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Cases, Regulations, and Statutes

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"net proceeds."[11]

In 1995, the taxpayer attempted to defer the year-end value added payment for 1995 to 1996 (as the taxpayer had done in 1994 and in each year since becoming a member of MCP "in the early 1980s."[12]

Citing the regulations[13] and *Warren v. United States*,[14] in which a cotton gin acted as taxpayer's agent in collecting and holding the proceeds of cotton sale, the Tax Court held that MCP served as taxpayer's agent for making the corn sales and receiving sales income with the only limitations placed on taxpayer's receipt of income being self-imposed. Therefore, the limitations were ineffective to achieve a deferral for tax purposes with the taxpayer constructively receiving the year-end value added payments during the taxable years in issue.[15]

Possible Solution

In the 1982 Fifth Circuit Court of Appeals case, *Busby v. United States*,[16] the sale of a cotton crop on a deferred basis was successful in withstanding an IRS challenge where an irrevocable escrow account was established by the cotton gin with no right by the taxpayer to the funds until the following year.[17] The deferred payment was the result of an arm's length agreement and was held by the court to shift the income to the next year.[18] Although there may be resistance to the time and possible expense involved with such an irrevocable escrow account, and there is always the risk of an IRS challenge, particularly in another Court of Appeals area, the irrevocable escrow does offer one possible solution.

FOOTNOTES

1 Treas. Reg. § 1.451-2. See generally, 4 Harl, *Agricultural Law* § 25.03[2] (2004); Harl, *Agricultural Law Manual* § 4.01[1][b] (2004).

2 E.g., Warren v. United States, 613 F.2d 591 (5th Cir. 1980).

3 Scherbart v. Comm'r, T.C. Memo. 2004-143.

4 Treas. Reg. § 1.451-2(a).

5 *Id*.

6 Walter v. United States, 148 F.3d 1027 (8th Cir. 1998) (cash basis seller of livestock).

7 Romine v. Comm'r, 25 T.C. 859 (1956).

8 Rev. Rul. 68-44, 1968-1 C.B. 191.

9 Arnwine v. Comm'r, 696 F.2d 1102 (5th Cir. 1983), *rev'g*, 76 T.C. 532 (1981) (cotton gin (acting on seller's behalf insofar as distribution of proceeds of crop sales concerned) received proceeds which were income to producer-seller); Williams v. United States, 219 F.2d 523 (5th Cir. 1955) (receipt by agent is receipt by principal; escrow arrangement unilateral and not product of bona fide arm's length negotiation); Warren v. United States, 613 F.2d 591 (5th Cir. 1980) (cotton gin acted as taxpayer's agent in collecting and holding proceeds of cotton sale); P.R. Farms, Inc. v. Comm'r, 820 F.2d 1084 (9th Cir. 1982), *aff'g*, T.C. Memo. 1984-549 (sale of fruit by agent; proceeds includible in taxpayer's income in year of sale even though not remitted to taxpayer until later year). Compare Busby v. United States, 679 F.2d 48 (5th Cir. 1982) (sale of cotton crop on deferred basis with irrevocable escrow account established by cotton gin with no right by taxpayer to funds until following year.

10 T.C. Memo. 2004-143.

11 *Id*.

12 *Id*.

13 Treas. Reg. § 1.451-2(a).

14 613 F.2d 591 (5th Cir. 1980).

15 Scherbart v. Comm'r, T.C. Memo. 2004-143.

16 679 F.2d 48 (5th Cir. 1982).

17 *Id*.

18 *Id*. See Maurer and Harl, "Using Escrow Accounts and Letters of Credit to Assure Payment Under Credit Sales Agreements," 14 *J. Agr. Tax & L.* 3, 17 (1992). See also Reed v. Comm'r, 723 F.2d 138, 145-148 (1st Cir. 1983) (taxable income not recognized until funds payable from escrow account).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr

BANKRUPTCY

GENERAL

SETOFF. The farm debtor originally filed for Chapter 7 and that case was closed and the debtor personally discharged of debts, including secured debts owed to the FSA. The creditor sought foreclosure of those secured debts but the foreclosure was delayed by the debtor's filing for Chapter 12. The debtor was allowed to enroll in federal farm programs post-petition and became entitled to payments under those programs. The USDA sought a setoff of the farm program payments against the secured debts. The court held that, because the debtor was relieved of personal liability for the secured debts in the prior Chapter 7 case, there existed no mutual personal debts between the USDA and the debtor to support a setoff under Section 553(a). ***In re* Myers, 362 F.3d 667 (10th Cir. 2004), *aff'g*, 284 B.R. 478 (Bankr. 10th Cir. 2002)**.

CHAPTER 12

ELIGIBILITY. As part of a settlement of federal farm loans, the debtor transferred title to the debtor's farm by deed to the FmHA (now the FSA). About five years later, the FSA offered to rent the land to the debtor with an option to purchase the farm at the end of the lease. The debtor notified the FSA that the debtor wanted to exercise the option but the debtor did not sign the purchase contract; instead the debtor filed administrative appeals over the purchase price and then filed for Chapter 12 in an attempt to cramdown the amount to be paid under the purchase option. The FSA filed a motion for the debtor to assume or reject the option purchase contract and the court ordered the debtor to assume or reject the contract. The debtor refused to do either action because the debtor argued that the debtor had always retained an ownership interest in the farm. The court held that the farm was owned by the FSA under the voluntary conveyance by the debtor to satisfy the original FmHA debts; therefore, because the debtor had allowed the option to lapse and refused to assume the option contract, the farm was not estate property and the debtor was not eligible for Chapter 12. ***In re* Dye, 360 F.3d 744 (7th Cir. 2004)**.

FEDERAL TAX

DISCHARGE. The debtor was an attorney who had failed to pay taxes for 1990 and 1991. The debtor entered into negotiations with the IRS for payment and made several offers in compromise and was the subject of several levies against the taxpayer's bank accounts and distributions from the law firm. However, during this time the debtor established several nominal bank accounts in other persons' names in order to hide income from the IRS. Also during this time the debtor continued a lavish lifestyle and made payments on retirement funds and country club memberships. The court held that the debtors' failure to make payments on the taxes owed when the taxpayer received substantial income and the use of the nominal bank accounts to hide assets were sufficient actions to demonstrate a willful attempt to evade payment of the 1990 and 1991 taxes, making the taxes nondischargeable under Section 523(a)(1)(c). ***In re* Gardner, 360 F.3d 551 (6th Cir. 2004)**.

ENVIRONMENTAL LAW

ENDANGERED SPECIES ACT. **Submitted by Roger A. McEowen**. In 1994, in an attempt to ease the burdens of the Endangered Species Act on private landowners, the Department of Commerce and the Department of Interior announced, without any prior public notice and comment, the immediate implementation of a "No Surprises" policy. The policy required that, upon approval of a habitat conservation plan (HCP), landowners would be given assurance that once an incidental take permit was approved, even if circumstances subsequently changed in a manner that would render the HCP inadequate to conserve listed species, additional conservation and mitigation requirements which would increase the costs or further restrict the use of natural resources beyond the original plan would not be imposed. The "no surprises" assurances were incorporated in all HCPs approved after August of 1994. The final rule implementing the "no surprises" policy provided that "no additional land use restrictions or financial compensation will be required of the permit holder (without the permittee's consent) with respect to species covered by the permit, even if unforeseen circumstances arise after a permit is issued indicating that additional mitigation is needed for a given species covered by a permit." *50 C.F.R. §§ 17.22; 17.32*. Even if foreseeable changed circumstances arise, the rule prohibits the federal government from requiring any conservation and mitigation measures in addition to those provided for in an HCP unless the HCP specifically authorizes imposition of such additional requirements, even where "additional conservation and mitigation measures are deemed to be necessary to conserve a species." In addition, HCPs are not required to authorize additional measures designed to address foreseeable changes in circumstances. Also, the rule does not require the agencies responsible for administering the ESA to take any specific remedial actions when, based on "unforeseen circumstances" or foreseeable "changed circumstances" not provided for by an HCP, activities undertaken pursuant to an incidental take permit place a listed species in danger of extinction or significantly impaired recovery. In 1999, the Fish and Wildlife Service promulgated a permit revocation rule incorporating the "no surprises" rule, and also promulgated a second rule exempting incidental take permits from the general permit revocation regulations. The general permit revocation regulations authorize revocation of any FWS permit when "populations of the wildlife or plant that is the subject of the permit declines to the extent that continuation of the permitted activity would be detrimental to maintenance or recovery of the affected population." In late 2003, however, the United States District Court for the District of Columbia ruled that both the "no surprises" rule and the "permit revocation" rule were invalid as having been promulgated in violation of the notice and comment requirements of the Administrative Procedures Act. *Spirit of the Sage Council, et al. v. Norton, 294 F. Supp. 2d 67 (D. D.C. 2003)*. In 2004, the court ordered that all incidental take permits issued by the FWS are subject to the general revocation standard applicable to other FWS permits until such time that the FWS adopts new revocation rules for incidental take permits in compliance with the notice and comment requirements of the APA. Until that time, no new incidental take permits can be issued that contain the "no surprises" assurances. **Spirit of the Sage Council, et al. v. Norton, No. 98-1873 (EGS), 2004 U.S. Dist. LEXIS 10789 (D. D.C. Jun. 10, 2004)**.

FEDERAL AGRICULTURAL PROGRAMS

ANIMAL VACCINATIONS. The plaintiffs owned racehorses which were treated with vaccines manufactured by the defendant. The plaintiffs alleged that the vaccines injured the horses and brought suit in state court for negligence, strict liability, breach of implied and express warranty. The defendant moved the case to federal court and the court sua sponte reviewed its proper jurisdiction over the case. The defendant argued that the case was governed by the Virus, Serums, Toxins, Antitoxins and Analogous Products Act, 21 U.S.C. § 151 et seq. which preempted all state law claims and created a federal question to support federal jurisdiction over the case. The court noted that all the claims were brought under state law and that the plaintiffs made no mention of violation or enforcement of federal law or regulations. The court held that the federal law and regulations did not provide "complete preemption" of all claims involving animal vaccines but provided only "conflict preemption" for claims which conflicted with the federal regulatory scheme. Therefore, because the court could not say that all of the claims were preempted by the federal law, the case was remanded to state court for trial. **Arnold v. Intervet, Inc., 305 F. Supp.2d 548 (D. Md. 2003)**.

CONSERVATION SECURITY PROGRAM. The CCC has issued interim regulations for administering the Conservation Security Program which provides financial and technical assistance to agricultural producers who, in accordance with certain requirements, conserve and improve the quality of soil, water, air, energy, plant and animal life, and support other conservation activities. **69 Fed. Reg. 34501 (June 21, 2004)**.

LIVESTOCK IDENTIFICATION PROGRAM. The APHIS has announced that the Under Secretary for Marketing and Regulatory Programs, U.S. Department of Agriculture, will host a series of listening sessions to provide livestock producers and other stakeholders with the opportunity to offer their comments regarding the Department's implementation of a National Animal Identification System. The public meetings will be held in Prineville, OR on July 1, 2004; in Stockton, CA on July 10, 2004; in Socorro, NM on July 16, 2004; in Pasco, WA on July 23, 2004; in Greeley, CO on August 10, 2004; in Billings, MT on August 13, 2004; in Kissimmee, FL on August 16, 2004; in Columbus, OH on August 18, 2004; in Ames, IA on August 26, 2004; in Joplin, MO on August 27, 2004; in Appleton, WI on August 30, 2004; and in St. Cloud, MN on August 31, 2004. **69 Fed. Reg. 35575 (June 25, 2004)**.

PERISHABLE AGRICULTURAL COMMODITIES ACT. The plaintiffs had filed PACA trust claims against the defendant produce dealer. The plaintiffs' claims included interest and attorneys' fees which were provided for on the invoices originally submitted for payment for the produce. The trial court denied the claims for interest and attorneys' fees because the allowance of the extra amounts would result in a disproportionate distribution of the PACA trust funds. The appellate court reversed and held that the interest and attorneys' fees provided by the invoices were recoverable from the PACA trust funds. The court examined the statute, 7 U.S.C. § 499e(c)(2), which allowed claims for "full payment of the sums owing in connection with [commodities] transactions." The court held that this language did not exclude expenses also bargained for by the parties. **Country Best v. Manning, 361 F.3d 629 (11th Cir. 2004)**.

The debtor operated a factoring business which purchased the accounts receivable of a PACA licensed produce handler. The handler's cash flow deteriorated and the debtor was forced to provide loans to the handler in order to protect the value of the accounts receivable. As part of the loan process, the debtor became involved in the finances of the handler, sought additional investors in the handler and took control of the accounting and stock of the handler. However, the debtor did not become an officer or director of the handler nor did the debtor control the day-to-day business operations of the handler. Unpaid produce sellers sought to make the debtor personally liable for the PACA trust obligations of the handler. In addition, the sellers sought to have the amounts owed by debtor under PACA declared nondischargeable in the debtor's Chapter 11 bankruptcy case for breach of fiduciary duty. The court held that the sellers failed to prove that the debtor's involvement was sufficient to apply PACA trust liability to the debtor. The court held that the evidence did not show that the debtor had actual or assumed legal responsibility for the handler's actions but showed only that the debtor attempted to maintain the financial health of the handler long enough to protect the accounts receivable purchased from the handler. Because the debtor did not have any fiduciary responsibility under the PACA trust, any debts owed to the sellers were not nondischargeable for breach of fiduciary duty. The court also noted that the sellers failed to provide evidence of any breach or impropriety by the debtor in handling the handler's financial affairs. ***In re* Steinberg, 307 B.R. 310 (Bankr. S.D. Fla. 2004)**.

FEDERAL ESTATE AND GIFT TAXATION

FAMILY-OWNED BUSINESS DEDUCTION. The decedent's estate failed to file its Form 706 with the family-owned business deduction election, although the tax return preparer had been instructed to make the election. The IRS granted the estate an extension of time to file an amended return with the FOBD election. **Ltr. Rul. 200425034, March 4, 2004**.

RECIPROCAL TRUSTS. The taxpayers, husband and wife, each established an irrevocable trust for the benefit of the other taxpayer, funded with cash and insurance policies. The reminder interests in both trusts passed to the taxpayers' children. The trusts were generally identical except the husband's trust provided that the wife had the right to withdraw specified amounts of trust principal after one child's death. The husband's trust also granted to the wife an inter vivos special power, effective at the child's death, to appoint trust principal among any of the husband's issue and their spouses or any trust created primarily for the benefit of one or more of those persons. Further, to the extent the wife did not exercise her inter vivos special power, the husband's trust granted to the wife an inter vivos or testamentary special power, effective at the child's death, to appoint trust principal among any of the husband's issue and any charities the wife designated or any trust created primarily for the benefit of one or more of those persons. Finally, if a marital trust is established, the husband's trust granted to the wife a testamentary special power to appoint the assets remaining in the marital trust among any of the husband's issue and any charities the wife designated or any trust created primarily for the benefit of one or more of those persons. Under the wife's trust, with respect to any trust established under the wife's trust except a marital trust, the husband could not be a beneficiary until three years after the wife's death and then will only be a beneficiary at any time when his net worth is under a certain amount and his income from personal services is under a certain amount. Distributions to the husband under this provision were limited to an amount reduced by the husband's income from personal services during the calendar year of the distribution. The IRS ruled that the provisions unique to each trust were sufficient to prevent the trusts from being deemed reciprocal to as to include the trust property in the grantor's estate. **Ltr. Rul. 200426008, March 10, 2004**.

TRUSTS. Prior to September 25, 1985, an irrevocable trust was established and funded for the grantor's three children. No contributions to the trust were made after the trust was established. Each beneficiary's portion of the trust was teated as a separate trust. The remainder of each child's trust passed either by a special power of appointment held by the beneficiary or to the issue of the child. The trust obtained a ruling by a state probate court for the separation of the trust into three distinct trusts, with a pro rata distribution of the original trust property equally among the three trusts. The IRS ruled that the division of the trust into the three trusts did not cause the trusts to be subject to GST. **Ltr. Rul. 200426005, March 22, 2004**.

FEDERAL INCOME TAXATION

BUSINESS USE OF RESIDENCE. The taxpayers, husband and wife, purchased a house in a ski resort area and initially rented the house through a management company when they were not using the house. In the tax years involved, the house was rented only to persons known by the taxpayers for a rent less than fair market rental value. The court held that, because the house was rented below fair market rental, under I.R.C. § 280A, the rental was considered personal use and the taxpayers were limited to deductions which did not exceed income from the property. In the second tax year, the rent was above fair market rent and the rental periods exceeded 14 days or 10 percent of the personal use by the taxpayers; therefore, Section 280A did not apply but the deductions were limited by I.R.C. § 183(a) because the taxpayers did not own the property with an intent to make a profit. The court found that the property was held by the taxpayers primarily for investment purposes because they did not actively market the property, keep full records of the rental activity, charge full market rent and received personal use of the property. Thus, the court held that the property was held for two purposes, as a residential rental property business and for investment. The court held that the expenses had to be rationally allocated between the two uses with the deductions limited to the income from each use. **Rivera v. Comm'r, T.C. Summary Op. 2004-81**.

CONSERVATION EASEMENTS. The IRS has issued a warning that the IRS may disallow charitable contribution deductions for participation in two types of transactions: (1) transfers of easements on real property to charitable organizations, and (2) payments to charitable organizations in connection with a purchase of real property from the charitable organization. In the case of easement transfers, the IRS may disallow deductions for failure to comply with the I.R.C. § 170 substantiation requirements. The IRS announced that they are considering changes to forms to facilitate compliance with and enforcement of the requirements. If inappropriate charitable deductions are made for cash payments or easement transfers in connection with a taxpayer's purchase of real property, the IRS may treat the total of the buyer's payments to the charitable organization as the purchase price paid by the buyer for the property. In addition, the IRS may impose failure to file penalties under I.R.C. § 6652, excess benefit transaction penalties under I.R.C. § 4958, and penalties against promoters and appraisers under I.R.C. §§ 6700, 6701 and 6694. Further, the IRS may challenge the tax-exempt status of an organization, based on the organization's operation for a substantial nonexempt purpose or impermissible private benefit. **Notice 2004-41, I.R.B. 2004-27**.

DEPRECIATION. The IRS has adopted as final regulations which exclude from the definition of passenger automobile any truck or van that is a qualified nonpersonal use vehicle as defined in Treas. Reg. § 1.274-5T(k). Qualified nonpersonal use vehicles include not only the trucks and vans listed in Treas. Reg. § 1.274-5T(k)(2), but also trucks and vans described in Treas. Reg. § 1.274-5T(k)(7) (relating to trucks and vans that have been specially modified, such as by installation of permanent shelving and painting the vehicle to display advertising or the company's name, so that they are not likely to be used more than a de minimis amount for personal purposes). These specially manufactured or modified vehicles do not provide significant elements of personal benefit, and a taxpayer is unlikely to purchase these vehicles unless motivated by a valid business purpose that could not be met with a less-expensive vehicle. The IRS also noted that future revenue procedures providing the depreciation limits for passenger vehicles will provide higher limits for light trucks and vans because these vehicles have a higher price inflation rate. **69 Fed. Reg. 35513 (June 25, 2004)**.

DISCHARGE OF INDEBTEDNESS. The taxpayer was a general partner in a partnership which operated a continuing care facility. The partnership obtained loans which were personally guaranteed by the taxpayer. The partnership filed for Chapter 11 bankruptcy but filed a liquidation plan. The bankruptcy trustee negotiated a settlement with the partnership creditors under which the partners provided contributions to the bankruptcy estate to help pay creditors' claims and the creditors accepted less than full payment. The Bankruptcy Court granted the partnership and partners, including the taxpayer, a discharge for all partnership debts. The Bankruptcy Court claimed jurisdiction over the taxpayer as part of its discharge order. The partnership Form K-1 for the tax year of discharge allocated a portion of the discharged obligations to the taxpayer as discharge of indebtedness income. The taxpayer argued that the discharge of indebtedness income was not taxable, under I.R.C. § 108(d)(2), because the discharge occurred as part of a bankruptcy case. The Tax Court agreed and held that the discharge of indebtedness income was excluded from gross income. **Gracia v. Comm'r, T.C. Memo. 2004-147; Mirarchi v. Comm'r, T.C. Memo. 2004-148; Price v. Comm'r, T.C. Memo. 2004-149; Martinez v. Comm'r, T.C. Memo. 2004-150**.

DISASTER LOSSES. On June 18, 2004, the President determined that certain areas in Wisconsin were eligible for assistance under the Disaster Relief and Emergency Assistance Act (42 USC 5121) as a result of severe storms and flooding, which began on May 19, 2004. **FEMA-1526-DR**. On June 18, 2004, the President determined that certain areas in Kentucky were eligible for assistance under the Act as a result of tornadoes, flooding, severe storms and flooding, which began on May 26, 2004. **FEMA-1523-DR**. On June 11, 2004, the President determined that certain areas in Missouri were eligible for assistance from the government under the Act as a result of severe storms, tornadoes, and flooding that began on May 18, 2004. **FEMA-1524-DR.** On June 15, 2004, the President determined that certain areas in Virginia were eligible for assistance from the government under the Act as a result of severe storms, tornadoes, and flooding that began on May 24, 2004. **FEMA-1525-DR.** On June 8, 2004, the President determined that certain areas in Louisiana were eligible for assistance from the government under the Act as a result of severe storms and flooding that began on May 12, 2004. **FEMA-1521-DR.** Accordingly, taxpayers in the affected areas who sustained losses may deduct them on their 2003 federal income tax returns.

HEALTH SAVINGS ACCOUNT. The IRS has provided relief for taxpayers in states which require health insurance plans without a deductible or with a deductible amount less than that required for a "high deductible health plan" as required for the federal HSAs. The IRS stated that low deductible plans will be treated as qualifying under I.R.C. § 223(c)(2) if the only reason the plans are not HDHPs is because of state-mandated benefits. **Notice 2004-43, I.R.B. 2004-27**.

IRA. The decedent died owning an interest in an IRA which had the surviving spouse taxpayer as the beneficiary. After the death of the decedent, the company maintaining the IRA transferred the funds to a money market account in the name of the taxpayer. The taxpayer was unable to get immediate tax advice as to the IRA but when the taxpayer received advice, the advice was incorrect that the 60 day rollover period had expired. By the time the taxpayer received correct advice, the 60-day period had expired and the taxpayer sought a waiver of the 60-day period in order to rollover the funds to an IRA without tax. The IRS granted the waiver. **Ltr. Rul. 200425049, March 22, 2004**.

RETURNS. The IRS has released on its website, at www.irs.gov/charities/index.html, previews of two new publications: IRS Publication 4302, A Charity's Guide to Car Donations, and IRS Publication 4304, A Donor's Guide to Car Donations.

S CORPORATIONS

BUILT-IN GAIN. Under the current rules, (Treas. Reg. §§ 1.337(d)-4 through 1.337(d)-7, 1.1374-1 through 1.1374-10) if an owner C corporation, elects to be an S corporation when it owns all of the stock of another C corporation, the net unrealized built-in gain (NUBIG) will reflect the built-in gain or built-in loss in the other C corporation's stock. That built-in gain or built-in loss may be duplicative of the built-in gain or built-in loss in the other C corporation's assets. If the other C corporation later transfers its assets to the owning C corporation in a liquidation to which I.R.C. §§ 332 and 337(a) apply, the built-in gain and built-in loss in the other C corporation's assets may be reflected twice: once in the NUBIG attributable to the assets the S corporation owned on the date of its conversion (including the stock of the other C corporation) and a second time in the NUBIG attributable to other C corporation's former assets acquired by the S corporation in the liquidation of the other C corporation. A similar result would obtain if, on the date of its conversion to an S corporation, the owner C corporation owned less than 80 percent of the stock of the other C corporation and later acquired the assets of the other C corporation in a reorganization to which I.R.C. § 368(a) applies. The IRS has issued proposed regulations which adjust (increase or decrease) the NUBIG of the pool of assets that included the stock of the liquidated or acquired C corporation to reflect the extent to which the built-in gain or built-in loss inherent in the redeemed or canceled C corporation stock at the time the pool of assets became subject to the tax under I.R.C. § 1374 has been eliminated from the corporate tax system in the liquidation or reorganization. The proposed regulations provide that, if I.R.C. § 1374(d)(8) applies to an S corporation's acquisition of assets, some or all of the stock of the corporation from which such assets were acquired was taken into account in the computation of NUBIG for a pool of assets of the S corporation, and some or all of such stock is redeemed or canceled in such transaction, subject to certain limitations, the NUBIG of the pool of assets that included the C corporation stock redeemed or canceled in the transaction (other than stock with respect to which a loss under I.R.C. § 165 is claimed) is adjusted to eliminate any effect any built-in gain or built-in loss in the redeemed or canceled C corporation stock had on the initial computation of NUBIG for that pool of assets. For this purpose, stock that has an adjusted basis that is determined (in whole or in part) by reference to the adjusted basis of any other asset held by the S corporation as of the first day of the recognition period (i.e., stock described in I.R.C. § 1374(d)(6)) is treated as taken into account in the computation of the NUBIG for the pool of assets of the S corporation. Adjustments to NUBIG under the proposed regulations, however, are subject to two limitations. First, the NUBIG is only adjusted to reflect the amount of the built-in gain or built-in loss that was inherent in the redeemed or canceled stock at the time the pool of assets became subject to tax under I.R.C. § 1374 that has not resulted in recognized built-in gain or recognized built-in loss at any time during the recognition period, including on the date of the acquisition to which I.R.C. § 1374(d)(8) applies. Second, an adjustment cannot be made if it is duplicative of another adjustment to the NUBIG for a pool of assets. This rule is intended to prevent more than one adjustment to the NUBIG of a pool of assets for the same built-in gain or built-in loss stock. Any adjustment to NUBIG under these proposed rules will only affect computations of the amount subject to tax under I.R.C. § 1374 for taxable years that end on or after the date of the liquidation or reorganization. It will not affect computations of the amount subject to tax under I.R.C. § 1374 for taxable years that end before the date of the liquidation or reorganization. **69 Fed. Reg. 35544 (June 25, 2004)**.

TAX SCHEMES. The IRS has issued a warning that some tax schemes involving the U.S. Virgin Islands are tax avoidance schemes and the claimed tax effects will be ignored. The tax schemes purport to allow U.S. residents to take advantage of a reduction for USVI income tax rates which were allowed as an incentive for investments in USVI corporations. The tax schemes represent that (1) a person can continue to live and work in the United States and, nevertheless, be a bona fide resident of the USVI; (2) USVI source income includes income from services performed in the United States; (3) for purposes of determining the source of income, USVI includes the U.S.; and (4) non-USVI source income can be legitimately connected with the conduct of a trade or business within the USVI even if equivalent income would not be considered effectively connected with the conduct of a trade or business within the U.S. **Notice 2004-45, I.R.B. 2004-27**.

NEGLIGENCE

IRRIGATION SYSTEM. **Submitted by Roger A. McEowen**. The plaintiff expanded its farming operation to include leased land on which the defendant operated a gas well. The plaintiff notified the defendant that a compressor shed located near the well was in the path of a circle pivot irrigation system. The defendant remedied the problem by constructing a cement bag ramp to allow the irrigation system to clear the oil and gas structures. Shortly thereafter, the irrigation system collapsed, rendering it non-functional and leaving the plaintiff's corn crop without water for a week. The plaintiff sued the defendant for negligent design, construction and placement of the ramp. The trial court found the defendant 100 percent at fault, awarding damages at $75,717. On appeal, however, the appellate court ordered a new trial on the basis that the trial court improperly excluded evidence of the defendant's experience with similar irrigation ramps and disallowed expert witness testimony. The court specifically noted that the mechanical operation of farm equipment is not an area of general knowledge for juries. **Norton Farms, Inc. v. Anadarko Petroleum Corporation, No. 90,820, 2004 Kan. App. LEXIS 610 (Kan. Ct. App. Jun. 25, 2004)**.

NUISANCE

HOG CONFINEMENT FACILITY. The defendants owned and operated ten hog confinement facilities at different locations. The facilities were all constructed and began operation more than one year before the suit was filed by 68 plaintiffs who were neighbors of one or more facilities. The plaintiffs filed suit in nuisance for injunctive relief and compensatory and punitive damages. The defendant sought a summary judgment and argued that Miss. Code § 95-3-29 prohibited the suit because it was not brought within one year of the beginning operation of the facilities and the facilities had not been substantially changed since their inception. The plaintiffs argued that seven of the facilities had, within one year before the suit, constructed animal carcass incinerators on the facilities which substantially changed the operations. The plaintiffs also argued that the facilities violated the Mississippi Air and Water Pollution Control Law (MAWPCL) which was not subject to the one year limitation. The court held that, if the construction of the incinerators was a substantial change in the operation of the hog facilities (the court did not rule on this issue), the suit would be allowed only as to the incinerators and not as to the entire facilities. The court also held that an issue of fact remained as to whether the MAWPCL provided a private right of action to enforce its provisions and whether the facilities violated any provision. Because the defendant had not shown that the defendant was entitled to summary judgment on all issues, the court denied the motion. ***In re* Moore, 306 B.R. 849 (Bankr. N.D. Miss. 2004)**.

PROPERTY

RAILROAD RIGHT-OF-WAY. **Submitted by Roger A. McEowen**. A railroad was conveyed a fee simple interest in a tract of land in the late 1800s. The railroad eventually abandoned the rail line and later transferred by quitclaim deed the land to the defendant school district. The school district hired a third party to remove fill dirt from the tract to backfill a hole on other school property, and the plaintiffs, as adjacent landowners, sued for trespass. The plaintiffs claimed that they owned the tract at issue because the railroad only held an easement which reverted to them upon abandonment of the rail line. The trial court agreed, based on a 1905 Kansas Supreme Court case holding that a railroad cannot obtain a fee simple interest in land to be used for right-of-way purposes. On appeal, the court reversed. The appellate court noted that Kan. Stat. Ann. § 66-501 allows railroads to acquire land in fee simple absolute and that prior Kansas caselaw has held that fee title is conveyed where the deed does not contain use limitations, irrespective of the size of the tract. The court distinguished the 1905 case on the basis that the court, in that case, was dealing with an ambiguous deed (concerning the interest conveyed) that was eventually construed through the use of extrinsic evidence to convey a right-of-way. In the present case, however, the court noted that the deed was not subject to any use restrictions or a reversion clause. As such, the railroad held a fee interest that it had been conveyed to the school district. **Stone v. U.S.D. No. 222, No. 90,317, 2004 Kan. LEXIS 409 (Kan. Sup. Ct. Jun. 25, 2004)**.

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STATE TAXATION

AGRICULTURAL USE. The plaintiff had petitioned the Minnesota Tax Court for review of a county appraisal of the plaintiff's rural land. The plaintiff argued that the land was eligible for taxation as "green acre" valuation at use value. The plaintiff refused the county's settlement offer and the Tax Court ruled in the plaintiff's favor. The plaintiff filed a motion for court costs and disbursements more than 90 days after the Tax Court's final order. The Tax court denied the plaintiff's motion for court costs because the motion was not filed within 90 days after the final order. The appellate court affirmed the Tax Court and held that the Minnesota Rules of Civil Procedure, which allowed a longer time for post-order motions, did not apply to the Tax Court because the Tax Court had its own rule for filings of motions. **Raisanen v. County of Hennepin, 678 N.W.2d 669 (Minn. 2004),** ***aff'g*****, 2003 Minn. Tax LEXIS 12 (Minn. T.C., Apr. 11, 2003)**.

CITATION UPDATES

In re **Barranco, 307 B.R. 539 (Bankr. W.D. Va. 2004)** (bankruptcy discharge of taxes) see p. 99 *supra*.

Keller v. Bolding, 678 N.W.2d 578 (N.D. 2004) (lease termination) see p. 70 *supra*.

T.R. Incorp. of Ashland, Kansas v. Brandon, 87 P.3d 331 (Kan. Ct. App. 2004) (lease term) see p. 63 *supra*.

IN THE NEWS

PATENTS-SAVED SEED. On Jun. 25, 2004, Rep. Marcy Kaptur (D-OH) introduced into the U.S. House the Seed Availability and Competition Act of 2004. The bill would decriminalize the act of saving patented seed as long as a producer reports the quantity and type of seed retained and pays a techical fee to the USDA. The USDA will then compensate the patent holders. **H.R. 4693**.

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