking: What must we do when an employee asserts a religious exemption? This article provides a brief outline of the private[1] employer's obligations whenever an employee requests a reasonable accommodation for a religious belief, practice, or observance.

Religious Beliefs are Defined by the Law, Not the Employer.

Title VII of the Civil Rights Act of 1964 (Title VII) requires employers with 15 or more employees to reasonably accommodate the religious beliefs, practices, and observances (collectively, "religious belief") of applicants and employees. Federal law broadly defines religious beliefs. There is no obligation to become an encyclopedia of all religions or moral belief systems.

Protected religious beliefs include "moral or ethical beliefs as to what is right and wrong" that "are sincerely held with the strength of traditional religious views."[2] The belief does not have to be adopted by a religious group or even theistic. Any "sincere and meaningful belief that occupies a place in the life of its possessor parallel to that filled by the orthodox belief in God" is religious belief protected by Title VII.[3] But passionate feelings, personal preferences, and political beliefs alone are insufficient. The distinction between passionate feelings and protected religious beliefs can be difficult to identify. But employers should not inquire about the moral or theological merits of an asserted religious belief or test the logic or accuracy of that belief. Instead, employers should assume the asserted religious belief is sincerely held unless specific circumstances cause the employer to doubt the sincerity or religious nature of the asserted belief.

Conduct a Limited Inquiry into the Nature and/or Sincerity of the Religious Belief.

Employers may inquire about the sincerity or religious nature of an asserted belief. Considering the following questions can assist employers complete this inquiry:

- Has the employee behaved in a manner markedly inconsistent with the asserted belief?
- Is the timing of the request or asserted belief suspicious?
- Are there any facts or circumstances that undermine the individual's credibility?
- Is the accommodation requested a desirable benefit likely to be sought for non-religious reasons?[4]

Religious beliefs protected by Title VII are broad and can be *individual* to each applicant or employee. A best practice is to

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[1] Public employers cannot infringe upon an employee's right to engage in religious expression, practice, or observance provided by the First Amendment of the U.S. Constitution. The same prohibition does not apply to private employers.

[2] 29 C.F.R. § 1605.1.

[3] *U.S. v. Seeger*, 380 U.S. 163, 165-66 (1965); *see also Section 12: Religious Discrimination*, EEOC at A(1) (Jan. 15, 2021), *available at* https://www.eeoc.gov/laws/guidance/section-12-religious-discrimination#_ftnref21 (hereinafter, "*EEOC Religious Discrimination*").

have the employee complete a reasonable accommodation request form to provide the following information:

- Describes the religious belief, practice, or observance with specificity
- Provides a timeframe for how long the employee held the religious belief
- Identifies the employment task(s) that conflict with the religious belief
- Outlines potential accommodations requested
- Affirms the religious belief is sincerely held

Employers should discuss this information and any questionable observations or conduct undermining the employee's credibility with the employee. This practice is similar to the interactive process required when an accommodation is requested by a qualified disabled person.

Provide a Reasonable Accommodation

Sincerely held religious beliefs must be reasonably accommodated, unless the accommodation poses an undue hardship on the employer. An undue hardship is presented when the accommodation has more than a *de minimis* cost (financial or figurative) on the employer's business operations. Beyond monetary costs, safety, job efficiency, legal requirements, and infringement on other employees' rights can constitute an undue hardship. Employers must engage in a careful evaluation of the impact proposed accommodations will have on their business and deny only those that present an actual and articulable undue hardship.

Utilize EEOC Resources and Seek Legal Counsel

The EEOC updated guidance on religious accommodations during the COVID-19 pandemic. Those resources include the following:

- *Section 12: Religious Discrimination, EEOC Compliance Manual* (updated Jan. 15, 2021)
- *What You Should Know About COVID-19 and the ADA, the Rehabilitation Act, and Other EEO Laws* (updated Dec. 14, 2021)

Employers are encouraged to review this guidance and consult with legal counsel to ensure best practices are used.

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[4] *EEOC Religious Discrimination* at A(2).

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Choosing a Business Structure For Your Family Farm

by Christopher Kamath

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Farming isn't just a business, it's a commitment to family values and a different way of life. You work hard to feed your family and others, raise your children, and earn a reasonable living at the same time. And if you're reading this article, chances are that you're a farmer and you know this better than me. What you may not know is that your decision not to establish a business entity for your farm can have significant consequences for your farm's operations and ultimately its success. Handshake deals and informal partnerships are becoming a thing of the past —and for good reason (discussed below). Formal business entities, such as limited liability partnerships, limited liability companies, and corporations, can help protect your personal assets from the hazards of operating a farm, minimize taxes, and ease transition of the farm from one generation to the next.

The Danger with Sole Proprietorships and Informal Partnerships

Many farmers have traditionally operated as sole proprietors or as partners in a general partnership. The sole proprietorship is a common type of business structure among farms and is not a legal entity separate from its owner. A sole proprietorship is an unincorporated business owned and operated by a single individual for profit. In comparison, a general partnership is formed when two or more persons carry on as co-owners of a business for profit. You do not have to file any documents with the Minnesota Secretary of State to establish these types of businesses, nor do you have to draft any organizational documents.

While these business structures are easy to set up and relatively simple to use, both have disadvantages. The first major disadvantage is that these arrangements do not provide any liability protection. The personal assets of a farmer are not shielded from liability arising out of the farming operation.

A second major disadvantage applies to general partnerships. As mentioned above, you do not have to follow many legal formalities to create a general partnership. A general partnership is created under Minnesota law when two or more persons carry on as co-owners of a business for profit. A partnership can even be formed when the parties don't intend to form a partnership.

Imagine for a minute that the cousin or friend you engage to haul and market grain ends up being treated as your partner under Minnesota law. What are the terms of this implied partnership? What portion of your operation does he receive upon liquidation? How much of your profit will this supposed partner be entitled to claim? Unfortunately, litigation may be necessary to resolve these questions.

Farmers can mitigate these risks by formalizing their partnership with a partnership agreement. At a minimum, a partnership agreement should describe how profits and losses are allocated to the partners, how new partners are admitted to the partnership, how partners may withdraw

from the partnership, how and when partners may sell their ownership interests, and how management conflicts are to be resolved between partners. It is also advisable to use written contracts for independent contractors and when leasing farmland.

Entity Types and Structures

In addition to the sole proprietorship and general partnership, several other types of entities can be used in farming operations. Each comes with its own set of positives, negatives, and tax consequences:

Formalized Partnerships. In contrast to a general partnership, farmers can establish a limited partnership by filing a Certificate of Limited Partnership with the Minnesota Secretary of State. Limited partnerships must have at least one general partner and one limited partner. General partners make decisions on behalf of the partnership, but are jointly and severally liable for all obligations of the limited partnership. The limited partners do not have any management rights, but their personal assets are shielded from partnership debts. Limited partnerships are typically governed by a written partnership agreement.

Both general partnerships and limited partnerships can register with the Secretary of State to create a liability shield to protect the general partners' personal assets. These partnerships are referred to as limited liability partnerships (LLPs) and limited liability limited partnerships (LLLPs), respectively.

Corporations. A corporation is the most formal and complex business structure used in farming. A corporation has at least three levels of governance: its board of directors, officers (including CEO and CFO), and shareholders. The corporation's shareholders elect a board of directors, which is in charge of making all major decisions for the corporation. The board of directors in turn appoints officers to carry out the board's decisions, sign documents, and take other actions on behalf of the corporation. The rules for how a corporation conducts business and makes decisions are usually set out in the Articles of Incorporation filed with the Secretary of State and written By-Laws. Corporations offer strong asset protection, but must strictly comply with certain legal formalities, such as holding shareholder and director meetings. Liability protection can be lost when the shareholders fail to observe these formalities.

Corporations can elect to be taxed as a C corporation or S corporation. C corporations are subject to two levels of taxation: one at the corporate level when income is earned and another at the shareholder level when profits are distributed to shareholders in the form of dividends. Items of income and deductions flow through to the individual shareholders of an S corporation, similar to taxation of partnerships. And shareholders of an S corporation typically do not pay a separate income tax on dividends they receive.

Limited Liability Companies. Limited liability companies (LLCs) are now a common operating entity to use in farming. This is due to their strong liability protection and flexibility in governance structure. An LLC's owners are referred to as "members" under Minnesota statute. The LLC can be operated by its members (similar to a general partnership), by one or more managers (similar to a limited partnership), or by a board of governors (similar to a corporation). The members can also customize any of

these three structures by drafting their own, personalized governance rules in a document called an operating agreement. In order to establish a limited liability company, the organizer must file Articles of Organization with the Secretary of State.

An LLC with only one member is treated as a "disregarded entity" for tax purposes, unless the LLC elects to be taxed as an S corporation. A disregarded entity is totally ignored for tax purposes; all items of income and deductions of the LLC are reported directly on the member's individual tax return. If the LLC has more than one member, it can elect to be taxed as a partnership or S corporation.

The Benefits of Farming with an Entity

When a farmer forms a business entity, the farmer transfers farm assets out of his or her name and into the name of the business entity. In exchange for this contribution, the farmer receives ownership interests in the business entity, such as shares of stock, membership interests, or partnership interests.

As mentioned above, one of the primary benefits of using a formalized entity is the liability protection afforded to the company's individual owners. The company is a separate legal entity. Generally speaking, the debts, obligations, and liabilities arising from the operation of the farm belong to the company and not its owners. For example, if an employee of the company is injured while operating the company's tractor, the employee is normally limited to recovering against the company's assets. The employee (at least in most cases) cannot recover from the farmer's personal assets held outside of the company.

Business entities also provide an effective way to transfer the farming business from one generation to the next. Rather than splitting up the farmland among children who farm and those who do not, a farmer can gift ownership interests in the entity to all children during his life or at his death. The benefit of this arrangement is that the farmland is kept together, while the "non-farming children" still receive some benefit in the form of future profit distributions. To the extent that the farmer needs income in retirement, the farmer can sell some of his ownership interest in the entity to children or other family members.

Using business entities in farm-succession planning can also minimize gift and estate tax. As a general rule, for gift and estate tax purposes, transfers of interests in closely-held businesses like family farms are valued at their fair market value. Unlike shares in a public corporation, there is no readily available market for the sale of interests in closely-held business entities. Consequently, the value of the interest is often discounted for this lack of marketability. Discounts may also be applied for non-controlling or minority interests.

Minnesota Corporate Farm Law

If you're going to farm through a business entity, the entity must be eligible to farm in Minnesota. In the early 1970s, Minnesota passed a law that is commonly referred to as the Minnesota Corporate Farm Law (the "Law"). LLCs, corporations, most types of trusts, and other business entities cannot own agricultural land or engage in specified farming activities within the state of Minnesota unless they meet the Law's requirements. The Law is fairly long and complex, and its requirements vary based on the type of entity used to farm. However, to generalize broadly, there are two categories of entities that may farm in Minnesota—Family Farm Entities and Authorized Farm Entities.

A Family Farm Entity is a company formed for the purpose of farming and owning agricultural land. A majority of the ownership interest in the entity must be held by persons within three degrees of kinship—think grandparents, parents, children, siblings, nieces and nephews. At least one of those persons must be residing on the farm or actively operating the farm; or, in the case of LLCs and LPs, one of the persons must have owned the agricultural land for a period of at least five years prior to transferring the land to the entity.

An Authorized Farm Entity must comply with even stricter requirements. An Authorized Farm Entity can only have one class of ownership interests and up to five owners, although married couples are counted as one owner. Its revenue from rent, royalties, dividends, interest, and annuities cannot exceed 20 percent of its gross receipts. And the Authorized Farming Entity cannot own more than 1,500 acres. There are additional requirements, but these are some of the more important restrictions to keep in mind when deciding between the two categories of farm entities.

Family Farm Entities and Authorized Farm Entities must file a corporate farm application with the Minnesota Department of Agriculture. The cost of filing the application is $15.00. Annual renewal forms are sent out every February via U.S. mail. The renewal must be processed every year to remain compliant with the Law. Failure to file a required corporate farm report is a gross misdemeanor and can be punished with a $500 civil penalty. The Law also authorizes the Attorney General to seek a court order forcing a business entity or trust owning agricultural land in violation of the Law to divest itself of the land within five years.

It should be noted that the Law only restricts the farming activities of corporations, limited liability companies, pension or investment funds, most types of trusts, and limited partnerships. Sole proprietorships, general partnerships, limited liability partnerships, qualifying revocable trusts, and certain grandfathered entities are entirely exempt from the Law and do not have to register with the Minnesota Department of Agriculture.

Conclusion

It is important to treat your family farm like a business. The extra burden associated with formalizing your family farm is minor in comparison to the benefits offered by using entities such as LLPs, LLCs, and corporations. What entity works best for you will ultimately depend on the size of your operation and the activities it engages in, among other things. Farmers should consult with their attorney or CPA to help determine which option is best for them.

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California's Proposition 12: What Does It Mean and What Comes Next?

by Matthew Berger

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In November 2018, California voters passed Proposition 12. This ballot initiative was pushed by animal-rights extremists and seeks to regulate the production of pork, eggs, and veal throughout the United States (and beyond). This law has been subject to multiple court challenges over the last year. But these legal challenges have (so far) been unsuccessful, and the law became fully effective on January 1, 2022. This article will provide answers to key questions that pork producers may have about the new law.

What does Proposition 12 actually say? On the surface, Proposition 12 does not appear to be very controversial. The law prohibits a business from "knowingly engag[ing] in the sale within California" of pork that the business "knows or should know is the meat of a [breeding pig] who was confined in a cruel manner, or is the meat of immediate offspring of a [breeding pig] who was confined in a cruel manner." Nobody favors cruel treatment of animals.

Of course, as with many things, the devil is in the details (or, in the case of a new law, the definitions). Proposition 12 uses the definition of the term "confined in a cruel manner" to impose two confinement standards applicable to breeding pigs:

- First, a breeding pig is confined in a cruel manner if it is confined "in a manner that prevents the animal from lying down, standing up, fully extending the animal's limbs, or turning around freely"; or
- Additionally, a breeding pig is confined in a cruel manner if, after December 31, 2021, it is confined "with less than 24 square feet of usable floorspace per pig."

In other words, the law prohibits the use of gestation crates in commercial sow farms to protect and provide individualized care and treatment to gilts and sows and, as of January 1, 2022, establishes an arbitrary minimum space requirement for breeding pigs.

How does Proposition 12 impact pork producers in Minnesota and Iowa (and anywhere else not in California)? On its face, Proposition 12 only restricts sales of pork within California and does not appear to directly regulate farmers located outside of California. But this benign appearance hides a far more sinister practical reality. In order to avoid liability under the new law, businesses who sell pork in California (e.g., retailers, wholesalers, and food distributors) face civil and criminal sanctions if they violate the law. Accordingly, these businesses will almost certainly require their suppliers to provide written certification that the pork they purchase was produced in compliance with the requirements of Proposition 12. These certification requirements will continue to ripple upwards through the supply chain to packers who process the pork, the hog farmers who finish the pigs from which the pork is produced, and ultimately, the sow farms that produce the weaned pigs. In other words, Proposition 12 is a wolf in sheep's clothing that uses its benign appearance to hide a deeper purpose to regulate hog farmers throughout the United States.

The true purpose of Proposition 12 is more evident in the proposed regulations that the California Department of Food & Agriculture has published (but that have not yet been finalized). Under the proposed regulations, all distributors who sell pork in California must register with the state. And in order to obtain this registration, a distributor must maintain records by which they can trace all pork sold in California to a sow farm that is certified by the State of California as complying with Proposition 12. In other words, the proposed

regulations would require hog farmers (wherever they are located) to subject themselves to the regulatory authority of the State of California (including, as described more fully below, annual farm inspections) if pork produced from the farmers' hogs may eventually be sold in California.

What is required for a sow farm to be certified? During the first year when the new law is fully in effect (i.e., January 1, 2022 through December 31, 2022), the proposed regulations allow a sow farm to self-certify that the farm complies with the requirements of Proposition 12. Beginning on January 1, 2023, however, the proposed regulations would require a sow farm to obtain certification from either the California Department of Food & Agriculture or a third-party "certifying agent" who has been approved by the department. Certification would specifically require an annual inspection of "each production unit, facility, and site," including the actual production areas, that produces pigs that will be processed into pork that may be sold in California. The proposed regulations would also allow additional, unannounced inspections by certifying agents (which could include animal rights activists who become accredited by the department). Finally, a certified producer is required to maintain (and make available to a certifying agent on request) detailed transaction and facility records about their hog production. Thus, a hog farm in Iowa or Minnesota would be subject to intrusive inspections by California regulators (and the significant biosecurity risks that these inspections would pose) if a farmer's customers may sell the pork produced from the pigs in California.

What happens now? The short answer is—nobody knows for sure. As of today (January 10, 2022), the requirements of California Proposition 12 are fully in effect. Multiple lawsuits have been filed to challenge the legality of Proposition 12 or delay its implementation. Some of these suits are still active

(for example, a request by the National Pork Producers Council and American Farm Bureau Federation asking the United States Supreme Court to review Proposition 12 is pending before the Court), and other suits have been brought to delay the implementation of the law. So far, however, these lawsuits have not been successful. As a result, the State of California could begin enforcing the law at any time. Additionally, Proposition 12 creates a private cause of action that would allow private parties (such as animal rights groups) to file lawsuits to enforce the law.

To add further confusion, Proposition 12 required the California Department of Food & Agriculture to finalize regulations to implement the law by September 1, 2019. More then 2 years after this deadline, however, the regulations still have not been finalized. As a result, hog farmers are left to guess about significant questions about how the law will be applied and enforced (such as how the square footage will be calculated).

What can hog farmers do today? During this period of uncertainty, hog farmers may be pulled in multiple directions. Some packers and pork distributors have announced that they do not intend to sell pork in California under the new law, while others are actively seeking out sources of compliant pigs in the marketplace. In the short term, this uncertainty will likely create significant disruptions (and opportunities) in the hog market.

One step that hog farmers can take is to carefully review their existing contracts—including any contracts to acquire weaned pigs and contracts to sell finished hogs—to clearly understand their rights and obligations. In reviewing these contracts, hog farmers should clearly understand whether the existing contract would require the farmer to comply with the requirements of Proposition 12 and, if this is not required now, whether a purchaser can add those requirements during the contract. If a farm already complies with the requirements of Proposition 12, can the farm charge a premium for those pigs based on supply and demand or whether the contract price is already locked in? Further, if a contract requires compliance with Proposition 12 (either now or in the future), the farmer should begin planning the necessary facility and operational changes or consider whether there is any right to terminate a contract early. Finally, if a purchaser requests (or requires) written certification from a farmer, the farmer needs to carefully read and understand exactly what the farmer is (and is not) certifying before signing the document.

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Last Will and Testament

ARTICLE I: Funeral expenses & payment of debt

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What Preserves the Integrity of the Derivatives Market?

by Daniel Schwartz

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Agricultural producers are no strangers to risk. They grow, buy, and sell commodities in a global economy subject to the unpredictability of floods, droughts, and trades disputes, the whims of governments and politicians, and the devastations caused by pandemics and disease. Many if not most producers develop and employ hedging strategies in an attempt to manage these threats, judiciously buying and selling financial instruments called "derivatives", such as futures contracts and options.

In simple terms, buying and selling derivatives allows a producer to offset or reduce the financial impact of declining prices for the commodities the producer raises and sells (called "going short") and of rising prices for the commodities the producer buys (called "going long"). This process of buying and selling derivatives affords producers some ability to, in effect, "lock in" acceptable prices for these commodities and (hopefully) make a profit.

The effectiveness of these strategies and instruments as risk-management tools, though, is dependent upon the laws and intermediaries which regulate and facilitate the derivatives market. Indeed, many will recall MF Global and the circumstances of its demise a little over a decade ago. A prominent brokerage firm and a "clearing member" of the Chicago Mercantile Exchange, MF Global misplaced about $1.6 billion of its customers' monies that, by law, were supposed to be segregated and protected.[1]

The MF Global disaster was a painful reminder that there are no riskless endeavors in life—even risk management itself. For many agricultural producers these events also served to bring from obscurity the complex web of laws, agencies, and intermediaries on which producers rely to protect and ensure the integrity of the derivatives market.

Futures Commission Merchants.

MF Global was regulated under a federal law called the Commodity Exchange Act as a "futures commission merchant" (FCM).[2] Any entity that accepts orders to buy or sell futures contracts and options and accepts money or other assets from customers in respect of such orders, as did MF Global, must

[1] Most of these funds were margin payments posted by customers as security for their open futures positions. *See* Rena S. Miller, *The MF Global Bankruptcy, Missing Customer Funds, and Proposals for Reform, Congressional Research Service*, August 1, 2013, at pp. 2, 4 n.20.
[2] *Id*. at Summary.

qualify and register as an FCM with the Commodity Futures Trading Commission (CFTC), the federal agency charged with implementing and enforcing the Commodity Exchange Act.[3]

The CFTC has adopted exacting financial and reporting standards in order for an institution to qualify as an FCM. Not the least of these is the requirement that FCMs hold all customer funds – including all margin payments – in separate accounts and not commingle customer funds with the FCMs' own monies or use the customer funds for other, non-customer transactions. The segregated-accounts requirement helps ensure customers can access their funds no matter the financial condition or other business activities of the FCM – even if the FCM holding the customer funds is insolvent or has filed for bankruptcy protection.[4]

All FCMs are required to make reports to the CFTC on a monthly basis demonstrating their financial wherewithal and compliance with the requirements of the Commodity Exchange Act. Selected financial data from each FCM is published and publicly available on the CFTC's website. This information includes each FCM's adjusted net capital and the value of each FCM's customer-segregated accounts.[5]

Derivatives Clearing Organizations and Clearing Members

As noted above, MF Global was a "clearing member" of the Chicago Mercantile Exchange (CME). CME is a registered "derivatives clearing organization" (DCO) under the Commodity Exchange Act. A DCO acts as an intermediary between buyers and sellers in the derivatives market. Through the clearing process, a DCO effectively becomes the buyer to each seller, and the seller to each buyer, in respect of every derivatives transaction. A DCO executes this role through the several FCMs that serve as its clearing members.[6]

The Commodity Exchange Act requires DCOs, like CME, to adhere to several "core principles". One principle is the obligation to establish financial and operational standards for participation as a clearing member in the DCO. Another is that DCOs institute procedures to mitigate the effects of a clearing member's insolvency or other default of its obligations, however unlikely that may be.[7]

CME currently lists around sixty institutions as clearing members.[8] CME has established comprehensive standards for its clearing members and procedures in the event any one of these members defaults due to its insolvency. For example, CME's clearing members must maintain sufficient capital requirements, post a performance bond, and contribute to a "guaranty fund". The proceeds of the performance bond and guaranty fund may be accessed to cover losses caused by a clearing member's insolvency or other default. CME's policies and procedures, moreover, permit CME to transfer a defaulting member's customer accounts and collateral to another of its clearing members that is solvent and not in default.[9]

Systemically Important Financial Market Utility

Recognizing that not all DCOs are of equal significance, in July 2012 the U.S. Department of the Treasury's Financial Stability Oversight Council designated CME as one of eight systemically important financial market utilities. CME garnered this distinction based on the unparalleled volume of U.S. futures and options cleared by CME and the Council's opinion that no other DCO could serve as an adequate substitute for CME in the event of its disruption or failure. The Council's decision is hardly surprising. The year prior to its designation CME cleared 96% of the U.S. futures and options market volume.[10]

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[3] *See* 7 U.S.C. § 1a(28) (defining futures commission merchant); *id.* § 6d(a) (requiring futures commission merchants to be registered with the CFTC).

[4] *See id.* § 6f(b) (describing financial requirements for futures commission merchants); 17 CFR § 1.20 (describing customer account segregation requirements and comingling prohibition); Rena S. Miller, *The MF Global Bankruptcy, Missing Customer Funds, and Proposals for Reform, Congressional Research Service*, August 1, 2013, at p. 4 (noting that the bankruptcy code is structured to permit an FCM to transfer customer accounts to another solvent FCM so that the customers may continue to access their funds).

[5] *See* Commodity Futures Trading Commission, Financial Data for FCMs, https://www.cftc.gov/MarketReports/financialfcmdata/index.htm (last visited January 8, 2022).

[6] *See* Commodity Futures Trading Commission, Derivatives Clearing Organizations (DCO), https://sirt.cftc.gov/sirt/sirt.aspx?Topic=ClearingOrganizations (last visited January 8, 2022); 7 U.S.C. § 1a(15) (defining derivatives clearing organization); CME Group, What is Clearing, https://www.cmegroup.com/education/courses/clearing/what-is-clearing.html (last visited January 8, 2022).

[7] *See* 7 U.S.C. § 7a-1(c)(2).

[8] *See* CME Group, Clearing Firms, https://www.cmegroup.com/clearing/financial-and-regulatory-surveillance/clearing-firms.html (last visited January 10, 2022).

[9] *See* CME Group, CME Clearing's Financial Safeguards, https://www.cmegroup.com/clearing/cme-clearing-overview/safeguards.html (last visited January 8, 2022); CME Clearing Risk Management and Financial Safeguards, available at https://www.cmegroup.com/clearing/files/financialsafeguards.pdf.

[10] *See* U.S. Department of the Treasury, Financial Stability Oversight Council, Designations, https://home.treasury.gov/policy-issues/financial-markets-financial-institutions-and-fiscal-service/fsoc/designations (last visited January 8, 2022); Appendix A, Designation of Systemically Important Financial Market Utilities, available at https://home.treasury.gov/system/files/261/here.pdf.

The designation of CME as "systemically important" subjects it to a more demanding regulatory regime. These requirements include, among others, the maintenance of additional financial and liquidity resources, heightened business continuity and disaster recovery plans, the adoption of rules and procedures to adequately address losses resulting from a clearing member's default, and recurring "stress tests" and other analyses regarding its financial and liquidity resources.[11]

Conclusion

Few agricultural producers could withstand the sometimes dramatic, and oftentimes unpredictable, commodity price fluctuations absent the ability to flatten and soften them by taking offsetting positions on the derivatives market. The various laws, institutions, and participants regulating and supporting the derivatives market is what makes this risk-management option available to producers. Some may view the demise of MF Global ten years ago as evidence that these laws, institutions, and participants were flawed then and remain so today. And to some extent they may be right.

A more charitable and realistic view, however, is that the events surrounding the MF Global bankruptcy and its fallout were an unfortunate aberration. Indeed, given all of its transactions and participants, there is an awful lot that must – and does – go right every day in order to maintain stability and confidence in the derivatives market. That so many agricultural producers have continued to utilize hedging strategies following MF Global's devasting failure is a testament to this fact.

Ultimately, each producer must decide for itself whether and the extent to which it is comfortable using derivatives as part of its risk-management strategy. MF Global taught us that the laws and participants underlying the derivatives market are imperfect and, unfortunately, may at times be susceptible to failure. While the possibility of such systemic failure may not be eliminated entirely, agricultural producers are wise to balance this prospect with the perils of attempting to absorb the peaks and valleys of the commodities markets without a derivatives-based risk management strategy.

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[11] *See* 17 CFR § 39.30 *et seq.*

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General Partnership: The Catch-All Relationship To Avoid

by Cory Genelin

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Here's a common story: Farmer A gets a good deal on a neighboring farm that includes 16 acres of marginal hay ground in a low, wet area. Farmer A has no use for hay and no haying equipment. It's been a dry spring with forecasts of drought and high hay prices.

Neighbor B is a hobby farmer with haying equipment and a few horses. Neighbor B approaches Farmer A and generously offers to "take care of that hay ground for you this year." Farmer A wants to stay on good terms with Neighbor B, but also wants a share of what could be lucrative hay prices. Farmer A offers to rent the field to Neighbor B for $50 an acre, but Neighbor B, being a hobby farmer, isn't sure if he'll have time to hay it and doesn't want to commit. Both men understand that there may or may not be any profit given unpredictable weather and prices.

They make the following deal: Neighbor B may hay the field if he gets time but doesn't have to. If he does hay it, Neighbor B will do all of the work including marketing the hay and storing it until it sells. Once it's sold, Neighbor B will get his fuel costs, plus $25 an hour labor for all time spent on the project. The two men will split whatever money is left over, with Neighbor B being paid partially "in kind" in any hay he elects to keep.

All of this dealing takes place in a ten-minute conversation at a little league game. They put nothing in writing. They shake hands and never talk about this again.

The weather stays dry. The usually soggy hayfield comes on nicely and hay prices keep climbing. During the 4th of July weekend Neighbor B is putting up the hay while Farmer A watches happily from his patio while smoking some ribs and staying refreshed with some grain-based beverages. Demand and prices are so high that Neighbor B has found a buyer at a fantastic price. In fact, since Neighbor B is getting fuel and time paid for as part of the bargain, he has sold the hay, delivery included, to a buyer three hours away in the driest part of the state, cash on delivery. Neighbor B loads up his gooseneck and heads north, waiving to Farmer A on the way out the driveway.

On the way, a strap comes loose. A few bales fall off and break apart. Neighbor B immediately notices, pulls over, puts on his flashers and starts cleaning up the hay. He gets all of the full bales off the highway and then does his best to pick up the loose hay or kick it off the road. Along comes Genius C who stops—in the lane of traffic—to ask if Neighbor B needs help. Then comes Driver D. Driver D does not slow down for the flashers and does not touch his brakes until it's too late. The loose hay prevents him from stopping and he plows into Genius C. Driver D's passenger, Plaintiff E, is not buckled in and is paralyzed from the neck down.

Plaintiff E sues: Driver D, Genius C, Neighbor B . . . and Farmer A.

Farmer A is in shock. Of course his initial response is: "I had nothing to do with this!" Plaintiff E's lawyer responds: "At the time of the accident, you and Neighbor B were acting in a general, *un*limited partnership. You are as liable as he is." And unfortunately for Farmer A, that lawyer could be right.

Partnership is an area of law that is factually complex but legally simple. It's like this: (1) there are a limited number of legal relationships that two persons can have; (2) general partnership is basically a fallback relationship which applies

when no other relationship fits; and (3) a general partnership is a relationship that almost no one would choose if they gave it any thought or effort.

Under the law of nearly every state, a partnership is simply an association of two or more persons to carry on as co-owners a business for profit. A partnership can be in writing, oral, or implied. A partnership is a partnership regardless of the label applied to the relationship by the parties. A partnership can exist even if the parties had no intention of forming a partnership, so long as they intended the basic elements of partnership.

The biggest problem is that a simple general partnership includes none of the liability limiting benefits of a corporation, LLC, or LLP. Additionally, each partner is deemed to have authority to act on behalf of the partnership.

In our story above, Farmer A and Neighbor B agreed to work together for a profit. They didn't talk about owning anything together but the baled hay was the product of Farmer A's land and Neighbor B's efforts so it was jointly owned up to the point of sale. So, arguably, the entity that may have caused the accident was not Neighbor B, it was the partnership of Farmer A and Neighbor B.

Of course, farmers and businesspeople get into situations like this all the time. In fact, this story is a combination of two cases I'm currently litigating . . . and how I dealt with my hay field this summer. When things go wrong it's usually because the deal is small and those involved don't think it's worth the time and effort to put something in writing, or to think through the possible pitfalls. But legal safeguards in these situations need not be complicated.

Farmer A and Neighbor B could have reached the same practical result of shared risk and profit, without shared liability, in a number of ways. In this case, Neighbor B could have leased the land, with rent being contingent on the same formula as agreed upon, and with Neighbor B taking complete ownership of the hay. Or Farmer A could have hired Neighbor B to custom farm the land as an independent contractor and then sold him back the hay in a separate transaction. There are probably a dozen other simple ways the problem could have been solved.

Many businesspeople take pride in doing business "on-a-handshake" as a sign of their trustworthiness. However, betrayal by a business partner is only one possible problem with handshake deals. Remember that every business relationship must fall into a limited number of buckets. These include—employer/employee, landlord/tenant, independent contractors, or co-owners. Even in a handshake deal, take care to think through which of those buckets you want to land in and how to get there. Otherwise, you could fall into the default bucket and be surprised to be a general partner.

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