Cash Renting After Death: A Problem for Installment Payment of Federal Estate Tax?

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amount is scheduled to be paid in October, as the second half of the 2003 crop direct payment. Furthermore, the first installment of the 2004 crop direct payment will be received in December, again for the same dollars as the 2003 payments.

Counter Cyclical Payments

Counter cyclical payments (CCP) are less predictable. They depend on the national season average price for each crop. For corn and soybeans this price is the weighted average cash price paid from September through August. Soybean prices for the 2002 crop have been high enough that there will be no counter cyclical payment made. It is possible but not likely that there will be a small payment for corn.

Monthly corn and soybean prices, along with estimates of the percentage of the crop that is marketed each month, is presented in Table 1. Estimates of the simple average and monthly average prices so far this year are shown at the bottom.

For the 2002 corn and soybean crops, USDA price projections through July 2003 indicate that marketing year average prices will be above the level that will generate CCPs as shown in Table 2.

If the USDA projects a season average market price below $2.32 for corn or below $5.36 for soybeans for next year’s (2003) crop, an advance counter-cyclical payment may be made. Up to 35 percent of the expected counter-cyclical payments will be paid in October and again in February, with the balance payable next September.

Loan Deficiency Payments

Loan deficiency payments were not available for the 2002 crop. It remains to be seen if they will be available for the 2003 crop. Any time that the posted county price in a county is below the county loan rate, a loan deficiency payment or marketing loan can be requested on bushels that have been harvested but not sold.

### Table 2. Possible CCPs for 2002 Crop Corn and Soybean

<table>
<thead>
<tr>
<th></th>
<th>Corn</th>
<th>Soybean</th>
</tr>
</thead>
<tbody>
<tr>
<td>Breakeven Price</td>
<td>2.32</td>
<td>5.36</td>
</tr>
<tr>
<td>Simple Avg. Price*</td>
<td>2.35</td>
<td>5.62</td>
</tr>
<tr>
<td>Possible CCP</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Est. Weighted Avg. Pr.*</td>
<td>2.32</td>
<td>5.52</td>
</tr>
<tr>
<td>Possible CCP</td>
<td>0</td>
<td>0</td>
</tr>
</tbody>
</table>

*Approximate simple and weighted national average prices (Sept. through July)

Cash Renting After Death: A Problem for Installment Payment of Federal Estate Tax? *

by Neil E. Harl, Charles F. Curtiss Distinguished Professor in Agriculture and professor of Economics

Ordinarily, land that is cash rented after death which is subject to an election to pay federal estate tax in installments is considered “distributed, sold, exchanged, or otherwise disposed of” and the deferred tax is accelerated if the value of assets involved (plus all previous distributions, sales or disposition of assets after death) equals 50 percent or more of the date-of-death value of the interest in a closely-held business which qualified for installment payment. However, a recent private letter ruling has allowed cash renting of farmland after death without acceleration being triggered.

General rule on cash renting

The rule is well established that assets which are cash rented after death cease to be an “interest in a closely-held business” which is necessary in order to maintain continuing eligibility for installment payment of federal estate tax and to avoid acceleration. Indeed, a 1983 private letter ruling specifically so held. It has generally been thought that, to avoid acceleration, it was necessary for the lessor of the asset or assets to be bearing the risks of

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production and the risks of price change with evidence that there was some involvement in management, albeit short of material participation.

The 2003 Ruling

In Ltr. Rul. 200321006, the Internal Revenue Service ruled that a cash rent lease did not accelerate the deferred tax or count against the 50 percent that would lead to acceleration. In the facts of that ruling, a farmer who had been operating as a sole proprietorship and who had been actively involved in farming operations until the date of death, left a will leaving a majority of the decedent’s assets to a residuary trust with three primary beneficiaries. The beneficiaries were two sons and a third individual (unrelated) who had been raised by the decedent. The decedent’s will authorized the trust to lease portions of the land to the trust beneficiaries provided the beneficiaries were to operate the farm personally. The will further provided that, in the event the trust beneficiaries (individually or in combination) were the sole owners of the farming entity, a lease to the entity was authorized. Accordingly, the trust entered into cash rent leases with limited liability companies set up specifically by two of the beneficiaries.

Ordinarily, such post-death cash rent leases have been the occasion for acceleration of federal estate tax. However, in this instance the limited liability companies had single owners and, therefore, were considered disregarded entities. As a result, the rental arrangement was considered a lease directly to the respective heir and did not result in acceleration. The arrangement was viewed as not materially altering the business.

The ruling cites to Rev. Rul. 66-62 as authority. That ruling involved the change from a corporation to an unincorporated form with IRS holding that the transformation did not materially alter the business.

Lease by Residuary Trust

The interesting question is why the ruling did not discuss the fact situation as involving a cash rent lease by the residuary trust. The rule is well established that a cash rent lease, even to a family member of the decedent, fails the test of being a business. Thus, a cash rent lease directly to a family member as heir would ordinarily be expected to trigger acceleration. That literally is the result of the characterization of the arrangement as a cash rent lease to a disregarded LLC.

The important point is that it is the lessor who is expected to maintain the assets involved as a business. As the lessor, the residuary trust seemingly failed to meet that requirement.

There has been an exception, at least in the pre-death qualification period, for trusts that were grantor trusts which was not the case in the 2003 letter ruling. Obviously, a residuary trust is not a grantor trust. It is noted that the residuary trust in question had three beneficiaries, only one of which was the lessee. Thus, it would appear that the trust was no longer meeting the “business” requirement in the period during which acceleration could occur.

In Conclusion

Care is needed for all post-death leasing, entity transformations or other distributions, sales or dispositions. The latest ruling should be used carefully as authority. It provides only limited authority for post-death cash rent leasing of assets subject to an election to pay federal estate tax in installments. The safe approach is to assure that the post-death owner of the assets, including a trust, meets a “business” test during the entire period during which acceleration could occur.