Cases, Regulations and Statutes

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Agricultural Law Digest

ENDNOTES
7 I.R.C. § 1(a).
8 I.R.C. § 1(b).
9 I.R.C. § 1(c).
10 Act, § 101(b). Note that the rate structure in the Act is not the same as the Clinton-era rates of 15, 28, 31, 36 and 39.6 percent rates.
11 I.R.C. § 1(f).
12 I.R.C. §§ 1(h)(5)(A), (6).
13 Act, § 104, amending I.R.C. §§ 26(c), 55(b)(1).
14 See note 4 supra.
21 Act § 315(a).
23 Act § 315(c), amending I.R.C. § 179(c)(2).
26 Act § 405(a), amending I.R.C. § 40A(g).
28 Act § 408, amending I.R.C. § 45L(g).
29 Act § 401(a), amending I.R.C. § 25C(g)(2).
30 Act § 409, amending I.R.C. § 45M(b).
32 Act § 103(a), amending I.R.C. § 25A(i).
33 Act § 103(b), amending I.R.C. 24(d)(4).
34 Act § 103(c), amending I.R.C. § 32(b)(3).
35 Act § 326(a), amending I.R.C. § 1374(d)(7).
40 Act § 207, amending I.R.C. § 222(e).
44 Act § 201, amending I.R.C. § 108(a)(1)(E)

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

BANKRUPTCY

FEDERAL TAX

DISCHARGE. The debtors filed for Chapter 7 in February 2012. The bankruptcy case included taxes for 2007. After the 2007 taxes were assessed in 2009, the debtors filed a Form 12153, Request for A Collection Due Process Hearing. The due process hearing was concluded in March 2010. The debtors sought to have the 2007 taxes declared discharged in the Chapter 7 case but the IRS argued that the three-year period in Section 507(a)(8) was tolled during the due process hearing and the taxes were not dischargeable. The court looked at the restraints on the IRS collection efforts during a due process hearing and held that the three-year period of Section 507(a)(8) was tolled during the hearing, making the 2007 taxes nondischargeable. In re Lastra, 2013-1 U.S. Tax Cas. (CCH) ¶ 50,116 (Bankr. D. N.M. 2012).

REFUNDS. The debtors (the case involves three separate bankruptcy debtors) filed for chapter 13 prior to 2011 and received a discharge in 2011. The debtors received a refund of 2011 taxes which the trustee sought to include in the estate under General Court Order 2010-01 which provided for distribution of refunds paid directly to trustees by the IRS. In 2011 the IRS stopped the policy of paying refunds to trustees and the trustee in these cases had to file a motion to obtain the debtors' tax returns and refunds. The court held that refunds arising after confirmation were estate property but that the trustee could not compel turnover from the debtors. In re Hymond, 2013-1 U.S. Tax Cas. (CCH) ¶ 50,115 (Bankr. N.D. Tex. 2012).

FEDERAL FARM PROGRAMS

ANIMAL WELFARE ACT. The APHIS has adopted as final regulations amending the Animal Welfare Act regulations to add

FARM BILL. The American Taxpayer Relief Act of 2012 includes a nine-month partial farm bill extension of the milk subsidy program through December 31, 2013. The Act also extends subsidies for commodities such as corn and soybeans. Other programs including conservation, organic growing, fruit and vegetable, and beginning farmer and rancher programs were also extended but at lower funded levels. Congress will now have until October 1 when the new fiscal year begins to pass a more typical five-year extension. Pub. L. No. 112-240, § 701, 126 Stat. 2313 (2012). Available online at http://www.govtrack.us/congress/bills/112/hr8/text

TRANSPORTATION. The APHIS has adopted as final regulations establishing minimum national official identification and documentation requirements for the traceability of livestock moving interstate. Under the final rule, unless specifically exempted, livestock belonging to species covered by this rulemaking that are moved interstate would have to be officially identified and accompanied by an interstate certificate of veterinary inspection or other documentation. The final regulations specify approved forms of official identification for each species but would allow the livestock covered under this rulemaking to be moved interstate with another form of identification, as agreed upon by animal health officials in the shipping and receiving states or tribes. 78 Fed. Reg. 2039 (Jan. 9, 2013).

FEDERAL ESTATE
AND GIFT TAXATION

GIFTS. The decedent created a limited liability company to which the decedent contributed 12 works of art. After an appraisal of the value of the LLC was obtained, the decedent gave interests in the LLC to several nieces equal in value to the unified credit at the time plus the annual exclusion amount. The purpose of the gifts was to reduce estate tax liability for the art works. The decedent initially planned to make annual gifts of additional LLC interests to the nieces in amounts equal to the annual exclusion amount. However, after the decedent remarried, the decedent sued the nieces in two state courts to have the gifts declared incomplete, but both courts held the gifts to be complete. The court held that the decedent’s estate was collaterally estopped from arguing that the gifts were not complete. Estate of Sommer v. Comm’r, T.C. Memo. 2013-8.

FEDERAL INCOME
TAXATION

AMORTIZATION. The taxpayer owned and operated an accounting practice until the taxpayer suffered a brain aneurysm, after which the taxpayer sold the business to another accountant. The taxpayer claimed the gain as income. Just over four months later, the buyer accountant suffered a stroke and sold the practice back to the taxpayer for the same amount. The taxpayer claimed amortization based on the purchase price of the business. The court upheld the amortization deductions because the initial sale and subsequent repurchase were not related transactions because they occurred as a result of unforeseen medical issues. Fitch v. Comm’r, T.C. Memo. 2012-358.

DISCHARGE OF INDEBTEDNESS. The IRS has withdrawn its ruling in the following letter ruling. The taxpayer was a publicly traded corporation engaged in the asset finance business whose financing products are offered through a nationwide network of dealers. A class action lawsuit was filed by consumers in one state against the taxpayer alleging violations of state law with respect to asset financing contracts entered into with the taxpayer. The lawsuit alleged several violations of state law, including that the taxpayer charged post-maturity interest and fees in excess of amounts due and that notices related to collections did not meet statutory notice requirements. The taxpayer and class plaintiffs settled the entire class action lawsuit. The settlement agreement provided that the taxpayer, with respect to all lawsuit class members, was to write off any deficiency balances remaining and to write off all charges (interest, fees, etc.). The IRS ruled that the taxpayer was not required to file Forms 1099-C, Cancellation of Debt, with respect to the write-off of balances and charges under the settlement agreement because there was no identifiable event as provided by Treas. Reg. § 1.6050P-1(b)(2) because the discharge occurred by operation of state law. On review, the IRS reversed its position and held that the discharges occurred not by operation of state law but rather as a result of an agreement by the parties to discharge the debt. Therefore, the transaction was an “identifiable event” under Treas. Reg. § 1.6050P-1(b)(2) and the reporting requirements applied. Ltr. Rul. 201301001, Oct. 1, 2012, revoking, Ltr. Rul. 200802012, Oct. 4, 2007.

The taxpayers, husband and wife, purchased furniture through a credit card promotion which deferred interest on the purchase so long as the principal was fully paid by a set time. The taxpayers failed to pay off the principal and the credit card company charged the back interest. A dispute arose and the taxpayers incurred more interest and penalties during the dispute. The dispute was settled after the credit card company removed the additional interest and penalties. The IRS assessed taxes on the forgiven interest and penalties as discharge of indebtedness income. The taxpayers argued that no taxable discharge of indebtedness income arose because the interest and penalties were removed as part of a contested liability or the settlement was a purchase price adjustment. The court held that the discharge of indebtedness was taxable income because the taxpayers did not contest the liability, which was clear under the credit card terms, but merely misunderstood the credit terms. The court also rejected the purchase price adjustment argument because the taxpayers did not negotiate with the seller of the merchandise but with the lender. Bross v. Comm’r, T.C. Summary Op.
2012-122.

EMPLOYEE BENEFITS. The IRS has issued proposed regulations that provide guidance under I.R.C. § 4980H with respect to an “applicable large employer’s” shared responsibility for employee health coverage. I.R.C. § 4980H is effective for months beginning after December 31, 2012. An applicable large employer is an employer that employed an average of at least 50 full-time employees on business days during the preceding calendar year. A full-time employee with respect to any month is an employee who is employed on average at least 30 hours of service per week. For purposes of determining whether an employer is an applicable large employer, full-time equivalent employees, which are statutorily determined based on the hours of service of employees who are not full-time employees, are taken into account. Under I.R.C. § 4980H(b), liability for the shared responsibility payment is contingent on whether the employer offers minimum essential coverage under an eligible employer-sponsored plan, and whether that coverage is affordable and provides minimum value, as determined by reference to the cost and characteristics of employee-only coverage offered to the employee. The proposed regulations generally incorporate the provisions of Notice 2012-58, 2012-2 C.B. 436, as well as many of the provisions of Notice 2011-36, 2011-1 C.B. 792; Notice 2011-73, 2011-2 C.B. 474; and Notice 2012-17, 2012-1 C.B. 430 with some modifications. 78 Fed. Reg. 217 (Jan. 2, 2013).

FIRST TIME HOMEBUYER CREDIT. Under a deceased parent’s will, the taxpayer received a half share in the parent’s home. The taxpayer’s sibling received the other half. The full title was transferred to the taxpayer in exchange for $215,000 paid to the executor and eventually to the other sibling. The taxpayer claimed the first time homebuyer credit for the purchase of the home. The court noted that I.R.C. § 36(c)(3)(A)(i) defines a “purchase” for purposes of the FTHBC as “any acquisition, but only if * * * the property is not acquired from a person related to the person acquiring such property.” Although a sibling is not a related person under I.R.C. § 36(c)(5), an executor or beneficiary of an estate is a related person; therefore, the court held that the taxpayer was not eligible for the first time homebuyer credit because the home was not a qualifying purchase from an unrelated party. Zampella v. Comm’r, T.C. Memo. 2012-359.

INFLATION-ADJUSTED ITEMS. The IRS has published a revenue procedure setting forth inflation adjusted items for 2013, including some items whose values for 2013 are specified in the American Taxpayer Relief Act of 2012, Pub. L. No. 112-240, 126 Stat. 2313: the beginning of the new 39.6 percent income brackets; the beginning income levels for the limitation on certain itemized deductions; and the beginning income levels for the phaseout of personal exemptions. (1) For taxable years beginning in 2013, under I.R.C. § 23(a)(3) the credit allowed for an adoption of a child with special needs is $12,970. For taxable years beginning in 2013, under I.R.C. § 23(b)(1) the maximum credit allowed for other adoptions is the amount of qualified adoption expenses up to $12,970. The available adoption credit begins to phase out under I.R.C. § 23(b)(2)(A) for taxpayers with modified adjusted gross income in excess of $194,580 and is completely phased out for taxpayers with modified adjusted gross income of $234,580 or more. (2) For taxable years beginning in 2013, the value used in I.R.C. § 24(d)(1)(B)(i) to determine the amount of credit under § 24 that may be refundable is $3,000. (3) For taxable years beginning in 2013, the exemption amounts under I.R.C. § 55(d)(1) (alternative minimum tax) are:

For taxable years beginning in 2013, under § 55(b)(1), the excess taxable income above which the 28 percent tax rate applies is:

- Married Individuals Filing Separate Returns: $89,750
- Joint Returns, Unmarried Individuals (other than surviving spouses), and Estates and Trusts: $179,500

For taxable years beginning in 2013, the amounts used under § 55(d)(3) to determine the phaseout of the exemption amounts are:

- Joint Returns or Surviving Spouses: $153,900
- Unmarried Individuals (other than Surviving Spouses): $115,400
- Married Individuals Filing Separate Returns and Estates and Trusts: $76,950

(4) For taxable years beginning in 2013, the standard deduction amounts under § 63(c)(2) are as follows:

- Married Individuals Filing Joint Returns and Surviving Spouses: $12,200
- Heads of Households: $8,950
- Unmarried Individuals (other than Surviving Spouses and Heads of Households): $6,100
- Married Individuals Filing Separate Returns: $6,100

(5) For taxable years beginning in 2013, the applicable amounts under § 68(b) are $300,000 in the case of a joint return or a surviving spouse, $275,000 in the case of a head of household, $250,000 in the case of an individual who is not married and who is not a surviving spouse or head of household, $150,000 in the case of a married individual filing a separate return. (6) For taxable years beginning in 2013, the personal exemption amount under § 151(d) is $3,900. For taxable years beginning in 2013, the personal exemption phases out for taxpayers with the following adjusted gross income amounts:

<table>
<thead>
<tr>
<th>Filing Status</th>
<th>AGI – Beginning of Phaseout</th>
<th>AGI – Completed Phaseout</th>
</tr>
</thead>
<tbody>
<tr>
<td>Married Filing Joint Returns, Surviving Spouses: Heads of Households;</td>
<td>$300,000</td>
<td>$472,500</td>
</tr>
<tr>
<td>Unmarried Individuals (other than Surviving Spouses and Heads of Households):</td>
<td>$275,000</td>
<td>$397,500</td>
</tr>
<tr>
<td>Married Individuals Filing Separate Returns:</td>
<td>$250,000</td>
<td>$377,500</td>
</tr>
<tr>
<td>Married Individuals Filing Separate Returns:</td>
<td>$150,000</td>
<td>$211,250</td>
</tr>
</tbody>
</table>

INNOCENT SPOUSE RELIEF. The taxpayer was a widow and during the last year of the decedent’s life, the decedent received distributions from a pension plan which resulted in taxable income. The taxpayer did not know about the distributions until after the death of the decedent but filed a final joint tax return with the distributions included. The taxpayer sought innocent spouse tax relief from the taxes owed for the distributions. The IRS agreed that the taxpayer met all the initial conditions of Rev. Proc. 2003-61, 2003-2 C.B. 297. However, the court held that relief could not be granted under the equitable relief of I.R.C. § 6015(f) because the taxpayer knew the decedent would not pay the taxes when the return was filed. The court then examined the equitable relief available under Rev. Proc. 2003-61 under the facts and circumstances tests and held that the taxpayer met only two of the eight factors, not
being married to the decedent and complying with federal tax laws; therefore, the taxpayer was not entitled to equitable innocent spouse relief. The appellate court affirmed in a decision designated as not for publication. Haggerty v. Comm’r, 2013-1 U.S. Tax Cas. (CCH) ¶ 50,127 (5th Cir. 2013), aff’g., T.C. Memo. 2011-284.

INSTALLMENT REPORTING. The taxpayer was a member of a partnership which sold land to another company. The transaction was initially a cash sale but the parties modified the sale before closing to include cash plus a promissory note. The taxpayer did not elect out of the installment method for the gain from the sale. The taxpayer argued that the change in payment method was instituted by the buyer and the buyer had intended to make the sale all cash but ultimately failed to do so. The court held that, although the intention was a cash sale, the tax consequences had to be based on the actual form of the sale as an installment sale; thus, the gain had to be reported on the installment method. Parker v. Comm’r, T.C. Memo. 2012-357.

LETTER RULINGS. The IRS has issued its annual list of procedures for issuing letter rulings. Appendix A contains a schedule of user fees for requests. Rev. Proc. 2013-1, 2013-1 C.B. 1. The IRS has corrected a typographical error in the Schedule of User Fees found in Appendix A, paragraph (4)(a) of Rev. Proc. 2013-1. The procedure incorrectly lists the reduced user fee for a letter ruling, method or period change or closing agreement request involving a personal or business tax issue from a person with gross income of less than $250,000 as $1,000. The user fee is $2,000. Ann. 2013-9, I.R.B. 2013-4.

The IRS has issued its annual revision of the general procedures relating to the issuance of technical advice to a director or an appeals area director by the various offices of the Associate Chief Counsel. The procedures also explain the rights a taxpayer has when a field office requests technical advice. Rev. Proc. 2013-2, 2013-1 C.B. 92.

The IRS has issued its annual list of tax issues for which the IRS will not give advance rulings or determination letters. Rev. Proc. 2013-3, 2013-1 C.B. 113.


The IRS has released an updated revenue procedure which explains when and how the IRS issues technical advice memoranda in the employee plans areas (including actuarial matters) and exempt organizations areas. Rev. Proc. 2013-5, 2013-1 C.B. 170.


The IRS has issued a revised revenue procedure which provides guidance for complying with the user fee program of the Internal Revenue Service as it pertains to requests for letter rulings, determination letters, etc., on matters under the jurisdiction of the Commissioner, Tax Exempt and Government Entities Division; and requests for administrative scrutiny determinations under Rev. Proc. 93-41, 1993-2 C.B. 536. Rev. Proc. 2013-8, 2013-1 C.B. 237.

LIKE-KIND EXCHANGE. The taxpayer had owned a residential rental property in one city. The property was sold through a 1031-exchange facilitator as part of a plan to purchase like-kind property in order to obtain I.R.C. § 1031 treatment. The replacement property was purchased in another city where the taxpayer’s brother lived. The brother agreed to fix up the house in exchange for the first three months rents. After the house repairs were completed, the brother paid less than fair market rent while living in the house but continued to perform maintenance and additional remodeling. The court held that the sale and purchase of the houses were eligible for like-kind exchange treatment, although the taxpayer had to include in income the boot received for the first house over the amount paid for the second house and the costs of remodeling. Adams v. Comm’r, T.C. Memo. 2013-7.

LOAN OR SALE. The taxpayer sold their company and purchased floating rate notes. The notes were transferred to another company in exchange for two loans. The loans were for 27 and 29 years and were non-callable, non-recourse, with no margin required, and a highly restricted payment to the principal directly, albeit immediately with approval from the taxpayers. The court held that the loans were properly characterized by the IRS as taxable sales because the “lender” had full control of the benefits of the floating rate notes and sold them. In addition, the court noted that the nonrecourse provision shifted all risk to the “lender.” Clark v. Comm’r, 2013-1 U.S. Tax Cas. (CCH) ¶ 50,119 (N.D. Calif. 2012).

PARTNERSHIP

PARTNER’S DISTRIBUTIVE SHARE. The IRS has adopted as final regulations removing Treas. Reg. § 1.704-1(b)(2)(iii)(e) (the de minimis partner rule) because the rule may have resulted in unintended tax consequences. The de minimis partner rule provides that for purposes of applying the partnership items allocation substantiality rules, the tax attributes of de minimis partners need not be taken into account and defines a de minimis partner as any partner, including a look-through entity that owns, directly or indirectly, less than 10 percent of the capital and profits of a partnership, and who is allocated less than 10 percent of each partnership item of income, gain, loss, deduction, and credit. 77 Fed. Reg. 76380 (Dec. 28, 2012).

PENSION PLANS. For plans beginning in January 2013 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 2.88 percent, the corporate bond weighted average is 5.01 percent, and the 90 percent to 100 percent permissible range is 4.51 percent to 5.01 percent. Notice 2013-2, I.R.B. 2013-6.

RETURNS. The IRS has issued proposed regulations that create a new taxpayer identifying number known as an IRS truncated taxpayer identification number, a TTIN. As an alternative to using
Agricultural Court to uphold the IRS denial of most of the expenses. T.C. Summary Op. 2013-1.

TREASURY BONDS. The IRS has adopted as final regulations that provide guidance on the tax treatment of Treasury Inflation-Protected Securities issued with more than a de minimis amount of premium. The IRS also issued temporary regulations that provide guidance on the tax treatment of a debt instrument with a bond premium carryforward in the holder’s final accrual period, including a Treasury bill acquired at a premium. 78 Fed. Reg. 666 (Jan. 4, 2013).

WITHHOLDING TAX. The IRS has published updated income tax withholding tables, reflecting the changes passed in the American Taxpayer Relief Act of 2012. The updated tables, issued after President Obama signed the changes into law, show the new rates in effect for 2013 and supersedes the tables issued on December 31, 2012. The newly revised version of Notice 1036 contains the percentage method income-tax withholding tables and related information that employers need to implement these changes. In addition, employers should also begin withholding Social Security tax at the rate of 6.2 percent of wages paid following the expiration of the temporary two-percentage-point payroll tax cut in effect for 2011 and 2012. The payroll tax rates were not affected by the legislation. Employers should start using the revised withholding tables and correct the amount of Social Security tax withheld as soon as possible in 2013, but not later than Feb. 15, 2013. For any Social Security tax under-withheld before that date, employers should make the appropriate adjustment in workers’ pay as soon as possible, but not later than March 31, 2013. IR-2013-1.

S CORPORATIONS

DISTRIBUTIVE SHARE. The taxpayer was the sole shareholder of an S corporation. An IRS audit determined that the corporation had underreported its revenues and overreported its expenses, resulting in an increase in the taxpayer’s income which passed through from the corporation. The taxpayer claimed that the taxpayer had sufficient basis in the corporation to shelter any distributions but the court noted that the assessment was not based on the tax of distributions but on the pass-through income from the corporation to the sole shareholder. Kim v. Comm’r, T.C. Memo. 2013-5.

SOCIAL SECURITY BENEFITS. The taxpayer had received benefits under a private disability insurance policy but was required by the policy to seek social security disability benefits to offset the private payments. The taxpayer was able to obtain the social security disability benefits which were paid in a lump sum for the several past years of the disability. The taxpayer was required to send most of the money to the insurer as reimbursement. The court held that the funds sent to the insurer were not deductible from the taxable social security benefits. Brady v. Comm’r, T.C. Memo. 2013-1.

TAX RETURN PREPARERS. The IRS has adopted as final regulations that provide rules relating to the disclosure and use of tax return information by tax return preparers. The regulations provide updated guidance affecting tax return preparers regarding the use of information related to lists for solicitation of tax return business; the disclosure or use of statistical compilations of data under I.R.C. § 7216 by a tax return preparer in connection with, or in support of, a tax return preparer’s tax return preparation business, including identification of additional limited circumstances when a tax return preparer who compiles statistical information may disclose the compilation without taxpayer consent, the placement of additional restrictions on the content of the compilation that may be disclosed under those circumstances without taxpayer consent, and the disclosure or use of information for the purpose of performing conflict reviews. 77 Fed. Reg. 76400 (Dec. 28, 2012).

TRAVEL EXPENSES. The taxpayers, husband and wife, were real estate agents in Nevada but lived in Florida. The taxpayers claimed travel expenses for trips from Florida to Nevada to perform business activities; however, the taxpayers did not provide written evidence or receipts to support their oral testimony as to the nature of the trips and the business conducted on the trips. The court upheld the IRS denial of most of the expenses. Martin v. Comm’r,
The Agricultural Law Press is honored to publish the completely revised and updated 16th Edition of Dr. Neil E. Harl’s excellent guide for farmers and ranchers who want to make the most of the state and federal income and estate tax laws to assure the least expensive and most efficient transfer of their estates to their children and heirs. This book contains detailed advice on assuring worry-free retirement years, using wills, trusts, insurance and outside investments as estate planning tools, ways to save on estate settlement costs, and an approach to setting up a plan that will eliminate arguments and friction in the family. Federal estate taxation has undergone great changes in recent years and this book sorts out these changes for you in a concise manner. FEBP also includes discussion of employment taxes, formation and advantages of use of business entities, federal farm payments, state laws on corporate ownership of farm land, federal gift tax law, annuities, installment obligations, charitable deductions, all with an eye to the least expensive and most efficient transfer of the farm to heirs.

Written with minimum legal jargon and numerous examples, this book is suitable for all levels of people associated with farms and ranches, from farm and ranch families to lenders and farm managers. Some lawyers and accountants circulate the book to clients as an early step in the planning process. We invite you to begin your farm and ranch estate and business planning with this book and help save your hard-earned assets for your children.