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Cases, Regulations, and Statutes

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buyer’s income tax basis for the property even though a part of that amount may be cancelled in the event of the seller’s death. It appears that a SCIN is subject to the usual unstated interest rules (and original issue discount provisions where applicable) although that is not completely clear. Apparently, the buyer does not have discharge of indebtedness income from cancellation of the remainder of the obligation at the death of the seller. It would appear that SCIN transactions could be subject to the penalties for valuation overstatement (more than 150 percent over the correct amount).21

Conclusion. Self-cancelling installment notes may be preferred over private annuities, primarily because the seller can retain a security interest in the property conveyed. With private annuities, retention of a security interest causes the transaction to be treated as a sale.22 That is not a problem with SCINs; security interests can be retained in the same manner as with installment sales.

Another advantage is that the buyer under a SCIN is entitled to an interest deduction; an obligor may not claim an income tax deduction for interest in a private annuity.23

Finally, in the event of default by the purchaser, a seller under a SCIN can repossess the property under the special relief provisions of I.R.C. § 1038. Such is not possible with a private annuity because the property does not stand as collateral for the debt obligation as is required.24 Therefore, reconveyance of property by the obligor under a private annuity to the annuitant does not appear to come within the relief provisions of I.R.C. § 1038.

FOOTNOTES

3 GCM 39503, May 7, 1986.
6 See 6 Harl, supra note 1, § 48.03.
7 See 6 Harl, supra note 1, ch. 49.
8 See Ltr. Rul. 8906002, September 11, 1988 (sale of stock in exchange for 10-year promissory note was installment sale where seller had life expectancy of 12.1 years).
9 See notes 2-3 supra and accompanying text.
10 See I.R.C. § 7872. See also Blackburn v. Comm’r, 20 T.C. 204 (1953).
11 E.g., Ltr. Rul. 8804002, Sept. 3, 1987 (installment sale of stock to shareholder’s children at below market rate was gift unless and to extent purchase price included premium sufficient to increase effective interest rate); Ltr. Rul. 8512002, Nov. 28, 1984 (promissory notes for purchase of stock with interest rate of 2.355 percent below interest rate of equivalent United States Treasury obligations constituted gift unless purchase price of stock contained premium for reduced interest rate).
12 See Fox v. U.S., 88-1 U.S.Tax Cas. (CCH) ¶ 13,770 (W.D. Va. 1988) (transfer of real property in exchange for promissory note was gift to extent fair market value of property exceeded amount of note).
13 Ballard v. Comm’r, T.C. Memo. 1987-128, rev’d, 854 F.2d 185 (7th Cir. 1988) (sale of property at below market interest rate was not gift to extent interest rate below market rate; for federal gift tax purposes market rate of interest equal to interest rate established in regulations under I.R.C. § 483 which applied to all tax treatment of installment sales).
14 Krabbenhoft v. Comm’r, 94 T.C. No. 56 (1990) (farmland sold to sons at 6 percent; IRS used 11 percent to calculate gift).
16 See Banoff & Hartz, note 5 supra.
18 See 6 Harl, supra note 1, § 48.03[4].
19 See I.R.C. §§ 483, 1274. See 6 Harl, supra note 1, § 48.03[7].
21 See I.R.C. § 6659.
22 See Est. of Bell v. Comm’r, 60 T.C. 469 (1973); 212 Corp. v. Comm’r, 70 T.C. 788 (1978).
24 Treas. Reg. § 1.1038-1(a)(1).

CASES, REGULATIONS AND STATUTES

ANIMALS

CATTLE. The defendant had borrowed a bull for breeding and had placed the bull in a fenced area. The bull escaped from the fenced area into another pasture which was similarly fenced. The defendant did not capture the bull and place it back in the original fenced area and the bull escaped from the pasture. The bull was later captured in a fenced in state park by park rangers but the bull escaped again and caused an accident with a truck owned by the plaintiff. The court denied summary judgment for the defendant and held that actions of the state park rangers was not a sufficient intervening cause by law to absolve the defendant of any negligence which a jury may find. T. M. Doyle Teaming Co., Inc. v. Freels, 735 F.Supp. 777 (N.D. Ill. 1990).

HORSES. A summary judgment for the defendant was upheld in an action involving injuries received by the plaintiff when a horse provided to the plaintiff by the defendant fell while the plaintiff was riding it. The court held that the plaintiff failed to allege any specific evidence as to the cause of the horse’s fall other than to allege that the horse was sick. The court held that the doctrine of res ipsa loquitur by itself was insufficient because the
injury could have occurred without any negligence by the defendant. **Sarver v. Martyn, 555 N.Y.S.2d 402 (App. Div. 1990).**

**BANKRUPTCY**

**GENERAL**

**AVOIDABLE TRANSFER.** Payments were made to a creditor pursuant to an assignment of milk proceeds within 90 days before the debtor filed bankruptcy. The assignment was collateral for a security interest held by the creditor in the debtor’s accounts receivable; however, the creditor failed to file a financing statement after the initial financing statement expired and the creditor was held to be unsecured before the 90 days before the bankruptcy filing. Thus, the court held that payments made to the creditor under the assignment of milk proceeds were voidable transfers. **In re Field, 113 B.R. 185 (Bankr. W.D. Pa. 1990).**

**ESTATE PROPERTY.** The parents of the debtors had transferred farm land to the debtor but reserved a life estate in the farm with the power to exchange, convey or sell the entire fee interest in the property. After the debtors had filed bankruptcy the debtors’ parents transferred the land to their grandchildren, preserving a life estate with the power to exchange, convey or sell the entire fee interest. The court held that the debtors’ interest in the farm land became bankruptcy estate property upon the filing for bankruptcy and that the attempt to transfer the land was a violation of the automatic stay. The court also allowed the property to be sold with the proceeds apportioned between the life estate and the remainder interests. **In re Rose, 113 B.R. 534 (W.D. Mo. 1990).**

**EXEMPTIONS.** Husband and wife debtors each claimed an exemption in stock which the husband received by testamentary devise from a relative. The stock was issued in the husband’s name alone and was placed in a safe to which the wife had access. Dividends from the stock were placed in a joint checking account. The court held that the husband had not proved that the stock was owned by both spouses as tenants by the entirety and that the husband was the sole owner and only debtor entitled to an exemption. **In re Grubbs, 113 B.R. 201 (Bankr. W.D. Pa. 1990).**

Debtors were allowed a homestead exemption in a metal building originally constructed as an office but used by the debtors as a residence. **In re Brown, 113 B.R. 320 (Bankr. W.D. Tex. 1990).**

The husband and wife debtors were allowed to claim a homestead exemption in a mobile home owned jointly by them and the husband was allowed to claim the remainder of his homestead exemption in the land on which the home sat and which was owned solely by him. **In re Williams, 113 B.R. 399 (Bankr. S.D. Ohio 1990).**

After deducting the nonexempt claims of a mortgage and a lien for taxes, the debtors had equity in their homestead of $20,000 which was available for their Wisconsin homestead exemption of $40,000. Thus, a judicial lien against the homestead was avoidable as impairing the exemption. **In re Hazard, 113 B.R. 494 (W.D. Wis. 1990).**

After discharge was entered, a creditor moved to reopen the case to revoke the debtor’s discharge because the debtor had claimed a homestead exemption in a house in which the debtor did not live at the time of the bankruptcy. The creditor had knowledge of the debtor’s true residence before the cutoff date for objections to the discharge but did not raise an objection before discharge. The court denied the motion because there was no authority in the bankruptcy statute for revocation of the discharge where the creditor knew about the fraud before discharge but failed to object before discharge. **Powell v. First Nat’l Bank of Nashville, 113 B.R. 512 (W.D. Ark. 1990).**

The debtor’s conversion of pre-bankruptcy nonexempt assets to buy down their mortgage on their homestead was permitted. Debtors who each owned a car jointly with their daughter were entitled to exempt a one-half interest in the cars. The Kansas IRA exemption was held not preempted by ERISA. The Kansas insurance policy exemption covered the proceeds of a policy on the life of one of the debtors who died after filing for bankruptcy. **In re Chadwick, 113 B.R. 540 (Bankr. W.D. Mo. 1990).**

The debtor was involved in an accident and incurred substantial medical expenses. The debtor received a court approved insurance settlement as a result of the accident and purchased an annuity just prior to filing the bankruptcy case in which the medical expenses were the main claims against the estate. The creditors objected to the debtor’s exemption for the annuity as not purchased more than one year before bankruptcy filing and as fraud against creditors. The court held that the North Dakota annuity exemption statute, N.D. Cent. Code. § 28-22-03, does not require the annuity to have been purchased more than one year before bankruptcy filing. The court also held that the pre-bankruptcy purchase of the annuity while the medical bills remained unpaid was not a fraud against the medical creditors where the medical treatment was not given in expectation of payment from the insurance proceeds nor were the creditors ever promised payment from the insurance proceeds. **In re Smith, 113 B.R. 579 (Bankr. D. N.D. 1990).**

**FRAUDULENT TRANSFERS.** More than one year prior to filing bankruptcy, the debtor transferred substantial assets to an irrevocable trust in which the debtor’s wife was life time beneficiary and the children were remainder holders. A creditor who had made farm loans to the debtor argued that the transfers were avoidable fraudulent transfers because the debtor continued to receive the benefits of the property transferred to the trust within one year of filing bankruptcy. The court held that the creditor failed to prove the debtor enjoyed the benefits of the property within one year of bankruptcy. **In re Serafini, 113 B.R. 692 (D. Colo. 1990).**

**DEATH OF DEBTOR.** The court held that the debtor’s bankruptcy case could be reopened to litigate the validity of liens against the debtor’s real estate, although the debtor had died after confirmation of the plan but before the plan was completed. **In re Walters, 113 B.R. 602 (Bankr. D. S.D. 1990).**

**AUTOMATIC STAY.** A creditor with secured liens against the Chapter 12 debtors’ farm land was allowed relief from the automatic stay where the debtors had no equity in the land and would not be able successfully to reorganize. The court applied the standard of **In re Timbers of Inwood Forest Assoc., 808 F.2d 363 (5th Cir. 1987),** requiring that estate property be necessary for a successful reorganization and that a successful reorganization be a reasonable possibility. The debtors in this case were unable to demonstrate sufficient

CONFIRMATION OF PLAN. The debtor's Chapter 12 plan was not confirmed where (1) the plan provided for discharge of the debtor upon "substantial compliance," (2) plan allowed for selling of secured property without creditor retaining lien upon proceeds, and (3) interest rate for deferred plan payments did not equal market rate for similar loans. In re Gore, 113 B.R. 504 (Bankr. E.D. Ark. 1989).

A Bankruptcy Court's confirmation of a Chapter 12 plan was reversed and remanded because the Bankruptcy Court failed to provide sufficient findings of fact to support its confirmation of the plan. In re Cornelison, 901 F.2d 1073 (11th Cir. 1990).

DISMISSAL. The debtors attempted a so-called "Chapter 19" wherein they filed a Chapter 12 petition after discharge in a Chapter 7 case but before the closing of the Chapter 7 case; thus, leaving the Chapter 7 trustee as the only claim in the Chapter 12 case. The court dismissed the Chapter 12 case as filed in bad faith and in following the majority of opinions holding against simultaneous filings. In re Bodine, 113 B.R. 134 (Bankr. W.D. N.Y. 1990).

ELIGIBILITY. A farmer placed all farm land in an irrevocable trust with the farmer's children and grandchildren as beneficiaries. The trust owned no farm equipment and rented the farm land to the grantor, the beneficiaries and third parties. The court held that the trust was a land trust and not a business trust and was not eligible for Chapter 12 because the trust did not operate the farm or manage a farming operation. In re Ralph Faber Trust, 113 B.R. 599 (Bankr. D. N.D. 1990).

FEDERAL TAXATION

ALLOCATION OF PLAN PAYMENTS FOR TAXES. The Chapter 7 debtor, a corporation, and an officer of the corporation petitioned for allocation of payments to the IRS to trust fund claims before payment of other tax claims, including post-petition claims. Although the court acknowledged that it had the authority to allocate tax payments even in Chapter 7, the court denied the petition because the allocation would benefit only the officer of the corporation who had the power to decide which debts were paid before bankruptcy of the corporation and would decrease the taxes collectible by the IRS. In re Looking Glass, Ltd., 113 B.R. 463 (Bankr. N.D. Ill. 1990).

Payments made to the IRS during the course of a Chapter 11 proceeding were held to be voluntary and thus allocated first to employment withholding taxes. In re T.M. Products Co., 113 B.R. 765 (Bankr. S.D. Fla. 1990).

CLAIMS. The IRS was not allowed to amend its claim for taxes from unsecured to priority status more than one year after confirmation of the Chapter 13 plan where the error to properly identify the claim was made by the IRS, the debtors had made substantial payments under the plan, and allowance of the amendment would result in dismissal of the case because the debtors would not be able to make the plan payments. In re Garner, 113 B.R. 352 (Bankr. N.D. Ohio 1990).

The IRS was not allowed to amend its claim 22 months after the bar date to add highway use taxes or to increase the penalty for late payment of FUTA taxes from $60 to over $1,000. An IRS amendment was allowed for additional FUTA taxes and small claims for interest. In re Milan Steel Fabrications, Inc., 113 B.R. 364 (Bankr. N.D. Ohio 1990).

The court held that an IRS claim for taxes, interest and penalties which was partially unsecured would be considered, to the extent of the remaining debtor's equity, secured first as to the taxes then to the interest and penalties. U.S. v. Specialty Cartage, Inc., 113 B.R. 484 (N.D. Ind. 1990).

FILING OF RETURN. The court held that testimony of a taxpayer was inadmissible to prove that the taxpayer mailed a filled out return to the IRS where the return was not sent by registered mail. In re Brookman, 90-2 U.S. Tax Cas. (CCH) ¶ 50,325 (Bankr. M.D. Fla. 1990).

POST-PETITION PENALTIES AND INTEREST. The debtor was held liable for post-petition interest on pre-petition tax liabilities which would be fully paid by the bankruptcy estate. The court held that the debtor was not liable for post-petition penalties for pre-petition tax liabilities which would be fully paid by the bankruptcy estate. In re Woodward, 113 B.R. 680 (Bankr. D. Or. 1990).

TAX COURT JURISDICTION. The Tax Court held that it had no jurisdiction to determine whether or to what extent the taxpayer's income tax liability was discharged in a prior bankruptcy case, although it had jurisdiction to determine the extent of an income tax deficiency which was a claim in the bankruptcy case. The reopening of the bankruptcy case was held not to stay the Tax Court proceeding on the deficiency. Terrell v. Comm'r, T.C. Memo. 1990-323.

TAX LIENS. Although the debtors' liability for the underlying taxes was discharged in bankruptcy, the IRS tax lien against their property was not released and remained effective against the property. In re Isom, 901 F.2d 744 (9th Cir. 1990), aff'd 95 B.R. 148 (Bankr. 9th Cir. 1989).

FEDERAL AGRICULTURAL PROGRAMS

Note: The Agriculture Decisions cited below were just published by USDA although some of the decisions are several years old.

ALIEN AGRICULTURAL WORKERS. Alien farm workers challenged the USDA's definition of vegetables to exclude sugar cane under the Seasonal Agricultural Workers program. The court held that the USDA's distinctions between sugar cane and other vegetables was reasonable. Wint v. Yeutter, 902 F.2d 76 (D.C. Cir. 1990).

BRUCELLOSIS. The respondent was charged with interstate shipment of postparturate cows without a certificate showing a negative test for brucellosis. The respondent purchased the cows in New Mexico but the seller paid for and arranged for the brucellosis testing of the cows, paid for the shipping of the cows to Texas, and refunded the purchase price of one of the cows which had died. The cows were shipped before the results of the tests were known or indicated on the Certificate of Livestock Inspection. The respondent argued that the title to the cows did not pass until the cows reached Texas and were accepted. The ALJ held that the respondent
acquired title to the cows when the purchase price was paid in New Mexico and was liable for the shipment before the test results were placed on the Certificate of Livestock Inspection. The respondent was fined $2,000. *In re Stine*, 47 Agric. Dec. 835 (1988).

**CROP INSURANCE.** The FCIC has added the Sugarcane Endorsement to the general crop insurance regulations, effective for the 1991 and succeeding crop years. 55 Fed. Reg. 25954 (June 26, 1990).

**FRUITS.** The AMS has adopted as final amendments to the container marking requirements for Max-Red Bartlett pears grown in California and to the grade requirements for such pears. 55 Fed. Reg. 25956 (June 26, 1990).

**MILK.** The petitioner was a milk handler which owned a pool supply plant in Delaware which supplied milk processing plants in Florida and New Jersey. Under the Florida marketing order, the petitioner was allowed a location adjustment of $1.59 per hundredweight of milk on the price paid for milk delivered to the pool supply plant by producers. However, some of the milk so priced was shipped to New Jersey. The Agricultural Marketing Service amended the milk marketing order for the pool supply plant to set the location adjustment for milk which was shipped to New Jersey according to the miles between the pool plant and the New Jersey processing plant. The petitioner challenged the amendment by arguing that the lower location adjustment for milk which was shipped to New Jersey was a surcharge and created a multiple price for milk at the pool supply plant. The Judicial Officer adopted the Administrative Law Judge's decision that the amendment was proper and necessary to protect the fairness of the pricing of milk within the marketing order areas. The amendment was necessary to prevent a pool supply plant from using its large location adjustment for shipments to a distant processing plant to unfairly reduce the cost of milk shipped to a closer processing plant in another marketing area. *In re Cumberland Farms Food Stores, Inc.*, 47 Agric. Dec. 809 (1988).

The AMS has adopted as final regulations governing the announcements of Class II milk prices on the 15th of the month preceding the month in which the prices will be effective. 55 Fed. Reg. 25962 (June 26, 1990).

The AMS has adopted as final regulations amending the Upper Midwest marketing order for milk by (1) revising the pooling requirements; (2) providing discretionary authority for the market administrator to make changes in the shipping requirements; and (3) changing the administrative assessment on pooled milk. 55 Fed. Reg. 26634 (June 29, 1990).

**ONIONS.** The AMS has announced proposed rules which change the definition of pearl onions to increase the maximum size from 1 1/2 to 1 3/4 inches. The reporting of shipments of such onions has been decreased to monthly. 55 Fed. Reg. 27825 (July 6, 1990).

The AMS has announced proposed rules which base the size and quality requirements for imported onions on the requirements for South Texas Onions instead of Idaho-Eastern Oregon onions. 55 Fed. Reg. 28049 (July 9, 1990).

**PACKERS AND STOCKYARDS ACT.** The respondents were two corporations operating as meat and poultry brokers and an individual who solely owned and controlled one of the corporations and who owned 51 percent and controlled the other corporation. Because of the individual's ownership and control of the corporations, the individual was also found to be a packer under the PSA and liable for bribery payments made by the corporations to employees of meat packing and retail food stores in return for contracts for meat and poultry products. Because the individual was already convicted of criminal mail fraud and required to make restitution, the ALJ issued a cease and desist order. *In re Associated Food Brokers, Inc.*, 47 Agric. Dec. 855 (1988).

In a reparation case, the complainants contended that the new rules were cashed, funds had been deposited. The respondent's defense that no violation occurred because no customer was injured by the unlawful practice was rejected by the administrative law judge. *In re Rodman*, 47 Agric. Dec. 885 (1988).

The parties to this reparation action had contracted for the sale of cattle. The sellers were two minor daughters whose father lent them the money to purchase the cattle for the sale. Although the daughters were named as the sellers, their father provided all the money and performed all the tasks connected with the sale. The buyer timely rejected the cattle as not conforming with the contract terms and purchased substitute cattle at a lesser price. The buyer had agreed to purchase at the contract price the cattle tendered which did conform to the contract but the father refused. The father attempted to tender conforming cattle but did so by telegram to the buyer's home one business day before the offered tender date although the father knew the buyer was away from home. After the conforming tender date, the minor daughters disaffirmed the contract and claimed the down payment as damages. The judicial officer held that the tender of conforming cattle was ineffective because untimely and that the father was the real party in interest in the contract such that the disaffirmance of the contract by the daughters was also ineffective. The judicial officer also held that because the buyer was able to purchase substitute cattle at a lesser cost, the buyer was not entitled to any damages under the liquidated damages clause of the contract, but the buyer was entitled to the return of the down payment. *McCormick v. Stoiber*, 47 Agric. Dec. 933 (1987).

In a reparation case, the complainants had contracted with the respondents for the respondents to sell cattle at auction on a certain day unless a good price was not obtainable, in which case the cattle were to be held for sale until the next day. The cattle were sold on the first day under what the evidence showed was their market price
on the next day. The judicial officer awarded the complainants the amount of the difference between the price the cattle were sold for and the market value of the cattle on the next day. **Moody v. Producers Livestock Marketing Ass'n, 47 Agric. Dec. 940 (1989).**

**PERISHABLE AGRICULTURAL COMMODITIES ACT.** In a reparation case, the complainant attempted to sell potatoes to the respondent but many of the shipments failed to meet the contract terms after federal grading inspections. After the potatoes were rejected as nonconforming, the buyer agreed to sell the potatoes for the seller on commission. However, the buyer either sold the potatoes at a lower grade or dumped them as unsellable. The judicial officer held that the buyer failed to "exercise reasonable care and diligence" in not promptly selling the potatoes and in dumping the potatoes too quickly. **East Coast Potato Distributors, Inc. v. Spiridis, 47 Agric. Dec. 947 (1988).**

**PESTICIDES.** Commercial pesticide applicators challenged a city ordinance requiring notification of application of pesticides by users and property owners and an ordinance enforcing the state and federal pesticide laws. The court held the first ordinance valid and not pre-empted by FIFRA. **Coparr, Ltd. v. City of Boulder, 735 F. Supp. 363 (D. Colo. 1989).**

**POTATOES.** The AMS has issued proposed rules establishing diameter measurements for scoring hollow heart and other internal defects for the U.S. Standards for Grades of Potatoes. **55 Fed. Reg. 28032 (July 9, 1990).**

**RAISINS.** The AMS has adopted as final regulations establishing an identification and surveillance system for raisins produced from grapes grown outside of California. **55 Fed. Reg. 28016 (July 9, 1990).**

**FEDERAL ESTATE AND GIFT TAX**

**GENERATION SKIPPING TRANSFERS.** The trustees of two trusts which were generally identical in provisions proposed to merge the trusts into one trust. The trusts were irrevocable on September 25, 1985. Because one of the trusts had additional requirements for a beneficiary to receive income from that trust, where a beneficiary did not meet those requirements, the merged trust would withhold a percentage of the income based on the percentage of the restricted trust assets to the total merged trust assets on the date of the merger. IRS ruled that the merged trusts would not be subject to the generation-skipping transfer tax. **Ltr. Rul. 9023007, Feb. 28, 1990.**

**GIFTS.** Under the decedent's will, property was bequeathed to the surviving spouse for life with the remainder to pass to the children surviving the death of the surviving spouse. If no children survive the surviving spouse, the property passes to the surviving spouse's estate. In a family settlement, the children received a remainder interest without the condition that they surviving the surviving spouse. IRS ruled that the settlement resulted in a gift of the surviving spouse's remainder interest to the children valued using the actuarial factor of $.00285. The gift was not eligible for the annual exclusion. **Ltr. Rul. 9023042, March 9, 1990.**

**GROSS ESTATE.** The surviving spouse had received a lifetime interest in a trust from the decedent. As part of a settlement of a court challenge to the trust provisions, the surviving spouse released her testamentary general power of appointment. IRS ruled that under the trust provisions, the surviving spouse was not required to release her general power of appointment, and therefore the surviving spouse did not receive any consideration for the release of the power of appointment. IRS ruled that the trust corpus was includible in the surviving spouse's gross estate and that no deduction would be allowed for the property transferred by the released power of appointment. **Ltr. Rul. 9023034, March 8, 1990.**

**INCOME IN RESPECT OF DECEdent.** On the date of the decedent's death a real estate contract was outstanding for the sale of the decedent's property. The contract provided a 45 day mortgage commitment requirement, which had not been met at the time of the decedent's death. The property was sold under the contract after the decedent's death. IRS ruled that the gain from the sale of the property was income in respect of decedent. **Ltr. Rul. 9023012, March 6, 1990.**

**MARITAL DEDUCTION.** The decedent spouse bequeathed property in trust for life to the surviving spouse with income to be distributed at least annually and with the surviving spouse having the power to require the conversion of unproductive property to productive property. IRS allowed the estate to make a QTIP election as to a portion of the property in the trust. **Ltr. Rul. 9023015, March 15, 1990.**

The decedent as the surviving spouse had executed mutual wills with each providing for the survivor to receive all marital property but bequeathing the property to their children upon the death of the last of the spouses to die. IRS ruled that under Texas law, such mutual wills give the surviving spouse a defeasible or conditional fee interest in the property, allowing the surviving spouse to transfer the property but only to third parties. Because the surviving spouse's interest was defeasible, the property passing under the decedent's will was not eligible for the marital deduction, even as QTIP property. **Ltr. Rul. 9023004, Feb. 20, 1990.**

The IRS has extended the period for the settlement procedures for QTIP trusts which are affected by **Est. of Howard v. Comm'r to December 31, 1990.** **55 Fed. Reg. 26803 (June 29, 1990).**

The decedent's will bequeathed to the surviving spouse a life estate in trust. The estate's executor marked the box for "no" on Form 706 indicating no election to treat the trust interest as QTIP property but listed the property in Schedule M as property for which a marital deduction was claimed, although without any indication that the property was to be treated as QTIP. The court granted summary judgment against the estate because the return provided no indication of intent to make an election to treat the trust interest as QTIP. **Harry C. Spohn Est. v. U.S., 90-2 U.S. Tax Cas. (CCH) ¶ 60,027 (N.D. Ind. 1990).**

**SAVINGS BONDS.** Savings bonds were owned by the decedent and a survivor. The decedent did not report the increases in the redemption price as income and the bonds were not mature at the decedent's death. IRS ruled that the surviving owner of the bonds would have to report the increase in the redemption price occurring during the life of the decedent either upon an election to do so or when the bonds
FEDERAL INCOME TAXATION

BAD DEBTS. Cash advances made to a corporation were not deductible as business bad debts where the shareholders of the corporation failed to demonstrate a bonafide debtor-creditor relationship, the shareholders expected repayment from corporate net income, and the initial capitalization of the corporation was inadequate. Also, the shareholders' guarantees of the corporation's expenses were not deductible by the shareholders as business expenses where the shareholders made the guarantees as investors and the shareholders did not operate as separate trades or businesses. Morris v. Comm'r, T.C. Memo. 1990-306.

C CORPORATIONS

CONSTRUCTIVE DIVIDENDS. Payments made by a corporation to the children of a controlling shareholder and payments on debts owed by the children were held to be constructive dividends where the corporation failed to provide evidence of services rendered by the children or evidence of a business purpose for the loan payments. Broad v. Comm'r, T.C. Memo. 1990-317.

INFORMATION RETURNS. IRS has issued proposed regulations implementing I.R.C. § 6043(c) governing the filing of informational return Form 8820 by a corporation when control of the corporation is transferred or the corporation has substantial changes in capital structure. The return is not required if the value of the stock acquired during the year before control is acquired is less than $10 million or the acquisition occurs in the first year after the first year of issuance the stock by the corporation. A substantial change in capitalization occurs in any distribution or exchange of stock valued at $10 million or more. The regulations are effective for transactions occurring after March 30, 1990. 55 Fed. Reg. 27648 (July 5, 1990).

EMPLOYEES. Workers who provided services as farm laborers and heavy equipment operators in the planting and harvesting of agricultural products were employees where the employer had the right to control the performance of the services and provided the tools and equipment and where the laborers reported daily to the employer and did not have an investment in the providing of the services. Ltr. Rul. 9023018, March 7, 1990.

INFORMATION RETURNS. The IRS has issued a notice of the changes to the penalties for failure to file and the filing of incorrect or incomplete information returns made by the Revenue Reconciliation Act of 1989. The penalties are $15 if the failure to comply is corrected within 30 days of the due date of the return and $30 if the failure is not corrected within 30 days after the due date for the return. The penalties may be waived on up to the greater of 10 returns or 1 percent of the total returns required if the returns are timely filed and corrected before August 1 (October 1 for 1990). Notice 90-45, I.R.B. 1990-28, July 9, 1990.

INSTALLMENT REPORTING. The taxpayer made an installment sale of a business and elected to report the gain on the installment method. Because of a change in the income tax rates and the acceleration of recognition of gain from the resale of the business, the taxpayer wanted to change the election to elect out of installment reporting. IRS ruled that neither of these reasons was sufficient to allow the revocation of the original election. Ltr. Rul. 9023010, March 5, 1990.

INCOME TAXATION

INTEREST. The taxpayers purchased a residence with a short term loan with a third year balloon payment. The short term loan was refinanced with a long term mortgage with which they paid off the short-term loan. The court held that points paid on the long-term mortgage were deductible as incurred with respect to a purchase of a principal residence. Huntsman v. Comm'r, 90-2 U.S. Tax Cas. (CCH) ¶ 50,340 (8th Cir. 1990), rev'g 91 T.C. 917 (1988).

PARTNERSHIPS

UNREALIZED RECEIVABLES. As part of a withdrawal agreement, a partner received an amount attributable to fees earned for legal services in the sale of a client's property. The partner argued that the amount was taxable as capital gain as payment for the partnership interest sold back to the partnership. The court held that because the amount was earned as a fee for services as a partner, the amount was an unrealized receivable taxable as ordinary income under I.R.C. § 751(c). Ware v. Comm'r, 90-2 U.S. Tax Cas. (CCH) ¶ 50,342 (2d Cir. 1990), aff'd T.C. Memo. 1989-165.

RE-ELECTION. A corporation was allowed to re-elect S corporation status within two years of a revocation of an S corporation election where the previous revocation was effective as of the date of the first election. Ltr. Rul. 9023032, March 8, 1990.
SHAREHOLDER BASIS. The two shareholders of an S corporation personally guaranteed loans made by the corporation used to purchase real property. The court held that the shareholders could not increase their basis in their stock by the amount of the guarantees. The shareholders had argued that the loans to the corporation were in substance loans to them, but the court held that the form of the transactions demonstrated that the loans were made to the corporation and not to the shareholders. Harris v. U.S., 90-2 U.S. Tax Cas. (CCH) ¶ 50,341 (5th Cir. 1990).

TERMINATION. A corporation's S corporation status was ruled inadvertently terminated where the corporation formed a subsidiary in another country and the corporation cured the termination immediately upon learning of the termination. Ltr. Rul. 9023088, March 14, 1990.

TRUSTS. Three trusts, each with one income beneficiary, held S corporation stock. The "net income" of the trusts was to be distributed at least quarter-annually and one-half of the corpus was to be distributed when the beneficiaries became age 25 and 30. IRS ruled that so long as the term "net income" was defined to mean "income" as defined in I.R.C. § 643(b), the trusts were qualified subchapter S trusts. Ltr. Rul. 9022006, Feb. 27, 1990.

ATTACHMENT OF SECURITY INTERESTS. The defendant agreed to feed some livestock owned by the plaintiff in exchange for the calf crop from the cattle. The defendant agreed to compensate the plaintiff for any loss exceeding two percent of the cattle with replacements from the offspring calves. The defendant had granted a security interest in the defendant's cattle to the FmHA which was perfected. During the winter, 51 cattle were lost and only 25 calves were produced; thus, under the agreement, the plaintiff was owed all of the calves. The court, in a rather sketchy opinion, held that the FmHA security interest attached to the calves because the defendant had a sufficient interest in the calves. Pleasant View Farms, Inc. v. Ness, 455 N.W.2d 602 (S.D. 1990).

FEDERAL FARM PROGRAM PAYMENTS. A creditor had a security interest in the farm debtor's accounts, contract rights and intangibles. The debtor received federal farm program deficiency and other payments after the secured loans were made by the creditor, except for two small advances for fuel and crop insurance. The court held that the federal farm program payments were not subject to the pre-existing security interests of the creditor under the anti-assignment regulations governing the program payments except as to the advances for fuel and insurance. Matter of Curry, 113 B.R. 546 (D. Neb. 1990).

HOMESTEAD EXEMPTION. The debtor lived on an 106 acre farm which the debtor farmed part-time. The debtor sought exemption of 40 acres under Wis. Stat. § 990.01(13), arguing that the 40 acres was necessary for the debtor to continue making a living from farming. The court held that the exemption amount encompassed only so much land as was necessary for use of the dwelling as a home and upheld the trial court allowance of a one acre exemption which allowed for the land to be used for a septic system. Farm Credit Bank of St. Paul v. Gibson, 455 N.W.2d 674 (Wis. Ct. App. 1990).

CITATION UPDATES

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