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Cases, Regulations and Statutes

Robert P. Achenbach Jr.
Agricultural Law Press, robert@agrilawpress.com

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discount should be limited to the costs of partitioning the property.[17] The Service position was that the issue of a discount was a question of fact.

The two recent cases

On December 29, 1999, the Tax Court decided *Estate of Brocato v. Commissioner*,[18] which involved several apartment buildings in San Francisco, some of which were held by the decedent in co-ownership. The court allowed a 20 percent fractional interest discount as well as an 11 percent blockage discount (because of the number of properties in the same market, the state of the local economy at the time and the limited pool of investors). The Tax Court specifically rejected the IRS expert's approach based on the costs of partitioning the properties. The Court cited to *Estate of Pillsbury v. Commissioner*,[19] *Mooneyham v. Commissioner*,[20] and *Estate of Williams v. Commissioner*.[21]

A week later, on January 5, 2000, the Tax Court decided *Estate of Busch v. Commissioner*,[22] which allowed a 10 percent discount for a co-ownership interest. The court stated that a 10 percent discount "would…be more than adequate to accommodate reasonable costs of partition."[23] The estate had sought a 40 percent discount for co-ownership of the 90.74 acre tract of land on the outskirts of Pleasanton, California. The Court rejected the IRS argument that the owners were trying to sell the property and so no discount should be allowed. In *Busch*,[24] the Court approved a value of $4,190,496 for the property. The land had been owned by the 98-year-old decedent and a trust for the 97-year-old surviving spouse of a deceased brother.

In conclusion

One possible interpretation of *Busch*[25] is that the value of the tract (over $4 million) did not justify a larger discount for co-ownership. But even at that the decision represents an attentiveness to the cost of partitioning beyond that found in the earlier cases. Another possible interpretation is that the Tax Court is becoming impressed with the IRS position. As noted above, the full meaning of *Busch*[26] will not be known until the case has been appealed or other cases have been decided or both.

FOOTNOTES

1 Estate of Brocato v. Comm'r, T.C. Memo. 1999-424; Estate of Busch v. Comm'r, T.C. Memo. 2000-3.
2 See, e.g., Ltr. Rul. 9943003, June 7, 1999.
3 See generally 5 Harl, *Agricultural Law* § 43.02[2] (1999); Harl, *Agricultural Law Manual* § 5.02[1] (1999).
4 See n. 1 *supra*.
5 Estate of Pudim v. Comm'r, T.C. Memo. 1982-606; Estate of Clapp v. Comm'r, T.C. Memo. 1983-721; Estate of McMullen v. Comm'r, T.C. Memo. 1988-500 (value of decedent's one-half interest in trust property not discounted as fractional share when trust property to be sold as entire fee simple interest).
6 Propstra v. United States, 680 F.2d 1248 (9th Cir. 1982). But see Estate of Haydel v. Comm'r, T.C. Memo. 1991-507 (no discount allowed where pre-trial stipulation set values of property interests).
7 T.C. Memo. 1989-138.
8 T.C. Memo. 1989-667.
9 90-2 U.S. Tax Cas. (CCH) ¶ 60,045 (S.D. Ga. 1990).
10 T.C. Memo. 1991-178.
11 T.C. Memo. 1992-97.
12 T.C. Memo. 1992-425.
13 T.C. Memo. 1993-526.
14 T.C. Memo. 1996-156.
15 T.C. Memo. 1998-59.
16 T.C. Memo. 1994-550, *rev'd on another issue*, 111 F.3d 1252 (5th Cir. 1997).
17 Ltr. Rul. 9336002, May 28, 1993; Ltr. Rul. 9943003, June 7, 1999.
18 T.C. Memo. 1999-424.
19 N. 12 *supra*.
20 N. 10 *supra*.
21 N. 15 *supra*.
22 T.C. Memo. 2000-3.
23 *Id*.
24 N. 22 *supra*.
25 N. 22 *supra*.
26 See n. 22 *supra*.

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

BANKRUPTCY

PENDING LEGISLATION. The U.S. Senate has passed the Bankruptcy Reform Act of 2000. In part the legislation (1) permanently enacts Chapter 12, (2) changes the base year for determining the 50 percent or more of income from farm operations from the year prior to filing the petition to "at least 1 of the 3 calendar years" preceding the filing of the petition, and (3) requires confirmation of a Chapter 12 plan if the plan provides for payment of all of the debtor's projected disposable income to allowed unsecured claims and the plan otherwise qualifies for confirmation. **Sen. 625**.

GENERAL-*ALM* § 13.03.*

EXEMPTION.

PARTNERSHIP PROPERTY. The debtor operated a farm as a partnership with the debtor's brother. The partnership dissolved upon the debtor's filing for Chapter

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12 and the debtor listed partnership property as part of the exempt assets. The court held that, under Arkansas law, a partnership did not terminate until after the winding up and final accounting had occurred. Therefore, the court held that the debtor had no interest in specific partnership property but only an interest in the partnership which could be included in any exempt property. ***In re* Burnett, 241 B.R. 438 (Bankr. E.D. Ark. 1999)**.

FEDERAL TAX-*ALM* § 13.03[7].*

AUTOMATIC STAY. The debtors had obtained a judgment that the IRS had violated the automatic stay. The Bankruptcy Court had awarded only $2500 in damages and the debtors sought review of that award. The appellate court upheld the award because the debtors failed to provide sufficient evidence of additional damages. The court also upheld denial of punitive damages as not awardable against the IRS. The appellate decision is designated as not for publication. ***In re* Herbert, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,206 (9th Cir. 1999), *aff'g*, 98-1 U.S. Tax Cas. (CCH) ¶ 50, 458 (Bankr. 9th Cir. 1998)**.

DISCHARGE. In 1996, the IRS had determined that another taxpayer was entitled to a $34,000 refund but in executing the refund, erroneously substituted the debtor's social security number on the refund claim and sent the refund to the debtor. The debtor had owed taxes from 1988 and the IRS first offset the tax owed from the refund before sending the remainder to the debtor. When the debtor failed to return the erroneous refund, the IRS filed suit and the debtor promptly filed for bankruptcy. The debtor claimed that the refund was dischargeable because the refund was used to offset the 1988 tax deficiency. The court held that the refund was to be considered as associated with the 1996 tax year; therefore, the refund was nondischargeable as a tax for which a return was filed less than three years before the filing of the petition. ***In re* Jackson, 241 B.R. 473 (Bankr. M.D. Ala. 1999)**.

MODIFICATION OF PLAN. The IRS had filed a priority claim in the debtor's Chapter 13 case. The debtor's plan, however, was confirmed without objection by the IRS even though the plan listed the priority claim at a lower amount. The debtor had objected to the IRS claim and was overruled; however, the IRS did not object to the lower claim amount included in the plan. The IRS sought to modify the plan to provide for the larger claim. The court found that if the larger amount was allowed, the debtor could not complete the plan and the case would have to be dismissed or converted to Chapter 7. The court held that the plan could not be modified such as to result in the impossibility of the plan being completed. ***In re* LaForgia, 241 B.R. 351 (Bankr. M.D. Fla. 1999)**.

POST-PETITION PENALTIES AND INTEREST. The IRS had filed undisputed pre-petition priority tax claims in the debtors' Chapter 12 case. Payment of the taxes was provided in the plan and a discharge was granted after all plan payments were made. The IRS then sought payment of interest and penalties which accrued post-petition on the priority tax claims. The court held that, as in Chapter 13 cases, post-petition interest on tax claims in Chapter 12 cases is discharged upon payment of the underlying tax claim. The court also held that I.R.C. § 6658(a)(2)(B)(ii) precludes imposition of tax penalties on tax claims during the pendency of a bankruptcy case. The District Court affirmed and remanded the case for assessment of costs against the IRS. ***In re* Mitchell, 241 B.R. 393 (N.D. Tex. 1997), *aff'g*, 210 B.R. 978 (Bankr. N.D. Tex. 1997)**.

RETURNS. The debtor had failed to file returns for several tax years and the IRS sought a court order to compel the debtor to file the returns. The court acknowledged that it had the power to compel the filing of the returns, but held that it could not exercise the power without some justification. The court found that the IRS provided no rationale to support a court order to file the returns. The court noted that the IRS had not (1) claimed any returns were required to be file, (2) claimed that the IRS could not file an accurate proof of claim for the taxes involved, (3) claimed that the debtor had not cooperated with financial information involving the taxes, and (4) attempted to prosecute the debtor for not filing the returns. The court held that an order to file returns was not appropriate without some justification from the IRS. ***In re* Farrell, 241 B.R. 348 (Bankr. M.D. Pa. 1999)**.

SETOFF. The debtor filed a Chapter 13 plan which provided for full payment of an IRS claim for 1996 taxes. The debtor's schedules listed a federal tax refund which the debtor claimed as exempt property. The plan was confirmed without objection from the IRS but on the very next day, the IRS filed a motion to offset the tax refund against the 1996 tax claim. The court held that the confirmation of the plan established the rights between the debtor and IRS and prevented any setoff. ***In re* Munson, 241 B.R. 410 (Bankr. C.D. Ill. 1999)**.

CONTRACTS

HEDGE-TO-ARRIVE CONTRACTS. This case involved an agricultural cooperative which bought and sold grain as part of its grain elevator and agricultural services business. The grain was produced by members and sold to the cooperative through hedge-to-arrive (HTA) contracts. The other parties were the producer/members. The parties had executed several thousand HTA contracts over the years with no problems until the price of grain began a steady increase over two years. In order to stem its losses from the contracts, the cooperative sought to terminate the HTA contracts in favor of regular sales contracts. The producers sought to completely terminate the contracts as unenforceable commodity futures contracts which did not comply with the Commodity Exchange Act. The producers pointed to the rollover provisions which made the contracts indefinite as to delivery and to the pricing terms which allowed future price changes. The court held that the contracts were cash forward contracts because the parties were both in the grain business, intended delivery and had established a pricing mechanism under the contracts. The court noted that, although the contracts had rollover provisions which could continue indefinitely, the parties had used the contracts for actual delivery over the years without problems. The producers also argued that the

unilateral termination of the HTAs by the cooperative was a breach of contract. The cooperative argued that the indefinite delivery and price-setting provisions of the contract created a contract at will which allowed unilateral termination. The court held that this argument contradicted the holding of the HTA as a cash forward contract and that the pricing system allowed the cooperative to set prices under the contract only if the producer did not set a price by a certain date. Because the cooperative cancelled the HTA contracts prior to the price setting date, the cancellation was a breach of contract. The court ordered the rescinding of the HTAs as null and void. ***In re* Grain Land Coop. Cases, No. 98-3217 (8th Cir. December 15, 1999), *aff'g*, 978 F. Supp. 1267 (D. Minn. 1997)**. See Harl, "Hedge-To-Arrive Contracts: Two Federal Court Cases," 8 *Agric. L. Dig.* 153 (1997).

In a similar case, the court again held that an HTA was not unenforceable as an illegal off-exchange futures contract merely because the producer could rollover the contract for an indefinite time, because the contract contemplated a delivery of the commodity at some point. **Haren v. Conrad Cooperative, No. 98-3803 (8th Cir. ____, ____)**.

ENVIRONMENTAL LAW

CLEAN WATER ACT. This is a second case involving a Washington dairy. The plaintiff brought actions under the federal Clean Water Act and the Washington Pollution Control Act against the defendants, livestock confinement facility operators for improper discharge of animal wastes. The defendants initially argued that they were not concentrated animal feeding operations (CAFOs) as defined in the CWA, but the court found that each facility confined and maintained more than 700 head of dairy cattle at each facility. The defendants also argued that the entire facilities were not point sources subject to the CWA, but that only the portions of the facilities which involved animal waste were regulated by the CWA. The court held that the CWA did not include any provision for classifying only a portion of a CAFO as a point source for pollution; therefore, the entire facility was subject to the CWA as a pollution point source. However, the court held that an issue of fact remained as to the extent the portions of the manure spreading operation on the land around the facility were part of the point source regulated by the CWA. The court also held that a fact issue remained as to whether the drains, ditches and canals around the facilities were regulated by the CWA as "waters of the United States." **Community Ass'n for Restoration v. Henry Bosma Dairy, 65 F. Supp.2d 1129 (E.D. Wash. 1999)**.

FEDERAL AGRICULTURAL PROGRAMS

ANIMAL WELFARE. The APHIS has announced that it is adopting two guides: The "Guide for the Care and Use of Agricultural Animals in Agricultural Research and Teaching," published by the Federation of Animal Science Societies, and the "Guide for the Care and Use of Laboratory Animals," published by the Institute of Laboratory Animal Resources. The APHIS is adopting these guides to assist regulated entities in meeting the standards in the regulations as they apply to the handling, care, treatment, and transportation of farm animals used for nonagricultural purposes (primarily research and exhibition). The recommendations in these guides represent the most current thinking on appropriate practices for the handling, care, treatment, and transportation of farm animals for nonagricultural purposes. **65 Fed. Reg. 5301 (Feb. 3, 2000)**.

COMMODITY PROGRAMS. The FSA has issued interim regulations amending several aspects of the commodity program regulations. Currently, the 7 C.F.R. § 718.2 "agricultural use" definition refers to certain specific crop, forage and conserving uses. The interim regulations more generally provide that "agricultural use" includes any agricultural activity. The interim regulations clarify the definition of "cropland" to specify that: (1) newly broken out land will be considered "cropland" for Part 718 purposes so long as the land is capable of, and is intended to be harvested using normal harvesting and production techniques and (2) land devoted to ponds, tanks, or trees will not generally be considered "cropland" for Part 718 purposes. The interim regulations clarify the "farm" definition to specify that a farm must (in addition to meeting other requirements) consist of tracts that: (1) have both the same owner and operator or (2) have the same operator but have multiple owners who have agreed in writing to have the tracts treated as one farm. The interim regulations also allow for combination of Production Flexibility Contract (PFC) and non-PFC farms where the non-PFC farm has potential PFC eligibility because of an existing CRP contract and the entirety of that farm is enrolled in the CRP. However, if, on the termination of the CRP contract, the new PFC eligibility is not exercised, the two farms would have to be divided back into separate farms.

The current priority list calls for using the following division and reconstitution methods in the following order as applicable: (1) estate method; (2) designation by owner method; (3) contribution method; (4) agricultural use method; (5) cropland method and (6) history method. The interim regulations add the "default method" between (4) and (5). Under the "default" method the tracts would be divided away from the parent farm based on the attributes of the individual tracts at the time of the division. In addition, 7 C.F.R. § 718.205 has been revised to specify that the FSA can adjust the results of any reconstitution when it believes that to do so would be more equitable or would further the purposes of the program which are impacted by decisions made under Part 718. Another amendment is that, where the division of the farm is going to be made using the landowner designation method, those persons with a security interest in the land must agree to the disposition. **65 Fed. Reg. 5444 (Feb. 4, 2000)**.

CROP INSURANCE. The FCIC has issued proposed regulations revising the fig, pear, walnut, almond, prune, table grape, peach, plum, apple and stonefruit crop

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insurance provisions. The proposed regulations amend the apple crop insurance provisions by allowing optional units and price elections by varietal group. The fig, pear, walnut, almond, prune, table grape, peach, plum, apple and stonefruit crop insurance provisions are revised by adding provisions to specify that the insured's elected or assigned coverage level or the ratio of the insured's price election to the maximum price election offered may not be increased and that each subsequent crop year coverage begins on the day immediately following the end of the insurance period for the prior crop year. The almond and walnut crop insurance provisions are revised by allowing insurance coverage for trees that have been grafted. The almond crop insurance provisions are revised by deleting the word “rejects” from the definition of “meat pounds.” **65 Fed. Reg. 6033 (Feb. 8, 2000)**.

FIRE ANTS. The APHIS has adopted as final regulations that amend the imported fire ant regulations by designating as quarantined areas all or portions of three counties in California, two counties in Georgia, one county in New Mexico, four counties in North Carolina, and one county in Tennessee. **65 Fed. Reg. 5221 (Feb. 3, 2000)**.

TUBERCULOSIS. The APHIS has adopting as final amendments to the tuberculosis regulations concerning the interstate movement of cattle and bison by raising the designations of California, Pennsylvania, and Puerto Rico from modified accredited states to accredited-free states. **65 Fed. Reg. 5998 (Feb. 8, 2000)**.

FEDERAL ESTATE AND GIFT TAX

INCOME IN RESPECT OF DECEDENT. The decedent’s estate held various bonds which had accrued but unpaid interest on the date of the decedent’s death which was paid to the estate along with post-death interest. The IRS ruled: (1) The accrued interest on the bonds as of the date of the decedent's death was income in respect of decedent (IRD) taxable to the estate under I.R.C. § 691(a)(1)(A). The accrued interest that constituted IRD to the estate was considered to have been acquired by the estate in the transaction in which the right to receive the income was originally derived and would have the same character that it would have had in the hands of the decedent, had the decedent lived and received the accrued interest. (2) The interest that accrued on the bonds after the date of decedent's death was ordinary income to the estate and includible in the estate's gross income under I.R.C. § 641. (3) To the extent such pre- and post-death accrued interest income was distributed to the beneficiaries, such distributions would be fully deductible by the estate and would be fully includible in the gross income of the beneficiaries if the total distributions from the estate to the beneficiaries did not exceed the estate's DNI for that year. If the amounts distributed from the estate to the beneficiaries exceeded the estate's DNI for that taxable year, then the amount deductible by the estate and includible in the beneficiaries' gross income will be limited by the estate's DNI. (4) The distributions of both pre- and post-death accrued interest from the estate to the beneficiaries had the same character in the hands of the beneficiaries as they did in the hands of the estate. If the distributions exceed the estate's DNI, the amounts shall be treated as consisting of the same proportion of each class of items entering into the computation of DNI as the total of each class bears to the total DNI of the estate. **Ltr. Rul. 200004030, Nov. 2, 1999**.

TAX BENEFIT RULE. The taxpayer established a trust for the taxpayer funded with an inheritance. The decedent’s estate was assessed a deficiency which included interest. The interest was paid by the trust which claimed the payment as a deduction on the trust return. Because the trust was a grantor trust, the interest deduction passed to the taxpayer. The IRS later refunded the entire interest payment assessed to the estate and the refund was passed on to the trust. The court held that, because the taxpayer received the tax benefit from the interest deduction, the return of the interest was included in the taxpayer’s taxable income. **Hornberger v. Comm’r, T.C. Memo. 2000-42**.

VALUATION. The taxpayer owned 14.3 acres of rural property. A residence and barn were located on a 2.5 acre parcel and the remainder was leased to a tenant farmer. The taxpayer placed the 2.5 acre residence parcel in a trust and retained title to the leased parcel. The IRS ruled that the 2.5 acres qualified as a personal residence such that the trust was a qualified personal residence trust. **Ltr. Rul. 200004037, Oct. 26, 1999**.

FEDERAL INCOME TAXATION

PENDING LEGISLATION. The U.S. Senate has passed the Bankruptcy Reform Act of 2000. The legislation also includes several tax changes, including increase of the expense method depreciation limitation to $30,000, full deductibility of health insurance costs for self-employed taxpayers starting in 2000, permanent extension of the work opportunity credit, 5 percent per year increase in the meal and entertainment expense allowance for small businesses, and many amendments to the IRA and pension plan provisions. **Sen. 625**.

BAD DEBTS. The case involved 16 business debts to the taxpayer which were declared worthless and claimed as deductions. The taxpayer supplied farm supplies to the debtors on account. In several of the accounts, at the end of each tax year, the taxpayer claimed the amount owed on account as worthless debt. However, the debt was carried over to the next year, during which the farmers paid off some of the debt but incurred more debt. However, the debtors continued to pay on the account and the taxpayer continued to charge interest in the following year. The court held that the debts were not worthless in the earlier years because the taxpayer continued to charge interest, extend new credit, and receive payments in later years. In one case, the debtor had ceased doing business in one tax year and had not made any payments on the account. The court held that one debt was totally worthless at the end of the tax year and allowed the bad debt deduction. **O'Neal's Feeder**

Supply, Inc. v. United States, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,193 (W.D. La. 2000).

The taxpayer was an attorney who owned a joint tenancy interest in a family corporation which operated a small retail store. The taxpayer provided some management assistance but received no income from the corporation. The corporation ceased business in 1993. The taxpayer made several loans to the corporation and deducted the amount of the loans as a bad debt in 1993. The taxpayer also paid some of the business expenses in 1993 and claimed those payments as a business expense deduction in 1993. The court held that the taxpayer was not entitled to a business bad debt because the taxpayer was not in the lending business nor the retail business but made the loans as shareholders or family members. The court also denied the business expense deduction because the expenses were liabilities of the corporation. **Martens v. Comm'r, T.C. Memo. 2000-46**.

CASUALTY LOSSES. The taxpayers owned a home near the home owned by O.J. Simpson. The taxpayers claimed a $750,000 casualty loss deduction for loss of value of their home, resulting from the publicity surrounding the O.J. Simpson trial which caused buyers to be less likely to pay the full fair market value for the property. The court disallowed the deduction because the taxpayers did not allege any physical damage to their property from either the murders or the media coverage. **Chamales v. Comm'r, T.C. Memo. 2000-33**.

EMPLOYEES. The taxpayer operated a business providing drivers to move vehicles owned by other companies. The taxpayer was found to have treated some drivers as employees and some as independent contractors. The court held that the taxpayer was not entitled to use the consistency safe harbor of I.R.C. § 530 because workers who performed similar work were not treated consistently as employees or independent contractors. In addition, the court held that the workers were all employees because the taxpayer retained sufficient control over the work of the employees and the employees did not independently contribute assets or profit from their work. **Leb's Enterprises, Inc. v. United States, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,182 (N.D. Ill. 2000)**.

HOBBY LOSSES. The taxpayers, husband and wife, were medical doctors and purchased four ranches for cattle raising and nut farming. The taxpayers built a new home on one farm which was intended as a retirement residence. The court held that the ranches were not operated for profit because (1) the taxpayer had no business plan and no records sufficient to determine the profitability of the ranches, (2) the taxpayers did not provide any evidence of appreciation of the ranch properties, (3) the taxpayers did not demonstrate that adverse weather and economic conditions prevented the ranches from being profitable, (4) the ranches produced only losses, (5) the taxpayers had no experience with cattle raising except for childhood experiences, and (6) the taxpayers waited two years to start planting nut trees which had a seven year preproductive period and built their retirement residence on that ranch. **Jorgenson v. Comm'r, T.C. Memo. 2000-38**.

IRA. The taxpayer was employed as a teacher in a city public school. The taxpayer participated in the Michigan public employees pension plan and also contributed to a personal IRA. The taxpayer argued that the participation in the pension plan did not prevent a deduction for the IRA because the pension plan was not established by the city public school system. The court held that the state pension plan was provided to the taxpayer through the city school system and prevented any deduction for the IRA contribution. **Neumeister v. Comm'r, T.C. Memo. 2000-41**.

INSTALLMENT SALE. The taxpayer sold an interest in a corporation to the other shareholders. The original sales agreement provided for payments over several years. Over the next 11 years, the taxpayer received some payments on the installment agreement but in other years no payments above interest were made. The taxpayer did not make any election out of the installment reporting of the gain from the sale. The agreement provided for early termination by either party and the buyer decided to require final payment in the twelfth year of the agreement. The final payment was negotiated and the taxpayer transferred most of the payment to two charitable trusts. The IRS ruled that, because the total payment was contingent upon how long the agreement existed, the taxpayer would be required to recover gain and basis per year equally over the maximum period of payments allowed by the sales agreement. In the years that the taxpayer received less than the basis and gain allocated to that year, the taxpayer recovered the basis and gain only up to the amount of money actually received, with the remainder carried over to the next tax year. **FSA Ltr. Rul. 200004009, Oct. 12, 1999**.

PASSIVE LOSSES. The taxpayer owned six light aircraft which were leased on a yearly basis to flight schools. The taxpayer was responsible for fuel costs, maintenance and insurance on the aircraft and spent more than 500 hours per year on the activity. The activity produced net operating losses for two years which the IRS disallowed as passive activity losses. The court held that the business of leasing personal property by yearly leases was a passive activity, whether or not the taxpayer materially participated in the activity; therefore, the losses were passive activity losses. **Kelly v. Comm'r, T.C. Memo. 2000-32**.

PENSION PLANS. For plans beginning in January 2000, the weighted average is 6.01 percent with the permissible range of 5.41 to 6.31 percent (90 to 106 percent permissible range) and 5.41 to 6.61 percent (90 to 110 percent permissible range) for purposes of determining the full funding limitation under I.R.C. § 412(c)(7). **Notice 2000-8, I.R.B. 2000-__**.

The taxpayer terminated employment and received a distribution of stock from an employer-funded ESOP. The taxpayer sold some of the stock in the same tax year and included all of the proceeds in income but did not include the value of the remainder of the stock in income. The court held that the taxpayer was required to include the value of all the stock received from the ESOP in income in the tax year it was received. The appellate decision is designated as

not for publication. **Villarroel v. Comm'r, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,176 (6th Cir. 2000)**.

S CORPORATIONS-*ALM* § 7.02[3][c].*

BUILT-IN GAINS. The taxpayer was an S corporation which contributed appreciated property to a charitable organization. The IRS ruled that the contribution was not subject to I.R.C. § 1374 and did not have to recognize any built-in gains in the property. **Ltr. Rul. 200004032, Oct. 26, 1999**.

DISCHARGE OF INDEBTEDNESS. The taxpayers owned 50 percent of an S corporation and had zero basis in their stock due to continuing losses incurred by the corporation. The corporation ceased operations and a portion of the corporation's remaining debt was forgiven by creditors, resulting in discharge of indebtedness income which was not recognized because of the insolvency exception. The taxpayers increased the basis of their stock by their share of the discharge of indebtedness income. The District Court held that the discharge of indebtedness income was to be determined at the S corporation level. The District Court determined that, since the discharge of indebtedness income was not recognized by the corporation, because of the insolvency exception, no discharge of indebtedness income passed to the shareholders which could be used to increase the basis of stock. The appellate court reversed, holding that, because I.R.C. § 108(b)(4)(A) provides that the reduction of tax attributes occurs on the first day of the tax year following the recognition of discharge of indebtedness income, the income pass-through to the shareholders occurs prior to being used to reduce tax attributes at the corporate level. Thus, the basis of the shareholders was increased and could be used to offset other deductions. This case represents a clear break with the Tenth and Seventh Circuit Courts of Appeal on this issue. See *Nelson v. Commissioner, 182 F.3d 1152 (10th Cir. 1999); Gitlitz v. Commissioner, 182 F.3d 1143, 1148 (10th Cir. 1999); Witzel v. Comm'r, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,165 (7th Cir. 2000), aff'g in part, T.C. Memo. 1999-64*. **United States v. Farley, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,179 (3d Cir. 2000), *aff'g*, 99-1 U.S. Tax Cas. (CCH) ¶ 50,370 (W.D. Pa. 1999)**.

SALE OF RESIDENCE. The taxpayers, husband and wife owned a residence. The title to the residence was transferred to a grantor trust established and owned by the taxpayers. The trust transferred the title to a partnership. The taxpayers each owned 1 percent of the partnership, with the trust owning the remaining 98 percent. The IRS ruled that the taxpayers would be treated as owning the residence at all times. **Ltr. Rul. 200004022, Oct. 28, 1999**.

SELF-EMPLOYMENT INCOME. The taxpayer was a cash method attorney who represented a client in 1975 on a contingent fee basis. The taxpayer and client disagreed on the amount of the fee and eventually negotiated payment of the fee in installments. Several installments were received in 1992 through 1995 and the taxpayer claimed that the installments were not subject to self-employment income tax because the services were performed in earlier years in which the taxpayer had paid the maximum self-employment tax. The taxpayer argued that Treas. Reg. § 1.1402(a)-1(c) allowed this result because the regulation provided for self-employment taxation of current payments if the services were performed in tax years in which the taxpayer was not subject to self-employment tax. The court held that, because the taxpayer was on the cash method, self-employment income was taxable in the year received and the regulation did not prohibit this result. **Walker v. United States, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,201 (10th Cir. 2000)**.

WAGES. The taxpayer was employed with a radio station over many years under an employment agreement which provided that all salary and bonuses would be wages. The agreement also contained provisions prohibiting the taxpayer from competing with the station or using station proprietary information if the employment was terminated. The station was sold and the taxpayer accepted a termination settlement which stated that the taxpayer would receive payment for future and past salary and bonuses. The court held that the termination payment was wages subject to FICA taxes because the payment was made for wages and in consideration of the noncompetition agreement. **Greenwald v. United States, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,197 (S.D. N.Y. 2000)**.

STATE REGULATION OF AGRICULTURE

PACKERS. The South Dakota legislature enacted a statute which prohibited livestock packers from discriminating on prices paid for livestock purchased for slaughter in South Dakota. The statute provided that if different prices were paid, the packer would be required to give public notice of the prices and the reasons for the different prices. The plaintiff was an organization of livestock packers, including packers on the South Dakota border which purchased for slaughter in South Dakota substantial quantities of livestock from other states. The statute allowed price discrimination only as to prices based on grade and yield. The plaintiff argued that the statute violated the dormant commerce clause which prohibits a state from enacting laws which benefit in-state economic interests to the detriment of economic interests of other states. The court held that the statute did not directly burden interstate commerce but held that the statute indirectly burdened interstate commerce because foreign state livestock producers would be deprived of some markets in South Dakota. The court held that the statute violated the dormant commerce clause because the detriment to interstate commerce outweighed the benefit to state residents. The court noted that the statute had the perhaps unintended effect of lowering prices paid to state producers and impacted heavily on foreign state producers because the South Dakota packers would find it almost impossible to either avoid differences in pricing or complying with the notice requirements of the statute. The court essentially found compliance with the statute to be so difficult that the packers would have to severely limit their purchases, both in and out of state. **American Meat Institute v. Barnett, 64 F. Supp.2d 906 (D. S.D. 1999)**.

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