fishing permit, which was exempt under Alaska law to commercial fishermen, was not excluded from the taxpayer's assets in determining insolvency. The taxpayer had financed the purchase of a boat for $202,451, in 1988, with a bank loan. In 1993, when the loan balance stood at $137,142, the bank foreclosed on the boat. The boat was sold for $95,000 as part of the foreclosure. The bank discharged the remaining $42,142 on the loan. As a result of the foreclosure sale, the taxpayers realized capital gain of $28,621 and discharge of indebtedness income of $42,142.

In determining whether the discharge of indebtedness amount was income,[23] the question was whether the taxpayer was solvent. The taxpayer had assets of $875,251 and liabilities of $515,930. However, the taxpayer's "limited entry" fishing permit had a fair market value of $393,400 and was exempt from creditors under Alaska laws.[24]

The taxpayer argued that exempt property should not count as "assets" for purposes of the insolvency determination with the result that the taxpayer would be insolvent and the discharge of indebtedness income of $42,142 would not be includible in income.[25] The Internal Revenue Service took the position that the exclusion of exempt property from "assets" was a judicially-created exemption that had not been codified in I.R.C. § 108 in 1980 when enacted as part of the Bankruptcy Tax Act of 1980.[26]

The Tax Court concluded that I.R.C. § 108(e)(1) (which states "there shall be no insolvency exception from the general rule that gross income includes income from the discharge of indebtedness" except as provided in I.R.C. § 108(a)(1)(B)), eliminated the judicially-created exception for exempt property. [27]

This decision has important implications for farm and ranch estates where the value of exempt property is often $60,000 or more.[28]

FOOTNOTES

1 I.R.C. § 108(a)(1)(B). See Frazier v. Comm'r, 111 T.C. 243 (1998) (insolvency exceeded amount of discharge of indebtedness so excludible). See generally, 5 Harl, *Agricultural Law* § 39.03[5] (2001); Harl, *Agricultural Law Manual* § 4.02[15][d] (2001).

2 I.R.C. § 108(g).

3 I.R.C. § 108(c).

4 I.R.C. § 108(e)(5).

5 I.R.C. § 61(a)(12).

6 I.R.C. § 108(a)(1)(B).

7 I.R.C. § 108(b). See 5 Harl, *supra* note 1, § 39.03[5][d] (2001); Harl, *Agricultural Law Manual* § 4.02[15][d] (2001).

8 I.R.C. § 108(d)(3).

9 I.R.C. § 108(d)(3).

10 Merkel v. Comm'r, 109 T.C. 463 (1997), *aff'd*, 192 F.3d 844 (9th Cir. 1999) (guarantee of partnership debt treated as contingent debt and not included in debts for purposes of insolvency determination).

11 Schrott v. Comm'r, T.C. Memo. 1989-346.

12 Ltr. Rul. 8920019, Feb. 14, 1989.

13 See 5 Harl, *supra* note 1, § 39.03[5][a] (2001); Harl, *Agricultural Law Manual* § 4.02[15][d] (2001).

14 E.g., Hunt v. Comm'r, T.C. Memo, 1989-335; Ltr. Rul. 9130005, March 29, 1991.

15 Cole v. Comm'r, 42 B.T.A. 1110 (1940), *nonacq*., 1941-1 C.B. 13.

16 Estate of Marcus v. Comm'r, T.C. Memo. 1975-9; Davis v. Comm'r, 69 T.C. 814 (1978); Hunt v. Comm'r, T.C. Memo. 1989-335.

17 Ltr. Rul. 9125010, March 19, 1991; Ltr. Rul. 9130005, March 29, 1991.

18 Ltr. Rul. 9125010, March 19, 1991.

19 Ltr. Rul. 9932013, May 4, 1999; Ltr. Rul. 9935002, May 3, 1999.

20 FSA Ltr. Rul. 9932019, May 10, 1999.

21 Carlson v. Comm'r, 116 T.C. No. 9 (2001).

22 *Id*.

23 I.R.C. § 61(a)(12).

24 Carlson v. Comm'r, 116 T.C. No. 9 (2001).

25 *Id*.

26 Pub. L. 96-589, Sec. 2(a), 94 Stat. 3389 (1980).

27 *Carlson v. Comm'r*, 116 T.C. No. 9 (2001). See Gitlitz v. Comm'r, 531 U.S. __ (2001) (judicially-developed exceptions not codified in I.R.C. § 108 are not applicable); Merkel v. Comm'r, 192 F.3d 844 (9th Cir. 1999), *aff'g*, 109 T.C. 463 (1997).

28 See Faiferlick and Harl, "The Chapter 12 Bankruptcy Experience in Iowa" 9 *J. Agr. Tax'n & L.* 302 (1988).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

BANKRUPTCY

GENERAL-*ALM* § 13.03.*

ADMINISTRATIVE EXPENSE. The debtor leased farm equipment from a creditor and was three months behind in the lease payments when the debtor filed for Chapter 11. The debtor continued to possess the equipment post-petition but made no use of the equipment. The case was later converted to Chapter 7 and the lessor obtained an order to reject the lease. The lessor sought an administrative expense claim in the Chapter 7 case for the lease payments incurred during the post-petition period of the Chapter 11 case. The trustee argued that the lease payments could not receive administrative claim priority because the estate did not benefit from the use of the equipment. The court held that, under Section 365(d)(10), the debtor was required to perform under the lease; therefore, the post-petition lease

**Agricultural Law Manual* (ALM).

payments were entitled to administrative expense priority even if the debtor did not use the leased property. The court also held that the administrative claim status of the lease payments continued after the case was converted to Chapter 7, although the claim would be subordinated to the administrative claims which arose after the conversion to Chapter 7. ***In re*** **Eastern Agri-Systems, Inc., 258 B.R. 352 (Bankr. E.D. N.C. 2000)**.

EXECUTORY CONTRACTS. The debtor was a hog producer who entered into a contract to supply hogs to a processor. Under the contract the processor agreed to purchase the hogs at a set price. If the market price is less than the contract price when some hogs are delivered, the deficit is merely recorded. If the market price is above the contract price when hogs are delivered, the excess is first applied against the deficit account and then split between the parties, a so-called ledger contract. So long as the contract was not breached or repudiated by the debtor, the deficit account could not be collected from the debtor. When the debtor filed for Chapter 11 the deficit account had exceeded $5 million and the processor sought, under Section 365(c), to force the trustee to reject the contract so that the deficit account could be a claim against the estate. The processor argued that the contract could not be assumed under Section 365; therefore, it must be rejected. The court held that the contract could be assumed under Section 365 because (1) it was not a financing arrangement but a contract for goods and (2) the processor failed to prove that the contract could not be assigned. The court noted that the processor's business significantly relied on the hogs produced by the debtor and had granted the deficit account feature to insure a steady supply of hogs. ***In re*** **Neuhoff Farms, Inc., 258 B.R. 343 (Bankr. E.D. N.C. 2000)**.

EXEMPTIONS

HOMESTEAD. The debtor lived on a farm which was separated by a road from a farm owned by the debtor and two siblings, subject to a life estate held by the debtor's parent. The debtor had farmed the parent's property but had only raised hogs in several buildings during the years before the bankruptcy filing. At the time of the petition, the debtor was cleaning the buildings and not raising any hogs. The debtor claimed the debtor's residence as exempt and also included the debtor's interest in the parent's farm as part of the homestead exemption. The court held that the debtor could not claim the interest in the parent's farm as part of the homestead exemption because the debtor did not have any legal right to possession of the property, even though the debtor did operate part of the debtor's business on the parent's farm. ***In re*** **Stenzel, 259 B.R. 141 (Bankr. 8th Cir. 2001)**.

FEDERAL TAX-*ALM* § 13.03[7].*

DISCHARGE. The debtor filed a Chapter 7 case in December 1998 and received a discharge in March 1999. The debtor filed a Chapter 13 case in August 1999 which included tax claims for 1995 and 1996. The debtor argued that the tax claims were dischargeable because the returns were due more than three years before the filing of the Chapter 13 case. The IRS argued that the three year period of Section 507(a)(8)(i) was tolled by the prior Chapter 7 case. The court held that the three year period was not tolled by law but that the period would be tolled under the court's equitable powers because the debtor used serial filings to prevent the IRS from collecting the taxes within the three years. ***In re*** **Evoli, 258 B.R. 839 (Bankr. M.D. Fla. 2001)**.

The debtor did not file or pay 1991 income taxes. In 1993 the IRS prepared a substitute return and assessed the debtor for the taxes. In 1996 the debtor filed a return but did not include wages and IRA distributions that the IRS had included in its return and assessment. The debtor sought discharge of the taxes because the return was filed more than three years before the bankruptcy petition. The court held that the late filed return would not be considered a return for purposes of Section 523(a)(1)(B) because (1) the IRS prepared a substitute return first, (2) the debtor's return did not include all income, and (3) the debtor did not provide any explanation as to why the debtor's return excluded items of income. ***In re*** **Shrenker, 258 B.R. 82 (Bankr. E.D. N.Y. 2001)**.

CONTRACTS

PRODUCTION CONTRACTS. The Oklahoma Attorney General has issued an opinion as to three issues involving farmer production contracts. These contracts generally provide for the raising of livestock, birds or crops with the farmer supplying the facilities and labor and the integrator supplying the livestock, birds or seeds and the feed or other supplies. The integrator generally retains title to the livestock, birds or crops and the contract generally establishes the amount paid to the farmer by the quantity and quality of the final product. The AG noted that many of these contracts are forms drafted by the integrator, with no terms negotiated by the parties. The AG opinion states that such contracts are contracts of adhesion and could be held to be void, depending upon whether the factual circumstances demonstrate unconscionability. The AG opinion notes that contracts of adhesion will be interpreted against the drafter. The AG opinion also states that the contracts would be governed by the laws of Oklahoma if the farmer's property and activities take place in Oklahoma, unless a clear choice of law clause provides for the governance of the laws of another state. The AG opinion described a production contract which sets forth in detail the manner in which the livestock or crop is to be raised. The AG opinion states that in such circumstances the contract establishes an employment relationship because the integrator has significant control over the farmer's activities. **Okla. A.G. Opinion 01-17, April 11, 2001**.

FEDERAL AGRICULTURAL PROGRAMS

BRUCELLOSIS. The APHIS has issued interim regulations amending the brucellosis regulations to change the classification of Oklahoma from Class A to Class Free. **66 Fed. Reg. 20899 (April 26, 2001)**.

CONSERVATION RESERVE PROGRAM. The CCC has issued final regulation amending the Conservation Reserve Program (CRP) regulations to implement provisions of Title XI of the Agriculture, Rural Development, Food and Drug Administration, and Related Agencies Appropriations Act, 2001, and provide for enrollment, in the States of Iowa, Minnesota, Montana, Nebraska, North Dakota, and South Dakota, of certain wetlands and buffer acreage on a pilot basis into the CRP under the Farmable Wetlands Pilot Program. **66 Fed. Reg. 22097 (May 2, 2001)**.

EDUCATION. The USDA has issued proposed regulations to implement the Outreach and Assistance for Socially Disadvantaged Farmers and Ranchers Program whereby the 1890 Land Grant Colleges, including Tuskegee University, Indian tribal community colleges and Alaska native cooperative colleges, Hispanic serving post-secondary educational institutions and/or other qualifying educational institutions and community-based organizations are eligible to compete for grants and cooperative agreements to provide outreach and technical assistance to socially disadvantaged farmers and ranchers. The program's objective is to reverse the decline of socially disadvantaged farmers and ranchers across the United States. **66 Fed. Reg. 21607 (April 30, 2001)**.

FOOT AND MOUTH DISEASE. “USDA will compensate livestock producers for their losses if efforts to keep the highly contagious foot-and-mouth disease out of the United States fail and animals have to be destroyed in order to contain the disease, Agriculture Secretary Ann Veneman told the House Appropriations subcommittee on agriculture last week.

“She said USDA has studied the matter and is prepared to pay direct costs for the fair market value for any animals that must be destroyed. The department has not worked out the details of any ‘associated costs’ that also might arise but have not been identified.

“Veneman told the committee that a paper outlining the details of the compensation program is still being drafted and would be available soon. The department is having additional discussions on the matter with the White House Office of Management and Budget.

“Veneman said she wanted to reassure producers that there would be an underlying program to help farmers devastated by livestock losses if the disease should make its way into the United States. ‘Producers have the assurance that they should report an outbreak,’ because they will be compensated, she said.” **The Food Chemical News, April 30, 2001**.

KARNAL BUNT. The APHIS has issued proposed regulations which establish new areas to be regulated because of the existence of Karnal bunt disease. The proposed regulations also remove other areas from regulation. **66 Fed. Reg. 20204 (April 20, 2001)**.

FEDERAL ESTATE AND GIFT TAX

CLAIMS. The IRS had assessed a decedent’s estate for an income tax deficiency resulting from the decedent’s improper claim for earned income credit. The executor of the estate argued that the IRS claim was not allowed because the claim was filed after the time period allowed for claims against a decedent’s estate under state law. The court held that the IRS was not subject to the state statute of limitations because no law or regulation has waived the IRS governmental immunity to the state statute. **United States v. Stevenson, 2001-1 U.S. Tax Cas. (CCH) ¶ 50,371 (M.D. Fla. 2001)**.

FAMILY-OWNED BUSINESS DEDUCTION. The IRS has issued a Chief Counsel Advice letter as to two issues involving FOBD. The first issue was whether and how the IRS could file a lien against personal property if there is insufficient real property to which a lien can attach to secure the possible recapture of FOBD benefits. The IRS ruled that, when a FOBD election is made, a lien against estate property arises under I.R.C. §§ 2057(i)(3)(P), 6324B. The IRS noted that guidance will be supplied by forthcoming regulations. The second issue was whether an estate can designate as subject to the FOBD lien only estate FOBD business interests sufficient to satisfy the recapture liability. The IRS ruled that all FOBD interests for which the election was made are subject to the lien. The IRS noted that the lien amount is limited to the recapture amount but that all FOBD interests remain subject to the lien until the recapture liability has ended. The Digest will publish an article on this ruling by Neil E. Harl in a future issue. **CCA Ltr. Rul. 200116001, April 23, 2001**.

GIFT. The decedent bequeathed property in trust to the surviving spouse. The surviving spouse disclaimed a portion of the trust, resulting in the trust property passing to the decedent’s children. The disclaimer was conditioned upon the donees paying the gift tax resulting from the disclaimer. The IRS ruled that the amount of the taxable gift would be reduced by the amount of gift tax paid by the donees. **Ltr. Rul. 200116006, Dec. 14, 2000**.

INSTALLMENT PAYMENT OF ESTATE TAX. The decedent’s estate had elected to pay the estate tax over 15 years. After the 15 years had expired, the IRS notified the estate that a substantial portion of the estate tax remained to be paid. The estate sent a payment with an offer in compromise, which was rejected by the IRS. The IRS then assessed the estate for the unpaid taxes. The estate filed an action under I.R.C. § 7422(j), claiming that the estate had paid all taxes due. The case does not identify the estate’s reason for contesting the tax amount. However, the estate admitted that it had not paid all the taxes and that it was not current in the installment payments. The court held that the court did not have jurisdiction, under I.R.C. § 7422(j), to hear the claim because the estate was not current on payment of all installments. **Hansen v. United States, 2001-1 U.S. Tax Cas. (CCH) ¶ 50,382 (8th Cir. 2001)**.

MARITAL DEDUCTION. The decedent's will provided for an annuity trust for the surviving spouse, in which the surviving spouse received $100,000 annually with increases for inflation. The remainder was held by a charity. The executor elected QTIP status for the annuity trust interest passing to the spouse and claimed a marital deduction based on the $100,000 annuity amount. The estate argued that the value of the marital deduction should be increased to reflect the inflation provision. The court held that the marital deduction could not include the inflation provision because the inflation provision was defeasible upon the contingency that inflation not occur. **Estate of Sansone v. Comm'r, 2001-1 U.S. Tax Cas. (CCH) ¶ 60,399 (C.D. Calif. 2001)**.

SPECIAL USE VALUATION-*ALM* § 5.03[2].* The IRS has issued the 2001 list of average annual effective interest rates charged on new loans by the Farm Credit Bank system to be used in computing the value of real property for special use valuation purposes:

District	Interest rate
Columbia	9.90
Omaha/Spokane	7.98
Sacramento	7.99
St. Paul	8.13
Springfield	8.87
Texas	8.22
Wichita	8.22

Rev. Rul. 2001-21, I.R.B. 2001-__.

VALUATION. The taxpayer established a trust and transferred a vacation residence to the trust. The taxpayer claimed to use the residence for at least the greater of 14 days or 10 percent of the time the property is leased to others. The IRS ruled that the property was a qualified personal residence for purposes of I.R.C. § 2702. **Ltr. Rul. 200117021, Jan. 25, 2001**.

FEDERAL INCOME TAXATION

LEGISLATION. Legislation has been introduced in the U.S. House of Representatives which excludes from income the gain from the sale of livestock raised as part of an FFA or 4H project by minors. **H.R. 1599**.

CORPORATIONS-*ALM* § 7.02.*

CONTRIBUTIONS. The taxpayers were members of one family who had operated a farm as a joint venture. The taxpayers incorporated the farm, with each member contributing assets subject to liabilities. The corporation assumed the liabilities but the taxpayers retained personal liability for the liabilities assumed by the corporation. Because the assumed liabilities exceeded the taxpayers' basis in each asset, the IRS assessed tax for the gain, measured by the difference between the basis of each asset and the liability assumed by the corporation for that asset. The gain was long-term or short-term, depending upon the holding period for each asset. The taxpayers argued that the gain should not be recognized because the taxpayers remained personally liable for the corporate debt. The taxpayers sought to characterize the personal liability as similar to a loan to the corporation from the shareholders. The court rejected this characterization and held that the taxpayers recognized gain from the contribution of property to the corporation with assumed liabilities in excess of the taxpayers' basis. The Digest will publish an article on this case by Neil E. Harl in a future issue. **Seggerman Farms, Inc. v. Comm'r, T.C. Memo. 2001-99**.

COST-SHARING PAYMENTS. The USDA has determined that all state cost-share payments made to individuals as part of a Brownfields Grant by the Wisconsin Department of Commerce are made primarily for the purpose of restoring the environment, for the purposes of I.R.C. § 126. The determination permits recipients of these cost-share payments to exclude them from gross income to the extent allowed by the I.R.C. **66 Fed. Reg. 20965 (April 26, 2001)**.

COURT AWARDS AND SETTLEMENTS-ALM § 4.02[14]. The taxpayer's employment was terminated and the taxpayer believed the termination was solely because the taxpayer knew too much about the employer's environmental violations. The taxpayer's lawyer negotiated a termination settlement which exceeded the normal termination payment by $280,000. The taxpayer excluded the entire settlement from gross income, arguing that the settlement was a payment for personal injuries. The District Court held that, although no suit was filed and the taxpayer made no personal injury claim to the employer, the settlement was paid, in part, to compensate the taxpayer for wrongful employment termination. The court allocated the settlement to the personal injury only to the extent the settlement exceeded the normal termination payment, $280,000. The appellate court affirmed the lower court's holding that some of the payment above the normal termination amount was excludible from income as compensation for personal injuries. However, the appellate court remanded the case for a determination of the portion of the $280,000 which was compensation for the personal injuries. On remand, the trial court held that the entire $280,000 was excludible from income as payment for personal injuries. **Greer v. United States, 2001-1 U.S. Tax Cas. (CCH) ¶ 50,377 (E.D. Ky. 2001), *on rem from*, 207 F.3d 322 (6th Cir. 2000), *aff'g in part*, 98-2 U.S. Tax Cas. (CCH) ¶ 50,821 (E.D. Ky. 1998)**.

The taxpayer was employed for several years by a drugstore chain. The taxpayer experienced various physical and mental problems from the strain of working long hours and irregular hours. A class action suit was filed by other parties against the drugstore chain for unpaid overtime compensation. The taxpayer joined in the suit as a class member but did not assert any claims for physical or mental injuries. The drugstore agreed to a monetary settlement and the settlement mentioned that the taxpayer's payment was for personal injuries. The taxpayer excluded the settlement payment from income as a payment for personal injuries. The court held that the payment was included in income because the class action petition made no mention of claims for personal injuries but sought damages only for unpaid compensation. **Fawcett v. Comm'r, T.C. Summary Op. 2001-65**.

DISASTER PAYMENTS. On April 10, 2001, the President determined that certain areas in Massachusetts were 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 March 5, 2001. **FEMA-1364-DR**. On April 10, 2001, the President determined that certain areas in Vermont were eligible for assistance under the Act as a result of record snow fall on March 5-7, 2001. **FEMA-3167-EM**. Accordingly, a taxpayer who sustained a loss attributable to the disasters may deduct the loss on his or her 2000 federal income tax return.

EARNED INCOME CREDIT. The U.S. Supreme court has denied certiorari in the following case. The taxpayer claimed welfare payments under AFDC and SSI programs, Social Security disability benefits, and gifts as wages on the taxpayer's income tax return. No other wages or income were reported such that, after the standard deduction and exemptions, the taxpayer had zero taxable income. The taxpayer also claimed earned income credit. The Tax Court held that earned income does not include welfare payments such as AFDC and SSI, Social Security disability benefits or gifts. The appellate court affirmed in an opinion designated as not for publication. **Powers v. Comm'r, T.C. Memo. 2000-5, *aff'd*, 2000-1 U.S. Tax Cas. (CCH) ¶ 50,838 (6th Cir. 2000), *cert. denied*, __ U.S. __ (2001)**.

FUEL CREDIT. The IRS has announced that the reference price that is to be used in determining the availability of the I.R.C. § 29 tax credit for the production of fuel from nonconventional sources for calendar year 2000 is $26.73. Since this amount does not exceed $23.50 multiplied by the inflation adjustment factor, the I.R.C. § 29(b)(1) phaseout of the credit will not occur for any qualified fuel based on the above reference price. **Notice 2001-31, I.R.B. 2001-17, 1093**.

HOME OFFICE. The taxpayer was a professional violinist who claimed a home office deduction for the living room in the taxpayer's apartment which was used solely for practicing and storage of music. The taxpayer performed at several film studios. The court applied two tests from *Commissioner v. Soliman, 506 U.S. 168 (1993)*, (1) the relative importance of the activities performed at each business location and (2) the amount of time spent at each location. The court held that the first test was inconclusive because the practice and performance activities had similar importance. The appellate court held that the taxpayer was allowed a deduction for the living room as a home office because the taxpayer spent significantly more time practicing than performing. **Popov v. Comm'r, 2001-1 U.S. Tax Cas. (CCH) ¶ 50,353 (9th Cir. 2001)**.

IRA. The taxpayer owned four IRAs and was required by a divorce decree to transfer ownership in two IRAs to the taxpayer's former spouse. At the time of the transfer the taxpayer was receiving annual distributions from the IRAs. After the transfer, the total annual payments were less but the payments from the remaining IRAs were the same. The IRS ruled that the transfer of the two IRAs pursuant to the divorce decree was nontaxable. In addition, the reduction in total annual payments did not violate I.R.C. § 72(t)(4) as a substantial modification because the distributions from the remaining IRAs remained the same. **Ltr. Rul. 200116056, Jan. 26, 2001**.

INNOCENT SPOUSE DEFENSE. The decedent was married during the tax years involved. The decedent was predeceased by the spouse. The decedent's spouse separately owned partnership interests in those tax years. After the decedent's and spouse's deaths, the IRS made administrative adjustments to the partnership tax items, resulting in assessments against the decedent and spouse. The decedent's executor filed Form 8857, "Request for Innocent Spouse Relief" on behalf of the decedent as to the partnership-related assessment. In a Chief Counsel Advice letter, the IRS ruled that a executor could not make the election for innocent spouse relief but could only pursue the claim if the decedent had made the election while still alive. **CCA Ltr. Rul. 200117005, Jan. 12, 2001**.

PASSIVE LOSSES. The taxpayers owned the majority of the stock of an S corporation which provided management services for several partnerships in which the taxpayers owned an interest. The taxpayers actively participated in the management activities of the corporation but received passive income and losses from the partnerships. The taxpayers offset the passive income and nonpassive losses, arguing that was allowed by the legislative history of I.R.C. § 469 because the S corporation and partnerships were related entities with income and deductions arising from the same activities. The IRS argued that the offset was not allowed because the statute and regulations under the statute allowed such offset only for interest items by lenders. The Tax Court held that the failure of the IRS to promulgate regulations in keeping with the legislative history did not prevent the offset which was otherwise allowable under the letter and intent of the statute. The appellate court reversed, holding that the statute was plain and unambiguous in prohibiting the offset of passive income against nonpassive losses. **Hillman v. Comm'r, 2001-1 U.S. Tax Cas. (CCH) ¶ 50,354 (4th Cir 2001), *rev'g*, 114 T.C. 103 (2000)**.

PENSION PLANS. For plans beginning in April 2001, the weighted average is 5.85 percent with the permissible range of 5.26 to 6.14 percent (90 to 106 percent permissible range) and 5.26 to 6.43 percent (90 to 110 percent permissible range) for purposes of determining the full funding limitation under I.R.C. § 412(c)(7). **Notice 2001-32, I.R.B. 2001-18, 1146**.

RETURNS. The IRS has released revised Publication 969 (Rev. April 2001), Medical Savings Accounts. This document is available at no charge (1) by calling the IRS's toll-free telephone number, 1-800-829-3676; (2) via the internet at http://www.irs.gov/prod/cover.html; (3) through FedWorld; or (4) by directly accessing the Internal Revenue Information Services bulletin board at (703) 321-8020.

S CORPORATIONS-*ALM* § 7.02[3][c].*

BASIS. The taxpayer owned an S corporation formed for the purpose of acquiring another unrelated corporation. The funds for the acquisition were borrowed from a bank and structured in such a way as to include a personal loan by the taxpayer. However, the court found that, in substance, the taxpayer's personal loan was actually a personal guarantee

*Agricultural Law Manual (ALM).

of the S corporation's loan because the taxpayer did not receive any funds and was not required to make any payments on the loan unless the S corporation failed to make payments. The court held that the taxpayer could not increase the taxpayer's basis in the corporation for the guarantee of the S corporation loan. This resulted in disallowance of the taxpayer's share of corporate losses. **Grojean v. Comm'r, 2001-1 U.S. Tax Cas. (CCH) ¶ 50,355 (7th Cir. 2001), *aff'g*, T.C. Memo. 1999-425**.

SALE OF RESIDENCE. A federal District Court held that the TRA 1997 provision amending the home sale rules does not violate the Constitution's due process or equal protection clauses by being made retroactive to home sales occurring on or after May 7, 1997, and not to home sales occurring earlier that year. **Buerer v. United States, No. 1:00CV269 (W.D. N.C. April 25, 2001)**.

SELF-EMPLOYMENT TAX. The taxpayer was self-employed as a sales representative. The taxpayer's spouse was also self-employed in other business and did not participate in the taxpayer's business. The taxpayer and spouse filed separate returns. The taxpayer was the resident of a community property state. The taxpayer filed a timely income tax return but claimed only one-half of the income from the sales representative business as taxable income. The taxpayer argued that, under the state community property rules, one-half of the taxpayer's income belonged to the spouse. The court held that all of the income from the sales representative business was earned by the taxpayer and was taxable to the taxpayer. **Landsberg v. Comm'r, T.C. Memo. 2001-105**.

SOCIAL SECURITY BENEFITS. The taxpayer had begun receiving social security benefits at retirement at age 62 in 1992. The taxpayer was employed in 1997 but received full social security benefits. The SSA determined that the taxpayer had received excess benefits in 1997 because of the employment income and began withholding social security benefits until the excess was eliminated. The IRS assessed taxes for 1997 by including the social security benefits in income. The taxpayer argued that the excess benefits received should not have been included in income because the excess was only a loan from the SSA until it was paid back. The court held that the excess social security benefits were included in income in 1997 because they were not a loan. The court noted that I.R.C. § 86(d) provided rules for mitigating the harsh effects of excess social security payments and that the mitigating calculations were properly applied here. **Zavatto v. Comm'r, T.C. Summary Op. 2001-62**.

THEFT LOSS. The taxpayer had owned a residence subject to a mortgage. When the taxpayer defaulted on the loan payments, the lender foreclosed and the property was sold at a foreclosure sale. The taxpayer challenged the foreclosure order in state court on procedural issues but the state trial and appellate courts held that the foreclosure order was properly made. The taxpayer claimed the value of the residence as a theft loss deduction, characterizing the loss as "judicial theft of real estate." The court held that the foreclosure order was fully adjudicated in the state courts and was binding on the taxpayer; therefore, no theft occurred and the deduction was not allowed. **Johnson v. Comm'r, T.C. Memo. 2001-97**.

SECURED TRANSACTIONS

PRIORITY. The plaintiff loaned money to a farmer for operating expenses to grow a crop of corn in 1995. In March 1995, the farmer granted the plaintiff a security interest in the crop and other farm products. The security interest was perfected. In February 1995, the farmer had executed a contract to deliver 30,000 bushels of corn to the defendant. The plaintiff notified the defendant about the security interest in the corn. The farmer delivered a portion of the contracted corn but notified the defendant that no more corn would be delivered. The defendant purchased replacement corn and deducted the price from the amount paid to the farmer for the corn delivered. The case does not discuss why the setoff was not limited to the difference in price for the cover corn as against the contract price. The plaintiff argued that its security interest had priority over the defendant's right to setoff the corn purchased to cover the contract. The court held that the defendant's right of setoff did not affect the security interest since the plaintiff was not a party to the contract. Therefore, the court held that the security interest had priority and the defendant was required to pay the setoff amount to the plaintiff. **Ag Services of America v. DeBruce Grain, 19 P.3d 188 (Kan. Ct. App. 2001)**.

STATE REGULATION OF AGRICULTURE

TUBERCULOSIS. The plaintiff had imported from Canada a herd of elk. Six of the elk responded positive to a tuberculosis test and were required to be destroyed in order to conduct a post-mortem test for tuberculosis. The issue was the value of the six elk for purposes of compensating the plaintiff under Mo. Stat. § 267.610. The plaintiff argued that the elk should have been valued as if they were disease free. The court held that the statute required an appraisal of the destroyed animal in its condition at the time of the appraisal, which included its condition as infected with tuberculosis. **Carmack v. Missouri Dept. of Agriculture, 31 S.W.3d 40 (Mo. Ct. App. 2000)**.

CITATION UPDATES

Catalano v. Comm'r, 240 F.3d 842 (9th Cir. 2001), *aff'g*, T.C. Memo. 1998-447 (S corporation business expenses) see p. 47 *supra*.

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