powers under the state's probate law than most fiduciaries would hold.[20]

FOOTNOTES

1 Castlerock Estates, Inc. v. Estate of Markham, 871 F. Supp. 360 (N.D. Calif. 1994).

2 E.g., United States v. Fleet Factors Corp., 901 F.2d 1550 (11th Cir. 1990) (absolute liability imposed on secured creditor).

3 City of Phoenix v. Garbage Services Co., 816 F. Supp. 564 (D. Ariz. 1993) (trustee); Castlerock Estates, Inc. v. Estate of Markham, 871 F. Supp. 360 (N.D. Calif. 1994) (conservator and executor).

4 *Id*.

5 871 F. Supp. 360, 362 (N.D. Calif. 1994).

6 *Id*. at 361.

7 42 U.S.C. § 9607 *et seq*.

8 871 F. Supp. 360, 363 (N.D. Calif. 1994).

9 *Id*.

10 *Id*.

11 *Id*.

12 *Id*. at 367.

13 *Id*.

14 *Id*. at 368.

15 *Id*. at 369.

16 816 F. Supp. 564 (D. Ariz. 1993).

17 *Id*. at 568.

18 42 U.S.C.A. § 9607.

19 See, e.g., Nurad, Inc. v. Hooper & Sons Co., 966 F.2d 837, 846 (4th Cir. 1992); United States v. Monsanto, 858 F. 2d 160, 168 (4th Cir. 1989), *cert. denied*, 490 U.S. 1106 (1989).

20 Castlerock Estates, Inc. v. Estate of Markham, 871 F. Supp. 360, 367 (N.D. Calif. 1994).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

BANKRUPTCY

GENERAL-*ALM* § 13.03.*

EXEMPTIONS

DISABILITY BENEFITS. The debtor was involved in an automobile accident and received benefits from an accidental death and dismemberment insurance policy for the loss of an eye. The payment was received pre-petition and deposited in the debtor's bank account. The debtor claimed the proceeds as an exempt disability payment under 11 U.S.C. § 522(d)(10)(C). The court held that the proceeds were not eligible for the exemption because the exemption was limited to the debtor's right to receive a disability benefit and the debtor no longer had a right to receive the benefit since the benefit was already paid. ***In re* Chapman, 177 B.R. 161 (Bankr. D. Conn. 1994)**.

INVOLUNTARY PETITION. Under a divorce judgment, the debtor was required to pay the former spouse $500 per week in alimony and $500 per week as child support for the couple's three minor children. The former spouse filed an involuntary petition against the debtor on the former spouse's behalf and on behalf of the three children. The debtor argued that the petition was insufficient in that at least three creditors did not sign the petition. The court held that the three children each qualified as a claimant sufficient to support the filing of an involuntary petition. ***In re* Hopkins, 177 B.R. 1 (Bankr. D. Me. 1995)**.

SUBORDINATION. The debtor was a closely-held corporation which operated several egg and chick production facilities. When the debtor began experiencing financial difficulties, several shareholders who were also officers made loans or advances to the debtor. Only two of the loans were documented on the corporation's books and officially approved by the directors. The shareholders filed unsecured claims for the amounts loaned to the debtor. Another unsecured creditor objected to the claims and sought denial of the claims or at least subordination of the claims to the other unsecured claims. The creditor alleged that the loans were inequitable conduct in that the loans were made when the debtor was undercapitalized and allowed the debtor to favor some creditors while harming other creditors who continued to provide credit. The court held that the creditor failed to demonstrate that the debtor was undercapitalized when the advances were made or that the advances were other than bona fide attempts to keep the debtor in business. Absent any showing of inequitable conduct, the court held that the claims of the shareholders could not be subordinated to other unsecured creditors. ***In re* Colonial Poultry Farms, 177 B.R. 291 (Bankr. W.D. Mo. 1995)**.

CHAPTER 12-*ALM* § 13.03[8].*

TRUSTEE FEES. The Chapter 12 debtor's plan provided for direct payments of all secured claims, real estate tax claims and attorney's fees. Because unsecured creditors would receive payments only if the debtor had disposable income, the trustee would not receive any fee unless disposable income was earned by the debtor. The court held that the secured claims could be paid directly to the creditors without the trustee fee but that the real estate taxes and attorney's fees were to be paid through the trustee. The court left open the question of whether the trustee would receive adequate compensation under the plan and allowed the trustee to petition for additional fees. ***In re* Beard, 45 F.3d 113 (6th Cir. 1995), *aff'g*, 177 B.R. 74 (S.D. Ohio 1993), *aff'g*, 134 B.R. 239 (Bankr. S.D. Ohio 1991)**. **Note**: An article by Dr. Harl is scheduled to appear in the May 5, 1995 *Agricultural Law Digest* on payment of trustee's fees in Chapter 12 bankruptcy.

FEDERAL TAXATION-*ALM* § 13.03[7].*

CLAIMS. The debtors had filed a Chapter 11 case which was closed in November 1989. The IRS had filed a

**Agricultural Law Manual* (ALM). For information about ordering the *Manual*, see the last page of this issue.*

claim for 1986 and 1987 taxes and had not objected to the plan or closing of the case. In 1991, the IRS audited the debtors' 1986 return and assessed the debtors for additional taxes for 1986 and 1987 with penalties. The debtors sought a declaratory judgment that the IRS assessments were precluded by the final judgment in the bankruptcy case. The IRS argued that the assessments were new claims. The District Court held that the assessments were sufficiently connected to the bankruptcy claims to be precluded by the final bankruptcy judgment. The appellate court reversed, holding that the IRS was not barred by res judicata because the taxes were nondischargeable whether or not the IRS filed a claim in the case. ***In re*** **DePaolo, 45 F.3d 373 (10th Cir. 1995),** ***rev'g*****, 165 B.R. 491 (D. Wyo. 1994)**.

DISCHARGE. The debtor did not file income tax returns for 1982, 1983, and 1984. The IRS made assessments in 1988 for those years based on substitute returns created by the IRS. The debtor claimed to have filed returns for those years in November 1989 when returns for other delinquent years were filed. In January 1993, the IRS filed notice of levy for the assessments of taxes for the three years. The court held that the substitute returns created by the IRS did not qualify as returns filed by the debtor for purposes of making the taxes dischargeable under Section 523(a)(1)(B)(i). The court also held that the taxes were also priority taxes under Section 507(a)(7)(A)(iii) because if the debtor did file returns in 1989, the taxes were assessable on the date of the petition (within three years after filing of the returns) but had not been assessed as of the date of the petition. **Matter of Delaney, 177 B.R. 251 (Bankr. E.D. La. 1994)**.

The debtors failed to file income tax returns for four tax years and the IRS sought to have the taxes declared nondischargeable for willful attempt to evade payment of the taxes. The court held that although mere failure to file and pay taxes was not sufficient, the IRS had demonstrated that the debtors had sufficient income to pay the taxes but purchased an expensive home instead and that the debtors had underreported their income when they did file the returns; therefore, the taxes were nondischargeable for willful attempt to evade taxes. **Matter of Halburg, 177 B.R. 101 (Bankr. N.D. Ala. 1995)**.

SETOFF. The debtors operated a reforestation business which reforested land under contracts with the USDA. In order to finance their operations, the debtors assigned these contracts to a third party lender. The IRS filed a notice of setoff with the USDA to setoff the amounts owed to the debtors against tax deficiency claims filed by the IRS in the debtors' bankruptcy case. The IRS also sought turnover of amounts paid to the lender. The court held that the assignments of the contracts were valid but that financing statement filed by the lender as to the contracts were not valid as against the IRS; therefore, the IRS could setoff amounts due under the contracts even though the contracts had been assigned and pledged as security. However, the court also held that the IRS could not recover amounts already paid to the assignee. ***In re*** **Medina, 177 B.R. 335 (Bankr. D. Or. 1994)**.

In 1990, the debtor claimed a net operating loss which was carried back to previous tax years and the debtor filed for a refund. The IRS paid the refund but miscalculated the interest owed such that the refund paid was $45,000 more than should have been paid. After the debtor filed for bankruptcy in 1991, the debtor also had another net operating loss which was also carried back and formed the basis for another refund claim. The IRS discovered the first error and setoff the overpayment against the new refund. The court held that the setoff was allowable. ***In re*** **Franklin Savings Corp., 177 B.R. 356 (Bankr. D. Kan. 1995)**.

TAX LIENS. The debtor filed for Chapter 11 in October 1989 and had the case converted to Chapter 7 in June 1990. The bankruptcy estate included a truck of which the Chapter 7 trustee took possession in July 1990 and eventually sold. The IRS filed a secured claim in February 1990 based on liens filed in 1988 and 1989. The trustee sought to avoid the tax liens under Section 545(2) and I.R.C. § 6323(b) as a bona fide purchaser. The court held that because the trustee had notice, upon the IRS filing of the claim, of the IRS lien before obtaining possession of the vehicle in July 1990, the trustee could not avoid the lien under I.R.C. § 6323(b). ***In re*** **Walter, 45 F.3d 1023 (6th Cir. 1995),** ***aff'g*****, 158 B.R. 984 (N.D. Ohio 1993),** ***rev'g*****, 139 B.R. 695 (Bankr. N.D. Ohio 1993)**.

CONTRACTS

MODIFICATION. The defendant entered into a written contract to purchase 91,000 pounds of basil leaves from the plaintiff over one year. The contract contained a provision prohibiting oral modification of the contract. The contract was modified several times, first to increase the per pound charge because the defendant wanted more of the stems removed before delivery and later to increase the per pound charge to reflect the increase in imported basil leaves prices. The defendant accepted several shipments at these new prices over several months but failed to pay for the last few shipments. The plaintiff sued for payment of the last deliveries and for breach of contract for the defendant's failure to purchase a total of 91,000 pounds. The defendant argued that the plaintiff breached the contract in orally modifying the contract. The court raised the issue of whether the oral modifications violated the statute of frauds but held that the acceptance of shipments and payments for them by the defendant waived any objection to the statutory or contractual provisions requiring all modification to be in writing. **Brookside Farms v. Mama Rizzo's, Inc., 873 F. Supp. 1029 (S.D. Tex. 1995)**.

FEDERAL AGRICULTURAL PROGRAMS

GRAIN STANDARDS. The Grain Inspection, Packers and Stockyards Admin. (GIPSA) has issued proposed regulations amending the grain standards for barley to include two classes, malting barley and barley; to remove the U.S. Choice grade for two-row malting barley; and to revise several grading procedures and inspection standards. **60 Fed. Reg. 15075 (March 22, 1995)**.

ORGANIC PRODUCTS. The AMS is seeking applications for approved synthetic and prohibited natural substances to be considered on a national list to be included in the standards for organic production and handling. **60 Fed. Reg. 15744 (March 27, 1995)**.

PERISHABLE AGRICULTURAL COMMODITIES ACT-*ALM* § 10.05[2].* In 1986, the debtor, a perishable agricultural commodities dealer subject to PACA, purchased several interests in a marketing terminal cooperative which entitled the debtor to lease shops in the terminal market. In 1989 and 1991, the debtor purchased perishable agricultural commodities from several sellers who were not paid for the produce. The sellers filed notices of intent to claim part of the PACA trust before the debtor filed for bankruptcy. The sellers sought to include in the PACA trust, the proceeds from the bankruptcy trustee's sale of the terminal shops' interests held by the debtor. The sellers argued that the rent paid for the shops was derived from the sale of the produce purchased from the sellers. The court held that the interests themselves could not be subject to the PACA trust because the interests were purchased before the commodities were purchased from the sellers. In addition, the rent payments were not included in the PACA trust because the payments were bona fide and made in the normal course of business. ***In re* Kornblum & Co., Inc., 177 B.R. 187 (S.D. N.Y. 1995)**.

The defendant was a secured creditor of a produce merchant subject to the Perishable Agricultural Commodities Act (PACA). The plaintiff had sold perishable produce to the merchant for which the merchant had not paid. During the time the produce was purchased and several months later, the defendant had received payments on the merchant's loans and the plaintiff sought to recover these payments as subject to the PACA trust. The plaintiff alleged that the defendant knew or should have known that the merchant was not paying for produce on a timely manner as early as July 1993 and certainly by October 1993. However, the defendant argued that it had diligently sought to discover the merchant's financial status but was not given complete information and was assured by the merchant that all PACA claims would be paid. The court held that although the defendant had some knowledge of the merchant's financial troubles, the defendant's diligence in its unsuccessful attempts to investigate the merchant's financial status established that the defendant was a bona fide purchaser for value and that the loan payments were not subject to the PACA trust. **Battle v. Fresh Preps Distribution, Inc., 873 F. Supp. 1062 (E.D. Mich. 1995)**.

SEEDS-*ALM* § 10.02.* The APHIS has issued proposed regulations to include in the definition of noxious weed seeds under the Federal Seed Act (FSA) all weeds listed in the Federal Noxious Weed Act (FNWA). The proposed regulations are designed to overcome the prohibition of application of the FNWA to imported shipments of seeds subject to the FSA regulations. The problem was most recently adjudicated in *Pennington Seed, Inc. v. U.S., 10 F.3d 6 (D.C. Cir. 1993)* (destruction of imported grass seed containing serrated tussock seed improper because grass seed governed by FSA which did not list serrated tussock seed as noxious weed). **60 Fed. Reg. 15257 (March 23, 1995)**.

WEEDS. The APHIS has issued proposed amendments to the noxious weed regulations to remove *Stratiotes aloides* Linnaeus (water aloe) and *Euphorbia prunifolia* Jacquin (painted euphobia) from the list of noxious weeds and to add *Ottelia alismoides* (L.) Pers and *Solanum viarum* Dunal (tropical soda apple) to the list. **60 Fed. Reg. 15260 (March 23, 1995)**.

WETLAND CONSERVATION EASEMENTS. The FmHA had obtained ranch land which included wetlands through foreclosure and decided to transfer the land to the priority secured lender (a bank) in exchange for relief from the debt. The bank sold the land to third parties who used the ranch land for grazing. The plaintiff brought suit against the FmHA, the bank and the buyers, alleging that the transfer of the land by the FmHA without retaining a conservation easement for the wetlands violated 7 U.S.C. § 1985(g). The FmHA argued that the statute did not apply because the land was abandoned to the creditor. The court held that the statute did apply because the transfer was in effect a sale in that the FmHA received consideration for the transfer from the relief from the debt. The court also held that the statute applied even though the FmHA held title subject to a debt, holding that the easement was required even if the FmHA had to pay part of the debt for the easement. The buyers argued that rescinding the sale to the extent of imposing an easement was inequitable. The court noted that the plaintiffs alleged that the buyers knew about the wetlands issue and removed a notice about the issue from the contract, thus indicating that the buyers had notice that an easement could be imposed; therefore, the action was not barred as inequitable and rescission could be allowed if the evidence demonstrated that the buyers did have notice of the wetlands issue. The court also held that, although the buyers were not subject to the statute involved, the buyers were proper parties to the action in order to provide full relief and to protect the buyers' interests. **National Wildlife Fed. v. Espy, 45 F.3d 1337 (9th Cir. 1995)**.

FEDERAL ESTATE AND GIFT TAX

CLAIMS AGAINST THE ESTATE. In 1951, the decedent entered into a settlement agreement with the decedent's spouse which provided for monthly support for the spouse and for the couple's two children. The spouse also received title to the marital home and the children received a promise to be included in a trust to be established in the decedent's will. The monthly payments were much less than the amounts needed to support the lifestyle the spouse had been accustomed to; however, the evidence was inconclusive as to whether the decedent could have afforded any higher payments. The decedent eventually divorced the spouse and the settlement agreement became the property settlement of the divorce order. The decedent's will failed to establish the trust for the two children and the children filed a claim against the estate. The estate settled with the children and claimed the settlement amount as a deductible claim against the estate. The IRS argued that the estate failed to prove conclusively that the spouse had given any consideration for the promise for the trust; therefore, the claim was not deductible. The court held that although the

**Agricultural Law Manual* (ALM). For information about ordering the *Manual*, see the last page of this issue.

estate failed to value precisely the consideration given by the spouse, the evidence was sufficient to demonstrate that some value be given in that the monthly support payments were less than the support provided before the agreement and the decedent's estate at the time of the agreement was substantially greater than the support payments. **Estate of Kosow v. Comm'r, 45 F.3d 1524 (11th Cir. 1995)**.

DISCLAIMERS-*ALM* § 5.02[6].* In order to increase the marital deduction, the surviving spouse asked several legatees of the decedent's will to disclaim their interests in the devises. Although no specific promises were made, the legatees testified that they understood that the surviving spouse would recompense them for the disclaimers, and indeed, these legatees did receive money or property equal to or exceeding the value of the disclaimed interests a short time after filing the disclaimers. The court held that the marital deduction could not include the disclaimed property because the disclaimers were not effective since the legatees still received a benefit. **Monroe v. Comm'r, 104 T.C. No. 16 (1995)**.

GENERATION SKIPPING TRANSFERS-*ALM* § 5.04[6].* The taxpayer was the beneficiary of four irrevocable trusts created before 1985. The remainder beneficiaries were the taxpayer's two children and their issue. One of the children had died. The taxpayer renounced all interests in the trusts, causing the trusts to terminate and all trust corpus to be distributed to the remaining child and the children of the deceased child. The IRS ruled that the taxpayer would be considered the transferor of the trusts' corpus, the renunciation of the trust interests did not subject the trusts to GSTT, and the children of the taxpayer's deceased child were not skip persons. **Ltr. Rul. 9510071, Dec. 15, 1994**.

In 1953, five irrevocable trusts were created for the grantors' five children. The trusts provided for five trustees and a minimum of three trustees in order to execute any fiduciary duties. The beneficiaries sought amendment of the trusts to provide for two trustees and consent of a minimum of two trustees to execute fiduciary duties. The IRS ruled that the changes would not subject the trusts to GSTT. **Ltr. Rul. 9511031, Dec. 16, 1994**.

In 1962 an irrevocable trust was created by the taxpayer's parent. The trust provided that the taxpayer was the income beneficiary for life with the trust to be split on the taxpayer's death into as many trusts as there were children of the taxpayer. If a child predeceased the taxpayer, a trust was to be formed for the surviving spouse or issue of that child. The children's trusts were to terminate when each beneficiary reached age 25, but the taxpayer had the right to extend the period of the trusts to the lifetime of each beneficiary. The children had the testamentary power to appoint the trust to the child's children in trust. The taxpayer exercised the power to extend the trusts to the lifetime of each beneficiary. The IRS ruled that the extension of the children's trusts did not subject the trusts to GSTT and that the trusts would not be included in the children's gross estates. The IRS cautioned, however, that the children's exercise of the power to appoint the trusts to their children in trust could cause extension of the trust beyond 21 years after the death of a person living at the creation of the original trust. **Ltr. Rul. 9511039, Dec. 20, 1994**.

GIFT-*ALM* § 6.01.* The decedents, husband and wife, and their child and grandchildren each owned farmland which was contributed to a corporation. Each contributor received stock in the corporation with the father receiving 62 percent of the stock. The executrix argued that the transaction had no gift element because the contributions were made in the ordinary course of business. The court rejected that argument because the transactions were between related parties, the circumstances indicated that the transactions were made to increase the income of the child, and the value of the stock received would not have been acceptable to an unrelated contributor. The court held that the value of the land contributed by the father exceeded the value of the stock received by the father, even with the stock value increased by 40 percent for the majority interest. **Estate of Trenchard v. Comm'r, T.C. Memo. 1995-121**.

MARITAL DEDUCTION-*ALM* § 5.04[3].* The decedent and spouse had established an inter vivos revocable trust with the decedent and spouse as beneficiaries. The trust provided that each beneficiary had the power to revoke or amend the trust. The trust also provided that at the death of one beneficiary, the remaining beneficiary was to receive all net annual income. However, the trust provided that if a beneficiary became incapacitated, trust income and principal were to be distributed only for the beneficiary's health, support and maintenance. The trust defined "incapacity" as being unable to manage one's financial affairs. The IRS ruled that the incapacity provision would normally cause the trust to not qualify as QTIP; however, because the surviving spouse had the power to amend or revoke the trust at any time, including during incapacity, the surviving spouse's interest in the trust would qualify for QTIP. **Ltr. Rul. 9511002, Dec. 2, 1994**.

TRANSFERS WITHIN THREE YEARS OF DEATH-*ALM* § 5.02[3].* The decedent had divorced from the former spouse but no property settlement was formally made in the court proceedings. Instead, the parties reached a private agreement that the former spouse would receive a life insurance policy on the decedent, a portion of the proceeds from another life insurance policy and a portion of the decedent’s retirement benefits from an employer. The court held that the life insurance policy was included in the decedent’s gross estate because it was transferred for no consideration within three years of the decedent’s death. The court also ruled that the portion of the proceeds of the life insurance policy and retirement benefits paid to the former spouse were also included in the gross estate because the former spouse had no ownership of the policy or retirement benefits before the decedent’s death. **Est. of Waters v. Comm’r, 95-1 U.S. Tax Cas. (CCH) ¶ 60,191 (4th Cir. 1995), *aff'g on points*, T.C. Memo. 1994-194**.

The decedent had established a trust funded with stock in a closely-held corporation. The decedent created a power of attorney in a son which granted the son the power to withdraw property from the trust and to make gifts. The son withdrew 91 shares of stock from the trust and had the stock transferred to the decedent. Then the stock was transferred to the decedent's spouse. The IRS argued that the transfer was a relinquishment of the decedent's power to revoke the trust as to the transferred stock; therefore, the stock was included in the estate as a transfer within three years of death. The court held that the form of the transfer was substantial enough to have the transfers considered as a withdrawal and gift since the son had specific authority to withdraw trust corpus and to make gifts and the corporation acknowledged the transfers by changing the names on the stock for each transfer. **Frank v. Comm'r, T.C. Memo. 1995-132**.

TRUSTS. In 1960, the decedent established a trust for the benefit of the decedent with a remainder in trust to the decedent's son and further remainders to the son's spouse and children. The trust provided that after the death of the grantor, any beneficiary or beneficiaries holding more than two-thirds of the trust's beneficial interests could change any trustee. The trust also provided that the son could become a co-trustee. At the death of the grantor, the son became a co-trustee and removed the bank trustee in favor of another bank trustee. Several years later, the son resigned as co-trustee and appointed the son's adult child as co-trustee. The trust provided that the trustees could distribute corpus for the beneficiary's "maintenance, support and welfare." The IRS ruled that "welfare" was not a requisite ascertainable standard; therefore, the son, as co-trustee, had a general power of appointment over the trust corpus. The IRS ruled that the son's resignation as co-trustee did not cause a gift from the lapse of the general power of appointment because the son still had the power to reappoint himself as co-trustee. The IRS also ruled that the resignation did not cause the trust corpus to be included in the son's gross estate or subject the trust to GSTT. **Ltr. Rul. 9510065, Dec. 14, 1994**.

VALUATION-*ALM* § 5.02[3][a].* Prior to reorganization the corporation operated four businesses as divisions of the corporation and two businesses as subsidiaries of the corporation. All of the corporation stock was owned by members of one family with both common and preferred stock issued and owned by all shareholders. The corporation reorganized three of the divisions as subsidiaries under tax-free incorporations. The corporation then formed a holding company to which all stock in all of the corporations was transferred in a tax-free reorganization. The shareholders received identical stock holdings in the holding corporation as were held in the original corporation. The IRS ruled that the reorganization did not subject the stock to valuation under I.R.C. § 2701. **Ltr. Rul. 9511028, Dec. 26, 1994**.

FEDERAL INCOME TAXATION

ACCOUNTING METHOD. The taxpayer was a cash basis nursery which sold citrus trees. The taxpayer collected advance payments in one tax year on orders to be delivered in the following tax year. Although the taxpayer had a policy of refunding the advance payments if the orders were cancelled before delivery, the court held that the advance payments were income in the year received. **Michaelis Nursery, Inc. v. Comm'r, T.C. Memo. 1995-143**.

C CORPORATIONS

STOCK BASIS. The taxpayers, as husband and wife in a community property state, owned shares of stock. As part of a divorce settlement, the husband borrowed $2 million, using the stock as collateral, and paid the wife $1.7 million when the divorce became final. The wife did not report the payment as income. The husband later sold the stock and reported the gain based on an increase in basis in the stock by the $1.7 million. The wife and IRS argued that the loan was a community property debt; therefore, the payment was a property division not a sale. The husband argued that the loan was his obligation solely and that the payment was a sale of the stock, allowing an increase in the stock basis. The court held that because the loan was made before the divorce decree was entered, the stock was still community property and the community was liable for any default on the loan; therefore, the loan was a community debt and the $1.7 million payment represented a property division which was not taxable to the wife and which did not increase the husband's basis in the stock. **Gaughan v. Comm'r, 95-1 U.S. Tax Cas. (CCH) ¶ 50,161 (5th Cir. 1995), *rev'g*, T.C. Memo. 1993-320**.

CONSTRUCTIVE RECEIPT. The taxpayers owned a closely-held corporation and rented commercial real estate to the corporation. The court held that the taxpayers received constructive income in the months the corporation did not pay rent for the property. **Hooper v. Comm'r, T.C. Memo. 1995-108**.

COOPERATIVES. The IRS has determined that dues received by tax-exempt agricultural organizations from associate members with less than full voting rights are not unrelated business income if the associate member category was created with the intent to further the organization's exempt purposes. **Rev. Proc. 95-21, I.R.B. 1995-15**.

DEPRECIATION-*ALM* § 4.03[4].* In 1983, the taxpayers purchased farm and ranch land which contained about 250,000 trees and schrubs which did not produce fruit or nuts and were not harvested for wood. The trees and shrubs were used primarily for a windbreak. The taxpayers assigned a $1 per plant value and claimed depreciation and investment tax credit on the trees and shrubs. The IRS denied the depreciation and investment tax credit. The court held that the trees and shrubs were not eligible for depreciation or investment tax credit because the trees and shrubs were not used for the production of fruit, nuts or wood; therefore, the trees and shrubs were part of the nondepreciable realty. **Everson v. U.S., 95-1 U.S. Tax Cas. (CCH) ¶ 50,150 (D. Mont. 1995)**.

DISCHARGE OF INDEBTEDNESS-*ALM* § 4.02[15].* A corporation was owned by a husband and wife. The corporation transferred preferred stock to two charitable organizations. The corporation later redeemed the stock from the charities in exchange for promissory notes. The corporation suffered financial difficulties but was not in bankruptcy nor was it insolvent when the corporation renegotiated the notes to waive unpaid interest, reduce the unpaid principal and to provide for early prepayment of the remaining principal. The IRS ruled that the renegotiation qualified as a purchase price adjustment under I.R.C. § 108(e)(5), the purchase price adjustment amount was not included in regular or alternative minimum tax income, the corporation's tax attributes were not reduced by the purchase price adjustment, and the corporation's earnings and profits were required to be increased by the amount of the purchase price adjustment. **Ltr. Rul. 9511045, Dec. 21, 1994**.

EMPLOYMENT TAXES. The IRS has issued guidance, in question and answer form, for application of the new "Nanny tax" law, Pub. L. No. 103-387. The notice modifies Rev. Proc. 70-6, 1970-1 C.B. 420 and Rev. Proc. 80-4, 1980-1 C.B. 581. **Notice 95-18, I.R.B. 1995-18**.

EXPENSE METHOD DEPRECIATION-*ALM* § 4.03[4][j].* The taxpayers were not allowed an expense method deduction for medical equipment used in the taxpayers' business because a proper election was not made. The taxpayer were allowed only regular depreciation on the equipment. **Steinberg v. Comm'r, T.C. Memo. 1995-116**.

INTEREST RATE. The IRS has announced that for the period April 1, 1995 through June 30, 1995, the interest rate paid on tax overpayments is 9 percent and for underpayments is 10 percent. The interest rate for underpayments by large corporations also remains at 12 percent. Note: the just-enacted GATT legislation reduces the interest rate on overpayments above $10,000 by 1.5 percentage points. **Rev. Rul. 95-33, I.R.B 1995-15**.

IRA. The IRS has cautioned that it does not officially "approve" IRA investment vehicles other than through letter rulings and cautioned taxpayers against investing in investments advertised as "IRS approved" or "IRA approved" investments without further investigation of the qualifications of the investment. **IR-95-26**.

LOSSES-*ALM* § 4.05.* The taxpayer converted a personal residence into a residential rental property. The taxpayer demonstrated that the fair market value of the property on the date of the conversion was less than the taxpayer's basis in the property; therefore, the basis of the property was the FMV on the date of conversion. The court held that the taxpayer had a deductible loss on the sale of the property for less than the new basis. **Adams v. Comm'r, T.C. Memo. 1995-142**.

NET OPERATING LOSSES. The taxpayers had regular net operating losses (NOLs) and alternative minimum tax (AMT) net operating losses in 1985. The taxpayers' return elected to carry forward only the regular net operating losses and the taxpayers carried the AMT NOLs back to previous tax years. The court held that under the legislative history of I.R.C. § 172(b)(3)(C) and Rev. Rul. 87-44, 1987-1 C.B. 3, the regular and AMT NOLs must be carried together either back or forward. **Miller v. Comm'r, 104 T.C. No. 14 (1995)**.

PARTNERSHIPS-*ALM* § 7.03.*

DEFINITION. The IRS has announced a proposal to amend the partnership and corporation definition regulations to allow unincorporated business organizations to elect to be taxed as a partnership or corporation, so long as the entity is not defined, for tax purposes, under a specific code section. **Notice 95-14, I.R.B. 1995-14**.

DISTRIBUTIONS. In exchange for management services as a general partner, the taxpayer received a one percent interest in the partnership. The court held that the value of the one percent interest was income to the taxpayer because most of the services were performed before the interest was transferred. **Johnston v. Comm'r, T.C. Memo. 1995-140**.

LIMITED LIABILITY COMPANIES. The taxpayers formed a limited liability company under the Texas Limited Liability Act. The Act provides that an LLC is dissolved upon the death, expulsion, withdrawal, bankruptcy or dissolution of a member or other terminating event, unless there is at least one remaining member and a number of the remaining members, as established by the LLC agreement, vote to continue the LLC. The Act also prohibited the assignment or transfer of an LLC interest unless allowed by the LLC agreement. The IRS ruled that the LLC would be a partnership under the I.R.C. **Ltr. Rul. 9510037, Dec. 9, 1994**.

The taxpayers converted a limited partnership into a limited liability company (LLC). The IRS ruled that the LLC would be taxed as a partnership because (1) the LLC lacked the corporate characteristic of continuity of life since the state LLC law and the LLC agreement required the consent of all members to continue the partnership after a terminating event, and (2) the LLC lacked the corporate characteristic of transferability of interests because the Act and agreement provided that if any other member objected to the sale or assignment of a member’s interest in the LLC, the transferee or assignee had no right to participate in the management of the LLC. The IRS also ruled that no gain was recognized from the conversion of the limited partnership to the LLC. **Ltr. Rul. 9511033, Dec. 19, 1994**.

PENSION PLANS. The IRS has issued guidance, in the form of questions and answers, on the minimum funding requirements of I.R.C. § 412(m) for plan years after December 8, 1994. **Rev. Rul. 95-31, I.R.B. 1995-15**.

For plans beginning in March 1995, the weighted average is 7.30 percent with the permissible range of 6.57 to 7.96 percent (90 to 109 percent permissable range) and 6.57 to 8.03 percent (90 to 110 percent permissable range) for purposes of determining the full funding limitation under I.R.C. § 412(c)(7). **Notice 95-11, I.R.B. 1995-13, 8**.

SELF-EMPLOYMENT-*ALM* § 4.06.* The President has signed H.R. 831 which reinstates the deduction (an above-the-line adjustment to income) for 25 percent of the health insurance costs for self-employed individuals for 1994. The deduction is increased to 30 percent after 1994.

The taxpayer was an attorney and failed to report and pay self-employment tax on self-employment income. The taxpayer argued that an instruction on Form 1040 for self-employment taxes on "wages" was misleading. The court held that reliance on the form instructions, even if they were ambiguous or misleading, was not justified in light of the clear statutory requirement. **Graham v. Comm'r, T.C. Memo. 1995-114**.

AGRICULTURAL LAW PRESS
P.O. BOX 5444
MADISON, WI 53705-5444

SECURED TRANSACTIONS

FERTILIZER LIEN. In 1992, the debtor had purchased fertilizer and other chemicals for use on 1992 crops. The supplier filed a statutory fertilizer and agricultural lien in August 1992 which expired in July 1993. In July 1993, the debtor had crops growing on the same land on which the fertilizer and other chemicals were applied in 1992. The creditor claimed that the lien included the crops growing in 1993. The debtor argued that the lien extended only to crops harvested within one year after the filing of the lien; therefore, the lien did not include crops still growing when the lien expired. The court held that the lien included all crops "produced" on the land within one year of the lien filing and that the term "produced" had to include growing crops because any other interpretation would make the one year limitation superfluous. **Matter of Schlote, 177 B.R. 315 (Bankr. D. Neb. 1995)**.

CITATION UPDATES

Sealy Power, Ltd. v. Comm'r, 46 F.3d 382 (5th Cir. 1995), *rev'g*, T.C. Memo. 1992-168 (investment tax credit) see p. 54 *supra*.

Glenwood Coop., Inc. v. U.S., 32 Fed. Cl. 568 (1995) (refund for net operating loss) see p. 38 *supra*.

The B.F. Goodrich Co. v. U.S., 32 Fed. Cl. (1995) (investment tax credit) see p. 38 *supra*.

Bud Antle, Inc. v. Barbosa, 35 F.3d 1355 (9th Cir. 1994), *pet. for rehearing denied*, 45 F.3d 1261 (9th Cir. 1994) (agricultural labor) see Vol 5, No. 24, p. 188.

ISSUE INDEX