"The Congressional reaction was to authorize installment sale treatment as another way to sell crops (and livestock).

"My belief is that the issuance of TAM 9640003, December 21, 1995, and the decision in the case of Coohey v. United States, N.D. Iowa 1996, represent an extension of the AMT concept to deferred payment sales. I believe that transitional relief is warranted inasmuch as contracts were in place based upon an expectation that AMT did not apply."

**FOOTNOTES**

[1] Harl, "Installment Sales of Commodities and AMT," 7 *Agric. L. Dig*. 93 (1996).

[2] Harl, "More on Installment Sales of Commodities and AMT," 7 *Agric. L. Dig*. 173 (1996).

[3] I.R.C. § 55(a).

[4] I.R.C. § 453(b)(2)(B).

[5] See Rev. Rul. 58-162, 1958-1 C.B. 234.

[6] See generally 4 Harl, *Agricultural Law* § 25.03[2](1996); Harl, *Agricultural Law Manual* § 4.01 [1][b][ii](1996).

[7] See Treas. Reg. § 1.6662-4(d)(3)(iii).

[8] TAM 9640003, Dec. 21, 1996. See Coohey v. United States, C 95-163 (N.D. Iowa 1996) (deferred payment sale of hogs treated as installment sale).

[9] I.R.C. § 55(a).

[10] See I.R.C. §§ 55(c)(1), 26(b) (defined as the Chapter 1 tax for the year with several specified adjustments).

[11] I.R.C. § 55(a).

[12] See Treas. Reg. § 1.55-1(a).

[13] Treas. Reg. § 1.446-1(e)(2)(ii)(a).

[14] TAM 9640003, Dec. 21, 1995.

[15] *Id*.

[16] I.R.C. § 481(a).

[17] See TAM 9640003, Dec. 21, 1995.

[18] I.R.C. § 481(b).

[19] TAM 9640003, Dec. 21, 1995.

[20] I.R.C. § 481(b)(l).

[21] *Id*.

[22] I.R.C. § 481(b)(2).

[23] *Id*.

[24] *Id*.

[25] The example is drawn substantially from an example prepared by Orville Bloethe, Victor, Iowa, and David Bibler, Algona, Iowa, for the Iowa State Bar Association Tax School, December 4-6, 1996, Des Moines, Iowa.

[26] I.R.C. §§ 55(d)(2), 55(b)(1)(B).

[27] I.R.C. § 55(b)(1)(A)(i)(II).

[28] I.R.C. § 55(d)(3).

[29] Treas. Reg. § 1.446-1(e)(3)(i).

[30] Treas. Reg. § 1.481-5(a).

[31] The request should be directed to Attention: T:R, Washington, D.C.

[32] Coohey v. United States, C 95-163 (N.D. Iowa 1996).

[33] TAM 9640003, Dec. 21, 1996.

# CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

## BANKRUPTCY

### GENERAL-*ALM* § 13.03.*

**DISCHARGE**. The debtors were three individuals who were shareholders and officers in a corporation which was a PACA-licensed produce dealer. The corporation purchased produce from a seller and failed to pay fully for the produce. The seller sued for payment in federal court and won a judgment for the unpaid amount. The District Court ruled that the judgment amount was nondischargeable in bankruptcy. The debtors then filed for bankruptcy and the seller filed a claim for the judgment amount and sought nondischargeability as to the claim for defalcation as a fiduciary, based upon the existence of the PACA trust for the unpaid amount. The court held that the debtors could be held accountable as fiduciaries as to the PACA trust amount; however, the seller failed to identify the amount of the PACA trust because the seller failed to demonstrate how much of the produce was resold and how much was lost due to spoilage. In addition, the court found that the seller failed to preserve its rights in the PACA trust by failing to serve the required timely notice of a PACA trust claim. The court refused to give *res judicata* effect to the District Court ruling as to dischargeability of the claim because the issue of dischargeability was not litigated in that action, nor was the action brought under the Bankruptcy Code. ***In re* Zois, 201 B.R. 501 (Bankr. N.D. Ill. 1996)**.

### CHAPTER 12-*ALM* § 13.03[8].*

**PLAN**. The debtors entered into a "Land Contract" with a creditor for the purchase of a farm, under which during the first two years, the debtors paid a rent of $1,150 per month. by the time of the bankruptcy petition, the lease period had expired. The contract provided that for years three through 20, the monthly payments increased and were to be applied against principal and interest due on the contract price. After the lease period, the debtors became liable for property taxes and insurance. The seller filed a claim for lease payments in default but did not specify the amount due on the lease portion of the contract. The debtors' plan provided for reduction of the secured portion of the contract to the fair market value of the property and unsecured status for the other amounts due. The court held that the first two years of the contract created a lease and that the remaining years were a traditional mortgage contract. The court held that once the lease expired, the amounts due under the lease merged with the mortgage contract; therefore, all payments were subject to the Chapter 12 cramdown provision, Sections 1222(b)(2), 1225(a)(5)(B). The plan was not confirmed, however, because the plan provided for only 3 percent interest on the unpaid portion of the claim. ***In re*** **Wilcox, 201 B.R. 334 (Bankr. N.D. N.Y. 1996)**.

The debtor was aged 65 and had operated the farm and cattle ranch for 40 years. The operation had five years of net losses. The debtor's plan provided for reduction of the number of acres owned by the debtor and the cash rental of the remaining acres, the growing of crops on newly rented acres, and a 40 head cow/calf operation. The plan provided for a streamlined farm operation, reducing labor and equipment expenses without explaining how those needs were to be otherwise met. The income from the wheat crop was based on the price of wheat at $5.00/bushel, although the current price was under $4.00 and testimony demonstrated that prices were not expected to go above $4.10/bushel. In addition, ranch income was based on the sale of 40 head of cattle per year which did not allow for any death or other loss of the herd. The Farm Credit Bank held a mortgage on the debtor's real property and $7,000 of FCB stock held by the debtor as required by the loan. The debtor's plan provided for 10 percent interest on the mortgage payments made under the plan and valued the secured portion of the claim by the fair market value of the real estate only. The debtor argued that the stock was not to be included in the secured claim because the stock could not be redeemed without the consent of the FCB. The court held that the interest rate was too low because the FCB offered 12.28 percent for similar loans. The court held that the value of the stock was included in the secured portion of the claim because the stock would be offset against the loan amount when the loan was paid off. The court also held that the plan was not confirmable because the debtor failed to provide a reasonable estimate of farm and ranch income. ***In re*** **Honeyman, 201 B.R. 533 (Bankr. D. N.D. 1996)**.

## CHAPTER 13-*ALM* § 13.03.*

**DISCHARGE**. The debtors filed for Chapter 13 and the plan was confirmed. The plan provided for monthly payments of $70 over an unspecified period for priority claims and $63 a month for a secured claim. The plan stated that all priority claims were to be paid in full. The debtors made all payments for 60 months and applied for a discharge. The payments, however, were not sufficient to pay all of the priority claims and the trustee moved for dismissal of the case. The court held that, because the plan period had expired, the plan could not be modified. Because the priority claims were not paid in full as provided in the plan, the case was dismissed. ***In re*** **Goude, 201 B.R. 275 (Bankr. D. Or. 1996)**.

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

**ALLOCATION OF TAX PAYMENTS**. The debtor was a corporation which filed for Chapter 11. The debtor's plan provided that payments made on an employment tax claim be applied first to the trust fund portion of the taxes before payment of interest and penalties. The effect of the plan provision was to relieve the corporate officers of their liability for the taxes under the responsible person provisions of I.R.C. § 6672. The court held that the allocation was not enforceable against the IRS because the debtor failed to demonstrate that the allocation would increase the likelihood of the successful reorganization of the debtor. ***In re*** **Oyster Bar of Pensacola, Inc., 201 B.R. 567 (Bankr. N.D. Fla. 1996)**.

**DISCHARGE**. In April 1985, the IRS mailed to the debtor a Notice of Deficiency as to the debtor's 1978 and 1981 individual income tax liabilities. In June 1985, the debtor petitioned the Tax Court for a redetermination of the deficiency. In March 1990, the debtor transferred title to the debtor's residence and van to the debtor's spouse for $10.00. The debtor's spouse was relieved of liability for the deficiencies by consent of the IRS under the innocent spouse rules. The debtor filed for Chapter 7 bankruptcy and sought discharge of the taxes. The IRS argued that the transfer of the residence and van was a willful attempt to evade payment of taxes and prohibited discharge under Sections 523(a)(1)(C) and 727. The court held that the transfer of essentially all of the debtor's assets to the spouse was a willful attempt to evade payment of taxes which were the basis of the IRS tax claim. ***In re*** **Schaeffer, 201 B.R. 282 (Bankr. D. Colo. 1996)**.

The debtor filed for Chapter 12 and the plan provided for full payment of all taxes owed as of the petition filing date. The debtor completed payments under the plan and sought a discharge. The IRS objected to the discharge, claiming that post-petition interest and penalties were still owed on the tax claims. The court held that the debtor was not liable for post-petition interest on tax claims which were paid in full under the plan. The court also held that the penalties on the taxes were not discharged because the failure to pay the taxes post-petition was the fault of the debtor and was not caused by operation of the bankruptcy law or rules. ***In re*** **Bossert, 201 B.R. 553 (Bankr. E.D. Wash. 1996)**.

The taxpayer was convicted of various crimes and was sent to prison. While in prison, the IRS contacted the taxpayer about unfiled returns for 1980 and 1981. The taxpayer cooperated with the IRS and eventually signed papers determining the amount of tax owed for those years. The taxpayer continued negotiations with the IRS after release from prison but was unable to make payments on the taxes and eventually filed for Chapter 7. The taxpayer argued that the taxes were dischargeable as assessed more than 240 days before the bankruptcy petition. The IRS argued that the taxes were not dischargeable because no returns were filed. The court held that the papers signed by the taxpayer in prison were intended as substitute returns and allowed discharge of the taxes. ***In re*** **Gless, 96-2 U.S. Tax Cas. (CCH) ¶ 50,639 (Bankr. D. Neb. 1996)**.

**SOVEREIGN IMMUNITY**. The debtor had received a discharge in a Chapter 13 case after paying all claims for federal income taxes, and the case was closed. However, the IRS filed liens, made levies and coerced the debtor into making post-discharge payments on the discharged taxes. The debtor brought suit to reopen the case and to recover the excess assessments and resulting costs for the suit. The IRS claimed the defense of sovereign immunity because the debtor's suit was not a claim of the bankruptcy estate. The court held that Section 106(a) provided a waiver of sovereign immunity only as to claims which were property of the estate at the commencement of the case or arising

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before the case is closed, Sections 541, 1306; therefore, because the debtor's case was closed and only the debtor would benefit from the suit, the IRS could not be considered to have waived its immunity under Section 106(a).The appellate court reversed, allowing the suit for nonpunitive monetary damages if the debtor could demonstrate that the IRS knew about the discharge injunction and intentionally violated the injunction. ***In re* Hardy, 97 F.3d 1384 (11th Cir. 1996), *rev'g and rem'g*, 171 B.R. 912 (S.D. Ga. 1994), *aff'g*,161 B.R. 320 (Bankr. S.D. Ga. 1993)**.

# FEDERAL AGRICULTURAL PROGRAMS

**PEANUTS**. The FSA has adotped as final regulations establishing the 1996 national peanut quota at 1,100,000 short tons. **61 Fed. Reg. 60509 (Nov. 29, 1996)**.

**TOBACCO**. The CCC has adopted as final regulations for the 1995 tobacco price support levels as follows:

| Kind and Type | Cents per pound |
|---|---|
| Virginia fire-cured(type 21) | 145.5 |
| Ky-Tenn. fire-cured(types 22-23) | 155.7 |
| Dark air-cured(types 35-36) | 133.9 |
| Virginia sun-cured(type 37) | 128.8 |
| Cigar filler & binder(types 42-44, 53-55) | 112.0 |
| Cigar filler (type 46) | 88.1 |

**61 Fed. Reg. 63697 (Dec. 2, 1996)**.

# FEDERAL ESTATE AND GIFT TAX

**GIFT-*ALM* § 6.01.*** The IRS has issued a modification of *Rev. Rul. 67-396, 1967-2 C.B. 351*. In Situation 1 of that ruling, the donor transferred a gift check on December 25 to a noncharitable donee, but the donee held the check until January 2 of the following year when the check was cashed by the drawee bank. *Rev. Rul. 67-396* held that the gift was not complete for federal gift tax purposes. Under *Metzger v. Comm'r, 38 F.3d 118 (4th Cir. 1994)*, the date of a gift by check relates back to the date of deposit by the donee so long as the check is paid by the drawee bank while the donor is alive, the donor intended to make a gift, delivery of the check was unconditional, and the donee presented the check for payment in the year gift tax treatment is sought and within a reasonable time of issuance. The IRS ruled that *Rev. Rul. 67-396* was revised to include the *Metzger* holding. However, the Situation 1 holding in *Rev. Rul. 67-396* remained unchanged. **Rev. Rul. 96-56, I.R.B. 1996-__.**

**TRANSFERS WITH RETAINED INTERESTS-*ALM* § 5.02[3].*** The decedent had sold the remainder interest in stock to an heir in exchange for an annuity valued at the same amount as the value of the remainder interest. The decedent retained a life estate in the stock and received more than a third of the annuity before death. The estate argued that the stock was not included in the decedent's estate because the decedent sold the remainder interest for full and adequate consideration, thus qualifying for the exception in I.R.C. § 2036(a). The Tax Court held that the stock was not eligible for the exception and was included in the decedent's gross estate, less the value of the annuity. The appellate court reversed, holding that the property was transferred for full and adequate consideration and was eligible for the exception. **Estate of D'Ambrosio v. Comm'r, 96-2 U.S. Tax Cas. (CCH) ¶ 60,252 (3d Cir. 1996), *rev'g*,105 T.C. 252 (1995)**.

**TRUSTS**. The taxpayer had established a qualified personal residence trust with a ten-year term and the taxpayer's grandchildren as remainder beneficiaries. The intent of the grantor in creating the trust was to minimize estate tax liabilities; however, the taxpayer had failed to consider the GSTT liability resulting from transfer of the remainder to the grandchildren and the taxpayer sought reformation of the trust to provide that the taxpayer's children would be the remainder holders. The court held that the reformation would be allowed under the Massachusetts rule of mistake. **Simches v. Simches, 96-2 U.S. Tax Cas. (CCH) ¶ 60,251 (Mass. 1996)**.

# FEDERAL INCOME TAXATION

**COURT AWARDS AND SETTLEMENTS-*ALM* § 4.02[14].*** The taxpayer received a jury award of compensatory and punitive damages in a personal injury action and sought to exclude the punitive damages from taxable income. The court reviewed the case law and acknowledged a split of authority and an inconclusive legislative history of I.R.C. § 104(a)(2), but held that, based on the doctrine of narrowly construing exclusions, the punitive damages were not excludible from income. **O'Gilvie v. United States, 96-2 U.S. Tax Cas. (CCH) ¶ 50,664 (S. Ct. 1996), *aff'g*, 66 F.3d 1550 (10th Cir. 1995), *rev'g*, 92-2 U.S. Tax Cas. (CCH) ¶ 50,567 (D. Kan. 1992)**.

The taxpayer filed a suit against the U.S. Postal Service alleging age, sex and handicap discrimination under title VII of the Civil Rights Act of 1964 and the Age Discrimination in Employment Act of 1967. The taxpayer received a negotiated settlement of that suit. The court held that the settlement proceeds were included in gross income because the suit was not for tort or tort-type rights involving personal injuries or sickness. **Rutt-Hahn v. Comm'r, T.C. Memo. 1996-536**..

**HOBBY LOSSES**. The taxpayers purchased a 7.5 acre ranch after the taxpayers retired. The farm never reported any net income. The farm operation consisted of 20 to 25 sheep, some chickens and peacocks, three horses and four cattle. The farm did not advertise animals or animal products for sale and sold only one sheep and eggs. The farm had an unlisted phone number. The taxpayers attended a few courses in animal husbandry but did not have any other experience with raising animals. The court disallowed deductions for farm expenses, depreciation and credits in excess of farm income because the farm was not operated with the intent to make a profit, since (1) the taxpayers did not keep separate, accurate records for the business, (2) did not have or seek expert advice, (3) did not devote substantial effort or time to the business, (4) did not expect any appreciation of assets sufficient to offset the losses, (5) did not have any successful past farming businesses, and (6) had a history of only losses and had substantial income from other sources which was offset by the net losses from the farm activity. **Whalley v. Comm'r, T.C. Memo. 1996-533**.

**INTEREST RATE**. The IRS has announced that for the period January 1, 1997 through March 31, 1997, the interest rate paid on tax overpayments is 8 percent and for underpayments is 9 percent. The interest rate for underpayments by large corporations is 11 percent. The interest rate on corporate overpayments above $10,000 is 6.5 percent. **Rev. Rul. 96-61, I.R.B 1996-__**.

**INVOLUNTARY CONVERSION**. The taxpayers owned interests in a ranch held for investment because the property was leased to third parties. A neighboring city notified the taxpayers of its intent to purchase the property for use as a site to construct a sewage plant. The city entered into sale negotiations but informed the taxpayers that if a price could not be negotiated, condemnation proceedings would occur. The IRS ruled that the negotiated sale of the ranch to the city was an involuntary conversion which would make purchase of qualified replacement property eligible for a tax-free exchange. **Ltr. Rul. 9649018, Sept. 3, 1996**.

**PARTNERSHIPS-*ALM* § 7.03[2].***

PARTNER'S DISTRIBUTIVE SHARE. The IRS has issued proposed regulations relating to the allocation of depreciation recapture among partners in a partnership. The proposed regulations amend existing regulations to require that any gain characterized as depreciation recapture must be allocated to each partner in an amount equal to the lesser of the partner's share of total gain from the sale of the property or the partner's share of depreciation from the property. **61 Fed. Reg. 65371 (Dec. 12, 1996)**.

**RETURNS**. The IRS has issued a reminder that all tax returns will be required to have valid taxpayer identification numbers for taxpayers, spouses and dependents born before December 1, 1996. Temporary, "applied for" and other substitute designations will not be accepted. Form W-7, Application for IRS Individual Taxpayer Identification Number can be obtained from the IRS web site: http://www.irs.ustreas.gov or calling the IRS toll-free number 1-800-829-3676.

CCH has reported that final regulations concerning the check-the-box entity classification are iminent. The regulations were expected to have been delivered to the Federal Register by December 13, 1996, for publishing by the end of theyear. The Federal Register may be searched and viewed online at:
**http://www.access.gpo.gov/su_docs/aces/aaces002.html**

**S CORPORATIONS-*ALM* § 7.02[3][c].***

TRUSTS. The taxpayer created an annuity trust for the benefit of the taxpayer. If the taxpayer survived the term of the annuity trust, the trust S corporation stock passed to one trust and other property passed to a family trust, both of which terminated at the later of the annuity term or the death of the taxpayer. The taxpayer had the power to acquire property in these trusts in exchange for property of identical value. At the termination of these two trusts, the corpus passed to the surviving spouse with remainders to separate trusts for the taxpayer's children. The IRS ruled that the trusts were grantor trusts during the life of the taxpayer and all income and deductions inured to the taxpayer. The IRS also ruled that the trust were QSSTs. **Ltr. Rul. 9648045, Sept. 3, 1996**.

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