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Cases, Regulations, and Statutes

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CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr

ADVERSE POSSESSION

EXCLUSIVE USE. The disputed strip of land was between parcels owned by two hunting clubs. The disputed land was included in the plaintiff's title description as demonstrated by a survey performed more than 10 years before the plaintiff brought suit to quiet title. Both parties provided evidence of use of the disputed area by hunters. Both owners placed deer stands in the disputed area and both removed stands placed by the other party. Although a barbed wire fence existed in the disputed area, the fence had not been maintained by either party and was not continuous. The court held that the defendant failed to prove exclusive use of the disputed area; therefore, title remained with the plaintiff as record title holder. **Riverland Plantation Partnership v. Klingler**, 2006 Miss. App. LEXIS 848 (Miss. Ct. App. 2006).

BANKRUPTCY

GENERAL

INSURANCE PROCEEDS. Prior to filing for bankruptcy, the debtor had been receiving disability insurance although the debtor was employed full time. The debtor filed for Chapter 7 in May 2000 and four days later ceased employment with an insurance company. The IRS filed claims for pre-petition taxes. One year later, the debtor filed a claim with the insurance company under a disability insurance policy and began receiving two payments under the two disability insurance policies. The second insurance policy benefits were paid retroactive to the date that the debtor ceased employment. The court held that the insurance benefits were included in the bankruptcy estate, were subject to a tax lien filed by the IRS but were exempt under Indiana law, Ind. Code § 27-8-3-23(b), only to the extent necessary for the "reasonable comforts of life," determined by the court to be \$6,000 per month. **In re Stinnett**, 2006-2 U.S. TaxCas. (CCH) ¶ 50,587 (7th Cir. 2006).

CHAPTER 12

INCOME TAX. The IRS has issued procedures for requesting determination of the income tax effects of a proposed Chapter 12 bankruptcy plan. See article by Harl and Peiffer in this issue. **Rev. Proc. 2006-52**, 2006-2 C.B. 995.

FEDERAL TAX

ALLOCATION OF TAX PAYMENTS. This case involved three consolidated Chapter 11 cases involving three brothers who had been part of a performing musical group. The trustee made several payments to the IRS for prepetition tax claims for all three debtors; however, the allocation of the funds to the taxes owed by the individual debtors was not equally allocated and one debtor objected to the unequal allocation. The court held that, as

consolidated bankruptcy debtors, the three debtors became jointly and severally obligated on the tax claims in the consolidated case. However, a substantial portion of the payments made to the IRS were not clearly explained by the IRS and the court remanded the case for accounting for those unclear payments. The case is designated as not for publication. **United States v. Isley**, 2006-2 U.S. Tax Cas. (CCH) ¶ 50,588 (3d Cir. 2006), *aff'g unpub. dec.* 2005-1 U.S. Tax Cas. (CCH) ¶ 50,115 (D. N.J. 2005).

FEDERAL AGRICULTURAL PROGRAMS

KARNAL BUNT. The APHIS has issued interim regulations removing areas in Maricopa and Pinal counties in Arizona and Archer, Baylor, Knox, McCulloch, San Saba, Throckmorton, and Young counties in Texas from the list of regulated areas subject to quarantine for Karnal bunt. **71 Fed. Reg. 67432** (Nov. 22, 2006).

PEANUTS. The CCC has announced that inventoried farmer-stock peanuts are available for sale as unrestricted use on November 29, 2006 on the internet at <http://www.theseam.com>. **71 Fed. Reg. 68529** (Nov. 27, 2006).

FEDERAL ESTATE AND GIFT TAXATION

GENERATION SKIPPING TRANSFERS. The grandparents of the current nine beneficiaries of a trust established the trust before September 25, 1985 and made no additions to the trust since that date. The current beneficiaries petitioned a state court to reform the trust into nine separate trusts, retaining the same trust provisions except that the original trust property was split equally among the new trusts. The remainder beneficiaries remained the same. The IRS ruled that the division of the trust would not cause the trust or the resulting trusts to be subject to GSTT. **Ltr. Rul. 200647022**, June 23, 2006.

IRA. The taxpayer's predeceased spouse had owned an IRA which had a trust as primary beneficiary. The taxpayer was the income beneficiary of the trust and had the power to require distributions of all property and income from the trust. The IRA funds were distributed to the trust at the request of the taxpayer but the funds were not transferred to the taxpayer's IRA because of a misunderstanding by the company holding the deceased spouse's IRA. The IRS ruled that the transfer of the IRA to the trust and then to the taxpayer's IRA was a qualified non-taxable rollover. The IRS stated that the trust would be ignored as part of the transfer

FEDERAL INCOME TAXATION

because the taxpayer had the right to require distribution of property from the trust. The IRS also waived the 60-day rollover requirement due to the misunderstanding which caused a delay in the transfer of the funds to the taxpayer's IRA. **Ltr. Rul. 200646026, Aug. 21, 2006.**

REFUND. The decedent's executor requested an extension of time to file the estate tax return and made a payment of \$140,000 in estimated taxes with the extension request. The extension was granted; however, the executor did not file the estate tax return for more than three years. The filed return claimed no estate tax due, which was not denied by the IRS, but the IRS denied a request for a refund as made more than three years after a payment of taxes. The estate argued that the three year limitation on refund requests did not apply because the \$140,000 was a deposit. The IRS argued that, under *Rev. Proc. 2005-18, 2005-13 C.B. 798*, a remittance would be designated a deposit if accompanied by a written statement that the remittance was a deposit. The court noted that the \$140,000 was paid before the executor made any determinations as to the possible estate taxes owed and that *Rev. Proc. 2005-18* also provided that remittances are to be considered deposits if made before the IRS informs the taxpayer in writing of any tax liability. Thus, the court held that the \$140,000 was a deposit not subject to the three year limitation on refund requests. **Blom v. United States, 2006-1 U.S. Tax Cas. (CCH) ¶ 60,527 (E.D Penn. 2006).** After this decision, the IRS filed a request for an entry of judgment for \$140,000 without interest. The estate objected, arguing that the judgment should include interest. Under I.R.C. § 6611(a) interest is allowed for repayment of an overpayment of tax. The court cited precedent that payment includes amounts paid on account of a verified return or in response to an assessment by the IRS. Under these concepts, the deposit made by the estate was not a payment because it was made before any return was filed or assessment made. The court also cited *Rev. Proc. 2005-18, 2005-1 C.B. 798* which states that no interest will be paid for repayment of deposits. The court entered judgment for the estate for \$140,000 without interest. **Blom v. United States, 2006-2 U.S. Tax Cas. (CCH) ¶ 60,533 (E.D Penn. 2006).**

TRUSTS. The taxpayer created a trust for the benefit of the taxpayer. The trust had a distribution committee consisting of the taxpayer and two members of the taxpayer's family. The distribution committee had the authority to distribute trust income and principal to the taxpayer or to anyone else. The trust provided that the taxpayer had a limited testamentary power of appointment over trust property and that the taxpayer could release the power or make the power more limited as to beneficiaries at any time. The IRS ruled that transfers to the trust were not completed gifts because of the power of appointment. The IRS ruled that the family members on the distribution committee did not have a power of appointment over trust property because distributions could not be made without the taxpayer's consent. In addition, the IRS ruled that no items of income, deduction or credit for the trust were includable in the taxpayer's income, deductions or credits. **Ltr. Rul. 200647001, Aug. 7, 2006.**

ALTERNATIVE MINIMUM TAX. The taxpayers, husband and wife, owned an S corporation which was a member of a limited liability company. The taxpayers received tax credits passed through these entities. The taxpayer had alternative minimum tax liability which limited the amount of the credit. The taxpayers failed to properly calculate the limit on the tax credit. In challenging the IRS recalculation of the allowed credit, the taxpayers argued that either I.R.C. § 26(a)(2), § 38(c)(4) or § 55(e)(1) applied to allow the full tax credit. The court held that these sections either did not apply to the tax credit sought or to the taxpayers. **Holloway v. Comm'r, T.C. Memo. 2006-256.**

CORPORATIONS.

JURISDICTION. The taxpayer was the sole shareholder of a corporation which was dissolved in 1996 under Illinois law for failure to file an annual report and to pay the annual franchise tax. The corporation untimely filed its 1996 return in 2001, more than five years after the dissolution. Under Illinois law, a dissolved corporation cannot bring an action more than five years after dissolution. In 2004 the IRS filed a notice of deficiency as a result of disallowed deductions on the 1996 return. The corporation filed a petition challenging the deficiency but the petition was dismissed for lack of jurisdiction. The taxpayer argued that the 2004 notice of deficiency was the basis for jurisdiction because the IRS should not be able to avoid a review of the notice by filing the notice after the state five year limitation period. The court noted that Congress had expressly allowed such practice in I.R.C. § 6212(b)(1) which allowed the filing of notices even if the corporation had terminated its existence. The taxpayer also sought jurisdiction as a shareholder filing on the corporation's behalf. The court held that the taxpayer/shareholder would have standing to challenge the deficiency only after the IRS filed a notice of transferee liability, which had not yet been done in this case. **L.V. Castle Investment Group, Inc. v. Comm'r, 2006-2 U.S. Tax Cas. (CCH) ¶ 50,589 (11th Cir. 2006).**

OUTSIDE DIRECTOR The taxpayer was a director of a corporation which belonged to a trade association. The taxpayer was not an officer of the corporation and received compensation only for service as a director. The taxpayer was also a less than five percent partner in a law firm which represented the trade association. The president and chief executive officer of the corporation was elected president of the trade association for a specified term. Other employees of the corporation also served on committees in the trade association. The IRS ruled that the taxpayer was an "outside director" for purposes of Treas. Reg. § 1.162-27(e)(3). **Ltr. Rul. 200647010, Aug. 22, 2006.**

DEPRECIATION. The IRS has published a fact sheet reviewing the general rules of depreciation. See also IRS Pub. 946, "How to Depreciate Property," IRS Pub. 551, "Basis of Assets," and IRS Pub.544, "Sales and Other Disposition of Assets." **FS-2006-27.**

EARNED INCOME CREDIT. The taxpayer cared for a mentally disabled aunt during the 1998 tax year and claimed an earned income tax credit on the basis that the aunt was a qualifying child. The court held that the taxpayer could not claim the earned income tax credit on the basis of caring for the aunt because the relationship was not equivalent to parental care for a child. **Jarman v. IRS, 2006-2 U.S. Tax Cas. (CCH) ¶ 50,605 (E.D. N.C. 2006).**

EMPLOYEE BENEFITS. The employer provided plastic smartcards or debit cards which could be used to purchase transportation on public transportation (unspecified in the ruling). The IRS ruled that the amounts on the cards were excludible from the employees' wages as a qualified transportation fringe benefit if the employer has a means of verifying the use of the cards only for transportation or the cards can only be used to purchase transportation. If the cards can be used for non-transportation purposes and their use cannot be verified, the value of the cards is wages to the employees. **Rev. Rul. 2006-57, 2006-2 C.B. 911.**

HYBRID VEHICLE TAX CREDIT. Effective for vehicles placed in service after December 31, 2005, an alternative motor vehicle credit is allowed which is the sum of (1) qualified fuel cell motor vehicle credit, (2) advanced lean burn technology motor vehicle credit, (3) qualified hybrid motor vehicle credit, and (4) qualified alternative fuel motor vehicle credit. I.R.C. § 30B(a). The IRS has announced the vehicle certifications and the credit amounts for four vehicles for the alternative motor vehicle credit, which will expire in the first calendar quarter after the quarter in which Honda Motor Sales records its sale of the 60,000th vehicle:

Year and Model	Credit Amount
2007 Honda Civic Hybrid CVT	\$2,100
2007 Honda Accord Hybrid AT	\$1,300
2007 Honda Accord Hybrid Navi AT	\$1,300
2007 Honda Civic GX (nat. gas)	\$4,000

See Harl, "Additional Items in the Energy Policy Act of 2005, 16 *Agric. L. Dig.* 131 (2005). **IR-2006-182; IR-2006-183.**

PENSION PLANS. Treas. Reg. § 1.401(1)-1(c)(7)(i) defines covered compensation for an employee as the average (without indexing) of the taxable wage bases in effect for each calendar year during the 35-year period ending with the last day of the calendar year in which the employee attains (or will attain) social security retirement age. A 35-year period is used for all individuals regardless of the year of birth of the individual. In determining an employee's covered compensation for a plan year, the taxable wage base for all calendar years beginning after the first day of the plan year is assumed to be the same as the taxable wage base in effect as of the beginning of the plan year. An employee's covered compensation for a plan year beginning after the 35-year period applicable under Treas. Reg. § 1.401(1)-1(c)(7)(i) is the employee's covered compensation for a plan year during which the 35-year period ends. An employee's covered compensation for a plan year beginning before the 35-year period applicable under Treas. Reg. § 1.401(1)-1(c)(7)(i) is the taxable wage base in effect as of the beginning of the plan year. Treas. Reg. § 1.401(1)-1(c)(7)(ii) provides that, for purposes of

determining the amount of an employee's covered compensation under Treas. Reg. § 1.401(1)-1(c)(7)(i), a plan may use tables, provided by the Commissioner, that are developed by rounding the actual amounts of covered compensation for different years of birth. The IRS has issued tables of covered compensation under I.R.C. § 401(l)(5)(E) for the 2007 plan year. For purposes of determining covered compensation for 2007, the taxable wage base is \$97,500. **Rev. Rul. 2006-60, 2006-2 C.B. 977.**

SAFE HARBOR INTEREST RATES

	December 2006			
	Annual	Semi-annual	Quarterly	Monthly
	Short-term			
AFR	4.97	4.91	4.88	4.86
110 percent AFR	5.47	5.40	5.36	5.34
120 percent AFR	5.98	5.89	5.85	5.82
	Mid-term			
AFR	4.73	4.68	4.65	4.64
110 percent AFR	5.22	5.15	5.12	5.10
120 percent AFR	5.70	5.62	5.58	5.56
	Long-term			
AFR	4.90	4.84	4.81	4.79
110 percent AFR	5.39	5.32	5.29	5.26
120 percent AFR	5.89	5.81	5.77	5.74

Rev. Rul. 2006-61, I.R.B. 2006-50.

PARTNERSHIPS

PARTNER LIABILITY. The plaintiff was injured when the plaintiff's vehicle struck a manure spreader truck driven by one of the defendants. The driver was moving the spreader truck to a farm owned by another defendant to spread chicken litter. The driver was employed by an individual defendant who was the brother of another defendant with whom both brothers also farmed as a partnership. The plaintiff named the individual employer, the partnership and the brother partner as defendants, arguing that all were liable as employer of the driver. The trial evidence showed that the partnership was operated separately from the individual farm operations, although there was some borrowing of equipment and employees. The court held that the partnership was operated sufficiently separate from the individual farm operations to not hold the partnership or the brother partner liable for the actions of the employee of the other brother's non-partnership farm operation. **Bradham v. Bush, 2006 U.S. Dist. LEXIS 84616 (M.D. Ga. 2006).**

SECURED TRANSACTIONS

DESCRIPTION OF CROP LAND. The defendant leased farm land to several farm corporations owned by an individual farmer. The defendant filed financing statements to secure the lease payments. The farmer obtained loans from a bank and the bank claimed that the defendant released the security interests in the

lease payments so that the bank would lend money to the tenant to raise crops for two years and pay the lease payments for both years. However, the tenant was unable to pay the first year's rent because the bank refused to authorize the payment. The defendant and tenant treated the lease as breached and terminated for failure to make the lease payment. Before the lease terminated, the tenant had already planted wheat which the defendant harvested after the termination of the lease. The buyer of the wheat refused payment after learning that the bank claimed a security interest in the crop. The bank sued for recovery of the crop proceeds as covered by its security interest in the tenant's farm products and proceeds. The trial court granted the bank summary judgment, holding that the bank's security interest was perfected and had priority over the defendant's lien. On appeal, the defendant argued that the security interest was not properly perfected because the description of

the crop land was insufficient. The defendant pointed to several inaccuracies in the description of the crop land location and omissions of descriptions and names in several documents. The court discussed Ark. Code § 4-9-108 which states that a description of real property is sufficient "if it reasonably identifies what is described." The court noted that the determination is a question of fact; therefore, the grant of summary judgment was improper, given the inaccuracies and ambiguities in the description of the crop land identified by the defendant. **Williams v. Peoples Bank of Paragould, 2006 Ark. App. LEXIS 775 (Ark. Ct. App. 2006).**

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