Cases, Regulations and Statutes

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**CASES, REGULATIONS AND STATUTES**

by Robert P. Achenbach, Jr

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**ANIMALS**

**HORSES.** The plaintiff was injured while participating in a trail ride as part of a horse camp run by the defendant. The plaintiff was riding a horse that the plaintiff’s father and the defendant knew had a tendency to go faster than the other horses. The plaintiff testified that the plaintiff had made repeated requests to ride a different horse or to have someone control the horse but the defendant refused the requests. The horse then sped up and the plaintiff was forced to jump off the horse at high speed, causing injuries. The plaintiff’s parent signed a release of liability which stated “I understand and am fully aware that riding and being around horses involves inherently dangerous risks of serious injury or death, and by participating I expressly assume all risks associated with my activities on the property . . . . I further agree to release and hold harmless [the defendant] from any liability, responsibility or negligence for any claims, damages, or injuries caused by myself or my horse(s).” The defendant raised the defense of primary assumption of risk because the plaintiff voluntarily engaged in an activity with known risks. The plaintiff argued that primary assumption of risk did not apply because the plaintiff made repeated requests to change horses and the defendant knew the horse had a tendency to spook. The appellate court held that the trial court should not have granted summary judgment on the issue of primary assumption of risk because material issues of fact remained as to whether the defendant expanded the risk by taking the plaintiff on a trail ride and not granting the requests to change horses. The trial court also determined that the release agreement signed by the plaintiff released the defendant from ordinary negligence but not greater-than-ordinary or gross negligence. The trial court had granted summary judgment on this issue because the material issues of fact which existed did not affect the issue of assumption of risk. The appellate court disagreed, holding that sufficient issues of fact remained as to whether the level of risk exceeded the normal risks of horseback riding: therefore, the court held that summary judgment should have been denied on the claim of negligence.  *Salinger v. Leatherdale*, 2012 Minn App. Unpub. LEXIS 958 (Minn. Ct. App. 2012).

The plaintiff and defendant were friends and the defendant had invited the plaintiff to the defendant’s farm to ride horses together. The defendant took time to assess the plaintiff’s ability and selected a calm horse for the plaintiff to ride. However, at the end of the ride, the defendant suggested that the plaintiff go for a solo ride with a more energetic horse. During that solo ride, the horse spooked and threw the plaintiff, causing injuries. The plaintiff sued in negligence and the defendant claimed the New Jersey Equine Act, N.J Stat. § 5:15-5 barred the action because the plaintiff assumed the risks of horseback riding. The trial court granted summary judgment for the defendant but the appellate court reversed. The appellate court held that sufficient issues of fact remained as to whether the defendant failed to properly assess the plaintiff’s riding ability and match it to the known propensities of the horse. The court noted that although the mismatch in this case was not extreme, a trier of fact could determine that the mismatch was sufficient to make one of the exceptions to the Equine Act apply to make the defendant liable even with the plaintiff’s assumption of risk.  *Stroman v. Bell*, 2012 N.J. Super. Unpub. 2144 (Superior Ct. N.J. 2012).

**BANKRUPTCY**

**GENERAL**

**EXEMPTIONS**

**ANNUITY.** The debtor had purchased an annuity with funds from a § 401(k) account and claimed the annuity as exempt under Section 522(d)(10)(E). The trustee objected to the exemption of the annuity because it was not a retirement annuity. The annuity date was set as the time the debtor became 69 years of age. An amendment to the contract provides: “The annuity date may not be changed to a date that is later than April 1st of the calendar year next following the end of the calendar year in which the annuitant would attain age 70 1/2.” The contract had a death benefit as well as the annuity feature. The amount of the annuity payments depended on the investment returns achieved by the investments selected by the debtor. Also, the debtor had the right to withdraw part or all of the amount in her investment account prior to the annuity date. During the first seven years of the contract the debtor would incur a sales charge for a withdrawal. The court held that the annuity was entitled to the exemption for retirement plans because (1) the payments began when the debtor reached age 70 1/2, (2) the taxes on the plan were deferred, and (3) early withdrawals were subject to penalty. In addition, the plan payments were intended to substitute for wages and the plan payments were reasonably necessary for the debtor’s support.  *In re Kiceniuk*, 2012-2 U.S. Tax Cas. (CCH) ¶ 50,605 (Bankr. D. N.J. 2012).

**PENSION PLANS.** The debtor claimed a profit-sharing plan and two IRAs as exempt retirement funds under Section 522(b)(4) (A) of the Bankruptcy Code. The court held that the profit-sharing plan was not eligible for the exemption because the debtor failed to get a favorable determination letter from the IRS for the plan. Because the IRAs received rollover funding from the plan, the IRA funds were also not qualified for the exemption. In addition, the court found that the plan was disqualified because the debtor had control of the fund and engaged in prohibited transactions.  *In re Daniels*, 2012-2 U.S. Tax Ca. (CCH) ¶ 50,607 (D. Mass. 2012), aff’d, 2011-2 U.S. Tax Cas. (CCH) ¶ 50,477 (Bankr. D. Mass. 2011).
FEDERAL FARM PROGRAMS

NO ITEMS.

FEDERAL ESTATE AND GIFT TAXATION

FAMILY-OWNED BUSINESS DEDUCTION. In a Chief counsel advice e-mail, the IRS stated “The applicable limitations period for the ‘additional estate tax’ under section 2057(f)(2) cannot be extended by agreement. Pursuant to section 2057(i)(3)(k), the additional three year period for assessment provided for in section 2032A(f) applies to the additional estate tax under section 2057(f)(2). There is nothing in section 2032A(f) that states that this period can be extended by agreement. Moreover, the period in section 2032A(f) is a minimum period of limitations, but it is not mutually exclusive from the general limitations period in section 6501. The language of section 6501(c)(4) explicitly exempts ‘estate tax provided in chapter 11’ from those taxes for which the limitations period may be extended by agreement. Although section 2057(f)(2) is an ‘additional’ estate tax, it is still a chapter 11 estate tax provision subject to this restriction.” CCA 201240023, Aug. 21, 2012.

FEDERAL INCOME TAXATION

BAD DEBTS. The taxpayer was employed by a company and performed work for several related companies. The employer entered into a business arrangement with a computer company which provided some financing for the computer company in exchange for computer services. The taxpayer also worked with the computer company as part of the arrangement. When the computer company had financial difficulties, the taxpayer purchased an automobile and sold it to the computer company owner in exchange for a promissory note. The taxpayer also allowed the computer company to make charges against the taxpayer’s credit card. The employer withheld employment taxes from the settlement payment because (1) the settlement agreement is silent as to the nature of the payments but includes a warning that the payments would be subject to employment taxes, and (2) the employer characterized the settlement payment as “Wages, tips, other comp.” on the Form W-2 that it issued to the taxpayer. Gerstenbluth v. Credit Suisse (USA) LLC, 2012-2 U.S. Tax Cas. (CCH) ¶ 50,612 (E.D. N.Y. 2012).

CHARITABLE DEDUCTIONS. The taxpayer owned and operated two golf courses on 277 acres. The taxpayer granted a conservation easement on the property “for the conservation of the open space, scenic natural resources, natural habitat and aesthetic qualities of the Property and to limit the future use thereof to such purposes.” In addition, the conservation easement agreement provided that the easement was intended to “further the policies of the State of Missouri designed to foster the preservation of open space or open areas, conservation of the state’s forest, soil, water, plant and wildlife habitats, and other natural and scenic resources” and “to implement the objectives set forth in 67.870 to 67.910 R.S.M.O.” The IRS denied a charitable deduction for the easement transfer because the easement agreement failed to specifically state that the taxpayer had not received any goods or services in exchange for the easement. The court held that, because the agreement stated that it stated the entire agreement between the parties, the agreement substantially complied with the goods and services requirement. The IRS also argued that the conservation easement did not: (1) protect a relatively natural habitat of fish, wildlife, or plants, or similar ecosystem under I.R.C. § 170(h)(4)(A)(ii), or (2) preserve open space pursuant to a clearly delineated federal, state, or local governmental conservation policy under I.R.C. § 170(h)(4)(A)(iii)(II). The court noted that R.S.M.O. § 67.870 limits the Missouri conservation policy to counties with more than 200,000 residents; therefore, the taxpayer’s easement did not further a state conservation policy under I.R.C. § 170(h)(4)(A)(iii)(II). However, the court held that issues of material facts remained regarding the easement preservation of a natural habitat within the meaning of I.R.C. § 170(h)(4)(A)(ii). RP Golf, LLC v. Comm’r, T.C. Memo. 2012-282.

COURT AWARDS AND SETTLEMENTS. The taxpayer had received settlement payments from a former employer in an age discrimination suit the taxpayer filed against the employer. The employer withheld employment taxes from the settlement payments and the taxpayer filed suit against the employer and IRS for recovery of those taxes. The court held that employment taxes were properly withheld from the settlement payment because (1) the settlement agreement is silent as to the nature of the payments but includes a warning that the payments would be subject to employment taxes, and (2) the employer characterized the settlement payment as “Wages, tips, other comp.” on the Form W-2 that it issued to the taxpayer. Gerstenbluth v. Credit Suisse (USA) LLC, 2012-2 U.S. Tax Cas. (CCH) ¶ 50,612 (E.D. N.Y. 2012).

DEPRECIATION. The taxpayer was a limited partnership which owned residential properties. The partnership agreement provided that the partnership would use the alternate depreciation system (ADS) for all tangible depreciable property unless otherwise approved by one of the limited partners. No approval was given in three tax years; however, although the ADS was used in the first tax year, the general partner did not elect to use ADS and the general depreciation system (GDS) was used in the second and third years. The IRS granted the taxpayer an extension time to file amended returns to make the election to use ADS in the second and third years. Ltr. Rul. 201240002, June 21, 2012.
DISASTER LOSSES. On September 21, 2012, the President determined that certain areas in Georgia are eligible for assistance from the government under the Disaster Relief and Emergency Assistance Act (42 U.S.C. § 5121) as a result of Hurricane Isaac which began on August 26, 2012. FEMA-4082-DR. On September 25, 2012, the President determined that certain areas in Washington are eligible for assistance from the government under the Act as a result of a severe storm and flooding which began on July 20, 2012. FEMA-4083-DR. On September 21, 2012, the President determined that certain areas in Alabama are eligible for assistance from the government under the Act as a result of Hurricane Isaac which began on August 26, 2012. FEMA-4084-DR. Accordingly, taxpayers in the areas may deduct the losses on their 2011 federal income tax returns. See I.R.C. § 165(i).

EMPLOYEES. The taxpayer provided temporary contracted legal services for two employment companies. The court held that the taxpayer was an employee of the agencies and was subject to employment tax withholding because (1) the companies controlled the work done by the taxpayer, (2) the taxpayer had no risk of loss from the income received, (3) the companies supplied all equipment and facilities for the work, (4) the companies retained the right to fire the taxpayer at will, and (5) the companies considered the taxpayer an employee. Rodriguez v. Comm’r, T.C. Memo. 2012-286.

IRA. The taxpayers, husband and wife, each owned a traditional IRA and converted the IRAs into Roth IRAs. The taxpayers, however, were not eligible to convert their IRAs to Roth IRAs because the taxpayers’ adjusted gross income exceeded $100,000 for that tax year. The taxpayers did not learn that they exceeded the AGI limit and that they could undo the conversion until after they had filed their income tax return for that tax year. In addition, the taxpayers transferred the funds from the Roth IRAs to non-IRA investment accounts. The taxpayers sought an extension of time to recharacterize the Roth IRAs as traditional IRAs. The IRS refused to grant the extensions because the funds were no longer in Roth IRAs but were held in non-IRA investment accounts. Ltr. Rul. 201239015, July 3, 2012.

INNOCENT SPOUSE RELIEF. The taxpayer and former spouse had financial difficulties and failed to pay taxes in several years. The taxpayer testified that the former spouse was in charge of the family finances. The taxpayer and former spouse sold their house and placed the proceeds in a joint checking account. Although the money was intended to pay debts, including the taxes, the former spouse used most of the funds for personal and family expenses and withdrew the remainder before moving to Mexico. The taxpayer sought innocent spouse relief from the unpaid taxes. The main issue was whether and to what extent the funds taken by the former spouse were a misappropriation of funds intended for payment of taxes. The court determined that the divorce decree made both parties equally liable for the taxes; therefore, at least one-half of the withdrawn funds were misappropriated by the former spouse. In addition, the taxes owed were about 38 percent of the debts owed at the time of the withdrawal. The court held that 38 percent of one-half of the funds withdrawn were misappropriated. The court held that the taxpayer was entitled to innocent spouse relief because (1) the taxpayer was divorced, (2) the taxpayer had no reason to know that the former spouse would not pay the taxes, and (3) the taxpayer did not receive substantial support from the unpaid taxes. The other factors were mostly neutral. Gallego v. Comm’r, T.C. Summary Op. 2012-97.

The taxpayer filed a joint income tax return with a former spouse while the couple was married. Although the return showed a refund was due, the IRS later assessed a deficiency based on unreported income earned by the former spouse. The taxpayer had prepared and filed the original return. The former spouse intervened in the taxpayer request for innocent spouse relief, arguing that the taxpayer was not entitled to innocent spouse relief because (1) the taxpayer prepared and filed the original return and should have known about the unreported income and (2) the original return was filed with the former spouse’s knowledge or permission. The court weighed the testimony of both parties and found the taxpayer’s explanations more credible that the former spouse hid the unreported income and that the former spouse had knowledge of and approved the original return in that the former spouse had filed an amended return with the taxpayer. Harrington v. Comm’r, T.C. Memo. 2012-285.

The taxpayer and former spouse filed joint returns while married but most of the returns were filed late and the couple never fully paid the tax due. After the couple divorced, the taxpayer filed for innocent spouse relief. The IRS conceded that the taxpayer met the threshold requirements of I.R.C. § 6015(f). The court held that the taxpayer did not meet the safe harbor requirements of Rev. Proc. 2003-61, 2003-2 C.B. 297, because the taxpayer failed to show that the taxpayer would suffer economic hardship from having to pay the owed taxes. The court then looked at the factors for equitable relief. The court held that the taxpayer was not eligible for equitable relief because (1) the taxpayer exercised control over the couple’s finances, (2) the taxpayer had knowledge of the couple’s financial difficulties and that the former spouse would not pay the taxes, and (3) the taxpayer would not suffer economic hardship from paying the taxes. Henson v. Comm’r, T.C. Memo. 2012-288.

IN Voluntary CONversions. The taxpayer’s residence was destroyed in a Presidentially-declared disaster. The taxpayer received insurance proceeds in an amount greater than the taxpayer’s basis in the old residence. The taxpayer purchased another residence and used that residence as the taxpayer’s principal residence, including making improvements. The taxpayer did not notify the IRS that the new residence was to be replacement property for the old residence. The IRS ruled that the taxpayer was deemed to elect to defer gain from the involuntary conversion of the old residence under I.R.C. § 1033, because the taxpayer did not recognize the gain from the insurance proceeds and used the new residence as a principal residence. The IRS ruled that the taxpayer could file an amended
return to designate the new residence as replacement property. 

**NET OPERATING LOSSES.** The taxpayers, husband and wife, had filed income tax returns in 2000 and 2001 as married filing separately. In 2004 the taxpayers suffered investment losses in excess of income and sought to carry back the losses to 2000, 2001, 2002 and 2003 and to obtain a refund of taxes in those years. The court held that the losses could not be carried back because the losses were not eligible losses arising from fire, storm, shipwreck, or other casualty, or from theft but were investment losses. The court also denied the taxpayers’ claim for a refund because the taxpayers failed to provide any allocation of the losses between the taxpayers for the years in which they filed separately. 


**PENSION PLANS.** For plans beginning in October 2012 for purposes of determining the full funding limitation under I.R.C. § 412(c)(7), the 30-year Treasury securities annual interest rate for this period is 3.69 percent, the corporate bond weighted average is 5.20 percent, and the 90 percent to 100 percent permissible range is 4.68 percent to 5.20 percent. Notice 2012-64, I.R.B. 2012-44.

**REGISTERED TAX RETURN PREPARERS.** A petition for review has been filed for the following case with the U.S. Supreme Court. The plaintiff was an attorney and CPA who obtained a preparer tax identification number (PTIN) under the new regulations for registered tax return preparers and paid the $64.25 fee. The plaintiff filed for a refund of the fee, arguing that the fee was improperly assessed because the IRS had no authority to assess the fee inasmuch as the PTIN used to be assigned without a fee. The appellate court upheld the fee because the new regulations required the PTIN in order for the plaintiff and other tax return preparers to prepare income tax returns for a fee, thus conferring a benefit on the plaintiff. 

Bramen v. United States, 2012-1 U.S. Tax Cas. (CCH) ¶ 50,390 (11th Cir. 2012). 

The IRS has announced a live web cast about the registered tax return preparer test. To sign up, go to [http://www.visualwebcaster.com/IRS/89770/reg.asp?id=89770](http://www.visualwebcaster.com/IRS/89770/reg.asp?id=89770)

**SAME SEX COUPLES.** The IRS has posted answers to frequently asked tax questions about same-sex couples, as well as tax questions and answers for registered domestic partners and same-sex spouses in community property states. 2012 FED (CCH) ¶ 46,491; 2012 FED (CCH) ¶ 46,492.

**THEFT LOSSES.** The taxpayer made several investments with a financial services company. The company later filed for Chapter 7 and the taxpayer recovered only a small portion of the investments. The taxpayer claimed a theft loss for the amount of unrecovered investments. Although the court agreed that, under Ohio law, theft includes the depriving of another of property, the taxpayer failed to prove that the investment company intended to steal the taxpayer’s investments. The court noted that the company made several interest payments and that the investments were freely made by the taxpayer. Therefore, no theft occurred under state law and no theft deduction was allowed. Labus v. United States, 2012-2 U.S. Tax Cas. (CCH) ¶ 50,597 (N.D. Ohio 2012).

The taxpayer made investments in a company which was in the business of buying and selling real estate. The taxpayer received regular monthly payments from 1998 through December of 2004 when the payments stopped for a few months, restarted sporadically, and finally stopped when the company filed for bankruptcy in 2006. The taxpayer claimed a theft loss of the remaining investment in 2004 which was denied by the IRS. The court looked solely at the condition of the investments in December 2004 and found that the taxpayer failed to show that the taxpayer had no reasonable expectation of recovery in 2004 since the payments had been current through November 2004 and no other event occurred with the company to indicate that the investment would be lost. McGee v. United States, 2012-2 U.S. Tax Cas. (CCH) ¶ 50,613 (S.D. Ohio 2012).

**VEHICLE EXPENSES.** The taxpayer was employed full time as an engineer and purchased a van for traveling to work from home. The taxpayer claimed that the van was necessary to transport tools used on the job; however, the employer provided all the tools needed at the workplace and did not provide any compensation for the use of the van or for the taxpayer’s tools. In addition, the taxpayer did not keep any records of the costs of the van, the amount of personal and business use of the van and the dates, places and business purpose of the use of the van. The court held that the taxpayer could not claim depreciation deductions for the cost of the van because of the lack of substantiation records. 

ZONING

FARM STAND. The defendants purchased a 1.8 acre farm which had an existing agricultural labor residence and a portable farm stand. Both items violated current zoning restrictions but were allowed as pre-existing property. The defendant petitioned the local zoning board for permission to remove the existing agricultural labor residence and build a new one. The request was approved with conditions that only two agricultural laborers were allowed to reside in the residence and that the defendant prove annually that they were farming at least five acres of crops. The defendants also sought a permit to replace the portable farm stand with a permanent building. That permit was also allowed with restrictions that the food served be raised or produced on the farm. The zoning board sought an injunction against the use of the buildings by the defendants because (1) the agricultural labor residence was not being used to house agricultural laborers, (2) the defendants failed to show that they annually farmed at least five acres of crops, and (3) the farm stand was operating as a Mexican restaurant and did not serve at least 50 percent of its food from food produced on the farm. The court held that material issues of fact remained as to the defendants' compliance with the zoning restrictions on the agricultural labor residence. However, the court upheld summary judgment for the zoning board on the farm stand, where it was clear that the restaurant did not serve food produced by the farm. Town of Riverhead v. Taste of Country, Inc., 2012 N.Y. Misc. LEXIS 4596 (Sup. Ct. N.Y. 2012).

PRODUCTS LIABILITY

HERBICIDES. The plaintiff owned a vineyard next to the defendant’s farm. The defendants were the owners of the land and the tenant who raised grass sod on the farm. The tenant sprayed the sod with a herbicide, 2, 4-D, and the plaintiff alleged that the spray drifted on to 30 rows of grape vines, destroying the plants. The plaintiff filed actions in negligence, trespass and nuisance. The defendant land owner sought summary judgment on the basis that the defendant had no control over the use of the land or application of herbicides. The court granted the summary judgment, holding that the land owner did not owe a duty to the plaintiff for a condition for which the defendant had no knowledge and had no obligation under the lease to repair dangerous conditions. The court denied summary judgment against the defendant tenant because significant material issues of fact remained as to the manner in which the herbicide was sprayed, whether the spraying violated any agreements, and whether the spray caused the destruction of the vines. Pindar Vineyards, LLC v. Vitti, 2012 N.Y. Misc. LEXIS 4711 (Sup. Ct. N.Y. 2012).

WORKERS’ COMPENSATION

NEGLIGENCE. The plaintiff was an employee of the defendant and performed general farm duties on the defendant’s farm. The plaintiff suffered symptoms of a heart attack while plowing fields on the defendant’s farm but continued to work and did not report the symptoms to the defendant. The plaintiff only asked to leave work because the plaintiff was feeling ill. The defendant did not carry workers’ compensation insurance. The plaintiff filed suit in negligence for failure to provide adequate medical attention and for workers’ compensation coverage. The trial court dismissed the claim for workers’ compensation for lack of jurisdiction. The appellate court agreed, holding that, although the court had jurisdiction over the issue of whether the plaintiff was an employee coverable by workers’ compensation, jurisdiction over the extent of coverage was exclusive with the workers’ compensation bureau. The trial court grant summary judgment for the defendant on the issue of negligence, ruling that the defendant owed no duty to provide medical assistance for a heart attack. The appellate court agreed, holding that, although the parties had an employer-employee relationship, the defendant could not foresee the plaintiff’s medical needs since the existence of the heart attack was not immediately apparent. Based on what the plaintiff told the defendant at the time, the defendant could not have known that the plaintiff was suffering a heart attack and needed special medical attention. Lapka v. R & R Farms, Inc., 2012 Mich. App. LEXIS 1942 (Mich. Ct. App. 2012).

IN THE NEWS

TAX RETURNS. The Internal Revenue Service urged taxpayers whose tax-filing extension runs out on Oct. 15 to double check their returns for often-overlooked tax benefits and then file their returns electronically using IRS e-file or the Free File system. IR-2012-73.

The IRS announced that the 2013 IRS Tax Calendar for Small Business and Self Employed, Publication 1518, (English and Spanish) will ship in December. Call (800) 829-3676 or order online: http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Small-Business-Products-Online-Ordering.
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by Neil E. Harl

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