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**Regulatory Preemption and Federal Common
Law: The Post-State Enforceability of
Farmers Home Administration Liens**

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REGULATORY PREEMPTION AND FEDERAL COMMON LAW: THE POST-SALE ENFORCEABILITY OF FARMERS HOME ADMINISTRATION LIENS

INTRODUCTION

The doctrines of federal common law and regulatory preemption both define the extent to which federal interests may intrude on state interests. Regulatory preemption analysis determines when a valid legislative regulation will preempt state law. Federal common-law analysis, on the other hand, is used by the courts to decide if the federal interest involved is strong enough to warrant creation of a uniform federal rule, displacing state law. In cases involving the release of Farmers Home Administration ("FmHA" or "Agency") liens, the courts have engaged in a federal common-law analysis, even though a valid legislative regulation exists restricting the release of liens. This regulatory restriction is contrary to many states' commercial laws which provide that good faith purchasers take free of a security interest.¹

This Note argues that federal common-law analysis is inapplicable when a valid legislative regulation² preempts relevant state law and that the FmHA regulation, when pertinent, therefore preempts state law. Part I examines the different approaches used by the circuit courts to resolve these FmHA disputes and discusses the use of federal common law in general. Part II compares regulatory preemption with the doctrine of federal common law, and concludes that when a valid, pertinent, legislative regulation exists, a federal common-law approach is inappropriate. Part III shows that FmHA regulation section 1962.17(a) is a valid legislative regulation that, when on point, precludes a resort to federal common law.

I. RESOLVING THE DISPUTE OVER FMHA LIENS IN THE CONTEXT OF A CONFLICT BETWEEN STATE AND FEDERAL LAW

The Farmers Home Administration, under statutory authority from Congress, provides loans to farmers under the Emergency Agricultural Credit Act of 1984³ (the "1984 Act"). To protect its interests, the Agency files liens on farmers' chattel, and Agency regulations provide that the liens remain in place until released by a County Supervisor. Some states, however, provide that a good-faith purchaser of farm chattel takes free and clear of all liens.

1. See *infra* note 9 (listing states that have adopted this rule by modifying U.C.C. § 9-307(1) (1987)).

2. See *infra* notes 63-65 and accompanying text (defining legislative regulations).

3. 7 U.S.C. §§ 1921-1989 (1982 & Supp. IV 1986). Prior to 1984, the statute was referred to as the Agricultural Credit Act of 1978, Pub. L. No. 75-334, 92 Stat. 420, which replaced the Consolidated Farm and Rural Development Act, Pub. L. No. 87-128, 75 Stat. 307 (1961) (codified as amended in scattered sections of 7 U.S.C.).

Federal courts have split on their approach to this problem. Some apply straightforward federal common-law analysis to decide whether the liens involve sufficient federal interests to warrant a judicially created rule, and if so, whether federal or state law best advances the overall interests involved. Other courts first apply a regulatory analysis to decide whether the regulations carry the force of law, and only upon a negative finding at this first step will these courts then apply the federal common-law doctrine.

A. *Disputes Over the Release of FmHA Liens*

The FmHA is responsible for providing and administering loans to farmers under the 1984 Act. Pursuant to its substantial rulemaking authority,⁴ the Agency has issued a regulation—section 1962.17(a)—that restricts the manner in which FmHA liens on chattel may be released.⁵ To “protect [its] financial interest,”⁶ the FmHA often files liens on farmers’ chattel. Because the sale of chattel that serves as security for the FmHA loan may put the Agency’s lien in jeopardy, its regulations provide that the lien is not released until the “County Supervisor” (an FmHA administrator) releases it.⁷

However, the Uniform Commercial Code (U.C.C.) as adopted by many states allows good-faith purchasers of farm products to take free of a security interest. Although the U.C.C. provides that a “person buying farm products from a person engaged in farming operations [does not] take[] free of a security interest,”⁸ in the states that have modified or eliminated this language,⁹ farm-products purchasers are put in the same position as purchasers of other goods. Thus, in these

4. 7 U.S.C. § 1989 (1982). This section states: “The Secretary is authorized to make such rules and regulations, prescribe the terms and conditions for making or insuring loans, security instruments and agreements, except as otherwise specified herein, and make such delegations of authority as he deems necessary to carry out this chapter.” *Id.*

5. 7 C.F.R. § 1962.17(a) (1988) provides: “When the borrower sells security, the property and proceeds remain subject to the lien until the lien is released by the County Supervisor.”

6. *Id.* § 1962.2.

7. See *supra* note 5.

8. U.C.C. § 9-307(1) (1987). This rule is often referred to as the “farm products exception” because it is an exception to the general rule that “[a] buyer in ordinary course of business . . . takes free of a security interest created by his seller even though the security interest is perfected and even though the buyer knows of its existence.” *Id.*

9. The following states have either deleted the farm products exception from their version of U.C.C. § 9-307(1), or have sufficiently altered the related sections so that the exception does not apply in the same manner as it would under the original wording: California, Delaware, Georgia, Illinois, Indiana, Iowa, Kentucky, Maryland, Michigan, Minnesota, Nebraska, North Dakota, Ohio, Oklahoma, Tennessee, Texas, Utah and Washington. For a listing and explanation of the relevant changes, see 6A Willier and Hart U.C.C. Reporter—Digest (MB) § 9-307, at 1-968.1-10(18) (W. Willier, F. Hart, R. Desiderio & B. Ohline eds.) (1988).

states the post-sale enforceability of FmHA liens depends upon whether the federal regulation or state law governs. The choice of federal or state law will, in turn, often depend on whether the court applies federal common-law¹⁰ or regulatory-preemption analysis.¹¹

B. Federal Common Law and the Priority of Government Liens

Both courts¹² and commentators¹³ have recognized that federal common law exists when Congress either expressly or implicitly confers on the judiciary the authority to fashion federal rules. The seminal post-*Erie*¹⁴ case that developed the parameters of this limited federal common law is *Clearfield Trust Co. v. United States*,¹⁵ in which the Court declared that "[i]n absence of an applicable Act of Congress it is for the federal courts to fashion the governing rule of law according to their own standards."¹⁶

While the basis for a limited federal common law has been articulated in various ways, the doctrine's legitimacy is primarily grounded in structural constitutional principles.¹⁷ Consequently, the courts have applied the *Clearfield Trust* justification of federal common law to a broad range of federal interests. Thus, for example, the Supreme Court created a federal common law of torts when a member of the armed services was injured by an oil truck;¹⁸ of labor relations based on

10. See *infra* notes 12-35 and accompanying text.

11. See *infra* notes 55-71 and accompanying text.

12. See cases cited *infra* notes 18-23.

13. See, e.g., Friendly, In Praise of *Erie*—And of the New Federal Common Law, 39 N.Y.U. L. Rev. 383, 405 (1964); Mishkin, The Variousness of "Federal Law": Competence and Discretion in the Choice of National and State Rules for Decision, 105 U. Pa. L. Rev. 797, 799-800 (1957); Comment, Adopting State Law as the Federal Rule of Decision: A Proposed Test, 43 U. Chi. L. Rev. 823 (1976); Note, Rules of Decision in Nondiversity Suits, 69 Yale L.J. 1428, 1437 (1960).

14. *Erie R.R. v. Tompkins*, 304 U.S. 64 (1938). *Erie* denounced the existence of a general federal common law, *id.* at 78, but since then, federal common law has been recognized in limited situations, see *infra* notes 17-23 and accompanying text.

15. 318 U.S. 363 (1943).

16. *Id.* at 367. The decision in *Clearfield Trust* has been praised as providing "[t]he enduring contribution [of a] clear establishment of power in the federal courts to select the governing law in matters related to going operations of the national government." Mishkin, *supra* note 13, at 833. But cf. Friendly, *supra* note 13, at 410 (criticizing the *Clearfield Trust* Court as too quick to displace state law with a uniform federal rule); Note, The Federal Common Law, 82 Harv. L. Rev. 1512, 1526-27 (1969) (same).

17. See, e.g., Field, Sources of Law: The Scope of Federal Common Law, 99 Harv. L. Rev. 883, 931-34 (1986) (federalism); Merrill, The Common Law Powers of Federal Courts, 52 U. Chi. L. Rev. 1, 12-27 (1985) (federalism, separation of powers, electoral accountability).

This Note does not extensively review the widely accepted legitimacy of courts' federal common-law powers. Both federal common-law and regulatory-preemption analyses are assumed to be legitimate.

18. *United States v. Standard Oil Co.*, 332 U.S. 301, 307 (1947) ("[F]ederal judicial power to deal with common-law problems . . . remain[s] unimpaired for dealing independently, wherever necessary or appropriate, with essentially federal matters, even

a grant of jurisdiction to federal courts;¹⁹ of the pollution of interstate waters;²⁰ of certain aspects of international law;²¹ and, in *United States v. Kimbell Foods*,²² of the priority of liens stemming from federal loan programs based on the federal government's rights as a party to the transactions.²³ The common thread running through these applications of federal common law is that the courts have viewed their decisions as necessary judicial gap filling.

The Supreme Court in *Kimbell Foods*, explaining that "[w]hether to adopt state law or to fashion a nationwide federal rule is a matter of judicial policy,"²⁴ engaged in essentially a two-stage federal common-law analysis.²⁵ This approach entails first a determination of whether to apply federal common law and then, if it is to be applied, a determination of which rule gives content to the federal common law.²⁶ The *Kimbell Foods* Court, citing *Clearfield Trust*, quickly resolved the first issue, explaining that federal lending programs involve sufficient federal interests to warrant application of federal common law.²⁷ It thus rejected the notion that state law is or should be applied of its own force because, in light of the government's interest in such cases, "the Constitution and Acts of Congress 'require otherwise.'"²⁸ This "requirement" stems from the broad proposition that "effective Constitutionalism requires recognition of power in the federal courts to

though Congress has not acted affirmatively about the specific question."). The interests involved here were similar to those in *Clearfield Trust*: a uniform rule was chosen because of the actual or potential federal involvement in the particular area of the law throughout the country. *Id.* The government still lost the case under the new uniform federal rule. *Id.* at 314-17.

19. *Textile Workers Union v. Lincoln Mills*, 353 U.S. 448, 450-51 (1957) (section 301(a) of the Labor Management Relations Act of 1947 "is more than jurisdictional—[i]t authorizes federal courts to *fashion a body of federal law.*") (emphasis added) (citations omitted).

20. *Hinderlider v. La Plata River & Cherry Creek Ditch Co.*, 304 U.S. 92, 110 (1938) (decided the same day as *Erie*) (expressing concern about goals of federalism and the possible bias of state courts); *Illinois v. City of Milwaukee*, 406 U.S. 91, 107 n.9 (1972) (quoting *Texas v. Pankey*, 441 F.2d 236, 241-42 (10th Cir. 1971)) (noting desirability of uniform law).

21. *Banco Nacional de Cuba v. Sabbatino*, 376 U.S. 398, 427 (1964) (determining scope of the act of state doctrine under federal law).

22. 440 U.S. 715 (1979).

23. *Id.* at 726-27. See generally P. Bator, D. Meltzer, P. Mishkin & D. Shapiro, *Hart & Wechsler's The Federal Courts and the Federal System* 857-63, 895-901 (3d ed. 1988) (giving examples of the broad application of federal common law).

24. 440 U.S. at 728.

25. *Id.* at 726-40. For a general critique of the two-stage approach, see Field, *supra* note 17, at 950-82; see also Comment, *supra* note 13, at 834-35 (criticizing the pre-*Kimbell* courts' cursory treatment of the factors involved in determining the applicable rule of decision).

26. See Field, *supra* note 17, at 950.

27. 440 U.S. at 726.

28. 440 U.S. at 726-27 (quoting *United States v. Little Lake Misere Land Co.*, 412 U.S. 580, 592-93 (1973)).

declare, as a matter of common law or 'judicial legislation,' rules which may be necessary to fill in interstitially or otherwise effectuate the statutory patterns enacted by Congress."²⁹ Where a gap exists in an area with sufficient federal interests, therefore, the courts have asserted the right to engage in the creation of federal law.

In determining which rule would give content to federal common law, the *Kimbell Foods* Court was faced with a state law that denied the priority of federal government liens³⁰ and an area in which there was no valid legislative regulation on point.³¹ The Court explained that although there was a sufficient federal interest to require federal common law on the lien priority issue, "absent a congressional directive" the issue would be determined under state law.³² The Court reached this conclusion after detailing and following federal common-law analysis. It considered the need for uniform rules as opposed to ones differing by state, the potential disruption to commercial relationships as a result of adopting a federal rule and the need for a federal rule to protect federal interests.³³

The Court explained that "state rules determine the priority of F[m]HA liens when federal statutes or agency regulations are not controlling,"³⁴ and found that the only applicable FmHA regulations at that time expressly incorporated state law. While recognizing that if important national interests were implicated in federal lending programs it would be necessary to have a uniform federal rule, the Court chose "to adopt the readymade body of state law as the federal rule of decision until Congress strikes a different accommodation."³⁵

C. *The Circuit Courts' Divergent Approaches*

Federal judges have approached the conflict between the FmHA regulations and state laws differently. One court has considered the preemptive nature of the regulation, but decided that it did not control.³⁶ Others have ignored the regulation entirely and applied the same federal common-law approach enunciated by the Supreme Court in *Kimbell Foods*.³⁷ Even among these courts, there is disagreement as to whether the state law should be incorporated as the federal rule.³⁸

29. Mishkin, *supra* note 13, at 800.

30. 440 U.S. at 740.

31. See *id.* at 731-32.

32. *Id.* at 740.

33. *Id.* at 727-33.

34. *Id.* at 732.

35. *Id.* at 740.

36. See *United States v. Walter Dunlap & Sons*, 800 F.2d 1232 (3d Cir. 1986).

37. In *Kimbell Foods*, however, the question was one of relative priority of federal liens, whereas in these cases the issue was whether the federal lien had been released or was still enforceable.

38. Compare *United States v. Missouri Farmers Ass'n*, 764 F.2d 488, 489 (8th Cir. 1985), cert. denied, 475 U.S. 1053 (1986) (*Missouri Farmers Ass'n I*) (concluding that

1. *The Dispute over the Impact of Regulations on a Federal Common-Law Analysis.* — In *United States v. Walter Dunlap & Sons*,³⁹ the government sued for the proceeds from the sale of chattel on which the FmHA had a lien. The Court of Appeals for the Third Circuit found that the regulation in question did not validly preempt state law, so that a federal common-law analysis was necessary.⁴⁰

Judge Adams, in his concurrence, argued that before engaging in federal common-law analysis a court must determine if the applicable regulation has “the ‘force and effect of law.’”⁴¹ After analyzing the applicable regulations and showing that they were valid legislative regulations, Adams concluded that there was no need for federal common law and that the FmHA regulations should apply.⁴²

2. *The Pure Federal Common-Law Approach.* — The Fourth and Eighth Circuits have both directly applied a federal common-law analysis to decide an FmHA suit against a good-faith purchaser for conversion of the FmHA’s secured collateral.⁴³ However, even this direct use of federal common-law analysis has not yielded consistent results.

In these cases, a farmer had sold the collateral without remitting the proceeds to the FmHA.⁴⁴ The Fourth Circuit, without discussing the relevance of the Agency regulations at all, twice applied federal common law to determine that state law should be used as the rule of decision.⁴⁵ By contrast, the Eighth Circuit, applying federal common law to a virtually identical fact pattern, adopted the federal regulation as the uniform federal rule.⁴⁶

FmHA regulations govern) with *United States v. Tugwell*, 779 F.2d 5, 7 (4th Cir. 1985) (incorporating state law).

39. 800 F.2d 1232 (3d Cir. 1986).

40. *Id.* at 1239.

41. *Id.* at 1242 (Adams, J., concurring) (quoting *Chrysler Corp. v. Brown*, 441 U.S. 281, 295 (1979)).

42. *Id.* at 1245 (Adams, J., concurring).

43. See *United States v. Tugwell*, 779 F.2d 5 (4th Cir. 1985); *Missouri Farmers Ass’n I*, 764 F.2d 488 (8th Cir. 1985), cert. denied, 475 U.S. 1053 (1986); *United States v. Friend’s Stockyard, Inc.*, 600 F.2d 9 (4th Cir. 1979).

44. *Tugwell*, 779 F.2d at 5; *Missouri Farmers Ass’n I*, 764 F.2d at 488; *Friend’s Stockyard*, 600 F.2d at 10.

45. The court declared in *Tugwell* that “[t]he relevant federal law is, by adoption, local state law, . . . because the need for national uniformity is not great, adoption of [local] law will not frustrate the FmHA program, and adoption of a rule different from local law could disrupt local practice.” 779 F.2d at 7 (citing *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 726–27 (1979)). Similarly, the Fourth Circuit summarily concluded in *Friend’s Stockyard* “that the law of the State in which the transaction occurred would be incorporated into the Federal law and, in that character, would govern.” 600 F.2d at 10.

46. In *United States v. Missouri Farmers Ass’n*, 800 F.2d 185, 186 (8th Cir. 1986) (*Missouri Farmers Ass’n II*) (citing *Missouri Farmers Ass’n I*, 764 F.2d at 489), the court explained that “[t]his Court has previously held that FmHA regulations, not state law, governs the release of FmHA liens. . . . This panel is bound by that decision.” The Eighth Circuit in *Missouri Farmers Ass’n I* wrote that

Furthermore, the choice-of-law analysis does not necessarily determine who will prevail in court. Although both Fourth Circuit decisions were against the individual purchaser, the brief reasoning and strong reliance on *Kimbell Foods* indicate that the potential outcome was not a primary influence on the court's decision. In *Kimbell Foods*, the Supreme Court had chosen state law even though it resulted in an outcome unfavorable to the government.⁴⁷ In addition, the Eighth Circuit has opted for a federal rule of decision despite the district court's finding in favor of the government under relevant state law,⁴⁸ thus indicating that a uniform federal rule may be chosen even though the relevant state law affords the government adequate protection. That the Eighth Circuit has not based its choice of law solely on the desire to protect the federal interest involved is further evidenced by its willingness to use a federal rule of decision even when such a rule would result in a judgment adverse to the government.⁴⁹

3. *Implications of Regulatory Preemption for a Federal Common-Law Analysis.* — If Judge Adams' reasoning in *Walter Dunlap*⁵⁰ is correct,⁵¹ then *Kimbell Foods* is limited in scope to those situations in which neither a federal statute nor a validly promulgated legislative regulation is on point. If, instead, the other circuit judges are correct, then the federal common-law analysis, as elaborated by *Kimbell Foods*, controls even when a valid legislative regulation is on point, and the courts should merely consider the regulations as another factor in deciding whether

the [Supreme] Court also provided that state law could be adopted as the federal rule of decision so long as a national rule was not needed to protect the federal interests underlying the program. Adoption of state law in this case would conflict with the federal interests present in the FmHA loan program.

764 F.2d at 489 (citing *Kimbell Foods*, 440 U.S. at 726). Similarly, in a 1983 decision, the court of appeals stated in a footnote that "[t]o the extent that the district court opinion can be read as suggesting that [local] law rather than federal law applies . . . , we [dis]agree." *United States v. Farmers Coop.*, 708 F.2d 352, 353 n.2 (8th Cir. 1983).

The Eighth Circuit's decision in *Missouri Farmers Ass'n I* can also be viewed as implicitly accepting the conclusion reached by Judge Adams in *Walter Dunlap*, 800 F.2d at 1240 (Adams, J., concurring). There, the Eighth Circuit gave considerable weight to the fact that the use of state law as the rule of decision would negate the relevant FmHA regulations. 764 F.2d at 489. Coupled with dictum in *Farmers Coop.* that the particular federal regulation governed because "'federal law governs,'" 708 F.2d at 353 n.2 (quoting *Kimbell Foods*, 440 U.S. at 726), *Missouri Farmers Ass'n I* indicates the Eighth Circuit's implicit acceptance that valid regulations preclude the need to engage in federal common-law analysis.

Although the Eighth Circuit's choice of the federal regulation as the appropriate federal rule implicitly gave some weight to the notion that the regulations have preclusive effect, it nevertheless was based on a *Kimbell Foods* analysis, requiring a balancing of state and federal interests.

47. See 440 U.S. at 740.

48. See *Farmers Coop.*, 708 F.2d at 353.

49. See *Missouri Farmers Ass'n II*, 800 F.2d at 188.

50. 800 F.2d at 1240-45 (Adams, J., concurring).

51. See *supra* notes 41-42 and accompanying text.

state law or a uniform federal rule should govern.⁵² Thus, whether courts should apply federal common-law or regulatory-preemption analysis to FmHA conversion suits in light of section 1962.17(a) remains an unresolved issue.

II. FEDERAL COMMON LAW OR PREEMPTION? AGENCY REGULATIONS AS A LIMITATION ON THE SCOPE OF *KIMBELL FOODS*

The Administrative Procedure Act⁵³ requires that legislative rules carry the force of law.⁵⁴ Thus, agencies promulgating valid legislative regulations within the scope of their delegated powers act under congressional mandate. By contrast, federal common law is strictly a judicial mode of preemption applicable only in the absence of statutory direction. In the event an agency has promulgated a valid legislative regulation within the scope of its delegated powers, courts must apply that regulation before engaging in a federal common-law analysis. If the regulations are not directly on point or are interpretative in nature, courts should consider them as a factor in a common-law analysis, thus giving effect to congressional direction and agency expertise.

A. Regulatory-Preemption Analysis

At least since 1911, the Supreme Court has recognized the practical need for delegation of authority by Congress. In *United States v. Grimaud*,⁵⁵ the Court explained that agencies, in the capacity of administering and implementing statutes, can adopt regulations.⁵⁶ The Court, however, justified this authorization by claiming that such regulations were not an exercise of "legislative power to make laws, [but] administrative authority to make regulations."⁵⁷ This artificial distinction gradually faded, and by 1920 the Court was willing to grant regulations the "force and effect of law" as long as they did not conflict with "express statutory provision[s]."⁵⁸

In 1946 Congress passed the Administrative Procedure Act⁵⁹ (APA), which sets out the scope of judicial review of agency actions⁶⁰

52. This must be Justice White's conception, for in dissenting from a denial of certiorari in *Missouri Farmers Ass'n I*, he wrote that "[a] federal regulation is not a congressional directive" and that therefore the court of appeals' decision was "difficult to reconcile . . . with *Kimbell Foods*." *Missouri Farmers Ass'n I*, 475 U.S. 1053, 1054 (1986) (White, J., dissenting from denial of cert.).

53. 5 U.S.C. §§ 551-559, 701-706 (1982 & Supp. IV 1986).

54. See *infra* notes 64-65 and accompanying text.

55. 220 U.S. 506 (1911).

56. *Id.* at 518.

57. *Id.* at 517.

58. *Maryland Casualty Co. v. United States*, 251 U.S. 342, 349 (1920).

59. Ch. 324, 60 Stat. 237 (1946) (codified as amended at 5 U.S.C. §§ 551-559, 701-706 (1982 & Supp. IV 1986)).

60. 5 U.S.C. § 706 (1982).

and the required procedures for agency rulemaking.⁶¹ The APA recognizes the delegated legislative powers possessed by agencies and distinguishes these powers from agency "interpretative rules and statements of policy,"⁶² which do not involve the same procedural requirements. Under the APA, legislative rules are those that involve the agency's power to make law, while interpretative rules are those that are issued without the use of such power. Legislative regulations have the ability to create or alter legal rights. Interpretative regulations, however, merely express the agency's view of existing law.⁶³

The two types of regulations have very different effects. Interpretative regulations do not have the force of law, but "legislative regulations are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute."⁶⁴ Thus, a court cannot interpret a statute in a manner that conflicts with legislative regulations merely because it prefers a different application of the statute.⁶⁵

In order for a regulation to have the force of law, it must be promulgated in a procedurally proper manner⁶⁶ and be within the scope of the agency's delegated authority.⁶⁷ If the agency satisfies these requirements, courts must treat the regulations in the same manner as congressional statutes. Because Congress has the authority to delegate its legislative powers to the agencies, when an agency passes legislative regulations pursuant to that delegated power the regulations are entitled to have the "force and effect of law."⁶⁸ Consequently, when a valid legislative regulation conflicts with state law, it should preempt the state law under the supremacy clause of the Constitution,⁶⁹ even when Congress did not expressly authorize displacement of state

61. *Id.* § 553. These include "notice of [the] proposed rule . . . in the Federal Register" and the "consideration of the relevant matter presented" by the general public in response to the proposal. *Id.* § 553(b)-(c).

62. *Id.* § 553(d)(2).

63. 2 K. Davis, *Administrative Law Treatise* § 7:8 (2d ed. 1979). But see Saunders, *Interpretative Rules with Legislative Effect: An Analysis and a Proposal for Public Participation*, 1986 *Duke L.J.* 346, 352-58 (claiming that the distinction between legislative and interpretative rules has become "blurred."). See generally Feller, *Addendum to the Regulations Problem*, 54 *Harv. L. Rev.* 1311, 1320-21 (1941) (pre-APA explanation of the legislative-interpretative distinction). The ultimate determination of whether a regulation is legislative or interpretative is not always clear. See, e.g., *United States v. Walter Dunlap & Sons*, 800 F.2d 1232, 1238-39 (3d Cir. 1986).

64. *Chevron U.S.A., Inc. v. National Resources Defense Council*, 467 U.S. 837, 844 (1984) (using language from the APA); see also *Chrysler Corp. v. Brown*, 441 U.S. 281, 296 (1979) (requiring a "clear showing of contrary legislative intent").

65. See *United States v. Morton*, 467 U.S. 822, 834 (1984) (the court "must give the regulations legislative and hence controlling weight").

66. See *supra* note 61.

67. *Addison v. Holly Hill Fruit Prods., Inc.*, 322 U.S. 607, 616-19 (1944).

68. *Maryland Casualty Co. v. United States*, 251 U.S. 342, 349 (1920).

69. U.S. Const. art. VI, cl. 2; see *Fidelity Fed. Sav. & Loan Ass'n v. De La Cuesta*, 458 U.S. 141, 153 (1982) ("[f]ederal regulations have no less pre-emptive effect than federal statutes").

law.⁷⁰ However, "a federal agency may pre-empt state law only when and if it is acting within the scope of its congressionally delegated authority," and so the nature of an agency's authority must be examined to determine whether Congress intended that regulations promulgated by the agency pursuant to its rulemaking authority could displace state law.⁷¹ Thus, if the agency's regulation is permissible under its congressionally granted authority, and it has issued a procedurally valid legislative regulation, this regulation must preempt state law.

B. *Applying Preemption Analysis Before Federal Common Law*

Whereas valid legislative regulations are promulgated pursuant to congressional intent, a court's use of federal common-law analysis always results in judicially created law. Consequently, when a valid legislative regulation that is on point exists, courts should apply the regulation rather than legislate themselves.

1. *Federal Common Law as Court-Created Law.* — When a court makes federal common law, it essentially engages in a form of judicial preemption.⁷² Once it determines that a particular dispute involves a substantial federal interest, the court decides the case under federal common law so that state law no longer applies of its own force.⁷³ Even if the court chooses the state law, it does so only on a case-by-case basis,⁷⁴ for if a particular state's law "is plainly not in accord with the federal program . . . , [it] is not a permissible choice."⁷⁵ Thus, the Supreme Court has qualified the adoption of state law by repeatedly asserting that courts should not use "aberrant or hostile state rules" to give content to federal law.⁷⁶

Furthermore, under federal common law, the decision to adopt state law is itself based upon the advancement of federal policy.⁷⁷ As such, even when state law is applied, the judiciary still creates federal

70. *De La Cuesta*, 458 U.S. at 154; *Capital Cities Cable, Inc. v. Crisp*, 467 U.S. 691, 698–99 (1984). This analysis was recently reaffirmed in *City of New York v. FCC*, 108 S. Ct. 1637, 1642 (1988).

71. *Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 374 (1986).

72. See Merrill, *supra* note 17, at 36–39. Merrill contends that courts engage in "preemptive lawmaking" when they "fashion a federal rule of decision . . . by asking what collateral or subsidiary rules are necessary in order to effectuate or to avoid frustrating the specific intentions of the draftsmen." *Id.* at 36; see *infra* text accompanying notes 91–118 (extending this view of preemptive lawmaking to include the adoption of state law as the federal rule).

73. See *supra* notes 26–28 and accompanying text.

74. See, e.g., *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 735 n.34 (1979) ("We, of course, express no view on the proper priority rules to govern federal consensual liens in the context of *statutes other than those at issue here.*") (emphasis added).

75. *United States v. Little Lake Misere Land Co.*, 412 U.S. 580, 604 (1973).

76. *Id.* at 596; accord *Kimbell Foods*, 440 U.S. at 736 n.37; *De Sylva v. Ballentine*, 351 U.S. 570, 580–81 (1956).

77. Thus, even the choice to adopt state law is a form of federal preemption. In a given case, the state law becomes part of the federal common law; but only because the

law.⁷⁸

2. *The Superiority of Regulatory-Preemption Analysis.* — Although federal common law and legislative regulations both have binding effect akin to that of statutes, a valid legislative regulation trumps a court's power to fashion law. Thus, a court must determine if a regulation is implicated by the dispute before creating a common-law rule. As courts do not engage in federal common-law analysis when there is a statute directly on point, their ability to do so is similarly restricted when a pertinent, legislative regulation exists. In addition, a congressional grant of rulemaking authority to an agency is recognition of the agency's expertise and should be accepted as such by the courts.

When Congress grants an agency legislative powers, it has, in effect, allowed the agency to make law. The courts, in contrast, enjoy common-law powers often in the absence of direct congressional intent and only rarely upon an express indication.⁷⁹ Although the application of federal common law is also supported by the practical necessities of a federal system,⁸⁰ courts applying federal law generally can only rely on a federal statute—whose relation to the issue may be quite removed—for an inference of congressional intent to have federal law govern. Therefore, the court must first examine the regulations because, if valid, they should govern.⁸¹

In addition, even when the court bases its federal common-law powers on a grant of jurisdiction,⁸² it relies solely on an indirect congressional authorization to create law. The agency, on the other hand, creates legislative regulations because Congress has explicitly granted it the ability to create law through an empowering act. When courts create law, they are doing so merely because the statutory scheme has not expressly revealed what the applicable rule should be. Once the

particular state statute sufficiently comports with federal interests do courts adopt it rather than a new, uniform federal rule.

78. That the court creates federal law is even clearer when it chooses a uniform rule to displace state law.

79. See, e.g., *Textile Workers Union v. Lincoln Mills*, 353 U.S. 448 (1957) (Labor Management Relations Act). But see Justice Frankfurter's dissent in *Lincoln Mills*, arguing that the statute merely made a jurisdictional grant that did not alone "support [a finding of] congressional desire to impose . . . 'legislative' duties on the federal courts." *Id.* at 465 (Frankfurter, J., dissenting).

80. In areas with a strong federal interest, there may not be a federal statute directly involving the specific issue, yet the existence of state laws that do not account adequately for the federal interest may lead the courts to engage in the creation of federal common law.

81. Furthermore, the invalidity of the preemptive effect of the regulation may preclude a judicially created uniform federal rule. If the agency does not have the power to preempt state law, courts are unable to do so since the agency's authority to preempt is superior to the courts'.

82. See, e.g., *Lincoln Mills*, 353 U.S. at 456–57 (courts must decide labor issues under federal common law because the breadth of the statutory scheme and the grant of jurisdiction to the courts essentially mandate such an approach).

agency has validly promulgated regulations, there is no need for a court-created rule in order to consider adequately the federal interests involved.

The congressional grant of authority to promulgate regulations is also an acknowledgement of agencies' superior expertise and their procedural advantages over the court system. Agencies typically specialize in one area of the law and are thus able to develop their expertise, whereas courts must deal with all facets of the law.⁸³ Furthermore, agencies, when promulgating legislative rules, must provide for a period of public comment,⁸⁴ thus enabling them to factor into rulemaking the considerations and viewpoints of a wide range of parties. Although courts may receive, through amicus briefs, opinions other than those of the parties to the controversy, the variety of opinions that a court receives will generally be far less extensive than those received during the agencies' public comment period.⁸⁵

3. *A Two-Step Approach to the Federal-State Law Conflict.* — When a court is faced with a dispute that involves an agency, it must apply a two-step approach. First, it must examine the existing regulations. If it finds applicable regulations that are valid under the APA, legislative in nature and preemptive of state law, the analysis must end, for there is no need for the court to make "rules . . . to fill in interstitially or otherwise effectuate the statutory patterns enacted in large by Congress."⁸⁶ The agency has already done so in a proper fashion that is more directly authorized by the legislative body. Only if the regulations fail to pass this first step may the court take the second step and plunge into a federal common-law analysis.

If the regulations are not on point or are interpretative in nature, then the court should consider them as a factor in its federal common-

83. But cf. Note, *The Extent of OSHA Preemption of State Hazard Reporting Requirements*, 88 Colum. L. Rev. 630 (1988) (arguing that agency expertise does not extend to a determination of preemption issues).

84. 5 U.S.C. § 553(c) (1982).

85. See, e.g., 50 Fed. Reg. 45,740 (1985) ("In response to the proposed rule 255 written comments were received. . . . Two hundred eight of the comments were copies of four very similar letters." Thus at least forty-eight viewpoints were received.).

Additionally, as one commentator has recognized, the courts' ability to apply federal common law in the form of "delegated lawmaking" should be subject to a *more* restrictive [test] than the [one] applied in assessing the constitutionality of delegations to the executive branch This more stringent standard is justified because executive-branch and independent agencies are accountable, at least indirectly, to the President, and the President is elected. Thus, executive-branch lawmaking is less in tension with the norms of federalism and electoral accountability [(aspects legitimizing delegated lawmaking)] than is judicial lawmaking.

Merrill, *supra* note 17, at 41 n.182. This analysis also implies that judicial preemption is superseded by legislation or regulatory preemption and that in areas where a court is constitutionally prevented from choosing a uniform federal rule, an agency may still do so via regulations.

86. Mishkin, *supra* note 13, at 800.

law analysis and defer to them when appropriate. This approach allows the agency to retain some influence over the creation of federal common law in the field of its expertise. The *Kimbell Foods* Court, implicitly accepting this approach, referred to the existing FmHA regulations when it decided that state law should be adopted as the federal rule of decision in cases involving the priority of FmHA liens.⁸⁷

Perhaps because many aspects of regulatory preemption and federal common law are similar,⁸⁸ courts have applied *Kimbell Foods* to cases in which FmHA regulations have been directly on point.⁸⁹ This, however, is an incorrect approach. The existence of an applicable federal regulation requires the court to examine the specific regulation before miring itself in the morass of a *Kimbell Foods*-balancing analysis.⁹⁰

III. APPLYING THE TWO-STEP ANALYSIS TO DISPUTES CONCERNING THE RELEASE OF FMHA LIENS

In order for a regulation to preclude a federal common-law analysis, it must be pertinent, validly promulgated, legislative in nature and within the scope of the agency's statutory authority. FmHA regulation section 1962.17(a), which governs the release of Agency liens upon the sale of collateral, satisfies these criteria and preempts state law, thus rendering a federal common-law analysis unnecessary.

A. Section 1962.17(a)'s Relevance and Promulgation

Under the proposed two-step analysis, a court must first determine whether there are any regulations directly on point. FmHA regulation section 1962.17(a) explicitly deals with the release of liens upon the sale of security, granting the County Supervisor the exclusive authority to release liens.⁹¹ Thus, in *United States v. Missouri Farmers Association (Missouri Farmers Association I)*,⁹² for example, since the farmer sold his

87. *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 730-32 (1979).

88. For example, both require a comparison of the state law with federal interests, an examination of the underlying policy factors and a determination of congressional intent. See Monaghan, *The Supreme Court 1974 Term—Foreword: Constitutional Common Law*, 89 Harv. L. Rev. 1, 12 n.69 (1975) ("The close relationship between preemption principles and federal common law . . . has not been adequately discussed by the Court.") (citations omitted).

89. E.g., *United States v. Tugwell*, 779 F.2d 5, 7 (4th Cir. 1985); *Missouri Farmers Ass'n I*, 764 F.2d 488, 489 (8th Cir. 1985); *United States v. Friend's Stockyard, Inc.*, 600 F.2d 9, 10 (4th Cir. 1979).

90. At least one article, written shortly after the *Kimbell Foods* decision, recognized "that *Kimbell [Foods]* may be limited in application if . . . a regulation of a federal agency accords priority to federal agencies" under a different rule than the one chosen by the *Kimbell Foods* court. Greig & Althoff, *The Kimbell Decision: Applying State Laws as the Federal Rule of Decision in Priority Disputes Between Federal Agency and State, Private and Consensual Liens*, 86 Com. L.J. 447, 451 (1981).

91. See *supra* note 5.

92. 764 F.2d 488 (8th Cir. 1985).

collateral without release of the lien by the County Supervisor,⁹³ the regulation was directly on point and the court should not have used its federal common-law powers without first examining the regulation.

Section 1962.17(a) was also validly promulgated. The APA requires an agency to publish a general notice of its proposed rules, including a description of the nature of the rulemaking proceedings, the legal authority under which the rule is published and a description of the substance of the proposed rule.⁹⁴ The FmHA complied with these requirements when it promulgated the current section of the regulations. Section 1962.17(a) is essentially a result of changes made by the Agency in November 1985,⁹⁵ which had been published earlier as proposals in the Federal Register.⁹⁶ Publication in the Federal Register enables the general public to submit comments and the Agency to comply with the procedural requirements for promulgating legislative regulations under the APA.⁹⁷ Thus, since the regulation was promulgated with the proper procedures, if it is legislative and within the Agency's delegated authority, it preempts state law.

B. *The Nature of Section 1962.17(a)*

FmHA regulation section 1962.17(a) affects the legal rights of those dealing with FmHA liens, and therefore the regulation is legislative in nature. Writing for the majority in *Walter Dunlap*,⁹⁸ Judge Weis claimed that the regulation⁹⁹ was interpretative because it "instructs FmHA employees how to answer [purchasers'] inquiries [about liens], but does not by its terms impose a legal duty on purchasers."¹⁰⁰ Thus, he contended, the regulation merely explained the Agency's policy and did not alter or create legal rights as would a legislative regulation.

However, this reading of the regulation ignores the language specifically addressing the release of liens. As Judge Adams pointed out in his concurrence in *Walter Dunlap*, a restriction on the release of liens certainly affects legal rights and cannot be viewed as a mere policy

93. See *id.* at 488.

94. 5 U.S.C. § 553 (1982).

95. See 50 Fed. Reg. 45,741, 45,748 (1985). This provision, codified at 7 C.F.R. § 1962.18(b) (1985), was replaced by *id.* § 1962.17(a)(1) (1988).

96. 49 Fed. Reg. 47,007 (1984).

97. 5 U.S.C. § 553 (1982); see *Brock v. Cathedral Bluffs Shale Oil Co.*, 796 F.2d 533, 539 (D.C. Cir. 1986) (publication in the Code of Federal Regulations is only for legislative regulations).

98. 800 F.2d 1232 (3d Cir. 1986).

99. The case was decided under the 1985 version of the C.F.R. so that the relevant section was 7 C.F.R. § 1962.18(b) (1985). Although section 1962.17(a)(1) is more restrictive, potential conflict with state law still existed under section 1962.18(b), for if a sale of security was not "approved by the County Supervisor," chattel would still be "subject to the FmHA lien." *Id.* In states without the farm products exception, that would not be the result under state law. See *supra* notes 7-9 and accompanying text.

100. 800 F.2d at 1238.

statement or an interpretative rule.¹⁰¹ In fact, the majority opinion itself claims that the "FmHA attempts to impose a burden on the purchaser beyond that required under state law."¹⁰² Because the primary substantive distinction between an interpretative and legislative regulation is the ability to affect legal rights through creation of law,¹⁰³ the majority's claim that the regulation unduly restricts legal rights of purchasers directly contradicts its finding that the regulation in question is interpretive.¹⁰⁴

C. *The FmHA's Authority to Promulgate Section 1962.17(a)*

The remaining inquiry revolves around whether the regulation is within the scope of the Agency's powers, as determined under the APA's standards.¹⁰⁵ In *City of New York v. FCC*,¹⁰⁶ the Supreme Court held that if an agency's decision to preempt state law reasonably accommodates conflicting policies, its decision should be upheld unless it "is not one that Congress would have sanctioned" or contains aspects making it arbitrary, capricious, or directly unconstitutional.¹⁰⁸ FmHA regulation section 1962.17(a) conforms to these standards and is a reasonable accommodation of the conflicting policies of protecting the government's security interest and not disrupting state commercial laws. The disparity between various state laws on the release of liens, and the need of the FmHA to protect its loans, required the Agency to adopt this regulation. The reasonableness of this regulation is also confirmed by some courts' choice to adopt it as the federal rule under a federal common-law analysis.¹⁰⁹

Prior to passage of the Food Security Act of 1985¹¹⁰ (FSA), which unified standards for the release of liens on farm products, the only statutory language relating to the FmHA's security interests was con-

101. *Id.* at 1244 (Adams, J., concurring).

102. *Id.* at 1238 (Weis, J.).

103. 2 K. Davis, *supra* note 63, § 7:8, at 43.

104. The majority's real contention was that this regulation was not properly authorized. *Walter Dunlap*, 800 F.2d at 1238 ("No federal *statutory* source is cited for this additional dictate.") (emphasis added).

105. 5 U.S.C. § 706(2)(A)-(C) (1982) set out the general standards for invalidating agency regulations (for example, arbitrary, capricious, unconstitutional, or beyond the scope of delegated authority).

106. 108 S. Ct. 1637 (1988).

107. *Id.* at 1642 (quoting *United States v. Shimer*, 367 U.S. 374, 383 (1961)).

108. See *Fidelity Fed. Sav. & Loan Ass'n v. De La Cuesta*, 458 U.S. 151, 153-54 ("Federal regulations have no less pre-emptive effect than federal statutes. . . . When the administrator promulgates regulations intended to pre-empt state law, the court's inquiry is" limited "to whether he has exceeded his statutory authority or acted arbitrarily.").

109. See *Missouri Farmers Ass'n I*, 764 F.2d 488, 490 (8th Cir. 1985); *United States v. Farmers Coop.*, 708 F.2d 352, 353 n.2 (8th Cir. 1983).

110. Pub. L. No. 99-198, § 1324, 99 Stat. 1354, 1535 (codified at 7 U.S.C. § 1631 (Supp. III 1985)).

tained in the 1984 Act's general provision covering the liability of borrowers.¹¹¹ The FmHA's empowering section was very broad and did not explicitly indicate the extent to which the statutory scheme or regulations could preempt state law.¹¹² The enactment by Congress of the FSA confirms that the Agency's attempt to preempt state law via section 1962.17(a) is a reasonable accommodation of conflicting goals that Congress would have sanctioned.¹¹³

The FSA directly preempts state laws by setting out the general rules covering good-faith purchasers of farm products.¹¹⁴ The House Report accompanying the FSA explains that "[t]he bill is intended to preempt state law . . . to the extent necessary to achieve the goals of this legislation."¹¹⁵ With rules varying from state to state, the uniformity of the U.C.C. had disappeared, and the rule of law governing liens on farmers' chattel had become subject to significant uncertainty. The major impetus for the Food Security Act was a desire to alleviate this disparity between state laws.¹¹⁶

The FSA eliminated much of the conflict between state laws and section 1962.17 by creating a comprehensive legislative scheme covering the release of liens on much of farmers' chattel. Congress thus indicated its desire to have a uniform rule applied to this area, preempting states' laws. In fact, the only area in this field explicitly reserved to state law appears to be the determination of "[w]hat constitutes receipt" under the Act.¹¹⁷ The FSA, however, does not completely cover all situations involving FmHA liens. In cases in which the

111. 7 U.S.C. § 1946 (1982).

112. See *supra* note 4 (text of the empowering section).

113. Although FmHA regulations do not require the Agency to give written notice to buyers similar to the notice required by the FSA, as a practical matter the FmHA will comply with the FSA's requirements so that in cases in which the FSA applies, the Agency's lien will remain enforceable after sale of the collateral.

114. 7 U.S.C. § 1631(d)-(e) (Supp. III 1985). The Act states:

(d) Purchases free of security interest— Except as otherwise provided in subsection (e) of this section and notwithstanding any other provisions of Federal, State, or local law, a buyer who in the ordinary course of business buys a farm product from a seller engaged in farming operations shall take free of a security interest created by the seller, even though the security interest is perfected; and the buyer knows of the existence of such interest.

(e) Purchases subject to security interest— A buyer of farm products takes subject to a security interest created by the seller if [he receives a specified written notice within one year including notice of] any payment obligations imposed on the buyer . . . and . . . the buyer has failed to perform the payment obligations.

Id. Subsection (e) provides different limitations on buyers who claim to have taken free of security interest, in states with a "central filing system." Id. § 1631(e)(2).

115. H.R. Rep. No. 271, 99th Cong., 1st Sess. 109-10, reprinted in 1985 U.S. Code Cong. & Admin. News 1103, 1214. These goals included uniformity and equitable treatment of buyers and sellers alike. Id. at 1213-14.

116. Id.

117. 7 U.S.C. § 1631(g)(3) (Supp. III 1985).

FSA is not applicable, there exists a statutory gap.¹¹⁸ This gap, however, should not be filled with federal common law since the FmHA's regulation is directly on point.

CONCLUSION

The nature of the federal courts' authority to make common law has been subject to much scrutiny since the days of *Erie* and *Clearfield Trust*, and in *Kimbell Foods* the Supreme Court indicated its reluctance to displace state law "absent a congressional directive."¹¹⁹ Many courts, taking their cue from *Kimbell Foods*, forged ahead with a federal common-law analysis, ignoring the potentially preclusive effects of regulations on such an analysis. However, a valid legislative regulation that preempts state law must do so in all cases where it is applicable; and the courts should not intrude upon the delegated power of the agency by applying a federal common-law analysis when there is no legislative gap to fill. Recognition of this principle will effectively limit the scope of a pure, federal common-law test to those fields in which Congress has only planted the seeds of an overall statutory scheme without regulatory involvement, thus leaving the courts with the task of providing legal nourishment in the form of federal common law.

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118. For example, the Food Security Act does not apply to collateral that is not a farm product such as the tractor in *Kimbell Foods*. *Id.* § 1631(d). In addition, the FSA only applies to "a security interest created by the seller," and even then, only if the "seller [is] engaged in farming operations." *Id.*; see, e.g., *United States v. Continental Grain Co.*, No. 87-C-656-C (W.D. Wis. Aug. 8, 1988), in which the borrower sold collateral to a merchant who subsequently sold it to the defendant. Thus, the collateral was neither sold by a person engaged in farming operations, nor was the security interest in that collateral created by the seller.

119. 440 U.S. at 740.