non-recognition treatment.

· No later than five business days after the transfer of qualified indicia of ownership of the property to the EAT, the taxpayer and the EAT enter into a QEAA providing that the EAT is holding the property for the benefit of the taxpayer in order to facilitate a like-kind exchange and the taxpayer and the EAT agree to report the acquisition, holding and disposition of the property as provided in *Rev. Proc. 2000-37*.[12]

· No later than 45 days after the transfer, the relinquished property is properly identified.

· No later than 180 days after the transfer, the property is transferred to the taxpayer as replacement property[13] or is transferred to a person who is not the taxpayer or a disqualified person as relinquished property.

· Finally, the combined time period that the relinquished and replacement properties are held in QEAA does not exceed 180 days.[14]

The revenue procedure[15] states that property will not fail to be treated as held in a QEAA as a result of legal or contractual arrangements enumerated in *Rev. Proc. 2000-37.*[16] Also, property will not fail to be treated as being held in a QEAA merely because the accounting, regulatory or state, local or foreign tax treatment of the arrangement between the taxpayer and the EAT is different from the treatment in *Rev. Proc. 2000-37, § 4.02(3)*.[17]

Effective date

The procedure is effective for QEAAs entered into on or after September 15, 2000. There is, however, no inference intended for those entered into prior to that date.[18]

FOOTNOTES

1 602 F.2d 1341 (9th Cir. 1979). See generally 4 Harl *Agricultural Law* § 27.03[8][a][ii][C] (2000); Harl, *Agricultural Law Manual* § 4.02[16] (2001). See also Harl, “Identifying Property in a Like-Kind Exchange” 7 *Agric. L. Dig.* 101 (1998).

2 I.R.C. § 1031.

3 Starker v. United States, 602 F.2d 1341 (9th Cir. 1979).

4 I.R.C. § 1031(a)(3)(A). See Smith v. Comm’r, T.C. Memo. 1997-109, *aff’d*, 97-2 U.S. Tax Cas. (CCH) ¶ 50,928 (4th Cir. 1997) (no proof that replacement properties identified within 45 days after sale dates); Dobrich v. Comm’r, 99-2 U.S. Tax Cas. (CCH) ¶ 50,826 (9th Cir. 1999) (failure to identify replacement property within 45 days; also, taxpayers in constructive receipt of income).

5 I.R.C. § 1031(a)(3)(B); Treas. Reg. § 1.1031(k)-1(b)(2)(ii). See St. Laurent v. Comm’r, T.C. Memo. 1996-150 (replacement property transfer not completed within 180-day period; replacement property not like-kind); Christensen v. Comm’r, T.C. Memo. 1996-254, *aff’d*, 98-1 U.S. Tax Cas. (CCH) ¶ 50,352 (9th Cir. 1998) (transfers not completed within specified period; argument unsuccessful that four month extension of time to file could have been obtained).

6 The preamble to the final regulations on like-kind exchanges stated that the deferred exchange rules under I.R.C. § 1031(a)(3) do not apply to reverse-*Starker* exchanges (where the replacement property is acquired before the relinquished property is transferred) and that the final regulations do not apply to such exchanges. T.D. 8346, 1991-1 C.B. 150, 151. The preamble to the final regulations stated that the Department of the Treasury and the Internal Revenue Service would continue to study the applicability of the like-kind exchange rules to such transactions. *Id.*

7 I.R.B. 2000-40, 308.

8 I.R.B. 2000-40, 308 (allows accommodation party to be treated as owner of the property for tax purposes, enabling transactions to qualify as like-kind exchange).

9 *Id*

10 *Id*

11 *Id*

12 I.R.B. 2000-40, 308.

13 The revenue procedure (Rev. Proc. 2000-37, I.R.B. 40, 308) does not address why the safe harbor provisions do not state that the property must be received by the *earlier of* 180 days after the date of transfer of the taxpayer’s property or the due date, including extensions, of the transferor’s tax return for the tax year in which the transfer occurred. I.R.C. § 1031(a)(3)(B).

14 Rev. Proc. 2000-37, I.R.B. 2000-40, 308.

15 *Id*.

16 I.R.B. 2000-40, 308.

17 *Id*.

18 Rev. Proc. 2000-37, I.R.B. 2000-40, 308.

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

ANIMALS

EQUINE IMMUNITY STATUTE. The plaintiff was injured while riding on a practice sled pulled by two horses used in pulling competitions. The plaintiff fell off the sled when the horses suddenly started to move after the sled had been halted. The plaintiff sued for negligence in the design and maintenance of the sled. The defendant argued that the defendant was not liable for the injury under the equine immunity statute, Wis. Stat. § 895.481 and the recreational immunity statute, Wis. Stat. § 895.52. Only the first statute was applied in this case. The defendant argued that (1) the equine immunity statute applied only to equine professionals and (2) that an exception applied because the equipment was defective. The court held that the statute did not limit its application to professionals. The court also held that the statute applied to the accident involved in this case because there is an inherent risk that horses will move suddenly and without warning. The court held that the claim of a defect in the design and maintenance of the sled did not bar

Agricultural Law Manual* **(ALM).

application of the statute because the plaintiff failed to allege how any defect in the sled caused the plaintiff to fall. **Kangas v. Perry, 620 N.W.2d 429 (Wis. Ct. App. 2000)**.

BANKRUPTCY

GENERAL-*ALM* § 13.03.*

ABANDONED PROPERTY. The debtor filed for chapter 7 and the estate included a parcel of real property. The property remained in the estate for 26 months before the trustee abandoned the property back to the debtor. The debtor sought to charge the estate with the real estate taxes which accrued on the property during the administration of the estate until the property was abandoned. The trustee argued that the estate should not be held liable for the taxes because the estate did not benefit from the property. The court held that the estate was liable for the real estate taxes because the debtor had no control over the property while it was in the estate. The court noted that the trustee had 26 months to determine whether the property was beneficial to the estate and could have abandoned the property and reduced the tax burden much earlier. The court also noted that the trustee provided no reason for the delay in abandoning the property. ***In re* Mailman Steam Carpet Cleaning, Inc., 256 B.R. 240 (Bankr. D. Mass. 2000)**.

DISCHARGE. The debtor needed to purchase farm supplies on credit and filled out a credit application form provided by a supplier. The debtor understated the debtor's liabilities and overstated the debtor's assets on the form and failed to correct the amounts when the final loan documents were signed several days later. The loan was approved by a computerized scoring system, based entirely on the information on the loan application. The lender sought to have the loan balance declared nondischargeable under Section 523(a)(2)(B) as obtained with false information. The court held that (1) the asset and liability figures were materially false because the figures portrayed the debtor as having a positive net worth when the debtor had a negative net worth; (2) the lender reasonably relied on the figures because the application and the computerized scoring system were the regular method of making loan decisions; and (3) the debtor intended to deceive the lender because the debtor knew the figures were false and would be used by the lender to decide whether to make the loan. The court held that the loan balance was nondischargeable as obtained using false financial statements. ***In re* Webb, 256 B.R. 292 (Bankr. E.D. Ark. 2000)**.

EXEMPTIONS

HOMESTEAD. The debtors, husband and wife, filed for Chapter 7 and claimed their residence as an exempt homestead under Iowa Code § 561.16. The residence was purchased in 1998 and the schedules showed that at least some of the outstanding debts were incurred prior to the purchase of the residence. The trustee objected to the homestead exemption because, under Iowa Code § 561.21, a homestead was subject to execution to the extent that the debtors' debts were incurred prior to the purchase of the residence. The debtors argued that Section 522(c) preempted the Iowa exceptions to the homestead exemptions because Section 522(c) exempts exempt property from debts which arose prior to the bankruptcy petition. The court noted that *In re Weinstein, 164 F.3d 677 (1st Cir. 1999), cert. denied, 527 U.S. 1036 (1999)*, held that Section 522(c) preempted state law exceptions to exemptions, but the court declined to follow that decision and held that the debtors' residence was not exempt from debts which arose prior to the debtors' purchase of the residence. ***In re* Norkus, 256 B.R. 298 (Bankr. S.D. Iowa 2000)**.

FEDERAL TAX-*ALM* § 13.03[7].*

DISCHARGE. The debtors filed their 1992 tax return on October 15, 1993 without paying the taxes. The debtors made a few small payments on the taxes but then filed for Chapter 13 in May 1996. The 1992 taxes were included in the case and the case was voluntarily dismissed in March 1997 on the same day that the debtors filed for a new Chapter 7 case. The debtors argued that the 1992 taxes were dischargeable because they were filed more than three years before the Chapter 7 bankruptcy case. The court held that the three year period in Section 523(a)(1) was tolled during the Chapter 13 case; therefore, the taxes were nondischargeable. ***In re* Young, 233 F.3d 56 (1st Cir. 2000)**.

CORPORATIONS

DISSOLUTION. The plaintiff owned one-third of the stock of a family farm corporation, with the other two thirds owned by the plaintiff's brother and sister. The corporation's certificate of incorporation included a provision that a supermajority vote of 75 percent of the shareholder interests was required for several actions by the corporation, including dissolution. The parties began to disagree on corporate management and the plaintiff sought a dissolution of the corporation by filing an action in state court. The corporation argued that the certificate of incorporation controlled to require a vote by 75 percent of the shareholder interests to dissolve the corporation. Under Oklahoma law, 18 Okla. Stat. § 1006(B), shareholders could agree to increase the votes needed for any corporate action. However, 18 Okla. Stat. § 953(D) permits a minority shareholder to bring an action for judicial dissolution of a corporation. The court found that the certificate of incorporation provision requiring the supermajority affected only actions of the corporation and did not affect the right of a minority shareholder to bring a judicial action for dissolution. Therefore, the court held that the plaintiff was not barred by the certificate of incorporation from bringing an action for dissolution. **Sutter v. Sutter Ranch Corp., 14 P.3d 58 (Okla. 2000)**.

FEDERAL AGRICULTURAL PROGRAMS

ANNOUNCEMENT

A one-day conference, "Fixing the Fair Act," will be held at the National Press Club, Washington, D.C. on March 27, 2001. The conference is sponsored by Schnittker & Associates and the Iowa State University Center for International Agricultural Finance (Neil E. Harl is the Center Director). This is an opportunity to interact with some of the leading thinkers on the various dimensions of farm policy. Complete information may be obtained from John Schnittker, 1637 Calzada Avenue, Santa Ynez, California 93460, Tel. 805-686-5260 or via e-mail at jasjad@silcom.com.

PERISHABLE AGRICULTURAL COMMODITIES ACT. The Agricultural Marketing Service filed a complaint against the plaintiff for failure to make full payment promptly for 633 lots of produce. The Administrative Law Judge ruled that the plaintiff did violate PACA and recommended the revocation of the plaintiff's PACA license. The ALJ presented an oral decision and stated that the decision would be final in 35 days after service of the opinion unless an appeal was filed. A written opinion was filed later. The hearing clerk sent the written opinion to the plaintiff with a letter which stated that the plaintiff had 30 days after receipt of the opinion in which to appeal the decision. The plaintiff filled an appeal within 30 days after receiving the written opinion but more than 35 days after the oral opinion. The Judicial Officer refused to hear the appeal as untimely filed. The plaintiff argued that the USDA Rules of Practice, found at 7 C.F.R. §§ 1.142(c)(4), 1.145(a), were so inconsistent as to fail to provide adequate notice of the proper appeal time requirement. Section 1.142(c)(4) provided that an appeal must be filed within 35 days after issuance of an oral opinion. Section 1.145(a) provided that an appeal must be filed within 30 days after receipt of service of a judge's opinion. The court noted that the regulations do not state that "issuance" of an opinion was equivalent to "receipt of service" of an opinion. The court could find no interpretation of the regulations which was consistent with the plain language of both regulations; therefore, the court held that the regulations were so inconsistent as to fail to provide adequate notice of the appeal time requirement and ordered the Judicial Officer to hear the appeal because the plaintiff did file an appeal within the time allotted by one of the regulations. **PMD Brokerage v. USDA, 234 F.3d 48 (D.C. Cir. 2000)**.

FEDERAL ESTATE AND GIFT TAX

LEGISLATION. Legislation has been introduced which would increase to $10,000,000 the maximum estate tax deduction for family-owned business interests. **H.R. 585**. Legislation has also been introduced which would repeal the estate, gift and generation-skipping transfer taxes. The legislation would also repeal the step-up of basis of estate property received from a decedent. **S. 333**.

MARITAL DEDUCTION. The IRS has issued proposed regulations (see also *infra* under TRUSTS) governing the definition of trust income for purposes of QTIP. The proposed regulations provide that a spouse's interest satisfies the income standard set forth in Treas. Reg. §§ 20.2056(b)-5(f), 25.2523(e)-1(f) if the spouse is entitled to income as defined under a state statute that provides for a reasonable apportionment between the income and remainder beneficiaries of the total return of the trust and that meets the requirements of Treas. Reg. § 1.643(b)-1(a). As the examples under Treas. Reg. § 1.643(b)-1(a) make clear, reasonable apportionment can be accomplished through a unitrust definition of income or by giving the trustee the power to make equitable adjustments between income and principal. **66 Fed. Reg. 10396 (Feb. 16, 2001), amending Treas. Reg. §§ 20.2056(b)-5(f), 20.2056(b)-7(d).**

The taxpayer was the surviving spouse of a decedent. The decedent's will provided for passing of a portion of the estate in trust to the taxpayer. However, two trusts existed because the second trust did not terminate or supersede the first trust; therefore, a dispute arose among the taxpayer and other heirs as to which trust controlled. The parties reached a settlement which used the second trust as determining the property passing to the taxpayer but provided for distribution of the estate outside of the trusts. As part of the agreement, the taxpayer disclaimed a portion of the marital trust share and disclaimed any right to recover gift taxes which could arise from the disclaimers. The IRS ruled that the amount received by the taxpayer under the settlement was eligible for the marital deduction because the taxpayer's interest in the original trusts was QTIP. The IRS also ruled that the taxpayer made a gift of the disclaimed interest in the marital trust and the gift taxes which the taxpayer could have recovered as a result of the disclaimer. **Ltr. Rul. 200106029, Nov. 13, 2000**.

GENERATION SKIPPING TRANSFERS. The IRS has issued proposed regulations which provide that the administration of a pre-September 25, 1985 trust in conformance with a state law that defines income as a unitrust amount, or permits equitable adjustments between income and principal to ensure impartiality, and that meets the requirements of Treas. Reg. § 1.643(b)-1(a) will not be treated as a modification that shifts a beneficial interest to a lower generation beneficiary, or increases the amount of a generation-skipping transfer, subjecting the trust to GSTT. See also *infra* under TRUSTS. **66 Fed. Reg. 10396 (Feb. 16, 2001), amending Treas. Reg. § 26.2601-1(b)**.

INCOME IN RESPECT OF DECEDENT. The decedent's will bequeathed property in trust to the surviving spouse which was QTIP. The decedent also had substantial income in respect of decedent and the issue was how to calculate the deduction for IRD, under I.R.C. § 691, while allowing for the marital deduction. The court held that the proper calculation of the deduction was first to calculate the estate tax on the entire amount (including therein the ordinary consideration of marital share), and then to recalculate the estate tax by removing the IRD from the taxable estate (including therein a recomputation of the marital share). The difference in estate tax was the Section 691 deduction. **Estate of Cherry v. United States, 2001-1 U.S. Tax Cas. (CCH) ¶ 50,223 (W.D. Ky. 2001)**.

TRANSFERS WITH RETAINED INTERESTS-*ALM* § 5.02[3].* In 1951, the decedent and parent owned most of the stock of a family corporation. In order to meet the inheritance and control desires of the shareholders, the decedent and parent entered into an agreement for the transfer of the parent's stock at death to the decedent in trust for life with remainders to the parent's grandchildren. The decedent agreed to transfer the decedent's stock by will to the same trusts. The IRS argued that, although the agreement was reached in bona fide bargaining and the decedent did provide some consideration for the agreement, the consideration was not full and adequate; therefore, the stock in the trusts was included in the decedent's gross estate. The IRS argued that the consideration had to equal the value of the entire property transferred; whereas, the estate argued that the consideration only had to equal the value of the remainder interest transferred. The Tax Court held that the value of the decedent's future contribution of stock was not sufficient consideration for the parent's agreement to transfer stock to the trusts; therefore, the decedent's interest in the trust was not received for adequate consideration. The Tax Court included the value of the stock in the trusts in the decedent's gross estate, decreased by the value of the decedent's stock contributed to the trusts. The appellate court reversed, holding that the property would not be included in the decedent's estate if the decedent's consideration equaled the value of the remainder interest

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

transferred by the parent. The case was remanded for a determination of values. The appellate court also held that the valuation date was the date of the original agreement. On remand, the Tax Court held that the value of the life estate received by the decedent under the agreement was less than half the value of the remainder interest in the stock transferred to the decedent's children; therefore, the decedent did not receive full and adequate consideration of the transfer of stock and the value of the stock was included in the decedent's estate. **Estate of Magnin v. Comm'r, T.C. Memo. 2001-31, *on rem from*, 184 F.3d 1074 (9th Cir. 1999), *rev'g*, T.C. Memo. 1996-25**.

TRUSTS. The IRS has issued proposed regulations which amend the definition of income under Treas. Reg. § 1.643(b)-1 to take into account certain state statutory changes to the concepts of income and principal. Under the proposed regulations, trust provisions that depart fundamentally from traditional concepts of income and principal (that is, allocating ordinary income to income and capital gains to principal) will generally continue to be disregarded, as they are under the current regulations. However, amounts allocated between income and principal pursuant to applicable state law will be respected if state law provides for a reasonable apportionment between the income and remainder beneficiaries of the total return of the trust for the year, taking into account ordinary income, capital gains, and, in some situations, unrealized appreciation. Similarly, a state law that permits the trustee to make equitable adjustments between income and principal to fulfill the trustee's duty of impartiality between the income and remainder beneficiaries is a reasonable apportionment of the total return of the trust. In addition, the proposed regulations provide that an allocation of capital gains to income will be respected if directed by the terms of the governing instrument and applicable local law. Similarly, if a trustee, pursuant to a discretionary power granted to the trustee by local law or by the governing instrument (if not inconsistent with local law), allocates capital gains to income, the allocation will be respected, provided the power is exercised in a reasonable and consistent manner. The proposed changes to the regulations will permit trustees to implement a total return investment strategy and to follow the applicable state statutes designed to treat the income and remainder beneficiaries impartially. At the same time, the limitations imposed by the proposed regulations ensure that the provisions relying on the definition of income under I.R.C. § 643(b) are not undermined by an unlimited ability of the trustee to allocate between income and principal.

Under the proposed regulations, capital gains will be included in distributable net income under certain circumstances that are directed by the terms of the governing instrument and applicable local law. Thus, any capital gain that is included in the I.R.C. § 643(b) definition of income is included in distributable net income. Similarly, any capital gain that is used to determine the amount or the timing of a distribution to a beneficiary is included in distributable net income. Capital gains are also included in distributable net income if the fiduciary, pursuant to a discretionary power granted by local law or by the governing instrument (if not inconsistent with local law), treats the capital gains as distributed to a beneficiary, provided the power is exercised in a reasonable and consistent manner. Thus, if a trustee exercises a discretionary power by consistently treating any distribution in excess of ordinary income as being made from realized capital gains, any capital gain so distributed is included in distributable net income. **66 Fed. Reg. 10396 (Feb. 16, 2001), amending Treas. Reg. §§ 1.643(a)-3, 1.643(b)-1, 1.651(a)-2**.

FEDERAL INCOME TAXATION

LEGISLATION. Legislation has been introduced which would treat payments under the Conservation Reserve Program as rentals from real estate. **S. 315**. Legislation has been introduced which would (1) increase the deduction for health insurance for self-employed persons to 100 percent, (2) exclude gain from the sale of farmland just as gain is excluded from the sale of a residence, (3) allow farmers to use the lesser tax produced by either income averaging or alternative minimum tax, and (4) allow a deduction for FARRM accounts. **S. 333**.

BAD DEBTS. The taxpayer had made loans to the taxpayer's father but the loans were not evidenced by written notes and had no stated interest or repayment schedule. The taxpayer also failed to show that any payments were made. The taxpayer claimed that the debt became worthless when the father's business burned down; however, the taxpayer provided no evidence of the father's net worth or other financial status in the tax year when the loan was claimed as a bad debt deduction. The court held that the deduction was not allowed because the taxpayer failed to show the existence of a bona fide debt or that the debt was worthless in the tax year of the claimed deduction. **Flood v. Comm'r, T.C. Memo. 2001-39**.

BUSINESS EXPENSES. The taxpayer operated a laundry business and claimed business deductions for travel, meals, entertainment, office, rent, utilities and automobile reapir expenses. The deductions were disallowed, except to the extent allowed by the IRS, for lack of substantiation because the taxpayer did not have full and accurate records to distinguish the expenses from personal expenses. The taxpayer also claimed deductions associated with a home office. The deductions were disallowed because the taxpayer's primary business location was at the laundry. **Clark-Hernandez v. Comm'r, T.C. Summary Op. 2001015**.

DISASTER PAYMENTS. On January 5, 2001, the President determined that certain areas in Oklahoma were eligible for assistance under the Disaster Relief and Emergency Assistance Act, 42 U.S.C. § 5121, as a result of a severe winter ice storm on December 25, 2000. **FEMA-1355-DR**. On January 8, 2001, the President determined that certain areas in Texas were eligible for assistance under the Act as a result of severe a winter ice storm beginning on December 12, 2000. **FEMA-1356-DR**. On January 10, 2001, the d that certain areas in Michigan were eligible for assistance under the Act as a result of record snow beginning on December 11, 2000. **FEMA-3160-EM**. On February 5, 2001, the President determined that certain areas in Florida were eligible for assistance under the Act as a result of severe freezing beginning on December 1, 2000. **FEMA-1359-DR**. Accordingly, a taxpayer who sustained a loss attributable to the disasters may deduct the loss on his or her 1999 federal income tax return.

IRA. The taxpayer established an IRA in 1976 and made only deductible contributions over several years. In 1997 when the taxpayer was 56 years old, the taxpayer encountered financial difficulties and withdrew $6,000 from the IRA. The taxpayer did not use the money for any of the purposes entitled to an exception under I.R.C. § 72(t)(2) but used the money for personal expenses. The taxpayer argued that the withdrawal should not be included in gross income and should not be subject to the 10 percent additional tax because the money was withdrawn when the taxpayer was having financial difficulties. The court held that there was no financial difficulties exception under I.R.C. § 72(t); therefore, the the taxpayer had to include the withdrawn money in income and pay an additional 10 percent tax on that amount. **Gallagher v. Comm'r, T.C. Memo. 2001-34**.

INSTALLMENT METHOD OF REPORTING. The IRS has announced that, consistent with the change in law effected by the Installment Tax Correction Act, an accrual method taxpayer that entered into an installment sale on or after December 17, 1999, and filed a federal income tax return by April 16, 2001, reporting the sale on an accrual method (and, thus, an amount realized equal to the selling price) has the consent of the Secretary to revoke its effective election out of the installment method, provided the taxpayer files, within the applicable period of limitations, amended federal income tax return(s) for the taxable year in which the installment sale occurred, and for any other affected taxable year, reporting the gain on the installment method. Thus, a taxpayer may not revoke its effective election out of the installment method if the taxable year in which any payment on the installment obligation was received has closed. **Notice 2001-22, I.R.B. 2001-__**.

MILEAGE RATE. The IRS has informed CCH that there will be no change in the standard mileage rate of 34.5 cents per mile for 2001. See *Rev. Proc. 2000-48, I.R.B. 2000-49, 570*. The announcement was in response to questions about the new administration's review of regulations and letters from members of Congress suggesting that the increase in gas prices justified a larger mileage rate. See http://www.irs.ustreas.gov.

PARTNERSHIPS-*ALM* § 7.03*

DEFINITION. The decedent had farmed with the decedent's brother in an oral partnership for several years. The decedent had been more active in the farm and, after disagreements between them arose, the decedent excluded the brother from the farm. Several years later, during the tax years involved in this case, the brother sued for dissolution of the partnership. A state court ruling found that a partnership existed but that the decedent's capital account far exceeded the brother's. The court ordered the 50 percent split of partnership income after repayment of the capital accounts. The partnership property was sold with all proceeds used to repay the decedent. The decedent's estate argued that the state court adjudication proved that a partnership existed and that the brother's share of taxable income was 50 percent. The Tax Court held that a partnership existed but that the decedent held 100 percent of the partnership interests because the brother was excluded from the partnership business and the decedent's capital account far exceeded the value of the partnership assets. **Estate of Tobias v. Comm'r, T.C. Memo. 2001-37**.

PENSION PLANS. For plans beginning in January 2001, the weighted average is 5.91 percent with the permissible range of 5.32 to 6.21 percent (90 to 106 percent permissible range) and 5.32 to 6.50 percent (90 to 110 percent permissible range) for purposes of determining the full funding limitation under I.R.C. § 412(c)(7). **Notice 2001-15, I.R.B. 2001-589**.

S CORPORATIONS-*ALM* § 7.02[3]*

PASSIVE ACTIVITY LOSSES. The decedent died before reaching age 40 and was an income beneficiary of a trust which owned S corporation stock. The trust was a QSST and provided that, if the decedent died before age 40, the trust corpus passed to the decedent's heirs or the heirs of the grantor of the trust. The S corporation had nondeductible passive losses remaining when the decedent died and the estate claimed the trust's share of these losses on the decedent's last income tax return and elected to carry the excess losses back to the previous three income tax returns. The IRS ruled that, under I.R.C. § 469(g)(2), the passive losses became deductible against nonpassive income upon the death of the decedent and could be carried back under the net operating loss rules. **FSA Ltr. Rul. 200106018, Nov. 3, 2000**.

SHAREHOLDERS. The taxpayer owned S corporation stock and transferred some of the stock to a limited liability company for a 100 percent interest in the LLC. The taxpayer also transferred stock and all of the LLC interest to a limited partnership in exchange for 100 percent interest in the limited partnership. Neither the LLC or limited partnership elected to be taxed as a corporation. The IRS ruled that the ownership of the stock by the LLC and limited partnership, both disregarded entities, would cause the termination of the S corporation status. **Ltr. Rul. 200107025, Nov. 17, 2000**.

SAFE HARBOR INTEREST RATES
March 2001

	Annual	Semi-annual	Quarterly	Monthly
		Short-term		
AFR	4.86	4.80	4.77	4.75
110 percent AFR	5.35	5.28	5.25	5.22
120 percent AFR	5.84	5.76	5.72	5.69
		Mid-term*		
*AFR**	*5.07*	*5.01*	*4.98*	*4.96*
*110 percent AFR**	*5.59*	*5.51*	*5.47*	*5.45*
*120 percent AFR**	*6.10*	*6.01*	*5.97*	*5.94*
		Long-term		
AFR	5.58	5.50	5.46	5.44
110 percent AFR	6.14	6.05	6.00	5.98
120 percent AFR	6.71	6.60	6.55	6.51

Note: The CCH published Mid-term rates are identical to the February mid-term rates and may be in error. We will publish any correction in the next issue.* **Rev. Rul. 2001-12, I.R.B. 2001-__.

SALE OF JOINTLY OWNED PROPERTY. The taxpayer had been married and during that marriage, the taxpayer and former spouse had purchased as joint tenants a townhouse which was used as a rental property. The couple decided to sell the property and the property was sold at a gain. The sale proceeds were issued in a single check, although the taxpayer had requested separate checks because the couple were in the process of divorcing. The couple disagreed on how the proceeds were to be split and the taxpayer refused to endorse the check. The former spouse then deposited the check in an old joint checking account, used some of the proceeds to satisfy an old joint debt and slowing transferred the remainder to the spouse's individual account. The divorce decree ordered the former spouse to pay the taxpayer the taxpayer's one-half share of the proceeds. The taxpayer did not include the taxpayer's share of the gain in income, arguing that the taxpayer did not receive the proceeds until the next tax year. The court held that the taxpayer was liable for one-half of the gain from the sale of the property because the taxpayer was entitled to one-half of the proceeds, even though the taxpayer failed to protect the taxpayer's rights to the proceeds until the divorce decree. **Zimmerman v. Comm'r, T.C. Summary Op. 2001-13**.

Agricultural Law Manual (ALM).

SALE OF RESIDENCE. This case involved tax law in effect prior to amendments in 1997. On October 30, 1995, the taxpayers, husband and wife, sold their residence for $310,000. The taxpayers purchased a vacant lot on May 2, 1996 for $111,000 and, on July 7, 1997, entered into a contract to build a residence on the lot for a cost of $388,000. During the construction, the taxpayers lived on the lot in a mobile home set on concrete pillars. The new residence was completed on August 19, 1998 and the taxpayers moved in after October 30, 1998. The court held that the taxpayers were not allowed to rollover the gain from the sale of their first residence under I.R.C. § 1034 because the taxpayer failed to purchase a replacement residence of equal or greater value within two years after the sale of the first residence. The court noted that, even if the residence in the mobile home on the lot was considered a new residence, the cost of the lot and mobile home was less than the proceeds fo the sale of the first residence and rollover of gain would still not be allowed. **Swarthout v. Comm'r, T.C. Summary Op. 2001-16**.

The taxpayer operated a trucking business and had purchased a residence in New Jersey. The taxpayer discovered that the taxpayer could earn sufficient annual income by driving the truck in the winter in Florida. The taxpayer purchased rental property in Florida and used an apartment while working in Florida. The taxpayer obtained a Florida driver's license, a Florida registration for the truck and stopped paying New Jersey income tax. The New Jersey residence was still used in the spring and summer by the taxpayer as a residence. The New Jersey residence was sold in 1996 and the taxpayer permanently moved to Florida. The IRS argued that the taxpayer had changed residence to Florida prior to the sale of the residence and was not eligible for the exclusion of gain from the sale. The court held that the taxpayer had not abandoned the New Jersey residence and had lived there for at least 36 months of the five years before the sale; therefore, the taxpayer was eligible to the exclude the gain from the sale of the residence. **Taylor v. Comm'r, T.C. Summary Op. 2001-17**.

TAX RATE. The IRS has announced that it has issued Publication 533 which includes the adjusted 2001 tax-rate schedules for use in determining estimated taxes for 2001. The tax rates are lower than those included with the 2001 Form 1040-ES package. Taxpayers may use either set of tables for paying estimated taxes but must use Pub. 533 for all other purposes. See http://www.irs.ustreas.gov.

STATE TAXATION

USE TAXES. The plaintiff was a dairy cooperative which marketed the milk produced by its members. The Michigan Department of Treasury (the Department) assessed use taxes against the plaintiff's machinery, equipment and supplies used to test the members' milk as required by federal and state laws and regulations. The plaintiff argued that the property was exempt from use tax, under Mich. Stat. § 7.555(4)(f), as property used in agricultural production. The Department ruled that the agricultural production of milk ended when the milk was put into storage tanks. The Department argued that the testing was part of the marketing of the milk and not the production of the milk. The court held that the testing equipment, machinery and supplies were exempt from use tax because the testing of the milk was a part of the production process because the testing was required in order for the milk to be suitable for sale. The court also held that the exemption did not require that the plaintiff be directly involved with the milk production, only that the services provided by the plaintiff be a part of the milk production process. **Milk Producers v. Treasury Department, 618 N.W.2d 917 (Mich. Ct. App. 2000)**.

The taxpayer was a producer, processor and marketer of fresh shell eggs and maintained a flock of over 1.3 million laying hens. The taxpayer purchased day-old chicks and raised them in brooder houses which contain an automatic feeding, watering and ventilation system. The system used cages which were similar to the cages used for the laying hens in order to decrease the stress when the chickens are transferred to the laying cages. The plaintiff sought an exemption from use tax under Or. Stat. § 307.400(5)(e) as equipment used for producing fresh shell eggs. The court held that the exemption was properly denied because the raising of the chickens was not directly related to the production of eggs. The court noted that other use tax exemptions allowed for other agricultural uses did not contain the "directly related" language in order to qualify for the exemption; therefore, the court held that the legislature wanted to limit the exemption only to equipment used in the egg laying process. **Willamette Egg Farms, Inc. v. Department of Revenue, 14 P.3d 609 (Or. 2000)**.

WORKERS' COMPENSATION

EMPLOYER. The plaintiff was injured while employed by a professional S corporation wholly-owned by an orthodontist. The plaintiff sought damages from the corporation for assault, battery, intentional infliction of emotional distress and negligence. The corporation argued that the plaintiff was limited to claim only workers' compensation benefits as an employee of the individual orthodontist. The plaintiff argued that the actual employer was the corporation. The court held that an employer does not lose the protection of the workers' compensation statute by using the corporate form of business organization; therefore, the plaintiff was limited to claims under the workers' compensation statute. **Gunderson v. Harrington, 619 N.W.2d 760 (Minn. Ct. App. 2000)**.

ZONING

AGRICULTURAL AREA. The county had adopted a comprehensive land use plan under the Washington Growth Management Act and designated 40,000 acres in three Agricultural Production Districts (ADPs) for exclusive agricultural use. The county needed land for soccer fields and other recreational use and amended the land use plan to provide for temporary use of the ADP land for recreational uses. The amendments specified that the land would revert to agricultural use if needed. The county argued that the GMA allowed exceptions to the ADP exclusive use requirement. The court acknowledged that the GMA did promote the recreational use of land, but the court held that the GMA required agricultural land to be held exclusively for agricultural use if the land was suitable for agriculture. The court noted that all of the land involved in this case was prime farm land; therefore, the ADP land could not be used for nonagricultural purposes. **King County v. Central Puget Sound, 14 P.3d 133 (Wash. 2000)**.

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