# Agricultural Law Digest

An Agricultural Law Press Publication | Volume 7, No. 22 | November 15, 1996
Editor: Robert P. Achenbach, Jr. | Contributing Editor Dr. Neil E. Harl, Esq. | ISSN 1051-2780

# MORE ON INSTALLMENT SALES OF COMMODITIES AND AMT

— by Neil E. Harl*

In the June 21, 1996, issue of the Digest[1] we discussed in detail a technical advice memorandum[2] which imposed alternative minimum tax on the sale of potatoes on a deferred basis.[3] That TAM has now been formally released by the Internal Revenue Service.[4] In addition, a U.S. District Court case has upheld IRS in a deferred commodity sale.[5]

**Authority of the TAM**

IRS may impose a 20 percent accuracy-related penalty where there is a "substantial understatement of tax."[6] A substantial understatement exists when the understatement for the year exceeds the greater of (1) 10 percent of the tax required to be shown on the return (including self-employment tax) or (2) $5,000 ($10,000 for corporations other than S corporations or personal holding companies).[7] In general, taxpayers can avoid the penalty by showing - (1) that they acted in good faith and there was reasonable cause for the understatement, (2) that the understatement was based on substantial authority and (3) if there was a reasonable basis for the tax treatment of an item, the relevant facts affecting the item's tax treatment were adequately disclosed on Form 8275 (Form 8275-R for positions taken contrary to regulations).[8]

Technical advice memoranda issued after October 31, 1976, are considered "substantial authority."[9] Therefore, such authority should not be ignored.

**Coohey v. United States**

In late October, 1996, a U.S. District Court in Iowa decided a case involving deferred payment contracts for hogs.[10] The farmer had sold $915,967 of hogs on a deferred payment basis in late 1990 with payment to be made in early 1991.[11] IRS said the amount had to be reported in 1990 for AMT purposes, producing $151,791 of additional tax liability.

The farmer argued that it was a deferred payment sale and the AMT provisions[12] did not apply. The court sided with IRS and treated the transaction as an installment sale. The court stated that the taxpayer did not elect out of installment reporting so installment reporting applied automatically.[13] That meant AMT applied to the transaction.[14]

Ironically, had the taxpayer elected out of installment reporting, the regulations note that no other method of deferred reporting would have been available to the taxpayer.[15]

Another interesting feature of *Coohey v. United States* is that the taxpayer argued for a characterization of the transaction as a deferred payment arrangement.[16] Yet the Internal Revenue Service has consistently ruled that a sale of livestock to a buyer subject to the Packers and Stockyards Act is ineligible for deferral of income tax liability.[17] A U.S. District Court has disagreed, however, and has held that a cash basis farmer should be taxed in the year payment was received, which was the year following delivery of livestock to a market corporation that sold the livestock through an auction market.[18]

**Proposed Legislation**

Two bills have been introduced to eliminate the AMT problem on installment sales and deferred payment sales of commodities. S.368, which was introduced in 1995, and H.R. 4072, which was introduced in 1996, would address the problem. However, the 104th Congress adjourned without taking action on either bill. Thus, possible Congressional action was delayed until 1997.

**Any remaining distinction?**

An important issue, since the decision in *Coohey v. United States*,[19] is whether any meaningful distinction remains between installment sales of commodities[20] and deferred payment sales.[21] The *Coohey* case, blurred the line between the two marketing concepts. The 1995 TAM (issued in October of 1996), with different reasoning, implied that both types of arrangements were subject to AMT.[22] If *Coohey* is upheld on appeal, and is followed in later cases, the two approaches to commodity sales may be indistinguishable for AMT purposes. However, the two types of contracts are fundamentally different for other purposes.

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* Charles F. Curtiss Distinguished Professor in Agriculture and Professor of Economics, Iowa State University; member of the Iowa Bar.

**Agricultural Law Digest** is published by the Agricultural Law Press, P.O. Box 50703, Eugene, OR 97405 (ph/fax 541-302-1958), bimonthly except June and December. Annual subscription $100.  Printed with soy ink on recycled paper.

• Deferred payment contracts must be reported into income at year end unless made non-assignable and non transferable.[23]

• IRS has resisted the use of deferred payment contracts for sales of livestock where the purchaser was subject to the Packers and Stockyards Act.[24]

• Installment sale treatment is not available to taxpayers who maintain inventories under their method of accounting.[25]

Therefore, it is important to maintain an awareness of both types of transactions and to characterize particular transactions as one or the other, even though the two may be treated the same for AMT purposes.

**FOOTNOTES**

1 Harl, "Installment Sales of Commodities and AMT," 7 *Agric. L. Dig*. 93 (1996).
2 TAM 9640003, Dec. 21, 1995.
3 See generally 4 Harl, *Agricultural Law* § 25.03[2](1996); Harl, *Agricultural Law Manual* § 4.01[1][b][ii](1996). See also Harl, "Deferred Payment Sales: AMT Liability"; 4 *Agric. L. Dig*. 17 (1993).
4 TAM 9640003, Dec. 21, 1996.
5 Coohey v. United States, C 95-163 9 (N.D. Iowa 1996) (deferred payment sale of hogs treated as installment sale).
6 I.R.C. § 6662(d).
7 I.R.C. § 6662(d)(1)(A).
8 I.R.C. §§ 6662(d)(2); 6664(c).
9 Treas. Reg. § 1.6662-4(d)(3)(iii).
10 Coohey v. United States, No. C95-163 (N.D. Iowa 1996).
11 *Id*.
12 I.R.C. § 56(a)(6).
13 See I.R.C. § 453(d).
14 *Id*.
15 Temp. Treas. Reg. § 15A.453-1(d)(2).
16 See Rev. Rul. 58-162, 1958-1 C.B. 234.
17 Rev. Rul. 79-379, 1979-2 C.B. 204, Rev. Rul. 70-294, 1970-1 C.B. 13 (sale to buyer subject to Packers and Stockyards Act). See Rev. Rul. 72-465, 1972-2 C.B. 233.
18 Levno v. United States, 440 F. Supp. 8 (D. Mont. 1977).
19 See n. 5 *supra*.
20 See I.R.C. § 453(b)(2)(B).
21 See Rev. Rul. 58-162, 1958-1 C.B. 234.
22 TAM 9640003, Dec. 31, 1995, footnote 6.
23 See Ltr. Rul. 8001001, Sept. 4, 1979.
24 See n. 17 *supra*.
25 Sec I.R.C. § 453(b)(2)(B).

# CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

## ADVERSE POSSESSION

**FENCE**. In 1964, the plaintiff purchased property from a third party and the seller represented that a fence delineated the northern boundary of the property. The plaintiff continually maintained and mowed the land within the fence. The defendant purchased land north of the fence by sheriff's deed. The previous owner had purchased the land from the same third party who sold the southern portion to the plaintiff. The defendant ordered a survey of the property eight years after the purchase and discovered that the fence was located 10 feet onto the defendant's property. The defendant argued that the sheriff's deed conveyed title in preference to the title gained by the plaintiff by adverse possession. The court held that the defendant could acquire only the title held by the previous owner and because the plaintiff had acquired title by adverse possession before the sheriff's sale, the sheriff's deed was incapable of transferring title to the disputed strip. The defendant also argued that the failure of the plaintiff to pay property taxes on the disputed land prevented acquisition of the strip by adverse possession. The court held that because title by adverse possession provides no notice to the county tax assessor or to the adverse title holder, the failure to pay taxes on the strip does not affect acquisition by adverse possession. **Graham v. Lambeth, 921 P.2d 850 (Kan. Ct. App. 1996)**.

## ANIMALS

**COW**. A cow belonging to the plaintiff broke through a fence and wandered onto the defendant's property. The plaintiff went to the defendant's house and asked for permission to retrieve the cow; however, the plaintiff did not identify the cow or ask for return of the cow. Instead, the plaintiff filed suit for conversion and sought damages. The plaintiff argued that, under Ga. Code § 44-12-150, proof of conversion was not required because the defendant still possessed the cow. The court held that the statute did not apply because the defendant committed no unlawful act in acquiring possession of the cow. Therefore, because the plaintiff failed to provide any evidence that the defendant converted the cow or that the plaintiff had made a demand for the cow which was rejected, judgment for the defendant was proper. **Simmons v. Bearden, 474 S.E.2d 250 (Ga. Ct. App. 1996)**.

## BANKRUPTCY

**FEDERAL TAXATION-*ALM* § 13.03[7].***

**DISCHARGE**. The debtor timely filed the 1991 income tax return. In March 1994, the IRS discovered an error in the 1991 return and sent a notice to this effect to the debtor. The debtor did not respond to the letter. In December 1994 the IRS recorded the lack of response