Cases, Regulations and Statutes

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principal payments on installment note; not engaged in trade or business); Est. of Sussman v. Comm’r, T.C. Memo. 1978-344 (retired CPA who earned no income as accountant no longer engaged in trade or business).


11 Commissioner v. Groetzinger, 480 U.S. 23 (1987) ("constant and large-scale effort" by taxpayer in gambling activity was trade or business).

13 I.R.C. § 1402(b).

CASES, REGULATIONS AND STATUTES
by Robert P. Achenbach, Jr.

ANIMALS

HORSES-ALM § 1.01[2]. * The plaintiff’s decedent was killed when the decedent’s car struck the defendant’s horse on a highway. The horse had been confined by a low fence and the defendant testified that the gate to the pasture was found open after the accident. The trial court granted summary judgment to the defendant because the plaintiff had failed to provide evidence of the defendant’s negligence in fencing in the horse. The appellate court reversed, holding that Miss. Code § 69-13-111 provides a presumption that the owner of an escaped animal was presumed to have been negligent and required the owner to prove lack of negligence. Carpenter v. Nobile, 620 So.2d 961 (Miss. 1993).

BANKRUPTCY

GENERAL

DISCHARGE-ALM § 13.03[6]. * An insurance company hired the debtor to recover and sell a stolen tractor found by the police. The debtor made the highest bid and retained the tractor but failed to make any payment to the company. The debtor sold the tractor without paying the company and the company obtained a default judgment for the price of the tractor plus punitive damages. The company claimed that the judgment was nondischargeable, arguing that the Bankruptcy Court must give the default judgment issue preclusion as to the debtor’s willful and malicious injury of the company’s property. The court held that a default judgment may not be accorded either claim or issue preclusion in a subsequent bankruptcy proceeding. However, the court held that the facts of the case demonstrated the debtor’s willful and malicious injury of the company’s property and denied the debtor’s discharge of the judgment, including the punitive damages. In re Hale, 155 B.R. 730 (Bankr. S.D. Ohio 1993).

EXEMPTIONS-ALM § 13.03[3]. *

AUTOMOBILE. The debtor claimed the $2,000 exemption, under Va. Code § 34-26(8), for a vehicle which was collateral for a nonpurchase money loan. The trustee obtained an avoidance of the lien against the vehicle and sold the vehicle at an auction. The trustee argued that in avoiding the lien, the trustee became the lien holder and was entitled to the proceeds of the sale of the vehicle before the debtor could claim any exemption. The court held that under Va. Code § 34-26, nonpurchase liens against exempt property were void; therefore, because the lien was never effective against the exemption, the trustee’s lien status was junior to the exemption. The court also held that the debtor’s exemption carried over to the proceeds of the vehicle. In re Fenessy, 156 B.R. 22 (Bankr. E.D. Va. 1993).

AVOIDABLE LIENS. A creditor obtained a judgment against the debtors in 1989 and recorded the judgment lien. At the time the judgment lien attached, the debtor’s property was rented to third parties. The debtors moved into the property in 1992 and filed for bankruptcy in 1993. The debtors claimed the California automatic homestead exemption available in 1993 for $100,000 for residents over the age of 55 and income of less than $20,000. The creditor objected to the exemption, arguing that the exemption should be determined as of the date the judgment lien attached in 1989 when the property was not used as a residence. The court held that the debtors could create a homestead exemption by moving into the property pre- petition but that the lien was avoidable only to the extent of the homestead exemption available to the debtors at the time the lien attached to the property. In re Mayer, 156 B.R. 54 (Bankr. S.D. Cal. 1993).

HOMESTEAD. The debtor’s mortgagee obtained a foreclosure of the mortgage against the debtors’ residence. The debtors filed suit to invalidate the sale of the residence. Prior to filing for bankruptcy, the debtors had entered into a settlement with the mortgage holder to allow the debtors time to attempt to sell the residence. Before the time expired, the debtors filed for bankruptcy and the trustee renegotiated the settlement agreement and eventually sold the residence. The debtors filed an exemption for the residence. The trustee objected to the exemption, arguing that the foreclosure eliminated the debtors’ interest in the residence such that on the petition date, the debtors had no interest in the residence for which an exemption was allowed. The court held that because the validity of the foreclosure was never finally litigated, the debtors had a possible interest in the residence sufficient to claim the residence as a homestead exemption. The trustee also argued that because the sale was made post-petition, the debtor could not claim the exemption in the proceeds. The court held that the debtors’ exemption continued in the proceeds of the residence, whether sold pre- or post-petition. In re Donaldson, 156 B.R. 51 (Bankr. N.D. Cal. 1993).

The debtors had been residents of Wisconsin where the husband was a part owner of a small business for which the debtor had guaranteed several business loans. When the
business began to fail, the husband sold his interest in the business and the debtors sold their residence and moved to Florida. The debtors purchased a new residence using all of the proceeds of the previous residence and used all of their other non-exempt assets for living expenses until the husband found employment. The debtors admitted that the move to Florida was made to take advantage of the more liberal exemptions, especially the full exemption for homesteads. The debtors filed for bankruptcy one year and five days after moving to Florida and the holder of the guaranteed loan objected to the homestead exemption as impermissible pre-bankruptcy conversion of assets. The court held that the conversion of non-exempt assets and the move to Florida were impermissible pre-bankruptcy planning with the intent to evade creditors and the court reduced the homestead exemption to the amount allowed under Wisconsin law. *In re Coplan*, 156 B.R. 88 (Bankr. M.D. Fla. 1993).

**OBJECTIONS TO EXEMPTIONS.** A law firm obtained a judgment against the debtor. The judgment lien attached to a divorce decree payment to the debtor from the debtor’s ex-spouse. The payment was found to have been made in compensation for the debtor’s relinquishment of rights in the marital residence. The debtor claimed the divorce decree payment as a homestead exemption and the trustee sought to avoid the law firm’s lien as impairing the exemption. The law firm had not objected to the homestead exemption within the time limit and the debtor argued that the law firm was barred from objecting to the exemption. The court held that because secured creditors are not required to file claims or otherwise participate in the bankruptcy proceedings until forced by actions such as an avoidance or other challenge to the secured status of the claim, the law firm could challenge the exemption. The court held that the exemption was allowed since the divorce decree payment was in exchange for the loss of rights in the marital homestead; therefore, the judgment lien could be avoided. *In re Maylin*, 155 B.R. 605 (Bankr. D. Me. 1993).

**SALE OF EXEMPT PROPERTY.** The debtor owned a residence with the nondebtor spouse as tenants by the entirety. The house was the debtor’s only property available for payment of creditors and the trustee sought permission to sell the property to pay joint creditors of the debtor and nondebtor spouse. The trustee argued that the sale was allowed under Section 363(h) because without the sale no funds would be available to pay creditors. The debtor argued that the nondebtor spouse, who was elderly, would suffer emotional and psychological harm from the sale and forced move. The court held that the sale would be allowed because the debtor provided evidence of only possible harm to the nondebtor spouse and the debtor would still have substantial exempt funds for obtaining adequate new housing. The court also noted that the debtor had not attempted alternative methods of refinancing the house in order to pay creditors and still keep the house. *In re Harris*, 155 B.R. 948 (Bankr. E.D. Va. 1993).

WAGES. The debtor claimed the livestock raised and crops grown as exempt personal service earnings. No timely objection was made to the exemption. In a decision on avoidance of a lien impairing the claimed exemption in the livestock and crops, the Bankruptcy Court denied the exemption as having no statutory basis. The exemption issue was certified to the Wyoming Supreme Court which held that the claimed exemption was not allowable. The appellate court held that the exemption was allowed because no timely objection was made. *In re Coones*, 996 F.2d 250 (10th Cir. 1993), on rem. from, 113 S. Ct. 31 (1992), rev’g, 954 F.2d 596 (10th Cir. 1992).

**CHAPTER 12-ALM § 13.03[8].**

Chapter 12 has been extended through October 1, 1998. The legislation also amends Section 1221 to allow extension of the time for filing a plan if “the need for an extension is attributable to circumstances for which the debtor should not justly be held accountable.” Pub. L. No. 103-65, 107 Stat. 311 (1993).

**AUTOMATIC STAY.** The debtor filed for Chapter 12 three days before the commencement of a jury trial in which a creditor had sued the debtor on a promissory note. The creditor immediately sought relief from the automatic stay so that the state court case could proceed. The court held that (1) the debtor was a necessary party to the state action, (2) allowing the state action to proceed would not jeopardize the bankruptcy case and would assist the debtor in formulating a plan, and (3) the case would not be removed to the Bankruptcy Court because the state action was ready for trial and the delay caused by removal would prejudice the creditor and other parties. *In re Fay*, 155 B.R. 1009 (Bankr. E.D. Mo. 1993).

**ELIGIBILITY.** The debtor was a family farm partnership which had a nonrecourse loan in excess of $1.5 million from a bank. The loan was secured by partnership property, but the partners were not personally liable for the loan. The court held that the nonrecourse note was included in the amount of the partnership debt, thus making the partnership ineligible for Chapter 12 because the total debts exceeded $1.5 million. *Matter of Lindsey, Stephenson & Lindsey*, 995 F.2d 626 (5th Cir. 1993).

**FEDERAL TAXATION-ALM § 13.03[7].**

**DISCHARGE.** The debtor was found to have evaded the collection of taxes by the IRS after assessment. The IRS sought to have the taxes declared nondischargeable under Section 523(a)(1)(C) because the debtor attempted to “evade or defeat” the taxes. The debtor argued that Section 523(a)(1)(C) applied only to evasion of the assessment of taxes and not the collection of the taxes. The court held that the taxes were nondischargeable because the debtor’s interpretation of Section 523 would provide a loophole for dishonest debtors not intended by Congress. *Matter of Fridrich*, 156 B.R. 41 (D. Neb. 1993).

**CONTRACTS**

**AMBIGUITY.** The plaintiff wanted to purchase a farm on which the defendant was a tenant. Because the plaintiff wanted possession of the farm before the tenant’s lease expired, the plaintiff obtained an oral agreement from the defendant to release the land to the plaintiff after “harvest” of rye grass growing on 80 acres of the farm. The plaintiff
agreed to pay the rent on the remaining portion of the lease. Because the defendant was growing a licensed brand of ryegrass and was contractually required to destroy the rootstock before releasing the land to anyone not licensed to grow the ryegrass, the defendant discarded the field after harvesting the ryegrass seed. The plaintiff sued the defendant for trespass, breach of the release agreement and breach of the covenant of good faith and fair dealing because the defendant discarded the land after “harvest.” The trial court granted the defendant summary judgment, ruling that the term “harvest” referred to the time in which the release was to be granted and not the condition of the land. The appellate court reversed, holding that the term “harvest” was ambiguous and that a trial was required to discover the intent of the parties to the contract. **Hauge v. Vanderhave, 854 P.2d 1002 (Or. Ct. App. 1993).**

**BREACH OF WARRANTY.** The defendant orally agreed to sell the plaintiff some spring wheat. The plaintiff accepted a load of wheat from the defendant, cleaned it and resold the wheat as seed. However, the wheat delivered by the defendant was winter wheat which was unsuitable for seed and the buyers of the seed sued the plaintiff for lost crops. The plaintiff sought recovery from the defendant for its losses, including payments to the seed buyers. The appellate court upheld the trial court’s ruling that the defendant had breached the contract and was liable for the difference in value of the spring wheat contracted for and the winter wheat actually delivered. The remaining issue was the trial court’s award of consequential damages, the plaintiff’s payments to the seed buyers for the lost crops, with the plaintiff held to be 49 percent responsible and the defendant 51 percent responsible for those damages. The appellate court held that the defendant would be liable for consequential damages only if the defendant knew or should have known that the plaintiff intended to sell the wheat for seed. Because the trial court’s finding were inconsistent on this point, the case was remanded for clarification on this point. The appellate court upheld the apportionment of fault because the plaintiff failed to test the wheat for germination. **Dakota Grain Co., Inc. v. Ehrmantrout, 502 N.W.2d 234 (N.D. 1993).**

**FEDERAL AGRICULTURAL PROGRAMS**

**BORROWER’S RIGHTS—ALM § 11.01[2].** The defendant borrowed money from the FmHA and defaulted on the loan. When the FmHA brought foreclosure proceedings pursuant to the farm mortgage, the defendant sought a ruling that the Wisconsin one-year redemption period applied and that the FmHA would be required, under Wisconsin law, to sell the homestead separately. The court held that under **United States v. Kimbell Foods, 440 U.S. 715 (1979)**, the FmHA was not subject to state law in the foreclosure of the mortgage. **United States v. Einum, 821 F. Supp. 1283 (W.D. Wis. 1992), aff’d, 992 F.2d 761 (7th Cir. 1993).**

The debtors had granted the FmHA a mortgage on their farm and security interests in their farm equipment, livestock and crops. After the debtors defaulted on the loans, the FmHA sent to the debtors the Notification of Offer to Restructure Debt. Because of the debtors’ divorce, the FmHA failed to properly give the debtors further notices and a decision to deny loan servicing benefits was overturned on administrative appeal. A second restructuring process was started, ending with a denial of restructuring and a notice to accelerate the loans. The debtors failed to timely appeal this decision and the FmHA terminated the debtors’ appeal rights. The debtors argued that because the FmHA continued to send correspondence concerning the loan servicing after the period for appeal had expired, the FmHA should be required to allow an untimely appeal. The court held that the FmHA had given the debtors sufficient notice of the appeal rights, including an extra 10 days to file reasons for extending the appeal period; therefore, the debtors’ right to appeal had expired. The court also noted that the debtors had little chance of successful restructuring of their debts and that the appeal would be futile. **United States v. Kottcamp, 823 F. Supp. 609 (N.D. Ind. 1993).**

**BRUCELLOSIS.** The APHIS has adopted as final the adding of New Jersey to the list of brucellosis-free states. **58 Fed. Reg. 43068 (Aug. 13, 1993).**

**DISASTER ASSISTANCE—ALM § 10.03[4].** The plaintiff applied for payments under the Disaster Assistance Act of 1989 for losses to their cucumber crop. The ASCS determined that the plaintiffs were one “person” with their wholly-owned corporation which operated a farm implement business. Because the total gross revenues of the plaintiffs’ farm and corporation exceeded $2 million, the ASCS denied the plaintiffs’ application for disaster assistance. The plaintiffs argued that because the corporation was not involved in the farming operation, the revenues of the corporation should not be considered in the plaintiffs’ gross revenues. The court held that it found no requirement that the entities included in the “person” limitation be actively involved in the farming operation. The plaintiffs also argued that the “gross revenue” limitation should be defined as net profits and not gross receipts. The court held that the plaintiffs provided no support for this argument and pointed to the legislation which allowed the Secretary of Agriculture to define the term by regulations. **Hauhein Farms, Inc. v. Dept. of Agric., 824 F. Supp. 239 (D. D.C. 1993).**

The Disaster Assistance Act has been extended through 1993, with 100 percent payment of claims, subject to a $100,000 per person limit.

**FARM LOANS.** The FmHA has issued interim regulations amending the farm tract appraisal regulations, primarily renumbering the current regulations and incorporating Sections I and II of the Uniform Standards of Professional Appraisal Practice. **58 Fed. Reg. 44749 (Aug. 25, 1993).**

The FmHA has issued interim regulations extending the time to five years that an applicant may be eligible for direct and guaranteed farm operating, farm ownership and soil and water loans. **58 Fed. Reg. 44745 (Aug. 25, 1993).**

**FARMER-OWNED RESERVE.** The CCC has issued interim regulations under the farmer-owned reserve (FOR)

GRAZING FEES. The Forest Service has announced proposed regulations (1) to improve administration of permits, (2) to place greater emphasis on stewardship of the rangeland resources, (3) to manage the rangeland resources using an ecological approach, (4) to change the system used to determine the fees for grazing of privately owned livestock on national forests and grasslands in the west, and (5) to achieve greater consistency between the grazing management regulations of the Forest Service and the Bureau of Land Management. The annual fee for grazing livestock is scheduled to increase from $1.86 in 1993 to $2.56 in 1994, $3.26 in 1995, and $3.96 in 1996. 58 Fed. Reg. 43202 (Aug. 13, 1993).

MEAT AND POULTRY INSPECTION. The FSIS has announced a decrease from $38,300 to $37,800 in the amount of meat and poultry products which may be sold by retail stores to non-household consumers (e.g., hotels and restaurants) exempt from inspection. 58 Fed. Reg. 44158 (Aug. 19, 1993).

The FSIS has issued proposed regulations providing standard criteria by which FSIS inspectors will determine whether a bovine animal or carcass is properly identified as a calf or calf carcass. 58 Fed. Reg. 45296 (Aug. 27, 1993).

PESTICIDES-ALM § 2.04.* The EPA has issued a policy statement of the process whereby the EPA will make interim determinations of adequacy of state compliance of state pesticide applicator certification programs. 58 Fed. Reg. 43994 (Aug. 18, 1993).

TUBERCULOSIS. The APHIS has issued proposed regulations adding a definition, “accredited-free (suspended),” for states whose accredited-free status has been suspended due to detection of tuberculosis in any cattle or bison in the state and adding requirements for moving cattle and bison from states whose accredited-free status has been suspended. 58 Fed. Reg. 43086 (Aug. 13, 1993).

FEDERAL ESTATE AND GIFT TAX

CHARITABLE DEDUCTION-ALM § 5.04[4].* The decedent’s will left to an employee a monthly stipend from a trust and use of the decedent’s residence, including funds for the maintenance of the house. The provision for maintenance of the house included funds for improvements. The will also provided for payments from the trust corpus for the employee’s medical bills and state and federal income taxes. The will was originally executed in 1971 with codicils executed in 1972, 1977 and 1982. The estate executor obtained a state probate court order reforming the trust to provide the employee with a fixed annual annuity. The remainder of the trust passed to a charitable organization. The IRS denied the estate a charitable deduction for the remainder interest, arguing that because the will was changed after 1979, the reformation of the trust was not allowed to qualify the trust remainder interest for the charitable deduction. The court held that because the 1982 codicil made only minor changes in the original will and stated that it “republished” the original will, the will was considered executed prior to 1979. The IRS also argued that because funds from the income of the trust could be expended for house improvements and the employees medical and tax bills, the remainder interest was not ascertainable. The court held that the value of the remainder interest was ascertainable because the improvements would be limited to the maintenance of the house and the power to invade trust corpus for medical and tax costs was subject to a sufficiently objective standard. Wells Fargo Bank v. U.S., 93-2 U.S. Tax Cas. (CCH) ¶ 60,144 (9th Cir. 1993), aff’g, 91-1 U.S. Tax Cas. (CCH) ¶ 60,067 (C.D. Cal. 1991).

CLAIMS AGAINST ESTATE-ALM § 5.04[1].* The decedent made several gifts of money to the decedent’s children who transferred the money back to the decedent in exchange for a non-interest bearing note payable in 25 years or upon the death of the decedent. The decedent reported the gifts on federal gift tax returns. The court held that the estate could not deduct the notes as claims against the estate because the notes did not represent bona fide debts contracted for full and adequate consideration. Est. of Flandreau v. Comm’r, 994 F.2d 91 (2d Cir. 1993), aff’g, T.C. Memo. 1992-173.

SPECIAL USE VALUATION-ALM § 5.03[2].* The decedent died in 1981 and the taxpayer received a bequest of farm land for which special use valuation was elected. The taxpayer either directly farmed the land or leased part of the land on a crop share lease such that the material participation requirements were met. Part of the land was subject to a mortgage on which the taxpayer defaulted. The mortgagee foreclosed on the mortgage and the period of redemption expired; however, the taxpayer exercised a statutory right of first refusal and repurchased the land. The taxpayer had continuous possession of the land during the foreclosure period. The IRS ruled that under Minnesota law, foreclosure of a mortgage on farm land did not transfer all of the owner’s interest in the land until the right of first refusal was extinguished; therefore, the taxpayer had sufficient interest in the farm land throughout the period when the mortgage was foreclosed to prevent recapture of special use valuation benefits. The IRS also ruled that the foreclosure of the mortgage was not an involuntary transfer for purposes of I.R.C. § 1033 because the “seizure” of the property was not a public condemnation. The IRS cited Recio v. Comm’r, T.C. Memo. 1991-215. Ltr. Rul. 9333002, April 20, 1993.

TRUSTS-ALM Ch. 8.* When the taxpayers divorced, they established a trust for their child with both taxpayers as trustees. The trust provided for separate sub-accounts in which each taxpayer’s contributions were placed. The trust income was to be added to principal and the trustees had the power to distribute trust property to the child for educational and medical expenses, with each distribution coming equally from each sub-account. When the child reached age 35 or died before reaching age 35, each account in the trust...
reverted back to the taxpayers. Both taxpayers had a testamentary power of appointment over their sub-accounts and could amend or revoke the trust by consent of both taxpayers. The IRS ruled that (1) each taxpayer was the owner for federal tax purposes of their own sub-account, (2) each sub-account was includible in each taxpayer’s gross estate, and (3) the transfers to the trust were not completed gifts until trust amounts are actually distributed to the beneficiary. Ltr. Rul. 933028, May 21, 1993.

FEDERAL INCOME TAXATION

ACCOUNTING METHOD. The IRS has announced proposed regulations describing the events which trigger the recapture of LIFO benefits under I.R.C. § 1363(d) when a C corporation elects to become an S corporation or to merge with an S corporation in a tax-free reorganization. 58 Fed. Reg. 43827 (Aug. 18, 1993), adding Prop. Treas. Reg. § 1.1363-2.

FARM CREDIT SYSTEM.-ALM § 4.03[12].* The taxpayer was a direct lender bank in the Farm Credit System and was required to purchase stock in an FCA bank. The stock purchase funds were placed in a trust fund for protection against defaults by banks in the system. The stock purchase did not give the taxpayer any right to dividends or liquidation rights and the stock could not be sold to third parties. The IRS ruled that the cost of the stock purchase was not a capital expense but was currently deductible as an ordinary and necessary business expense under I.R.C. § 162. Ltr. Rul. 933005, May 7, 1993.

DROUGHT SALES OF LIVESTOCK.-ALM § 4.02[5].* Due to drought conditions in 1991, the taxpayer sold more cows than would be sold in a normal year. The taxpayer elected to defer the income from the drought induced sales under I.R.C. § 451(e). In 1992, the taxpayer purchased replacement calves and sought a revocation of the Section 451(e) election and an extension of time to defer income and replace the sold cattle in accordance with I.R.C. § 1033(e). The IRS ruled that the Section 451(e) election could be revoked; however, because the 1991 tax return had been filed, the ruling on the taxpayer’s eligibility for involuntary conversion treatment of the cattle and replacement calves had to be made by the District Director. Ltr. Rul. 933023, May 17, 1993.

HOBBY LOSSES.-ALM § 4.05[1].* Business loss deductions were disallowed for a horse breeding activity operated by a production manager at a manufacturing company where the expenses were consistent with operation of the business only for personal pleasure. Rohr v. Comm’r, T.C. Memo. 1993-373.

Although the taxpayers had eight years of losses from their horse breeding, training and sales activities, the court allowed deduction for the losses because an intent to make a profit was demonstrated by the expertise of the taxpayers, the amount of time spent on the business, the accurate records and the expectation that the assets would appreciate. Holbrook v. Comm’r, T.C. Memo. 1993-383.

INVESTMENT TAX CREDIT.-ALM § 4.04.* The taxpayers moved several 40 year old houses to a historic office subdivision and rehabilitated them, retaining over 75 percent of the existing external walls. The Tax Court held that the taxpayers were not entitled to rehabilitation credit for the houses because the houses were not rehabilitated in their original locations. The appellate court reversed, holding Treas. Reg. § 1.48-12(b)(5) invalid to the extent that it denied the credit to buildings which have been moved. Nalle v. Comm’r, 93-2 U.S. Tax Cas. (CCH) ¶ 50,468 (5th Cir. 1993), rev’g, 99 T.C. 187 (1992).

PARTNERSHIPS.-ALM § 7.03.*

ADMINISTRATIVE ADJUSTMENTS. The taxpayer was a joint venture which filed federal and state partnership returns. The partnership had two general partners. One partner was a Canadian corporation wholly owned by a Delaware corporation. The Canadian corporation and its Delaware owner possessed the partnership accounting and tax records and filed the partnership tax returns. The other partner, a Delaware corporation, had the largest interest in the partnership profits but did not possess the partnership records. The IRS ruled that the partnership could designate the Canadian corporation as its tax matters partners. Ltr. Rul. 9332027, May 17, 1993.

INTEREST DEDUCTION. The taxpayers were members of several partnerships and S corporations and owed income tax deficiencies and interest on several years of taxes. In order to claim the interest as a deduction before the effective date of the 1986 Tax Reform Act, the taxpayers paid the tax deficiencies and interest on December 31, 1986 and claimed the interest as a business expense. The IRS argued that the interest expense was a personal expense of the taxpayers and allowed the deduction only to the extent it did not exceed the taxpayers’ personal investment income. The court held that because partnerships and S corporations do not pay taxes but are pass-through entities, the interest expense could not be business related but was a personal liability of each member. True v. U.S., 93-2 U.S. Tax Cas. (CCH) ¶ 50,461 (D. Wyo. 1993).

LIMITED LIABILITY COMPANIES. The taxpayers formed a limited liability company (LLC) under the Illinois Limited Liability Company Act. The IRS ruled that the LLC would be taxed as a partnership because (1) the LLC lacked the corporate characteristic of continuity of life since the state LLC law required the consent of all members to continue the partnership after a terminating event and the LLC agreement required the approval of at least two-thirds of the members to continue the partnership, and (2) the LLC lacked the corporate characteristic of transferability of interests because the Act provided that if any other member objected to the sale or assignment of a member’s interest in the LLC, the transferee or assignee had no right to participate in the management of the LLC and the partnership agreement required the permission of the executive committee for any assignment or sale of an interest. Ltr. Rul. 933032, May 24, 1993.

* Agricultural Law Manual (ALM). For information about ordering the Manual, see the last page of this issue.
PENSION PLANS. The IRS has issued revised procedures governing the Voluntary Compliance Resolution (VCR) program to expand the types of defects which can be corrected under the program, to give additional guidance concerning the specificity of VCR compliance statement requests, to provide a standardized correction procedure for certain defects, and to extend the last day of the VCR program. Rev. Proc. 93-36, I.R.B. 1993-29, mod’g, Rev. Proc. 92-89, 1992-2 C.B. 498.

The IRS has adopted as final regulations interpreting the I.R.C. § 401(a)(4) requirement that contributions or benefits provided under a tax-qualified retirement plan not discriminate in favor of highly compensated employees. T.D. 8485, Aug. 30, 1993.

LANDLORD AND TENANT

FRUSTRATION OF COMMERCIAL PURPOSE. The defendant leased from the plaintiff farm land, including a lake and several ponds which the defendant planned to use for a public recreational fishing farm. The lease provided that the defendant did not warrant any of the real or personal property included in the lease. The defendant was unable to maintain sufficient water levels in the ponds because of a leak in the lake and the unavailability of other clean water. The defendant sought excuse from payment of the rent due to frustration of commercial purpose in that the property was no longer capable of supporting the defendant’s intended use. The court held that the defendant had not shown that the business use was impossible but that it was only more costly and difficult to maintain and the problems were foreseeable given the state of disrepair of the property when the lease was entered into. Williams v. Whitehead, 854 S.W.2d 895 (Tenn. Ct. App. 1993).

MORTGAGES

PRIORITY. A ranch was sold for cash and a promissory note secured by a deed of trust lien. The ranch was resold a year later to the plaintiff for a promissory note secured by a second deed of trust lien, with the plaintiff assuming the first promissory note. The plaintiff sold the ranch to a partnership which did not assume the first two notes. The partnership gave the plaintiff a promissory note for the ranch purchase price and a deed of trust lien. The partnership borrowed money from the defendant bank and used the proceeds to pay off the first two notes, giving the bank a deed of trust lien on the ranch. The bank sold the ranch at a foreclosure sale and three months later the plaintiff also sold the ranch at foreclosure and sued to invalidate the bank’s sale as a foreclosure of a junior lien. The court held that when the partnership paid off the first two liens, the plaintiff’s lien became the superior lien against the ranch and the bank’s sale was invalid. O’Dell v. First Nat’l Bank of Kerrville, 855 S.W.2d 1 (Tex. Ct. App. 1991).

PARTNERSHIPS

DEFINITION. -ALM § 7.03. The parties had agreed to raise purebred registered cattle together, with each party contributing property and services to the business. The parties were not married but lived together on the ranch. The parties had some joint bank accounts and joint loans but also had separate outside incomes and separate personal bank accounts. The business did not file federal partnership income tax returns and did not register the business as a partnership with the Secretary of State, nor did the parties identify their business as a partnership to third parties. The parties commingled business funds with their own funds haphazardly and had no agreement to share profits in any specific manner. The court held that sufficient evidence supported the trial court’s ruling that the parties did not operate as a partnership. Tondu v. Akerley, 855 P.2d 116 (Mont. 1993).

PROPERTY

JOINT TENANCY. The plaintiff was an heir to the decedent who owned cattle with another heir. The plaintiff objected to the decedent’s estate’s final distribution because the decedent’s interest in the cattle was not included in the distribution. The other heir argued that the cattle were owned in joint tenancy; therefore, the other heir took the cattle by survivorship and the cattle were not included in the testamentary bequests. The other heir claimed that the cattle were owned in joint tenancy because the official brand certificate listed the owners as the decedent “or” the other heir, and under Mont. Code § 81-3-105, a certificate is prima facie evidence of ownership by the persons whose names are on the certificate. The court held that Mont. Code § 70-1-314 controlled the creation of joint tenancies in property unless specifically changed by statute. Section 70-1-314 required specific language declaring the creation of a joint tenancy in order for a joint tenancy to exist. Because the brand certificate did not contain specific language creating a joint tenancy, the cattle were owned by the decedent and other heir as tenants in common. Matter of Est. of Shaw, 855 P.2d 105 (Mont. 1993).

SECURED TRANSACTIONS

STATUTE OF LIMITATIONS. In 1979, the FmHA made several loans to a corporation and six individuals. The loans were secured by a deed of trust and several parcels of real property. The parties defaulted on the loans in 1980 and 15 months later, the FmHA accelerated all of the loans. As a result of other suits by other parties, the FmHA was enjoined for 21 months from accelerating or foreclosing on any of its loans. In 1989, the FmHA sought foreclosure against the collateral and sold the property. When the FmHA sought deficiency judgments against the individuals, the debtors argued that the action was barred by the state six year statute of limitations or the federal six year statute of limitations under 28 U.S.C. §2415(a). The court held that the federal statute of limitations applied because the action was for money damages and was founded on a contract. The court also held that the accrual date of the foreclosure action was the date of the default for the defaulted payments and the date of the acceleration for the non-defaulted payments. The court held that the limitations period was not tolled as to the individuals by the bankruptcy proceeding of the corporation. Although the court did not specifically discuss the issue, the ruling implies that the injunction against the FmHA also did not toll the limitation period because the
court affirmed the trial court’s dismissal of the action as untimely. United States v. Dos Cabezas Corp., 995 F.2d 1486 (9th Cir. 1993).
The plaintiff owned a horse which was boarded at a third party’s stables. The third party hired the defendant veterinarian to perform castration on several horses, including the plaintiff’s. The plaintiff’s horse required special risky surgery which eventually led to the horse’s death from an infection. The plaintiff sued the defendant for malpractice but failed to provide any expert testimony as to the standard of care for veterinarians in the area. In a case of first impression involving veterinarians in Montana, the court held that as in other cases of professional negligence, expert testimony is required to prove negligence in the performance of a veterinarian’s work. The plaintiff argued that expert testimony was not required because the defendant admitted that the care was substandard. The court held that the admission exception to the expert testimony requirement was not applicable because the defendant also testified that the procedures were properly applied. *Zimmerman v. Robertson*, 854 P.2d 338 (Mont. 1993).

**CITATION UPDATES**