States[18] weaken the case as precedent for a situation involving a straightforward land contract purchase. Arguably, the latter would pose even less of a doubt as to whether the interest was "like-kind" with a fee simple interest. Conceivably, the interest in *Starker*[19] could be stretched over a period of some years, until the expiration of the life estate. In the usual land contract transaction, the purchaser acquires an equitable interest in the real estate with a known period to conveyance of formal title. It is true that a land contract purchaser's interest could be forfeited for non-performance under the contract but that feature presumably was present in *Starker v. United States*.[20]

Although Congress addressed another feature of the Starker holding, namely the fact that the exchange did not have to be contemporaneous, indeed that the court approved a substantial delay in the acquisition of replacement property,[21] Congress did not address the matter of whether a land contract purchaser's interest qualifies as "like-kind" to a fee simple interest. Presumably, the Congress was not greatly concerned about that feature of the case although there is no direct evidence in support of that conclusion. Nonetheless, the exchange of a contract purchaser's interest in land for a fee simple interest appears to be like-kind.

FOOTNOTES

1 See generally 4 Harl, *Agricultural Law* § 27.03[8][a][ii] (2000); Harl, *Agricultural Law Manual* § 4.02[16] (2000). See also Harl, "What Is 'Like-Kind'?"; 9 *Agr. L. Dig.* 149 (1998).

2 See Pieper & Harl, *Iowa Farmland Ownership and Tenure 1982-1997: A Fifteen-Year Perspective*, Iowa Agriculture and Home Economics Experiment Station, Iowa State University, January, 2000, p. 13 (9.5 percent of land acquired under installment land contracts in 1997).

3 See I.R.C. § 1031(a)(1).

4 See Harl, "What Is 'Like-Kind'?" 9 *Agr. L. Dig.* 149 (1998).

5 Rev. Rul. 60-43, 1960-1 C.B. 687.

6 Rev. Rul. 78-4, 1978-1 C.B. 256.

7 Ltr. Rul. 9143053, July 30, 1991.

8 Ltr. Rul. 9601046, Oct. 10, 1995 (perpetual conservation easement to Department of Interior).

9 Ltr. Rul. 9612009, Dec. 18, 1995.

10 Treas. Reg. § 1.1031(a)-1(c). See Rev. Rul. 78-72, 1978-1 C.B. 258 (unexpired term of lease includes renewal option periods).

11 602 F.2d 1341 (9th Cir. 1979).

12 *Id.*

13 *Id.*

14 *Id.*

15 *Id.*

16 *Id.*

17 *Id.*

18 602 F.2d 1341 (9th Cir. 1979).

19 *Id.*

20 *Id.*

21 See I.R.C. § 1031(a)(3) (establishing time limits on identifying replacement property and in receiving the replacement property).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

BANKRUPTCY

GENERAL-*ALM* § 13.03.*

EXEMPTIONS.

FALSE SCHEDULES. The debtor made several false lists of estate property and exempt property on the bankruptcy schedules throughout the Chapter 7 case, including omission of property and transfer of property through the debtor's business. The debtor had been denied a discharge because of the false schedules. The court held that the schedules became so unreliable that the debtor would also be denied all exemption claims. ***In re* Park, 246 B.R. 837 (Bankr. E.D. Tex. 2000)**.

CHAPTER 12-*ALM* § 13.03[8].*

CONVERSION. The debtors operated a fish farm and filed for Chapter 12. One debtor was the heir of a parent who died shortly before the Chapter 12 petition. The debtor disclaimed any interest in the estate one day before filing the petition, resulting in the inheritance passing to the debtor's children. The debtors failed to include several items of property on the bankruptcy schedules and had not filed amended schedules by the time of this decision. The court held that the Chapter 12 case was to be converted to Chapter 7 because the debtors attempted to defraud the creditors by concealing assets. The court chose conversion instead of dismissal because the debtors had made several preferential transfers which the Chapter 7 trustee could recover for the benefit of creditors. ***In re* Kloubec, 247 B.R. 246 (Bankr. N.D. Iowa 2000)**.

FEDERAL TAX-*ALM* § 13.03[7].*

DISCHARGE. The debtor had filed a previous Chapter 13 case and the issue was whether the previous case tolled the three year period for purposes of Section 507(a)(8)(A)(i) and whether the tolled period included the six month provision in I.R.C. § 6503(h)(2). The court held that the length of the previous bankruptcy case plus six months was to be added to the three year period of Section 507(a)(8)(A)(i) to determine which taxes were dischargeable. ***In re* Schultz, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,510 (Bankr. D. N.H. 2000)**.

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TAX YEAR. The taxpayer was the sole general partner in a partnership formed to purchase and develop real property. The taxpayer filed for bankruptcy on July 11, 1991 and argued that the partnership terminated on that date such that the partnership losses passed to the taxpayer. The taxpayer did not elect to terminate the tax year as of the bankruptcy filing. The court held that, under state and federal law, the partnership did not terminate until the partnership winding up was completed. The court also ruled that the bankruptcy filing did not cause the sale or exchange of the taxpayer's partnership interest because the transfer of the taxpayer's assets to the bankruptcy estate was not a sale or exchange under I.R.C. § 1398(f). Therefore, the bankruptcy estate succeeded to the partnership losses because the estate was active on the last day of the partnership tax year. The court also held that the losses were offset by the debt reduction in bankruptcy under I.R.C. § 108(b)(1); therefore, the debtor received only the partnership losses remaining after the close of the bankruptcy case. **Gulley v. Comm'r, T.C. Memo. 2000-190**.

FEDERAL AGRICULTURAL PROGRAMS

COTTON. The AMS has adopted as final regulations which set user fees for cotton producers for 2000 crop cotton classification services under the Cotton Statistics and Estimates Act at $1.35 per bale. **65 Fed. Reg. 35807 (June 6, 2000)**.

CROP INSURANCE. The FCIC has issued proposed regulations which add a new section for the insurance of millet crops. The provisions will be used in conjunction with the Common Crop Insurance Policy Basic Provisions, which contain standard terms and conditions common to most crops. The intended effect of this action is to convert the millet pilot crop insurance program to a permanent insurance program administered by FCIC for the 2002 and succeeding crop years. **65 Fed. Reg. 37919 (June 19, 2000)**.

DRY WHEY. The AMS is soliciting comments on its proposal to change the United States Standards for Dry Whey that would lower the bacterial estimate of not more than 50,000 per gram to not more than 30,000 per gram, incorporate maximum scorched particle content as a requirement for U.S. grade, and expand the test methods section to allow product evaluation using the latest methods included in Standard Methods for Examination of Dairy Products, in the Official Methods of Analysis of the Association of Official Analytical Chemists, and in standards developed by the International Dairy Federation. **65 Fed. Reg. 38235 (June 20, 2000)**.

EGGS. The AMS has announced changes in the United States Grade Standards for Shell Eggs, including deleting the general term "Inedible eggs" and its definition, revising the definition of the general term "Loss" eggs by including examples of inedible eggs, revising the term descriptive of an A quality white, and deleting specifications for packaging materials. **65 Fed. Reg. 38239 (June 20, 2000)**.

FEDERAL ESTATE AND GIFT TAX

PROPOSED LEGISLATION. Legislation has been introduced in the U.S. House of Representatives that would increase the family-owned business deduction by $500,000 per year for four years to $4 million in 2005 with a cost-of-living adjustment in years after 2005. **H.R. 4562**.

CHARITABLE DEDUCTION. The decedent had established a revocable trust which became irrevocable upon the decedent's death. The trust provided that an individual had the right to use rent free a house as a residence on trust property. In addition, the trust was to pay the taxes, insurance and maintenance costs of the house from trust income. The remainder of the trust passed to a charitable organization, subject to the individual's right to use the house, a restriction on the trustee's power to sell agricultural land in the trust and the requirement that the trustee was to offer a lease of the agricultural land to two specified individuals before offering the lease to the general public. Because the trust did not qualify as a charitable remainder trust, the trustee petitioned a state court to reform the trust to create two trusts. The individual would receive an annuity amount equal to a certain percentage of the first trust's income for life instead of the use of the house. The payments would be used to pay the fair rental value of the house plus the costs of maintenance, taxes and insurance. The charity would hold the remainder interest in the first trust corpus. The charity was the sole beneficiary of the second trust which included the agricultural property which was subject to the same sale and leasing restrictions as in the original trust. The IRS ruled that the reformation was valid and that the reformed first trust was a qualified charitable remainder trust with the value of the remainder interest eligible for the charitable deduction. The entire reformed second trust was eligible for the charitable deduction. **Ltr. Rul. 200024014, March 8, 2000**.

GENERATION SKIPPING TRANSFERS. The decedent's will provided for passing of a portion of the estate to two trusts for the surviving spouse. The first trust was to be funded from the estate residue with an amount equal to the maximum marital deduction reduced by the amount needed to use up the unified tax credit, with the remainder to fund the second trust. The will empowered the executor to elect QTIP treatment for the first trust, and the executor made that election. The executor also had the power to split the first trust into two trusts, one with a GSTT inclusion ratio of zero and one with an inclusion ratio of one. The executor requested an extension of time to make a reverse-QTIP election for the trust with the zero GSTT inclusion ratio. The IRS ruled that the split of the first trust was recognized for GSTT purposes and that an extension of time was granted to file the reverse-QTIP election. **Ltr. Rul. 200023026, March 9, 2000**.

GIFT. The decedent had sold land to a family farm corporation in exchange for a promissory note. In each of four years, the decedent had forgiven a portion of the note. The decedent considered the forgiveness a gift to the family

shareholders and claimed the annual exclusion for each gift. The corporation's bylaws required approval by 67 percent of the shareholders for any sale of corporate property and state law required a majority vote of shareholders for declaration of a dividend. The IRS argued that the forgiveness of the debt was not a gift eligible for the annual exclusion because the forgiveness did not transfer a present interest. The court agreed, holding that the shareholders did not have any individual right to immediate use or enjoyment of the gift because 67 percent of the shareholders would have to agree to any property sale and a majority was needed to declare a dividend. An article by Neil Harl on this case will appear in a future issue of the Digest. **Stinson v. United States, 2000-1 U.S. Tax Cas. (CCH) ¶ 60,377 (7th Cir. 2000)**.

The decedent's will bequeathed a portion of the estate to the surviving spouse in trust with a charitable foundation and the decedent's children as remainder beneficiaries. The estate elected to treat the trust as QTIP. The surviving spouse filed a nonqualified disclaimer of the spouse's interest in the trust and the trust agreed to pay any resulting gift tax. The IRS ruled that the value of the gift was reduced by the gift tax paid by the trust. **Ltr. Rul. 200022031, March 3, 2000**.

IRA. The decedent owned two IRAs which had a trust as the beneficiary. The surviving spouse became the sole trustee of the beneficiary trust upon the decedent's death. The beneficiary trust was to remain in existence until all assets were distributed to a subtrust. The surviving spouse was the sole trustee of the subtrust and had the discretionary authority to distribute trust corpus and income, including testamentary dispositions of the trust. The spouse distributed the IRA funds in the beneficiary trust to the subtrust and then to IRAs owned by the spouse. The IRS ruled that the distribution of the decedent's IRA funds to the spouse's IRA did not cause the IRA funds to be included in the spouse's income. **Ltr. Rul. 200023030, March 10, 2000**.

SPECIAL USE VALUATION-*ALM* § 5.03[2].* The decedent's estate included several parcels of farm and ranch property. The estate executor attempted to make the special use valuation election under I.R.C. § 2032A(e)(7) with the estate tax return but failed to provide information on the method of valuation based on cash rents on comparable land. The return failed to account for state and local taxes and to provide the actual annual rents of the comparable properties. The estate argued that the missing taxes were not essential and that taxes of zero should be used when the special use valuation notice fails to list the taxes. The estate provided only an average annual rent for the previous five years for the comparable properties. The court held that the estate could not make the I.R.C. § 2032A(e)(7) election because of its failure to identify and subtract the state and local taxes in the special use valuation calculations and failure to provide specific annual rents for the comparable properties. The estate then argued that the failure of the special use valuation election to qualify for the Section 2032A(e)(7) election automatically entitled the estate to use the Section 2032A(e)(8). method. The Section 2032A(e)(8) election required the IRS to provide the estate with notice that the election did not fully comply with the election requirements. See I.R.C. § 2032A(d)(3)l Treas. Reg. §20.2032A-4(b)(2)(i). The IRS had not provided the estate with any notice that the special use valuation election, under either section, was incomplete. The court held, therefore, that the estate could still make the special use valuation election under Section 2032A(e)(8) by providing the needed information. **Estate of Wineman v. Comm'r, T.C. Memo. 2000-193**.

TRANSFERS WITH RETAINED INTERESTS. The decedent had owned several farm and ranch properties and had transferred 24 percent of the homestead property to the decedent's children, although the decedent continued to live in the homestead residence until death. The court found that there was no implied agreement that the children would not sell or otherwise transfer their portion of the homestead; therefore, the transferred interest was not included in the decedent's estate because the decedent did not retain any control over the 24 percent interest. **Estate of Wineman v. Comm'r, T.C. Memo. 2000-193**.

TRUSTS. The taxpayers, husband and wife, owned a parcel of land with a residence which the taxpayers used for vacations, family gatherings and entertaining guests. The taxpayer's child owns a personal residence nearby and had the permission to use the taxpayers' property on occasion. The taxpayers transferred their interests in the property to an eight-year trust. The IRS ruled that the child's occasional use of the property did not disqualify the trust for qualified personal residence trust treatment. **Ltr. Rul. 200022020, March 6, 2000; Ltr. Rul. 200023020, March 6, 2000**.

UNIFIED CREDIT. The decedent and surviving spouse had owned a joint brokerage account and the decedent had intended that the brokerage account be transferred solely to the decedent in order to increase the size of the decedent's gross estate so as to fully use the unified credit. However, the transfer had not been accomplished prior to the decedent's death. The decedent's will provided for passing of the estate to the surviving spouse in trust. The surviving spouse alleged that the failure to transfer the account to the decedent's name was the brokerage's fault. The surviving spouse and brokerage company reached a settlement under which the surviving spouse would transfer funds to the brokerage company which would pay the additional funds to the trust. The IRS ruled that the additional funds would not be included in the decedent's gross estate and were not eligible for the unified credit because the funds did not pass from the estate to the trust. **Ltr. Rul. 200025032, March 23, 2000**.

VALUATION. The IRS has adopted as final regulations relating to the use of actuarial tables in valuing annuities, interests for life or terms of years, and remainder or reversionary interests. The regulations contain new actuarial tables. These regulations will affect the valuation of inter vivos and testamentary transfers of interests dependent on one or more measuring lives. **65 Fed. Reg. 36907 (June 12, 2000)**.

VALUATION OF STOCK. The decedent owned 184 of the 460 shares of stock in a family corporation which operated a garden products company. The company had pending litigation with a potential liability of more than $100 million. The court allowed a discount for stock of a

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small capitalization company, a discount of 10 percent for the litigation liability and 15 percent discount for lack of marketability. **Estate of Klaus v. Comm'r, T.C. Memo. 2000-191**.

FEDERAL INCOME TAXATION

PROPOSED LEGISLATION. Legislation has been introduced in the U.S. Senate that would allow a tax credit of up to $30,000 for "qualified value-added agricultural property" placed in service in the tax year. The legislation is similar to that introduced in the House of Representatives. See p. 92 *supra*. **S. 2746**.

BAD DEBTS. The taxpayers owned a company which was sold for a fixed sum plus a variable commission equal to $200,000 plus a percentage of the net sales over the next seven years. The buyers defaulted on the commission payments and the taxpayers claimed a bad debt deduction for the missing payments. The taxpayers did not provide evidence of the net sales or the amount due above the $200,000 minimum. The court held that no bad debt deduction was allowed above the $200,000 minimum because the amount owed was not fixed or determinable since the taxpayers did not provide sufficient evidence of the net sales. The decision is designated as not for publication. **Koenig v. Comm'r, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,503 (9th Cir. 2000)**.

COURT AWARDS AND SETTLEMENTS-ALM § 4.02[14]. The taxpayer had filed a sexual harassment suit against an employer and received a judgment for back pay, front pay, pension benefits, attorneys' fees and court costs. Under the taxpayer's legal fee arrangement with the taxpayer's lawyers, about one-half of the award was paid to the taxpayer's attorneys. The court held that all of the judgment was included in the taxpayer's income because none of the award was for personal injuries. The taxpayer could not exclude the attorneys' fees from income, because the attorneys did not have a property interest in the fee portion of the award. The taxpayer, however, could claim the fees as a miscellaneous deduction. **Hukkanen-Campbell v. Comm'r, T.C. Memo. 2000-180**.

The taxpayer had filed a wrongful suit against an employer and received a judgment for back pay, front pay, and pension benefits. Under the taxpayer's legal fee arrangement with the taxpayer's lawyers, about two-thirds of the award was paid to the taxpayer's attorneys. The court held that, under Alaska law, the lien for an attorney's fees did not create a property interest in the award. The court held that the taxpayer could not exclude the attorneys' fees from income, because the attorneys did not have a property interest in the fee portion of the award. The taxpayer, however, could claim the fees as a miscellaneous deduction. An article by Neil Harl on this case will appear in a future issue of the *Digest*. **Coady v. Comm'r, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,528 (9th Cir. 2000)**.

DEPRECIATION. The taxpayers owned a commercial building and remodeled a portion for additional storage and office space. The taxpayers did not provide evidence of the cost of the remodeling other than county assessment records. The court denied any depreciation deduction resulting from the improvements because of the failure to substantiate the costs. The taxpayers also claimed depreciation deductions based upon the increase in value of two outdoor signs. The court denied the deduction because the tax basis was to be based upon the taxpayer's cost and not the value of the signs. **Sandoval v. Comm'r, T.C. Memo. 2000-189**.

DISCHARGE OF INDEBTEDNESS. The taxpayers, husband and wife, were co-obligors on a debt which was discharged. In the year of the discharge, the taxpayers filed separate tax returns and the issue was the allocation of the discharge of indebtedness income between the taxpayers. In a Chief Counsel Advice, the IRS ruled that the determination was to be made on the basis of all facts and circumstances and included (1) whether either party had a right of contribution from the other obligor; (2) the extent either party enjoyed the benefits of the proceeds of the indebtedness; (3) the extent either party was allocated the basis from the indebtedness; and (4) the extent either party claimed the interest paid as a deduction. Although the IRS acknowledged that both taxpayers should not be assessed the full discharge of indebtedness income, the Assistant Chief Counsel advised that if the allocation could not be made under known facts and circumstances, each taxpayer should be issued a notice of deficiency based on the entire discharge of indebtedness. This places the burden of allocation on the taxpayers. **CCA Ltr. Rul. 200023001, Feb. 4, 1999**.

DISASTER PAYMENTS. The North Carolina legislature enacted a disaster relief program for state citizens who suffered losses from Hurricane Floyd in 1999. The recipients of the payments had to reimburse the state if the property was sold within five years. The IRS ruled that the payments could be excluded from income as social benefit program payments except to the extent the recipients had claimed a loss deduction on the property. **CCA Ltr. Rul. 200022050, April 5, 2000**.

On May 19, 2000, the president determined that certain areas in South Dakota are eligible for assistance under the Disaster Relief and Emergency Assistance Act, 42 U.S.C. § 5121, as a result of severe storms and flooding on April 18-20, 2000. **FEMA-1330-DR**. Accordingly, a taxpayer who sustained a loss attributable to the disasters may deduct the loss on his or her 1999 federal income tax return.

ENVIRONMENTAL CLEANUP COSTS. The taxpayer had purchased two existing retail store properties. The stores were not selling gasoline at the time of purchase and the taxpayer did not know that gasoline stations had been operated at the properties. Underground storage tanks were still in place and had leaked gasoline into the soil. The taxpayer claimed the soil cleanup expenses as a current business deduction but the IRS argued that the cleanup costs had to be capitalized into the purchase price of the properties. The court held that the cleanup costs had to be capitalized because the taxpayer did not cause the contamination and the cleanup improved the condition of the property, even though the value of the property did not

increase above what the taxpayer paid for them. **United Dairy Farmers, Inc. v. United States, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,538 (S.D. Ohio 2000)**.

INTEREST RATE. The IRS has announced that, for the period July 1, 2000 through September 30, 2000, the interest rate paid on tax overpayments is 9 percent (8 percent in the case of a corporation) and for underpayments is 9 percent. The interest rate for underpayments by large corporations is 11 percent. The overpayment rate for the portion of a corporate overpayment exceeding $10,000 is 6.5 percent. **Rev. Rul. 2000-30, I.R.B. 2000-25, 1266**.

LETTER RULINGS. The IRS has announced that the procedures in Rev. Proc. 2000-1, Rev. Proc. 2000-2, Rev. Proc. 2000-3, and Rev. Proc. 2000-7 for issuing letter rulings, determination letters, and information letters, and for furnishing technical advice, continue to apply to issues under the jurisdiction of the Office of Chief Counsel even though the offices and titles in these revenue procedures may have changed as a result of the reorganization of the Office of Chief Counsel of the IRS. Taxpayers should continue to send requests for letter rulings or pre-submission conferences on issues under the jurisdiction of the Office of Chief Counsel to the appropriate address stated in section 8.03(1) of Rev. Proc. 2000-1. Taxpayers may continue to address these requests to the associate chief counsel offices listed in section 8.03(1) even though some of these offices have changed names or some of the duties of the offices have been reassigned. The IRS will forward the requests to the appropriate office. Taxpayers who are requesting a pre-submission conference by telephone should continue to call the telephone numbers listed in section 11.07(1) of Rev. Proc. 2000-1. If the jurisdiction of the issue has been assigned to another office, The IRS will forward the call to the appropriate office. Also, district or appeals offices will continue to send requests for technical advice on issues under the jurisdiction of the Office of Chief Counsel to the appropriate address listed in section 9.03 of Rev. Proc. 2000-2. **Notice 2000-35, I.R.B. 2000-__**.

LIKE-KIND EXCHANGES. The taxpayers had owned a commercial property which was purchased by a city under threat of condemnation. The taxpayers purchased another commercial property as replacement property. The court found that the taxpayers had formed a partnership which purchased the replacement property with the proceeds of the sale of the first property. The court held that the transaction was not eligible for like-kind exchange treatment because the replacement property was purchased by the partnership. **Sandoval v. Comm'r, T.C. Memo. 2000-189**.

MARKET SEGMENT TRAINING GUIDE. The IRS has announced the publication of a revised Livestock Industry Market Segment Specialization Program Audit Technique Guide. **IRPO ¶ 208,501**.

PARTNERSHIPS-*ALM* § 7.03.*

DEFINITION. The taxpayer was a partner with another individual in a partnership which was formed to purchase and hold real estate, primarily a mobile home park. The other individual told the taxpayer that the partnership was dissolved, however, the other individual used the partnership name for the individual's engineering services business. The engineering income was treated by the individual as partnership income and the individual used partnership funds to purchase other real estate. The taxpayer continued to receive Form K-1 for the partnership in later years but the forms did not disclose the engineering income or other partnership activity carried on by the individual. The court held that the taxpayer remained a partner in the partnership but that the engineering income and other activity of the individual was not partnership income because the activity was beyond the scope of the partnership and was personal to the other partner. **Lang v. Comm'r, T.C. Memo. 2000-188**.

LIMITED LIABILITY COMPANIES. *Lawyers Weekly USA* has reported on a Maryland Court of Appeals case in which a husband and wife transferred real property to a wholly-owned LLC. The couple acquired title insurance on the property when they originally purchased the property but did not acquire title insurance by the LLC after the transfer. The court held that, because the LLC is a separate entity under state law, the LLC was not an insured under the original title insurance policy, relieving the insurance company from liability for a defect in title discovered after the transfer to the LLC. **Gebhardt Family Investment, LLC v. Nations Title Insurance, New York, Inc., No. 1510 (Md. Ct. App. June 6, 2000)**.

The taxpayers were partners in a general partnership which was converted to an LLC with no change in the partners' interests in the partnership profits, losses, assets or liabilities. The IRS ruled that the conversion (1) did not cause the partners to recognize gain or loss; (2) the conversion was not a sale or exchange; (3) the conversion did not terminate the partnership; (4) the LLC did not need to obtain a new taxpayer identification number; (5) the partners' holding periods for their respective interests in the LLC included the holding periods of their respective interests in the general partnership; (6) the partners' capital account balances in the LLC continued to be their capital account balances from the general partnership; and (6) the LLC's initial basis in the assets it received from the general partnership was the same as the general partnership's basis in such assets immediately prior to the conversion. **Ltr. Rul. 200022016, Feb. 29, 2000**.

PENSION PLANS. For plans beginning in June 2000, the weighted average is 6.01 percent with the permissible range of 5.41 to 6.31 percent (90 to 106 percent permissible range) and 5.41 to 6.61 percent (90 to 110 percent permissible range) for purposes of determining the full funding limitation under I.R.C. § 412(c)(7). **Notice 2000-31, I.R.B. 2000-__**.

RESEARCH AND DEVELOPMENT EXPENSES. The taxpayer was a member of partnerships formed for the purpose of investing in possible jojoba growing businesses. The partnerships were on the accrual method of accounting. Near the end of a tax year, the partnerships entered into a contract with a corporation for the investigation of whether it would be feasible to grow jojoba plants in a certain area in Arizona. The corporation was controlled by members of the partnership who did not have experience in agricultural research. The farms attempted to grow jojoba in the area but conducted no scientific tests or evaluation of the growing attempts. In *Utah Jojoba 1 Research v. Comm'r,*

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T.C. Memo. 1997-504, the court found that the corporation was formed in order to characterize investments in the partnership as research expenses which were actually contributions used to develop the farm land. In the instant case, the taxpayer was assessed additions to tax for negligence and for substantial understatement of tax. The taxpayer argued that the negligence penalty was not warranted because the taxpayer relied on the statements of the promoters and the taxpayer's own farming experience and research into jojoba growing. The court held that the taxpayer should have known that the research and experimentation was nothing more than regular farming of the jojoba and that the taxpayer did not investigate the legitimacy of the tax benefits gained from the claimed expenses. The court upheld the addition to tax for negligence. **Fawson v. Comm'r, T.C. Memo. 2000-195**.

RETURNS. The taxpayers, husband and wife, filed a joint return and listed their minor children as dependants. The taxpayers, however, did not include any social security numbers (SSN) for the children because the taxpayers objected, on religious grounds, to the use of universal identifiers. The IRS agreed that the religious objection was sincere and that the minor children were eligible dependants, but denied the personal exemption for the children, based on the failure to provide the social security numbers. The taxpayers argued that they should be allowed to use taxpayer identification numbers (TIN) for the children. The court held that the SSN requirement fulfilled a compelling governmental interest because the use of TINs for persons not exempt from social security taxes could increase the chances of fraudulent returns by persons who also acquire SSNs. **Miller v. Comm'r, 114 T.C. No. 32 (2000)**.

SAFE HARBOR INTEREST RATES
July 2000

	Annual	Semi-annual	Quarterly	Monthly
Short-term				
AFR	6.60	6.49	6.44	6.40
110 percent AFR	7.27	7.14	7.08	7.04
120 percent AFR	7.94	7.79	7.72	7.67
Mid-term				
AFR	6.62	6.51	6.46	6.42
110 percent AFR	7.29	7.16	7.10	7.06
120 percent AFR	7.96	7.81	7.74	7.69
Long-term				
AFR	6.40	6.30	6.25	6.22
110 percent AFR	7.05	6.93	6.87	6.83
120 percent AFR	7.70	7.56	7.49	7.44

Rev. Rul. 2000-32, I.R.B. 2000-27.

S CORPORATIONS-*ALM* § 7.02[3][c].*

DISCHARGE OF INDEBTEDNESS. The taxpayer was a 95 percent shareholder in an S corporation. The corporation had discharge of indebtedness income in one tax year which was not recognized because the corporation was insolvent. In addition, the corporation did not have any tax attributes to be reduced by the discharge of indebtedness income. The taxpayer increased the basis of the stock by the taxpayer's share of the discharge of indebtedness income and offset the basis by the amount of losses recognized on the value of the taxpayer's stock. The Tax Court held that the determination of discharge of indebtedness income was made at the corporation level and that the discharge of indebtedness income did not pass to the taxpayer. The discharge of indebtedness income was not recognized at the corporation level because of the insolvency exception. The appellate court reversed, holding that the S corporation's discharge of indebtedness income not used to reduce the S corporation's tax attributes flowed through to the shareholder and increased the basis of the taxpayer's stock. The court rejected the holding of *Nelson v. Comm'r, 110 T.C. 114 (1998)*, that discharge of indebtedness of a corporation does not pass to the shareholders. However, the court noted that the character of the discharge of indebtedness income is first determined at the corporation level, with any reduction of tax attributes taken at the S corporation level, before passing any remaining discharge of indebtedness income to the shareholders. **Pugh v. Comm'r, ¶ 50,514 (11th Cir. 2000), *rev'g*, T.C. Memo. 1999-38**.

WITHHOLDING TAXES. As the result of an employment tax audit, the taxpayer was assessed FICA taxes, income tax withholding, and backup withholding on meal allowances it had paid to its employees in prior tax years. The audit determined that such meal allowances had constituted additional compensation and were taxable as such when paid to the employees. The taxpayer paid the payroll taxes assessment in full in a later tax year. The taxpayer did not seek any recompense from its employees for the amounts representing the employees' share of the total. In a subsequent tax year, the taxpayer filed an income tax refund claim for the year the assessed amounts were paid, based upon a deduction for the additional amounts assessed and paid. The IRS ruled that the payment of the employees' share of the employment and income taxes was not an ordinary and necessary business expense and was not eligible for a deduction. **Ltr. Rul. 200025002, March 21, 2000**.

ZONING

WASTE TREATMENT FACILITY. The applicant owned land in an exclusive farm use zone area. The plaintiff applied for approval to operate a livestock waste treatment facility on the land. The processed waste was to be transferred by existing pipes to neighboring land to be spread on that land as fertilizer. The applicant and neighbor had obtained permits from the state department of environmental quality for the waste treatment and disposal. The plaintiffs were neighbors who challenged the approval of the conditional use of the land, arguing that the hearing officer should have included the application of the waste on the neighboring land because it was an integral part of the waste treatment operation. The court held that the permits obtained by the applicant and neighbor were separate permits for separate operations, allowing the local zoning board to consider each operation separately. The court held that, because the applicant had obtained the necessary permit for its portion of the operation, the board had the authority to grant the conditional use for the applicant's land separate from any approval of the neighbor's use of the neighbor's land. **Wilbur Residents v. Douglas County, 998 P.2d 794 (Or. Ct. App. 2000)**.

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