2-2-1990

Cases, Regulations, and Statutes

Agricultural Law Digest

Follow this and additional works at: http://lib.dr.iastate.edu/aglawdigest

Part of the Agricultural and Resource Economics Commons, Agricultural Economics Commons, Agriculture Law Commons, and the Public Economics Commons

Recommended Citation

Available at: http://lib.dr.iastate.edu/aglawdigest/vol1/iss6/3

This Article is brought to you for free and open access by Digital Repository @ Iowa State University. It has been accepted for inclusion in Agricultural Law Digest by an authorized administrator of Digital Repository @ Iowa State University. For more information, please contact digirep@iastate.edu.
With this approach, the income tax basis of the personal use of the automobile is reduced by the depreciation amount attributable to the personal use portion of the vehicle. It seems strange to be reducing the basis of personal use property by the amount of depreciation which would have been allowable had it been a business asset.

**ANOTHER APPROACH**

The other approach would involve separating the vehicle into two components—one for personal use and one for business use.

Income tax basis of automobile traded in on January 2, 1996–

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Business portion (basis)</td>
<td>$11,200</td>
</tr>
<tr>
<td>Less depreciation</td>
<td>$7,519</td>
</tr>
<tr>
<td></td>
<td>$3,681</td>
</tr>
<tr>
<td>Personal portion (basis)</td>
<td>$16,800</td>
</tr>
<tr>
<td>Less depreciation</td>
<td>$0</td>
</tr>
<tr>
<td>Fair market value on trade</td>
<td>8,400</td>
</tr>
<tr>
<td>Basis on trade</td>
<td>8,400</td>
</tr>
<tr>
<td>Basis of vehicle traded in</td>
<td>$3,681</td>
</tr>
<tr>
<td></td>
<td>$8,400</td>
</tr>
<tr>
<td></td>
<td>$12,081</td>
</tr>
<tr>
<td>Plus boot paid</td>
<td>$17,500</td>
</tr>
<tr>
<td>Basis of automobile acquired 1/2/96</td>
<td>$29,581</td>
</tr>
</tbody>
</table>

Whether one gains or loses from this approach (compared to the IRS approach) depends upon the fair market value of the auto at the time of the trade. The two approaches are obviously quite different. Note that the first set of calculations above represents the stated IRS position.

| *** |

**ERRORS IN THE FARMERS TAX GUIDE**

IRS PUB. 225 (1989)

1. On page 6, left column, the publication states, "unless you are a limited partner, your distributive share of income from a partnership is self-employment income." In various situations, including that of retired partners under Treas. Reg. § 1.1402(a)-17, distributive shares are not self-employment income.

2. On page 2, middle column, it is stated that "gross income from farming does not include . . . 2) Gains from sales of livestock held for draft, breeding, sport, or dairy purposes. . . ." The content of the statement is that the authors are trying to define Schedule F income, not gross income. Gains from the sales of livestock held for draft, breeding, sporting or dairy purposes are clearly included in gross income for purposes of calculating estimated tax. Rev. Rul. 63-26, 1963-1 C.B. 295, *mod. by Rev. Rul. 80-366, 1980-2 C.B. 343* (Section 175 meaning of "gross income" does not necessarily apply in all respects for estimated tax purposes). As "gross income" is defined for purposes of I.R.C. § 175, soil and water conservation expense (and used elsewhere by specific reference to I.R.C. § 175), income from livestock held for draft, dairy, breeding or sporting purposes is included. Treas. Reg. § 1.175-5(a)(2).

3. On page 66, right column, it is recited that the taxpayer in the example deducted the costs of raising breeding and dairy cows, thus making an election not to capitalize the costs for raised replacement dairy and beef animals as required by I.R.C. § 263A for the years 1987 and 1988. Yet the depreciation record on page 72 shows double declining balance depreciation and 150 percent declining balance depreciation claimed on some property acquired in 1987 and 1988. Such is not permissible. The taxpayer is limited to alternative depreciation for all property placed in service in the taxable year the election out is in effect. I.R.C. §§ 263A(e)(1), (e)(2)(A). See *Temp. Treas. Reg. § 1.263A-1T(c)(6)(vi)(B).*

4. On page 78, the Form 4797 shows that a raised heifer was sold on August 1, 1989, and was reported in Part I of Form 4797 (for property used in a trade or business and held long enough to merit the long-term capital gain treatment). Because the heifer was used in a farm business where the election had been made not to capitalize costs, the animal is subject to I.R.C. § 1245 recapture; thus, the gain should not be reported in Part I of Form 4797. Rather, gain from the raised heifer would be properly reported in Part III of Form 4797.

**Cases, Regulations and Statutes**

**BANKRUPTCY**

**GENERAL**

**ADMINISTRATIVE EXPENSES.** Lessor of grain storage facilities were entitled to administrative expense priority for rent due on postpetition storage of grain of debtor elevator under prepetition storage contracts. *In re Woods Farmers Co-op. Elev.* Co., 107 B.R. 694 (Bankr. D. N.D. 1989).

**AVOIDABLE TRANSFERS.** A farm debtor had purchased feed several months prior to filing bankruptcy but had requested that the seller not cash the checks until the debtor had sufficient funds in the checking account. The date the checks were finally cashed was within 90 days before the bankruptcy filing. The court held that the date of the issuance of the checks was the date of the transfer; therefore, the transfer of funds was not an avoidable pre-petition transfer. *In re Roehrich*, 107 B.R. 675 (Bankr. D. N.D. 1989).

**EQUITABLE SUBORDINATION.** A bank's secured loans to a farm debtor were subordinated to all unsecured creditors' claims and the bankruptcy estate's administrative expenses where the bank was found to
have misrepresented to the debtor that the bank would continue to lend the debtor additional funds for the debtor's farming operations. Under the influence of this misrepresentation, the debtor had pledged all assets as collateral for the operating loan and had incurred additional debts to the unsecured creditors. In re Slefco, 107 B.R. 628 (Bankr. E.D. Ark. 1989).

ESTATE PROPERTY. The debtor's estate included the debtor's interest in her deceased father's estate. Although under Wyoming law disclaimer related back to filing for bankruptcy, although under where debtor disclaimed interest after interest in her deceased father's estate included the debtor's interest. In re Duncan, 107 B.R. 754 (Bankr. W.D. Okla. 1989).

In a joint bankruptcy case, husband and wife debtors were allowed to exempt their interest in farm property held by the entireties only to the extent that claims against both debtors did not exceed their equity in the property. The debtors were denied exemptions for property not sufficiently identified on their bankruptcy schedules. In re Wenande, 107 B.R. 770 (Bankr. D. Wyo. 1989).

The Florida exemption for qualified ERISA plans was held not preempted by ERISA. In re Seilkop, 107 B.R. 776 (Bankr. S.D. Fla. 1989).

GRAIN ELEVATORS. In determining the share of each warehouse receipt holder's interest in the proceeds of grain held by debtor grain elevator, each receipt holder of a specific type and grade of grain would share in the proceeds of that type and grade of grain. If any holder of a receipt for a particular type and grade of grain did not receive full reimbursement from the proceeds of that type and grade of grain, the holder would receive any excess proceeds from lesser grades of the same type of grain remaining after holders of receipts for the lesser grade had received their share of the proceeds of the lesser grade. Contract seller of grain to the elevator who had not received payment held only liens as to any proceeds remaining after receipt holders were paid and was otherwise an unsecured creditor. In re Woods Farmers Co-op. Elev. Co., 107 B.R. 678 (Bankr. D. N.D. 1989).

In another hearing in the same case, the court held that the trustee could not avoid, under Section 545, the warehouse receipt holders' statutory liens, under N.D. Cent. Code § 60-02-25.1, against the debtor grain elevator's grain in so far as the receipt holders' grain was only stored in the elevator, because the grain was held in bailment and did not belong to the debtor elevator. However, the same statutory liens held by sellers of grain to the elevator were avoided under Section 545(2), because the liens were not enforceable against the trustee as a bona fide purchaser. In re Woods Farmers Co-op. Elev. Co., 107 B.R. 689 (Bankr. D. N.D. 1989).

LIEN AVOIDANCE. A Chapter 7 debtor was not allowed to avoid liens under Section 506(a) and (d) against real property abandoned to the debtor. Matter of D'Angona, 107 B.R. 448 (Bankr. D. Conn. 1989).

CHAPTER 7

LIEN AVOIDANCE. Chapter 7 debtors were allowed to avoid liens against their residence in excess of the fair market value of the property. Gagli v. First Federal Sav. & Loan Ass'n, 889 F.2d 1304 (3d Cir. 1989).

CHAPTER 13

PLAN. The interest rate for deferred payments under a Chapter 13 plan on an obligation secured by a four year old pickup truck was the current rate of Treasury Bills plus 1 percent for risk. In re Cassell, 107 B.R. 536 (Bankr. W.D. Va. 1989).

FEDERAL TAXATION

DISCHARGE. Federal taxes for which the debtor failed to file a return were nondischargeable although a substitute return was filed by the IRS. In re Pruitt, 107 B.R. 764 (Bankr. D. Wyo. 1989).

CONTRACTS

BREACH OF WARRANTY. The seller of fertilizer contaminated by herbicide was liable for breach of implied warranty of merchantability and fitness for a particular purpose where the seller had tested the soil and recommended particular fertilizer used. The amount of damages was the difference between the value of the crop if the fertilizer had been as warranted and the value of the crop as produced with the contaminated fertilizer. The seller of the fertilizer was also liable for negligence per se where the sale of the fertilizer violated Colo. Rev. Stat. § 35-12-112. Deacon v.

SALES. A grain producer sued a grain buyer for breach of contract on the sale of corn. Under the contract, the producer was to grow and deliver 15,000 bushels of white waxy premium corn. The buyer was held to have accepted several loads of the corn, under U.C.C. § 2-601, when the corn was inspected and loaded on to a barge. The acceptance was held not to be timely rejected where the grain was officially inspected as inferior but the buyer waited over a week to see what the price the corn would bring before notifying producer of nonacceptance as premium corn. Under the contract, the buyer was entitled only to a discount of three cents per bushel for under grade corn and not for the lesser value of the corn. Veath v. Specialty Grains, Inc., 546 N.E.2d 1005 (Ill. App. 1989).

COOPERATIVES

MILK PROCEEDS. A dairy cooperative paid member producers for milk sold through the cooperative based upon a system of production quotas for quota and over-quota milk produced. The plaintiff milk producer claimed that the lower amounts paid by the cooperative for over-quota milk violated Ariz. Rev. Stat. § 10-716(C) (which allows cooperatives to sell products of its members and pay the members the average sale price less costs of sale) because the cooperative did not require a minimum of the average price paid. Lueck v. United Dairymen of Arizona, 782 P.2d 708 (Ariz. App. 1989).


BORROWER'S RIGHTS. A Farm Credit Bank was held to have violated the Agricultural Credit Act of 1987, 12 U.S.C. § 2202(a)(b)(1), because it had not made a determination as to whether the debtor's farm loans were distressed. Therefore, the court denied the Bank's motions for relief from the automatic stay so that it could foreclose against the debtor's property and for dismissal of the petition because the debtor was ineligible for bankruptcy. In re Wagner, 107 B.R. 662 (Bankr. D. Neb. 1989).

A Farm Credit Bank's motion for relief from the automatic stay in order to foreclose on the debtor's farm property was denied because the bank had not made an official determination that the farm loan was distressed. Matter of Rudloff, 107 B.R. 663 (Bankr. D. Neb. 1989).

A Farm Credit Bank's motion for sequestration of rents and profits was denied where the bank failed to make a determination that the farm debtor's loans were distressed. Matter of Kramer, 107 B.R. 668 (Bankr. D. Neb. 1989).

FmHA did not have to comply with Agricultural Credit Act of 1987 where debtor had received discharge in Chapter 7. In re Duncan, 107 B.R. 754 (Bankr. W.D. Okla. 1989).

BRUCELLOSIS. The Animal and Plant Health Inspection Service has announced that West Virginia has been validated as a brucellosis-free state. 55 Fed. Reg. 419 (Jan. 5, 1990), amending 7 C.F.R. § 78.43.

CRANBERRIES. The Agricultural Marketing Service has announced hearings on proposed rules to amend the Marketing Agreement and Order No. 929 regulating handlers of cranberries in Connecticut, Massachusetts, Michigan, Minnesota, New Jersey, Oregon, Rhode Island, Washington, Wisconsin, and Long Island, New York. The proposed rules (1) authorize the Cranberry Marketing Committee to conduct production research and development, (2) calculate annual allotments based on sales, (3) amend the terms of the committee members, (4) establish provisions for excess production, and (5) provide assessments on the weight of acquired cranberries. The next hearings are February 6, 1990 in Medford, New Jersey, February 13, 1990 in Wisconsin Rapids, Wisconsin and February 15, 1990 in Portland, Oregon. 55 Fed. Reg. 295 (Jan 4, 1990), amending 7 C.F.R. Part 929.


FARM CREDIT ADMINISTRATION. The Farm Credit Administration has issued proposed regulations implementing statutory changes made by the Freedom of Information Reform Act of 1986, Pub. L. No. 99-570. The amendments include changes in the fees charged for FOI requests and procedures for notifying parties who have submitted confidential commercial or financial information which is the subject of an FOI request. 55 Fed. Reg. 440 (Jan. 5, 1990), amending 12 C.F.R. Part 602.

50,000 PAYMENT LIMITATION. Effective only for the 1989 crops, for the purposes of determining who is a "person" for the purposes of the $50,000 payment limitation under several farm programs, landlords renting their land on a cash or guaranteed crop amount basis are to be considered one "person" with tenants who make a significant contribution of active personal management but not of personal labor unless the tenant makes a significant contribution of equipment used in the farming operation. This rule does not apply if (1) a determination had been made that the tenant was a separate "person" from the landlord and (2) the landlord does not consent to or knowingly participate in the tenant's failure to qualify for separate person status. This exception, however, is
limited to the extent that the amount of payments the tenant may receive may not exceed the amount the tenant would receive if the tenant was considered one "person" with the landlord but for the exception. For the 1990 crops, tenants on a cash or guaranteed crop amount rent basis and who make a significant contribution of active personal management but not of personal labor are ineligible for farm program payments unless the tenant makes a significant contribution of equipment used in the farming operation. Pub. L. No. 101-217, 103 Stat. 1857 (1989).


The ASCS has also announced other changes in the $50,000 payment limitation regulations:
1. Irrevocable trusts are to be considered revocable if upon the termination of the irrevocable trust any of the assets of the trust may pass to the grantor. Also, irrevocable trusts will be considered revocable if the trust corpus is transferred to the remainder beneficiary in less than 20 years after establishment of the trust. 7 C.F.R. § 1497.10.
2. Grantors and beneficiaries are required to disclose any interests in any other trusts which receive payments or loans from the CCC. This rule was implemented to prevent circumvention of the trust rules by one producer transferring land to a trust with another producer as beneficiary in exchange for the other producer transferring land to a second trust with the first producer as beneficiary. 7 C.F.R. § 1497.10.
3. The combined interests of the income beneficiaries which provide the the active personal management and/or labor to qualify the trust as actively engaged in farming must be 50 percent. Note that trusts which are land owners qualify as actively engaged in farming under the landowner provisions. 7 C.F.R. § 1497.10.
4. Only individuals and not entities may be sharecroppers. 7 C.F.R. § 1497.3.
5. Only one set of "permitted entities" for all programs specified in 7 C.F.R. § 1497.1 are allowed. Corporations with a large number of shareholders may be relieved of the reporting requirements if the Deputy Administrator determines that because of the number of shareholders, no shareholder is likely to have a substantial beneficial interest and the reporting requirements would be burdensome. 7 C.F.R. § 1497.5.
6. If a significant amount of land is contributed to a farming operation by a landowner, the landowner is considered actively engaged in farming with respect to the land owned and contributed by the landowner. 7 C.F.R. § 1497.13.

FOOD STAMPS. The Food and Nutrition Service has announced the maximum allotment levels, the limits on gross and net income for eligible households and the standard deduction and maximum excess shelter deduction for 1990. 55 Fed. Reg. 887 (Jan. 10, 1990).

GRAIN INSPECTION. The Federal Grain Inspection Service has issued a final rule amending the maintenance tolerances for near-infrared spectroscopy instruments used in testing soybeans for oil and protein content. 55 Fed. Reg. 839 (Jan. 10, 1990), amending 7 C.F.R. § 801.7.


MILK. The support price for milk from January 1, 1990 to December 31, 1990, for milk containing 3.67 percent milkfat is $10.10 per hundredweight. The notice also publishes the purchase prices for butter, cheese and nonfat dry milk. 55 Fed. Reg. 450 (Jan. 4, 1990).


ORANGES. Due to the December freeze which damaged much of the Florida citrus crop, the Agricultural Marketing Service has issued a final rule relaxing the grade and size requirements for domestic shipments of Temple oranges and Honey tangerines. 55 Fed. Reg. 1786 (Jan. 19, 1990), amending 7 C.F.R. § 905.306.

PERISHABLE AGRICULTURAL COMMODITIES ACT. In an action by a seller of asparagus against the purchaser under the Perishable Agricultural Commodities Act (PACA) for failure of the purchaser to maintain a trust fund for the purchase price of the vegetables, an officer and 35 percent shareholder of the purchaser was held subject to PACA. The court also held that it had no jurisdiction to try the plaintiff's claim for an injunction against the purchaser to prevent spending any funds which could be used for a PACA trust fund. The only party which may pursue such an action is the Secretary of Agriculture. Frio Ice, S.A. v. Sunfruit, Inc., 724 F. Supp. 1373 (S.D. Fla. 1989).

A produce seller was held to have failed to comply with the PACA requirement that the maximum period for payment of produce be 30 days after delivery and acceptance of the produce where the seller and buyer had agreed that payment was to be made within 30 days after the invoice date. Thus, the seller failed to comply with PACA for the produce for which an invoice was written after the produce was delivered and accepted. As to the other invoices, the seller's notifications of intent to preserve rights to trust funds under PACA were held sufficient although the notices did not provide the sale contract terms and payment dates. A second notice was also held to be sufficient where the seller issued a third notice which corrected deficiencies on the second notice. In re Lombardo Fruit & Produce Co., 107 B.R. 654 (Bankr. E.D. Mo. 1989).
Sellers of produce to debtor were entitled to share in PACA trust funds although the sellers had not intervened or joined in motion for relief from automatic stay filed by other sellers. The intervention was not necessary because the trust funds were not part of the bankruptcy estate and the produce seller's rights in the trust funds did not depend on any rights or procedures in bankruptcy. In re Milton Poulos, Inc., 107 B.R. 715 (Bankr. 9th Cir. 1989).


PRODUCTION ADJUSTMENT PROGRAMS. The Commodity Credit Corporation has issued interim rules amending the rules involving reconstitution of a farm to provide that any person with an undivided interest in land which comprises a portion of a farm may request that the farm be decombined for farm program purposes. 55 Fed. Reg. 1557 (Jan. 17, 1990), amending 7 C.F.R. § 719.3.

The provision for allowing a producer to plant certain nonprogram crops on a farm and have a percentage of these crops be considered to have been planted to a program crop has been extended to the 1990 crop. Pub. L. 101-81, 103 Stat. 563 (1989). The regulations have been amended to implement the extension. 55 Fed. Reg. 1557 (Jan. 17, 1990), amending 7 C.F.R. § 1413.102.

As a result of implementation of an oats acreage reduction percentage lower than the percentage applicable to sorghum, corn and barley, a producer may not combine the acres of oats with the other grains in the crop acreage base. Acres of sorghum, corn and barley may still be combined. 55 Fed. Reg. 1557 (Jan. 17, 1990), amending 7 C.F.R. § 1413.7.

TOMATOES. The Federal Crop Insurance Corporation has issued a final rule adding a Fresh Market Tomato (Dollar Plan) endorsement to the general crop insurance regulations. 55 Fed. Reg. 1782 (Jan. 19, 1990), adding 7 C.F.R. § 401.139.


FEDERAL ESTATE AND GIFT TAX

ALTERNATIVE VALUATION. An estate was not allowed to elect valuation of estate property on the alternate valuation date because the estate tax return was not timely filed. Est. of Dixon v. Comm'r, T.C. Memo. 1990-17.

CHARITABLE DEDUCTION. At issue in this case was the date when a judicial proceeding had commenced to reform a charitable remainder bequest to qualify it for a charitable remainder trust deduction. The estate argued that the judicial proceeding commenced when the executor filled out a form inquiring as to whether the estate contained any charitable trusts. The court held that this form did not qualify as a judicial proceeding because the executor answered it in the negative and the form did not function as a pleading or petition. In addition, the estate did file a reformation petition 15 months after the estate tax return was due. The court also held that the retroactive effect of the probate court's ruling reforming the trust was not effective as to the federal estate tax deduction. Est. of Hall v. Comm'r, 93 T.C. No. 60 (1989).

An estate's charitable deduction was reduced by the estate's administrative expenses which were all allocated to the charitable bequest, although the probate court had reallocated the expenses to other bequests. Est. of Warren v. Comm'r, 93 T.C. No. 57 (1989).

DISCLAIMERS. A surviving child received property in trust from the decedent parent's estate a portion of which came from life insurance on the parent's life. The IRS ruled that the child could make a qualified disclaimer of the child's interest in trust in the insurance proceeds while retaining an interest in other property of the trust, if the disclaimer is timely made. Ltr. Rul. 8951041, Sept. 26, 1989.

A surviving spouse proposed to make a timely disclaimer of an interest in a joint savings account held with the decedent spouse. The surviving spouse contributed all of the funds to the account and one-half of the account was includible in the decedent's estate. IRS ruled that the surviving spouse may not make a disclaimer of an interest in property contributed by the surviving spouse. Ltr. Rul. 8951070, no date given.

FORMS. IRS has announced that although Form 709 "United States Gift and Generation-Skipping Transfer Tax Return" was revised in December 1989, use of the previous Form 709 by filers in December 1989 after the revised form was issued was sufficient. Ann. 90-4, I.R.B. 1990-3, Jan. 16, 1990.

GENERATION SKIPPING TRANSFER TAX. The division of a trust, irrevocable prior to September 25, 1985, into five trusts which form the corpus of a new trust was not a taxable generation skipping transfer where the creation of the new trusts was provided for in the original trust under the trustee's discretion. Ltr. Rul. 8951068, no date given.

GROSS ESTATE. Under I.R.C. § 2036(c), a person is considered to have retained the enjoyment of property of an enterprise transferred to a trust where the person held a substantial interest in the enterprise, the person retained an interest in the income of the enterprise, and the property transferred would receive a disproportionately large share of the appreciation of the enterprise. Under I.R.C. 2036(a), the above conditions would result in the transferred property being included in the person's gross estate. In a letter ruling, a taxpayer transferred a personal collection of art to an irrevocable trust which terminated at the earlier of the taxpayer's death (with the corpus transferred to the taxpayer's estate) or ten years (with undivided interests in the trust transferred to the taxpayer's children). The art collection had been displayed only in the taxpayer's homes. The trustees had the power to manage the collection, including the sale and purchase of art. The taxpayer was
entitled to any income from the trust and the rent-free possession of the art for display. The IRS ruled that the trust arrangement lacked significant business or investment aspects and that the trust would not be an enterprise. Therefore, the trust corpus would not be includible in the taxpayer's gross estate by reason of I.R.C. § 2036(c). Ltr. Rul. 8951065, Sept. 28, 1989. For further discussion of estate freezes, see Harl, Agricultural Law, § 43.02[6][a][i] (MB 1990).

A decedent had transferred an interest in real property to herself and her son as joint tenants. The son managed the property. The court held that the son's contribution of management services supplied adequate consideration for the transfer and held that half the value of the property was includible in the decedent's gross estate. Est. of Anderson v. Comm'rr, T.C. Memo. 1989-643.

LIFE ESTATES. A taxpayer established an irrevocable trust which paid the income to the grantor for the lesser of 17 years or upon termination of the trust for various reasons including the death of the grantor. IRS ruled that if the grantor died after the trust terminated, the trust was not includible in the grantor's estate, but if the grantor died before the trust terminated, the trust was subject to I.R.C. § 2036(c) and includible in the grantor's estate. Ltr. Rul. 8952032, Sept. 29, 1989.

LIFE INSURANCE PROCEEDS. The decedent and predeceased spouse had acquired a life insurance policy on the decedent's life and paid the premiums from community funds. Upon the predeceased spouse's death and for over three years, the decedent continued to pay the premiums but reduced the coverage amount and changed the beneficiary to the decedent's estate. IRS ruled that the entire amount of life insurance proceeds was includible in the decedent's estate. Ltr. Rul. 8951003, Sept. 14, 1989.

The proceeds of life insurance on the decedent were not includible in the decedent's gross estate where the decedent purchased the policy within three years of death but did not hold any incidents of ownership. Est. of Leder, 90-1 U.S.T.C. ¶ 60,001 (10th Cir. 1989), aff'g 89 T.C. 235 (1989).

MARITAL DEDUCTION. A surviving spouse received an interest in a trust the income from which was to be distributed at least quarterly and the corpus of which may be distributed for the spouse's support, health and education. The spouse has the noncumulative power to annually require the withdrawal of the greater of $5,000 or 5 percent of the value of the trust principal. The spouse has a general power of appointment over a portion of the trust. The IRS ruled that the trustee may elect to treat the spouse's interest in the trust as qualified terminable interest property (QTIP). Only the portion of the trust subject to the spouse's general power of appointment will be includible in the spouse's gross estate. Ltr. Rul. 8951049, Sept. 27, 1989.

A surviving spouse received an interest in trust in property which under the decedent spouse's will would qualify for a marital deduction to the extent the deduction would decrease the federal estate tax. The surviving spouse received all the income from the trust and held a general power of appointment over the corpus. The surviving spouse also received an interest in trust of other property but the trustee of this trust was not required to distribute the income to the surviving spouse and the spouse held a general power of appointment over the trust property. The decedent's estate was allowed a marital deduction for the first trust but not for the second trust. The property of the second trust was also ruled includible in the surviving spouse's estate. Ltr. Rul. 8951021, Sept. 22, 1989.

The decedent had received a life income interest in a trust established under a predeceased spouse's will. The trust did not provide for the frequency by which the trustee was to make payments to the decedent of trust income. State statutory law, Texas, did not require a trustee to make income payments at least annually and the IRS found no Texas Supreme Court ruling which required a trustee to make payments at least annually. However, the IRS concluded that under Texas common law, a trustee would be required to make the payments at least annually; thus, the decedent's interest in the trust would qualify for the marital deduction as Qualified Terminable Interest Property (QTIP) and the trust property would be includible in the decedent's gross estate. Ltr. Rul. 8951003, Sept. 14, 1989.

A surviving spouse's interest in a trust was not eligible for the marital deduction where the surviving spouse's power of appointment over the property was contingent upon the decedent's executor making an election on the estate state death tax return. Ltr. Rul. 8952002, Sept. 15, 1989.

A surviving spouse's life estate interest in a work of art in which the surviving spouse had the right to sell, lease, and encumber the life estate and to license and exploit any intellectual property right of the artwork was eligible for the marital deduction. Ltr. Rul. 8952024, Sept. 28, 1989.

A clause in a decedent's will devised an amount to the surviving spouse equal to the amount qualifying for the marital deduction necessary to reduce the federal estate tax to zero. IRS ruled that this was a formula clause subject to the ERTA transition rule which limited the marital deduction to $250,000 or 50 percent of the gross estate. Ltr. Rul. 8952025, Sept. 28, 1989.

SPECIAL USE VALUATION. The Seventh Circuit Court of Appeals has joined the growing list of courts holding that a remote possibility that property could pass to a nonqualified heir would not preclude special use valuation. A special use valuation election was allowed where only a remote possibility existed that contingent remainder interests in the farmland would pass to nonqualified heirs and where the surviving spouse had a limited power of appointment exercisable in favor of nonqualified heirs. The court approved a "wait and see" approach as to any later exercise of the power in a manner which would lead to recapture. The court said that exercising the power in favor of persons who were not qualified heirs could make the holder of the power liable for recapture tax on the interests so appointed. The court cited as support Est. of Thompson v. Comm'r, 864 F.2d 1128 (4th Cir. 1989); Est. of Davis v. Comm'r, 86 T.C. 1156 (1986); Est. of Pliske, T.C. Memo. 1986-311; Est. of Clindard v. Comm'r, 86 T.C. 1180 (1986). Smoot v. Comm'r, 90-1 U.S.T.C. ¶ 60,002 (7th Cir. 1989).
FEDERAL INCOME TAXATION

ALTERNATIVE MINIMUM TAX. For purposes of determining the alternative minimum tax of a trust and its beneficiaries the deduction for state taxes is apportioned between the trust and its beneficiaries according to the allocation of trust income to each beneficiary. For each beneficiary, the total state taxes are multiplied by a fraction, the numerator of which is the amount of the trust's income under I.R.C. § 643(b) less the amount of distributable net income distributed to the beneficiary and the denominator of which is the amount of the trust's income under I.R.C. § 643(b) less the amount of the trust's distributable net income. The amount of state tax deduction allocated to a beneficiary cannot exceed the amount of trust income distributed to the beneficiary less the amount of distributable net income distributed to the beneficiary. Ltr. Rul. 8951004, Sept. 19, 1989.

ASSESSMENT AND COLLECTION. IRS sent notice of deficiency to a former husband for taxes for year of joint return filed by both spouses prior to divorce. Because of a clerical error, the statute of limitations on the former husband had run out. The court held that the IRS was not required to send the notice of deficiency to both spouses because each spouse was jointly and severally liable for the entire deficiency. The court also held that the Tax Court was without equity powers to reduce the husband's liability because of the negligence of the IRS in allowing the statute of limitations on the wife to run out. Pearson v. Comm'r, 890 F.2d 353 (11th Cir. 1989).

IRS mailed a notice of income tax deficiency to the taxpayers within 90 days of sending a previous notice of tax deficiency for the same taxable year. However, the taxpayers did not receive the second notice. The court held that the second notice was not barred by I.R.C. § 6212(c) because the taxpayers did not file a petition with the Tax Court for a refund before the second notice was sent. Section 6212 was held not to bar subsequent notices for the 90 day period in which the taxpayer may petition the Tax Court for a refund. Also, the taxpayers were not allowed to sue to prevent collection based on the notice they did not receive because I.R.C. § 6212 requires proof only of the mailing of the notice and not proof of receipt.

COOPERATIVES. A cooperative sold its headquarters building and received money and property from the sale. Prior to the sale the cooperative had gained a number of new members from another terminated cooperative. The membership agreements with the new members excluded them from receiving any allocation of the gain received from the sale of the headquarters because the gain was acquired before the new members joined. The IRS ruled that the different allocation of the gain between new and old members did not affect the cooperative's tax exempt status. Ltr. Rul. 8952042, Sept. 29, 1989.

A nonexempt farmers' cooperative decided to liquidate. IRS ruled that I.R.C. §§ 1245 and 1250 recapture income recognized in the liquidation of cooperative assets is to be treated as patronage sourced income and section 1231 gains in excess of the recaptured amounts are to be treated as nonpatronage sourced income. The cooperative also established accounts receivable for its patrons to the extent the patrons are responsible for past and current cooperative losses. The accounts receivable were to be offset by the patrons' certificates of retain. IRS ruled that because the cooperative was an accrual method taxpayer, the accounts receivable were patronage sourced income. The offset of the receivables by the retain will not result in taxable income to the cooperative. The members whose certificates of retain are offset and redeemed for less than face value may deduct the loss if the patrons previously recognized income from allocations to the retains. Ltr. Rul. 8952019, Sept. 28, 1989.

HEDGES. A cattle rancher was held to have ordinary income from the sale of hedging transactions required as part of a loan agreement. Because the transactions was required as part of the business loan, the sales were an integral part of the rancher's cattle trading business. Crisp v. Comm'r, T.C. Memo. 1989-668.

HOBBY LOSSES. A psychiatrist was denied net loss deductions for a horse breeding activity because the operation was not engaged in for profit where (1) the operation had 12 years of losses, (2) the operation was run informally, (3) appreciation on the land was not considered in determining profit, (4) the unrealized appreciation of the horses was insufficient to offset the losses, and (5) personal pleasure was derived from raising horses. Lapinel v. Comm'r, T.C. Memo. 1989-685.

A horse breeding activity was held to be engaged in for profit where good accounting records were kept, effort was made to reduce costs, a substantial amount of time was spent in the operation, and the taxpayer either had experience with horses or sought expert advice. A cattle raising activity, however, was held not to be engaged in for profit because the above factors were missing. Givens v. Comm'r, T.C. Memo. 1989-529.

INVESTMENT TAX CREDIT. The taxpayers were noncorporate lessors of automobiles and trucks leased after December 31, 1980 and before June 26, 1981. For purposes of determining the useful life of the leased property, IRS ruled that the useful life of the property was either the Asset Depreciation Range upper limit life of the property or, if no upper limit life was assigned under ADR, the holding period life of the property. The holding period life was defined as "the period for which a particular owner will find it feasible and economic to use the property." Ltr. Rul. 8951002, Sept. 13, 1989.

LETTER RULINGS. The IRS has issued revised procedures to issuing advance rulings, information letters and closing agreements. Rev. Proc. 90-1, I.R.B. 1990-1, 8.

The IRS has announced the areas under the jurisdiction of the Associate Chief Counsel (Technical) in which the IRS will not issue advance letter rulings. Rev. Proc. 90-3, I.R.B. 1990-1, 54.

The IRS has announced the areas under the jurisdiction of the Associate Chief Counsel (International) in which the IRS will not issue advance letter rulings. Rev. Proc. 90-6, I.R.B. 1990-3, 6.
PENSION PLANS AND IRA'S. Taxpayers, both aged 54, proposed to have distributions from their pension plans (which were rolled over to IRA's) in equal periodic payments based on the joint life expectancies using Table VI of Treas. Reg. § 1.72-9. The interest rate on the payments will be determined using section 2619.41 et seq. of the Pension Benefit Guaranty Corporation regulations, Appendix B. IRS ruled that the payments would not be subject to the 10 percent tax under I.R.C. § 72(t)(2). Ltr. Rul. 8951017, Sept. 21, 1989.

Fees for transferring IRA funds between mutual funds and money market funds which were the sole liability of the IRA and paid out of IRA funds were not includible in the taxpayer's income or subject to the early withdrawal penalty. Ltr. Rul. 8951019, Sept. 18, 1989.

IRS has issued guidance for determining a reasonable interest rate on Section 412 plans to be used for determining the current liability of a plan. In addition, some guidance is provided for valuation rules to be used in calculating the current liability of a plan. Under OBRA 1987 the full funding limitation of a pension plan is the excess of (1) the lesser of 150 percent of the current liability or the accrued liability under the plan, over (2) the lesser of the fair market value of the plan's assets or the value of the assets under section 412(c)(2). Notice 90-11, I.R.B. 1990-5, January 29, 1990.

IRS has ruled that the distribution from an ERISA qualified accrued benefit pension plan to a bankruptcy trustee under a bankruptcy court order would result in disqualification of the plan. The ruling states that the anti-alienation requirements for qualified plans exempt the plans from a bankruptcy estate. Ltr. Rul. 8951067, Sept 29, 1989.

RENTAL INCOME. The Eighth Circuit Court of Appeals has affirmed consolidated Tax Court decisions involving recognition of rental income. In both cases, breeding swine were retained and leased to a family farm corporation under a row lease agreement. The corporation has possession of the sow herd and legal title to gilts farrowed but the individual taxpayers (who were also corporate shareholders) retained legal title to the sow herd. The corporation periodically culled the sows and returned possession of the culled to the lessor for sale. The corporation transferred 220 pound replacement gilts to the lessors. The corporation was entitled to all pigs farrowed except for the replacement gilts. The Tax Court held that the lessors realized rental income on receipt of the replacement gilts at their fair market value at the time of the transfer and additional rental income when the sows at 270 pounds were reintroduced into the herd. The Eighth Circuit agreed that the replacement gilts were income to the lessors at the time significant incidents of ownership were acquired by the lessor. The value to the lessors of the feed and care for the gilts during their preparation for breeding was also rental income, although IRS had not pressed the latter point on appeal. Dudden v. Comm'r, 90-1 U.S.T.C. ¶ 50,027 (8th Cir. 1990), aff'd Dudden v. Comm'r, 91 T.C. 642 (1988).

SAVINGS BONDS. Under I.R.C. § 135 added by TAMRA 1988, beginning in 1990 the interest on EE series United States savings bonds is excludable from income if the proceeds of the bonds are used for higher education expenses. The bonds must be issued either to the taxpayer or the taxpayer and spouse and the taxpayer must be at least 24 years old on the date the bonds were issued. The amount of interest excludable is proportional to the amount of the bonds redeemed which is used for the higher education expenses and the interest exclusion is phased out for taxpayers with modified gross income above $60,000 (joint filers) and above $40,000 (single filers). Taxpayers are to use Form 8818 Optional Form to Report Redemption of College Savings Bonds to substantiate the interest exclusion. IR-90-2, January 2, 1990.

S CORPORATIONS.

INADVERTENT TERMINATION. The transfer of one shareholder's S corporation stock to a bank in satisfaction of personal indebtedness of the shareholder was ruled an inadvertent termination where the other shareholder purchased the stock back from the bank as soon as the termination of S corporation status was learned. Ltr. Rul. 8952068, Oct. 4, 1989.

The termination of an S corporation status resulting from the retention of Subchapter C earnings for over three years when the S corporation had more than 25 percent passive investment income was ruled an inadvertent termination where the S corporation reduced the earnings and profits to zero. Ltr. Rul. 8952033, Sept. 29, 1989.

The termination of an S corporation status from failure of the corporation to elect on its tax return that distributions of C corporation earnings were dividends and the failure of an S trust to distribute all trust income to the beneficiary was ruled inadvertent. Ltr. Rul. 8952047, Oct. 2, 1989.

S TRUSTS. A trust with five beneficiaries was split up by court order into five separate trusts, each with one beneficiary. The corpus of the trusts was stock in a corporation. The trusts were held to be qualified subchapter S trusts where all the income from the trusts was to be distributed not less than quarterly, trust corpus could only be distributed to the income beneficiary, the trust terminates by its terms or upon the death of the income beneficiary and upon termination of the trust, all trust assets are to be distributed to the income beneficiary. Ltr. Rul. 8951073, Sept. 28, 1989.

The trustees of a residual testamentary trust proposed to split the trust into four separate trusts, each with one beneficiary who would receive all the income from the S corporation stock held by each trust. IRS ruled that the trusts as divided would qualify as subchapter S trusts. Ltr. Rul. 8951015, Sept. 20, 1989.

Stock in an S corporation was transferred to three trusts. Because of ambiguities in the trust provisions regarding powers of appointment and trustee power to transfer trust assets, the trusts petitioned a state court to construe the ambiguous provisions. The state court construed the trusts to provide feed deduction. A cash method cattle rancher was required to deduct in the year of purchase prepaid feed costs and was not allowed to include the cost of the feed in the basis of the cattle when sold the following year. The prepaid expense was held to meet the four tests--(1) the expense was not a deposit, (2) the expense had a business purpose, (3) the deduction did not distort income and (4) the expense met the at-risk requirements of I.R.C. § 465. Crisp v. Comm'r, T.C. Memo. 1989-668.
only a testamentary power of appointment to the beneficiaries and to require current distribution of income to the beneficiaries even if the trust assets are transferred. Thus, IRS ruled that the trusts were qualified S trusts. Ltr. Rul. 8952014, Sept. 28, 1989.

An S corporation with S trusts as shareholders was held to have substantially complied with S corporation election requirements although the beneficiaries of the trusts failed to sign the election for the trusts. Ltr. Rul. 8952052, Oct. 3, 1989; Ltr. Rul. 8952055, Oct. 3, 1989.

SAFE HARBOR INTEREST RATES

February 1990
Semi-annual annual Quarterly Monthly
Short-term
AFR 7.98 7.83 7.75 7.71
110% AFR 8.80 8.61 8.52 8.16
120% AFR 9.62 9.40 9.29 9.22
Mid-term
AFR 8.06 7.90 7.82 7.77
110% AFR 8.88 8.69 8.60 8.54
120% AFR 9.70 9.48 9.37 9.30
Long-term
AFR 8.12 7.86 7.88 7.83
110% AFR 8.95 8.76 8.67 8.60
120% AFR 9.78 9.55 9.44 9.37

TAXPAYER. The two shareholders who in reality owned and operated a dairy farm were liable for payment of income tax on income generated by the operation. The sale of the dairy farm assets to a corporation owned by the shareholders and members of their families was held to be a sham because no consideration was received for the assets, no corporate formalities were followed, and the transaction had no business purpose and was entered into solely for tax avoidance purposes. Scherping v. Comm’r, T.C. Memo. 1989-678.

WITHHOLDING. Taxpayer who was president, treasurer and shareholder in corporation was a “responsible person” liable for payment of withholding taxes and penalties owed by corporation. In re Clements, 107 B.R. 767 (Bankr. Wyo. 1989).

MORTGAGES

FORM AND EXECUTION. A mortgage against farm property was held valid as to form and execution where (1) the mortgage identified the mortgagor as "Arnol and Mildred Shafer Livestock Farms, Inc." instead of the correct "Arnol and Mildred Shafer Farms, Inc.," (2) the corporate officers signed the mortgage in their individual capacities, and (3) the acknowledgement referred to the corporate officers as husband and wife and not as corporate officers. In re Arnol & Mildred Shafer Farms, Inc., 107 B.R. 605 (N.D. Ind. 1989), rev’d 102 B. R. 712 (Bankr. N.D. Ind. 1989).

PRODUCTS LIABILITY

STRICT LIABILITY. A supplier of fertilizer contaminated with herbicide cannot be held strictly liable where, under Colo. Rev. Stat. § 13-21-402(1) and (2), the supplier did not manufacture the fertilizer and the injured party failed to demonstrate that jurisdiction could not be obtained over the manufacturer. Deacon v. American Plant Food Corp., 782 P.2d 861 (Colo. App. 1989).

SECURED TRANSACTIONS

CONFLICTING SECURITY INTERESTS. A farm debtor was in default to FmHA on a secured loan for more than six months prior to planting a spring crop but a payment on the loan became due within six months of the planting. Another creditor loaned the debtor the funds used to plant the spring crop. The court held that the creditor had priority under U.C.C. § 9-312(2) only as to the amounts in default over six months before the spring planting but not as to the loan payment first due within six months of the planting. In re Smith, 890 F.2d 22 (7th Cir. 1989), aff’g unrep. D. Ct. dec. aff’g 82 B. R. 62 (Bankr. S.D. Ill. 1988).

STATE REGULATION OF AGRICULTURE

WAREHOUSES. The Commodity Credit Corporation (CCC) held title to rice forfeited by a producer in satisfaction of a CCC loan. The rice was stored in a warehouse and the CCC entered into a contract to sell the rice to the warehouse but before final payment was made and before title to the grain passed to the warehouse, the warehouse’s license was revoked and irrevocable letter of credit called to compensate for a grain shortage. The court held that CCC was a protected storer of grain in the warehouse under Ark. Code Ann. §§ 2-17-201 to 2-17-238 and could receive a portion of the recalled letter of credit fund. Reynolds v. Commodity Credit Corp., 780 S.W.2d 15 (Ark. 1989).

WORKERS' COMPENSATION

SCOPE OF EMPLOYMENT. A dairy farm laborer was killed when a tractor he was helping to move tipped over on him. The tractor was being moved in order to allow access by a fire department which was to burn down a barn the laborer was helping his employer tear down. Although the laborer was held to have participated in the demolition of the barn as part of his employment, the laborer was ruled not to have been killed in the course of employment because the moving of the tractor did not benefit the employer. Progressive Casualty Ins. Co. v. Marca, 783 P.2d 19 (Or. App. 1989).