liability for the year would not change.

The obvious question is whether the AMT credit[12] would provide any relief against the regular tax in future years.

The AMT credit

The credit for prior year minimum tax is designed to reduce the regular tax liability by part or all of the AMT paid in previous years.[13] The credit can be carried forward indefinitely to offset regular tax in future years; therefore, it is not necessary to determine which prior year's minimum tax credit is being used in a particular year.[14] The minimum credit cannot be carried back.[15] The rules are different for individuals (using Form 8801) and for corporations (using Form 8827).[16]

Individuals. The alternative minimum tax credit is limited to the extent that regular tax liability (reduced by the other nonrefundable credits) exceeds the tentative minimum tax for the year.[17] The prior year minimum tax credit for individuals generally arises only in connection with deferral-type preferences and adjustments.[18] Exclusion-type adjustments include—(1) the standard deduction, (2) personal exemptions, (3) medical and dental expenses, (4) miscellaneous itemized deductions and (5) interest expense.[19] Real and personal property taxes and state, local and foreign income, war profits and excess profits taxes are also in that category[20] unless allowable in computing adjusted gross income.[21] Exclusion-type preference items include depletion, tax-exempt interest and gains from small business stock.[22] "Adjusted minimum tax" is the net minimum tax reduced by the amount that would have been the net minimum tax if only the exclusion-type preferences and adjustments had been considered.[23]

Corporations. A corporation AMT credit is limited to the amount the regular tax (reduced by the other credits) exceeds 25 percent of the excess of the corporation's regular tax over $25,000.[24] That limitation was added by the Tax Reform Act of 1997.

Example: The committee report contains an example of married taxpayers, filing a joint return with—(1) no regular taxable income, (2) deferral preferences in the amount of $300,000 and (3) exclusion preferences (including disallowed itemized deductions) of $240,000. Under the 25 percent alternative minimum tax rate and the $40,000 exemption amount (which were in effect at that time), minimum tax liability would total $125,000. However, if the taxpayers had only exclusion preferences, the minimum tax liability would have been $50,000 (25 percent of $240,000 as reduced by the $40,000 exemption). Thus, the amount of minimum tax available as a carryforward credit would be $75,000 ($125,000 less $50,000).[25]

In conclusion

Unless and until changed by Congress, those using income averaging will need to watch closely to see if AMT diminishes or eliminates the benefits from the averaging election.

FOOTNOTES

1 Tax Reform Act of 1997, Pub. L. 105-34, Sec. 403(a), 111 Stat. 844 (1977), repealing I.R.C. § 56(a)(6). See generally 4 Harl, *Agricultural Law* § 26.06[1][f][iii][E] (1999); Harl, *Agricultural Law Manual* § 4.01[1][b][ii] (1999).

2 4 Harl *supra* n. 1, § 26.08; Harl, *supra* n. 1, § 4.01[4].

3 Tax Reform Act of 1997, Pub. L. 105-34, Sec. 933(c), adding I.R.C. § 1301.

4 Pub. L. 105-277, Sec. 2011, 105th Cong., 2d Sess. (1998).

5 I.R.C. § 1301(a)(2).

6 I.R.C. § 1301(b).

7 See I.R.C. § 55.

8 I.R.C. § 1301(a).

9 Joint Committee on Taxation, General Explanation of Tax Legislation Enacted in 1997, Dec. 17, 1997, p. 131.

10 Conf. Rep. To H.R. 2014, 105th Cong., 1st Sess. (1997).

11 Bock and Harris, Farm Income Tax School Workbook 311 (1997).

12 I.R.C. § 53.

13 See I.R.C. § 53(a).

14 See I.R.C. § 53.

15 *Id*.

16 I.R.C. § 53(d)(1)(iv).

17 I.R.C. § 53(c).

18 See I.R.C. § 53(d)(1)(B).

19 I.R.C. §§ 53(d)(1)(B)(ii), 56(b)(1), 57(a)(1), (5), (7).

20 I.R.C. §§ 56(b)(1)(A), 164(a)(1), (2), (3).

21 I.R.C. § 56(b)(1)(A).

22 I.R.C. §§ 53(d)(1)(B)(ii), 57(a)(1), (5), (7).

23 I.R.C. § 53(d)(1)(B)(i).

24 I.R.C. § 53(d)(1)(B)(iv).

25 House Com. Rep't on Pub. L. 99-514, 1986.

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

BANKRUPTCY

FEDERAL TAXATION-*ALM* § 13.03[7].*

DISCHARGE. The debtors filed a previous Chapter 13 case in August 1990 and the IRS filed claims for unpaid taxes for 1987, 1988 and 1989. The Chapter 13 plan provided for payment of the taxes but the debtor failed to fully pay the tax claims before the case was dismissed in October 1994. The current case was filed in January 1995 and the IRS again filed its claim for the 1987 through 1989 taxes. The debtors argued that the tax claims were no longer entitled to a priority because the taxes were due more than three years before the petition was filed. The IRS argued, as several courts have held, that the three year period of Section 523(a)(2) was tolled during the first bankruptcy case. The court, however, held that the statute provided no authority for any tolling of the three year period. Instead, the court held that the Bankruptcy Court could give the tax claims priority based on the court's equity power under Section 105 and remanded the case

**Agricultural Law Manual* (ALM).

for a determination of the equities of allowing the tax claims to retain priority because of the previous bankruptcy case. ***In re* Morgan, 99-2 U.S. Tax Cas. (CCH) ¶ 50,712 (11th Cir. 1999)**.

After losing a Tax Court case which held that the debtor owed taxes, the debtor married his long-time companion and executed an antenuptial agreement which transferred all of the assets of a corporation owned by the debtor to the debtor's spouse's corporation. In return, the spouse transferred to the debtor debts owed to her by the debtor. Neither set of assets had much value because the debtor's corporation had been incurring substantial losses. However, because the debtor's corporation owned the debtor's residence and vehicles, the antenuptial agreement effectively removed from the debtor's estate all assets against which the IRS could levy to satisfy the Tax Court judgment. The IRS petitioned for nondischarge of the debtor on the tax claims for willful and fraudulent attempt to evade taxes. The court held that the tax debt was nondischargeable because the intentional and voluntary transfer of the debtor's assets without adequate consideration to a family member was a willful and fraudulent attempt to evade taxes. On appeal, the appellate court reversed, holding that, under *In re Haas, 48 F.3d 1153 (11th Cir. 1994)*, the mere non-payment of taxes did not amount to a willful attempt to evade taxes under Section 523(a)(1)(C). The court expressed reservations about the wisdom of *Haas* under the facts of this case but felt compelled to follow *Haas*. ***In re* Griffith, 99-2 U.S. Tax Cas. (CCH) ¶ 50,749 (11th Cir. 1999), *rev'g*, 210 B.R. 216 (S.D. Fla. 1997), *aff'g*, 161 B.R. 727 (Bankr. S.D. Fla. 1993)**.

POST-PETITION TAXES. The debtor filed for Chapter 11 in October 1995 but did not make the election to bifurcate the 1995 tax year as of the petition date. The debtor's plan provided for payment of the 1995 taxes and a lien securing the payments. The IRS had notice of the plan but did not object, and the plan was confirmed. The IRS then attempted to levy for collection of the 1995 taxes and the debtor filed a motion to enjoin the levy as violating the plan. The court held that the IRS could levy for the taxes because (1) the failure of the debtor to elect to bifurcate the 1995 tax year made the 1995 taxes post-petition taxes and a personal liability of the debtor, (2) the taxes were nondischargeable, and (3) the Anti-Injunction Act prohibited judicial interference with the levy. ***In re* Wood, 99-2 U.S. Tax Cas. (CCH) ¶ 50,730 (C.D. Calif. 1999)**.

SALE OF RESIDENCE. The Chapter 7 trustee sold the debtor's residence. The court held that the bankruptcy estate was entitled to exclude the gain on the sale under the I.R.C. § 121 exemption for sale of a personal residence. ***In re* Williams, 99-2 U.S. Tax Cas. (CCH) ¶ 50,738 (Bankr. D. Md. 1999); *In re* Slye, 99-2 U.S. Tax Cas. (CCH) ¶ 50,739 (Bankr. D. Md. 1999); *In re* Curran, 99-2 U.S. Tax Cas. (CCH) ¶ 50,742 (Bankr. N.D. Ga. 1999)**.

The IRS has now conceded the issue. **Chief Counsel Notice (35)-000-162, Aug. 10, 1999**.

TAX LIEN. The IRS filed a Notice of Federal Tax Lien and Levy on an administrator of a retirement plan in which the debtor owned an interest. Before the levy was executed by the administrator, the debtor filed for Chapter 7 bankruptcy. The IRS filed a claim in the bankruptcy case and the Bankruptcy Court approved the sale of all assets to the debtor, free and clear of all liens. The retirement plan was not excluded or exempted from the bankruptcy estate by the debtor. The debtor then received a discharge without objection from the IRS. The IRS also did not appeal the discharge. The IRS ruled that the discharge ruling was res judicata as to the taxes discharged and the tax lien did not attach to the debtor's interest in the retirement plan post-discharge. **Ltr. Rul. 9929005, March 25, 1999**.

CONTRACTS

HEDGE-TO-ARRIVE CONTRACTS. The plaintiffs were grain farmers who entered into cash forward contracts which contained provisions for rolling over the delivery date of the contract. The contracts were made with the defendant elevator which had sufficient facilities to take delivery. The plaintiff sought to avoid enforcement of the contracts by arguing that the contracts were off-exchange futures contracts which violated the Commodity Exchange Act. The court found that the front of each contract was a standard cash forward contract which called for actual delivery of a crop sold by the producer to the defendant elevator. The backs of the contracts contained similar provisions which allowed either party to request and approve rolling over the delivery date to the next crop year upon agreement of both parties. The court held that the rollover provisions did not convert the contracts into illegal, off-exchange futures contracts. **Barz v. Geneva Elevator Co., 12 F. Supp.2d 943 (N.D. Iowa 1998)**.

FEDERAL AGRICULTURAL PROGRAMS

CROP INSURANCE. The FCIC has adopted as final regulations amending the Catastrophic Risk Protection (CAT) endorsement regulations to (1) delete the provisions regarding the termination of the policy for failure to pay CAT administrative fees since those provisions have been incorporated into the Basic Provisions; (2) specify that the administrative fee for CAT coverage for each crop in the county will be $10 plus the greater of either $50 or 10 percent of the premium under the CAT policy; and (3) revise the date CAT fees will be due to coincide with when the premium is due for additional coverage. This last rule eliminates all references to refunding administrative fees in the event that the producer decided to change coverage levels prior to the sales closing date since fees would not have been paid. Also, this rule makes the provisions concerning the payment of administrative fees in the year of application consistent with the payment of administrative fees for limited coverage. This rule eliminates the termination provisions since they have been incorporated into the Basic Provisions. **64 Fed. Reg. 40738 (July 28, 1999)**.

FARM CREDIT SYSTEM. The FCA has issued final regulations on the release of information under the Freedom of Information Act (FOIA) to reflect new fees and make it easier for the public to get FCA records; revise the procedures for requests for testimony by FCA employees on official matters and for producing FCA documents in litigation when FCA is not a named party; and add procedures for getting records in public rulemaking files. **64 Fed. Reg. 41770 (Aug. 2, 1999)**.

MIGRANT AGRICULTURAL LABOR. The plaintiffs were migrant farm laborers hired by a farm labor contractor who was hired by the defendant to provide pickers to harvest snap beans in three crop years. In the first two years, the farm labor contractor was properly registered but in the third year the registration was not obtained and the contractor failed to obtain health and

accident insurance. The plaintiffs were injured in a truck accident while being transported to the defendant's fields. Also included as defendants were a bean processor and its president who purchased the bean crop under a contract with the defendant farmer. The plaintiffs sought to hold all of the defendants liable for their injuries because the defendants were joint employers with the labor contractor and for failing to require the labor contractor to certify registration under the MSAWPA. The trial court jury had found that the farmer was liable for failing to check the labor contractor's MSAWPA registration but awarded only statutory damages of $350 per plaintiff because the farmer's failure to check registration was too far removed from the cause of the injury. The court examined the seven factors of the regulations, 29 C.F.R. § 500.20, and case law to hold that the farmer was liable as a joint employer of the plaintiffs with the labor contractor because the plaintiffs were economically dependent upon the farmer: (1) the farmer exercised indirect control over the plaintiffs work, (2) the plaintiffs did not require much training for the work for the farmer, (3) the plaintiffs' work was integral to the farmer's business, and (4) the work was performed on the farmer's land. The processing company and its president were held not to be joint employers because there was no evidence of involvement with the plaintiffs' employment. The court also reversed on the issue of the farmer's liability for actual damages for the plaintiffs' injuries, holding that the farmer's failure to insure that the labor contractor was properly registered under the MSAWPA caused the plaintiffs to not have access to insurance which would have been required for the registration. **Charles v. Burton, 169 F.3d 1322 (11th Cir. 1999).**

The plaintiffs were hired by the defendant to harvest tobacco on the defendant's farm and filed suit for violations of MSAWPA by the defendant, including transportation of the plaintiffs on a tobacco harvester. One plaintiff was injured from a fall from the harvester while the plaintiffs were being transported on a highway between fields. The defendant sought summary judgment based on arguments that (1) the plaintiffs were not migrant workers under the Act because the plaintiffs lived in Georgia and did not have to stay away from their residence over night, (2) the defendant was exempt from the act as a family farm business, (3) the defendant was exempt from the act as a small business, and (4) the transportation of workers on a harvester is exempt from the motor vehicle safety provisions of the Act. The court found that the plaintiffs' residence was in Florida because that was where the plaintiffs returned each winter and stored all their furniture; therefore, the plaintiffs were migrant workers when they worked for the defendant in Georgia. In addition, one plaintiff was a nonresident alien and the Act defines a nonresident alien's residence as the alien's country of origin. The court held that the defendant was not eligible for the family farm exemption because the defendant did not perform all of the farm labor contracting activities. The court held that summary judgment could not be granted on the small business exemption because the defendant had not submitted sufficient information as to the defendant's employment of migrant labor in the past year. The court held that the transportation of the workers on a harvester on the highway was subject to the motor vehicle safety standards because the transportation was not incidental to the workers' jobs of harvesting tobacco. The court restricted this exemption to transportation on the harvester while the workers were harvesting crop in the field. **Soto v. McClean, 20 F. Supp.2d 901 (E.D. N.C. 1998)**.

FEDERAL ESTATE AND GIFT TAX

FAMILY-OWNED BUSINESS DEDUCTION. Legislation has been introduced in the U.S. Senate which would increase the FOBD from $1.3 million to $2.6 million. **Sen. 1413, 106th Cong., 1st Sess. (1999)**.

GENERATION SKIPPING TRANSFERS. The decedent owned a life interest in a trust established prior to 1985. The trust provided the decedent with the testamentary power to appoint trust corpus and the decedent's will appointed the trust property to the decedent's grandchildren. The court held that the exercise of the power of appointment did not subject the trust to GSTT because the power was exercised under the trust provisions which became irrevocable before September 25, 1985. **Simpson v. United States, 99-2 U.S. Tax Cas. (CCH) ¶ 60,351 (8th Cir. 1999), *rev'g*, 17 F. Supp. 2d 972 (W.D. Mo. 1998).**

INSTALLMENT PAYMENT OF ESTATE TAX. The decedent owned interests in a corporation which owned and leased various commercial properties. The corporation provided significant maintenance and other business services for most of the properties but one property was leased only for advertising. The IRS ruled that the decedent's interests in the corporation qualified as a trade or business for installment payment of estate tax purposes except for the property leased for advertising. **Ltr. Rul. 9929025, April 26, 1999**.

POWER OF APPOINTMENT. The decedent was the sole trustee of a trust established by the decedent's predeceased parent. The trust beneficiaries were the decedent's children and the trust was established to hold the stock in two family corporations in order to maintain the family ownership and continuation of the corporations. The trust authorized the trustee to amend the trust in whole or part. The IRS examined state law and the intent of the grantor and ruled that the decedent did not have a general power of appointment over trust corpus because the decedent could not amend the trust to distribute trust corpus to the decedent, the decedent's estate or the decedent's creditors. The trust also provided that the trustee could control the distributions of trust income to the trustee's children, but not the children of the trustee's siblings. The IRS ruled that this power did not amount to a power of appointment, even while the children were minors, because the decedent's fiduciary duty prohibited the use of trust funds to satisfy the decedent's legal obligation to support the children. **FSA Ltr. Rul. 9930026, April 26, 1999**.

FEDERAL INCOME TAXATION

CAPITAL GAIN. The IRS has issued proposed regulations which provide that, for purposes of applying section 1(h)(7)(B) (which provides that a taxpayer's unrecaptured section 1250 gain cannot exceed the taxpayer's net section 1231 gain), gain from the sale of a partnership interest that results in section 1250 capital gain is not treated as section 1231 gain even if section 1231 could apply to the disposition of the underlying partnership property. The IRS noted that, although section 1(h)(7) (in combination with section 751) applies a limited look-through rule for purposes of

determining the capital gain rate applicable to the sale of a partnership interest, no similar look-through rule applies for purposes of applying section 1231. **64 Fed. Reg. 43117 (Aug. 9, 1999), *adding* Prop. Treas. Reg. § 1.1223-3**.

COMMODITY FUTURES. The taxpayers donated commodity futures to a charity. The transaction was subject to I.R.C. § 1256 which required the taxpayers to mark the futures to market and realize gain upon the transfer to the charity. The taxpayers argued that I.R.C. § 1256(a)(2) provided an exception where the donor does not receive any actual proceeds from the donation. The court held that I.R.C. § 1256(a)(2) did not provide an exception for donations to charity but only protected the donor against taxation for any subsequently realized gain. Therefore, the taxpayers realize gain from the donation of the commodity futures to the charity. **Greene v. United States, 99-2 U.S. Tax Cas. (CCH) ¶ 50,701 (2d Cir. 1999), *aff'g*, 98-1 U.S. Tax Cas. (CCH) ¶ 50,291 (S.D. N.Y. 1998)**.

CONSTRUCTIVE PAYMENT. The taxpayer was a family-owned corporation which reported income and deductions on the accrual method. The taxpayer claimed a deduction for compensation accrued but not paid to family members. The taxpayer agreed that it should have used the cash basis method of reporting but argued that the compensation was still deductible prior to payment because the employees could have withdrawn the compensation in the tax year in which the wages were deducted. The court held that, although there was a doctrine of constructive receipt of compensation, there was no authority for allowing a deduction for constructive payments. In addition, the court noted that there was no need for such a rule where the employer and employee were both cash basis taxpayers. **Unico Sales & Marketing, Inc. v. Comm'r, T.C. Memo. 1999-242**.

CORPORATIONS

PURCHASE OF STOCK. The IRS has issued proposed regulations relating to the allocation of purchase price in deemed and actual asset acquisitions under I.R.C. § 338. The proposed regulations determine the amount realized and the amount of basis allocated to each asset transferred in a deemed or actual asset acquisition and affect transactions reported on either Form 8023 or Form 8594. **64 Fed. Reg. 43461 (Aug. 10, 1999)**.

COURT AWARDS AND SETTLEMENTS. The taxpayers were employees of a large corporation which instituted a downsizing program which included incentives for employees to terminate employment voluntarily. The company established a general release agreement and determined the termination payment. The taxpayers stipulated that, prior to signing the general release and covenant not to sue, they had not experienced any symptoms of personal injury, including any physical or emotional harm; had not asserted or threatened any claim against the employer for personal injury, including any physical or emotional harm; and had not communicated with the company regarding any personal injuries or claims for personal injury, including any physical or emotional harm. The company withheld employment taxes from the release payments. The taxpayers withheld a portion of the payments as settlement of tort or tort-like ADEA claims. The taxpayers argued that the company had anticipated that some of the employment terminations could lead to lawsuits; therefore, a portion of the release payments should be considered as paid in settlement of potential tort claims from the terminated employees. The court held that the payment were included in the taxpayers' incomes because no tort claims were ever made or settled by individual negotiations. **Abrahamsen v. United States, 99-2 U.S. Tax Cas. ¶ 50,697 (Fed. Cls. 1999)**.

DEPRECIATION. The taxpayer purchased a used bus and converted the bus to a motor home over two tax years. The taxpayer made significant improvements to the bus in the conversion but did not claim any depreciation deductions for the bus based on the costs of the improvements. The bus was found to be 5-year property for depreciation purposes and in the fifth year after placing the bus in service, the bus was destroyed by a fire. The taxpayer received insurance proceeds for the replacement cost of the bus but did not claim any gain from receipt of the proceeds. The court held that the basis of the bus in the year of loss was the total amounts expended on the bus and improvements less the amount of depreciation allowable over the first four years; therefore, the taxpayer recognized gain to the extent the insurance proceeds exceeded the basis. **Montoya v. Comm'r, T.C. Memo. 1999-269**.

Legislation has been introduced in the U.S. Senate which would reduce from 24 months to 12 months the capital gains holding period for horses. **Sen. 1409, 106th Cong., 1st Sess. 1999**.

The IRS has issued a correction to its 1998 instructions for Form 4562, Depreciation and Amortization, and Publication 527, Residential Rental Property, regarding the classification of certain personal property used in rental real estate activity, such as appliances, furniture and carpeting. The correct classification should have been five-year property rather than seven- year property. Further, the correct recovery period for the regular tax is five years under the General Depreciation System and nine years under the Alternative Depreciation System. Also, when using a five-year recovery period for this property for the regular tax, any alternative minimum tax adjustment must be figured using a nine-year recovery period. However, if the property was placed into service after 1998, the same recovery period applies for both the regular tax and the AMT. **Ann. 99-82, I.R.B. 1999-__**.

Pursuant to the directive in the Tax and Trade Relief Extension Act of 1998 (Pub. L. No. 105-277), the Treasury Department is conducting a comprehensive study of the recovery periods and depreciation methods under I.R.C. § 168 that must be sent to the House Ways and Means Committee and to the Senate Finance Committee no later than March 31, 2000. The public has been invited to submit comments regarding the determination of depreciation recovery periods and methods. The Treasury's Office of Tax Analysis will review and consider all comments and other information received in response to this notice in preparing its study. **Notice 99-34, I.R.B. 1999-__**.

HOBBY LOSSES-*ALM* § 4.05[1].* The taxpayers purchased a farm which was enrolled in the Conservation Reserve Program (CRP). The taxpayers had to apply to the USDA to take over the participation in the CRP from the previous owners and the USDA ruled that the taxpayers were actively engaged in the business of farming. The IRS, however, assessed tax deficiencies based on disallowance of deductions for farm expenses because the taxpayers were not engaged in farming for a profit. The taxpayers eventually won their appeal on that issue and sought litigation fees from the IRS because the IRS position was not substantially justified. The taxpayers argued that the USDA finding was binding on the IRS. The court held that the USDA finding was based on different criteria from those used by the IRS. The court noted that the taxpayers had not supplied the IRS with sufficient information to make a full determination early and that factual issues remained through most of the appeal process. The appellate

court affirmed in a decision designated as not for publication. **Hasbrouck v. Comm'r, 99-2 U.S. Tax Cas. (CCH) ¶ 50,731 (9th Cir. 1999), *aff'g*, T.C. Memo. 1998-249**.

The taxpayer was employed as a medical doctor and also operated a horse breeding activity. The court held that the horse breeding activity was not engaged in for profit under the nine factors of Treas. Reg. § 1.183-2(b): (1) the business records were not accurately maintained to reflect business and personal costs; (2) the taxpayer had no written business plan to make the activity profitable; (3) the taxpayer had little expertise in operating a breeding business, although the taxpayer had some expertise in breeding, and the taxpayer did not consult business experts except for tax professionals; (4) most of the taxpayer's time spent on the activity was devoted to the more enjoyable activities, with the most onerous activities hired out; (5) the taxpayer failed to show that the assets would appreciate sufficiently to create a profit; (6) the activity had losses for all six years and the taxpayers could not reasonably project further profits; (7) the taxpayer had income from other sources which was offset by the breeding activity losses; and (8) the taxpayer derived considerable personal pleasure from the taxpayer's participation in the activity. **Hillman v. Comm'r, T.C. Memo. 1999-255**.

ORIGINIAL ISSUE DISCOUNT. The IRS has announced that the original issue discount (OID) tables that appear in Publication 1212, List of Original Issue Discount Instruments, will no longer be available electronically from the IRS bulletin board (IRS-BBS) in Martinsburg, WV, after October 1999. Beginning in November 1999, the tables can be accessed on the IRS Internet web site at www.irs.ustreas.gov. **Ann. 99-71, I.R.B. 1999-31, 219**.

PASSIVE ACTIVITY LOSSES. The taxpayers owned a condominium unit which was rented to third parties when the taxpayers were not using it for vacation purposes. The unit was managed by a third party which charged the taxpayers 45 percent of the revenue from the rentals. The evidence showed that the taxpayers spent less than 100 hours per year in managing the renting of the unit; therefore, the court held that the losses from the unit were passive activity losses. **Rapp v. Comm'r, T.C. Memo. 1999-249**.

The taxpayer operated a car rental business which had tax losses. The deductions of the losses were disallowed under I.R.C. § 469 as passive rental losses. The taxpayer argued that the allowance of $25,000 of passive losses from real property rental activity violated the Equal Protection Clause of the Fifth Amendment to the U.S. Constitution. The court held that the distinction between real property rental passive losses, up to $25,000, and personal property rental passive losses was constitutional because it had a rational basis in Congressional intent to help small real estate investors who invested in rental real estate for non-tax purposes. **Schetzer v. Comm'r, T.C. Memo. 1999-252**.

PARTNERSHIPS-*ALM* § 7.03.*

SALE OF PARTNERSHIP INTEREST. The IRS has issued proposed regulations which provide rules relating to the allocation of a divided holding period with respect to an interest in a partnership. These rules generally provide that the holding period of a partnership interest will be divided if a partner acquires portions of an interest at different times or if an interest is acquired in a single transaction that gives rise to different holding periods under section 1223. The holding period of a portion of a partnership interest shall be determined based on a fraction that is equal to the fair market value of the portion of the partnership interest to which the holding period relates (determined immediately after the acquisition) over the fair market value of the entire partnership interest. A selling partner may use the actual holding period of the portion of a partnership interest sold if the partnership is a "publicly traded partnership" (as defined under section 7704(b)), the partnership interest is divided into identifiable units with ascertainable holding periods, and the selling partner can identify the portion of the interest transferred. Otherwise, the holding period(**s**) of the transferred interest must be divided in the same ratio as the holding period(**s**) of the partner'**s** entire partnership interest. **64 Fed. Reg. 43117 (Aug. 9, 1999), *amending* Treas. Reg. § 1.741-1(e), (f)**.

PREPRODUCTIVE PERIOD EXPENSES. The taxpayer, a partnership, planted nine month old fig trees in December of one year and January of the next year. Some of the trees produced sellable fruit in August of the third year and the rest did not produce fruit until after the third year. The taxpayer argued that some of the fig trees had a preproductive period of less than two years because sellable fruit was produced within two tax years after planting. The IRS disagreed, ruling that the preproductive period started with the propagation of the fig trees and includes the period before the tree is transplanted in the orchard. Secondly, the IRS ruled that the preproductive period is measured in calendar days and not in whole tax years; therefore, because the trees required more than two calendar years to produce marketable crops, the preproductive period exceeded two years. Third, the IRS ruled that the preproductive period ended only when the harvested crop was sufficiently large to generate enough revenue to offset the production costs and contribute enough revenue to the business to sustain the farming business. Finally, the IRS ruled that the preproductive period of fig trees exceeded two years because the USDA provided information that the national weighted average preproductive period for all fig trees exceeded two years. Therefore, the reproductive period expenses associated with the fig trees had to be capitalized in the trees. **Ltr. Rul. 9929001, April 6, 1999**.

PROFESSIONAL FEES. The taxpayer was a trustee and beneficiary of a trust which became irrevocable and funded upon the death of the grantor. One of the grantor's heirs filed a suit to challenge the validity of the trust, alleging incompetence of the decedent when the trust was established and undue influence by other heirs. The taxpayer defended the trust in the law suit and incurred legal expenses in successfully preserving the trust as valid. The taxpayer deducted the professional fees incurred as business expenses of the trust. The court held that the professional fees had to be capitalized in the basis of the trust assets because the fees were incurred in a suit involving the rights of the taxpayer in the property and not in a suit challenging the administration of the trust. **Stevens v. Comm'r, T.C. Memo. 1999-259**.

RETURNS. The IRS has published revised Instructions for Form 706-A (Revised August 1999), United States Additional Estate Tax Return. This document is available at no charge and can be obtained either: (1) by calling the IRS's toll-free telephone number, 1-800-829-3676; (2) at http://www.irs.ustreas.gov/prod/; (3) through FedWorld on the Internet; or (4) by directly accessing the Internal Revenue Information Services bulletin board at (703) 321-8020.

The IRS has issued temporary and final regulations that allow income tax return preparers to elect an alternative to their social

***Agricultural Law Manual* (ALM).**

security number (SSN) for purposes of identifying themselves on returns they prepare. **64 Fed. Reg. 43910 (Aug. 12, 1999)**.

The IRS has issued a revenue procedure that sets forth specifications governing the submission of 1999 Forms 1098, 1099, 5498 and W-2G electronically or on magnetic tape, tape cartridge or diskette for the 1999 tax year and for information returns for years prior to 1999 that are required to be filed. These specifications must be used to prepare current and prior year information returns filed beginning Jan. 1, 2000, and received by the IRS's Martinsburg Computing Center (IRS/MCC) or postmarked by Dec. 15, 2000. **Rev. Proc. 99-29 I.R.B. 1999-__**.

S CORPORATIONS-*ALM* § 7.02[3][c].

ELECTION. The taxpayers were shareholders in a corporation. The taxpayers claimed a share of the corporation's losses on their individual returns, based on the argument that a proper Subchapter S election was made for the corporation. However, the taxpayers had no written evidence of a mailing of Form 2553 and the IRS had no record of receiving the form. Therefore, the court held that no S corporation election was in effect and disallowed the loss deduction. **Barber v. Comm'r, T.C. Memo. 1999-260**.

NUMBER OF SHAREHOLDERS. Legislation has been introduced in the U.S. Senate which would consider all members of a family as one shareholder for S corporation purposes and would allow nonresident aliens to be shareholders. The legislation would also allow debt to be converted to stock and allow S corporations to issue preferred stock. **Sen. 1415, 106th Cong., 1st Sess. 1999**.

SALE OF RESIDENCE. This case involves law prior to passage of the exclusion of gain on the sale of a residence. The taxpayer received a residence as part of a divorce decree and sold the residence. The taxpayer failed to purchase a replacement residence within two years but also failed to report the gain from the previous sale of the residence. The taxpayer argued that the recognition of the gain should have occurred because the taxpayer was prevented from purchasing a second residence by the actions of the taxpayer's former spouse. The court held that no exception existed for the actions of third parties and held that the gain had to be included in the taxpayer's income. **Stilz v. Comm'r, T.C. Memo. 1999-245**.

SELF-EMPLOYMENT INCOME. The taxpayers were husband and wife and for many years both contributed labor to their farming operation. Some of the farm land was owned by the wife in her own name and was rented to the husband, with the wife continuing to provide services to the husband's farming operation under an agreement which provided compensation to the wife. The compensation was reported as wage income to the wife and was deducted as labor expense by the husband The taxpayers excluded the rental payments made by the husband to the wife from self-employment income of the wife. The court held that the rental income was included in self-employment income of the wife because the leasing of the land was made "under an arrangement" which included material participation of the landlord in the raising of agricultural commodities on the land. The case follows *Mizell v. Comm'r, T.C. Memo. 1995-571*. **Bot v. Comm'r, T.C. Memo. 1999-256**.

TAX LIENS. The taxpayer owed income taxes when the taxpayer became a beneficiary of a decedent's estate. After the taxpayer became a beneficiary, the IRS had filed a Notice of Federal Tax Lien. The IRS argued that the tax lien attached to the taxpayer's interest in the decedent's estate. The taxpayer, however, disclaimed any interest in the estate and argued that the disclaimer prevented the attachment of the tax lien. The court held that state law controlled the issue of whether the taxpayer had any property interest in the estate to which the lien could attach. The court held that Colorado law provided that an estate beneficiary did not have an interest in a decedent's estate until the beneficiary affirmatively accepted the bequest and that a beneficiary could disclaim an interest in the estate; therefore, the taxpayer's disclaimer prevented attachment of the tax lien. **Davidson v. United States, 99-2 U.S. Tax Cas. (CCH) ¶ 50,696 (D. Colo. 1999)**.

TAX PROTESTORS. The taxpayer filed a "common-law lien" against the property of an IRS revenue agent who was involved in collecting unpaid taxes owed by the taxpayer. In a ruling designated as not for publication, the court invalidated the lien because the taxpayer failed to show that the agent owed any debt to the taxpayer and ordered the taxpayer to show cause why a $2,000 fine should not be imposed for filing a frivolous appeal of the invalidation of the lien by the District Court. **United States v. Scott, 99-2 U.S. Tax Cas. (CCH) ¶ 50,745 (7th Cir. 1999)**.

THEFT LOSS. The taxpayer's home was burglarized and a 12 inch bronze statue was stolen. The statue was a gift in 1972 but the value of the statue was unknown to the taxpayer. The taxpayer never had the statue appraised or specifically identified as a casting made by the sculptor as compared to a copy made by third parties which was far less valuable. The taxpayer claimed a theft loss deduction for the value of the statue as an original. The court disallowed most of the deduction, setting the value at much less, based on two recorded sales of similar statues, because the taxpayer failed to provide sufficient proof that the statue was an artist's casting. **Vitale v. Comm'r, T.C. Memo. 1999-272**.

WATER LAW

PRESCRIPTIVE EASEMENT. The plaintiff owned land neighboring land leased by the defendant. A canal existed on the plaintiff's land which carried water to the defendant's and other neighbors' lands for over 40 years. The plaintiff took various actions which diverted water from the canal, eventually damaging the canal. The defendant installed a 10 inch PVC pipe on the plaintiff's property to replace the canal and the plaintiff brought this action in trespass for damages. The defendant claimed a prescriptive easement over the land where the pipe and canal existed. The trail court found that the defendant had proved the elements of a prescriptive easement. The plaintiff argued that the use of the land was permissive because the involved landowners had acted "neighborly" in regulating the water use. The court held that the use of the land for the canal was not permissive because the plaintiff failed to show that permission to use the land was ever sought or granted from the landowner. The court noted that cooperation between the neighbors did not amount to permission. The plaintiff also claimed that the installation of the PVC pipe was beyond the scope of the easement and was- an unreasonable use of the easement. The court held that the change in conveyance of the water was allowed where the change improved the water usage as to conservation. **Valcarce v. Fitzgerald, 961 P.2d 305 (Utah 1998)**.

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