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Discrimination Against Section 1231 Livestock for Sales Within One year After Death

-by Neil E. Harl*

A statute passed and signed into law on December 31, 1970, some 45 years ago, has continued to discriminate against those with sales of livestock used in a trade or business¹ in terms of a less advantageous treatment of animals eligible for § 1231(b)(3) treatment in the one year period after death.²

What did the statute state?

Based heavily on the argument that executors and administrators of estates often must sell some assets (capital assets or assets used in the trade or business) in the months after death, the 1970 legislation continued the status of a new basis at death for a year after the death occurred so that long-term capital gain treatment would be assured. The statutory language is as follows –

“In the case of a person acquiring property from a decedent or to whom property passed from a decedent (within the meaning of section 1014(b), if –

(A) The basis of such property in the hands of such person is determined under section 1014, and

(B) Such property is sold or otherwise disposed of by such person within 1 year after the decedent’s death, then such person shall considered to have held such property for more than 1 year.”³

So what is Section 1014?

That is the section that assures a new basis at death, equal to fair market value at that time, for property “. . . in the hands of a person acquiring the property from a decedent or to whom the property passed from a decedent. . .” if the property was not sold, exchanged or otherwise disposed of before the decedent’s death by such person.⁴ That provision states that the income tax basis is to be the fair market value of the property at the date of the decedent’s death, the alternate valuation procedure,⁵ the value determined under special use valuation,⁶ or the income tax basis in the hands of the decedent subject to a qualified conservation easement.⁷

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How does this affect livestock under I.R.C. § 1231(b)(3)?

The key statute, I.R.C. § 1223(9), refers to the period to be eligible for long-term capital gains treatment in the period after death is referring to property held for “. . . more than one year.”⁸

As is widely known, the statute in referring to property used in a trade or business, and thus eligible for long term capital gain and ordinary loss treatment, as 24 months or more for cattle and horses and, for other livestock, 12 months or more.⁹ That rules out the special treatment assuring long-term capital gains treatment for the first 12 months after death for animals held by the decedent.

IRS published *Rev. Rul. 75-361*¹⁰ making that very point and confirming the different treatment for trade or business livestock. The facts of that ruling were that cattle and other livestock acquired from the estate produced ordinary income on sale. The ruling points out that no exception was made in the statute for livestock used in a trade or business with specified holding periods of 12 and 24 months.¹¹

What about animals that are not held for use in a trade or business?

Those animals not held for draft, dairy, breeding or sporting purposes have a more than one year holding period.¹² Therefore, if considered to be a capital asset, rather than a trade or business asset, those animals would appear to come within the rule of an automatic more-than-one year holding period at death. Animals used for entertainment, research or other non-trade or business purposes would seem to be within the bounds of the 1970 enactment.

Is there hope for a favorable amendment?

That is unclear. However, in light of the fact that the statute has been firmly in place for 45 years, the odds of an amendment appear to be slim unless momentum somehow builds for a change.

ENDNOTES

¹ See I.R.C. § 1231(b)(3).

² I.R.C. § 1223(9), enacted into law in the Excise, Estate and Gift Tax Adjustment Act of 1970, Pub. L. No. 91-614, § 101(g), 85 Stat. 534 (1970). See S. Rep. No. 91-1444, 91st Cong., 2d Sess. 9 (1970).

³ I.R.C. § 1223(9).

⁴ I.R.C. § 1014(a).

⁵ I.R.C. § 2032.

⁶ I.R.C. § 2032A.

⁷ I.R.C. § 2031(c).

⁸ I.R.C. § 1223(9).

⁹ I.R.C. § 1231(b)(3).

¹⁰ 1975-2 C.B. 344.

¹¹ *Id.*

¹² See I.R.C. § 1231(b)(3).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr

ADVERSE POSSESSION

FENCE. In 1988, the plaintiff acquired land from the defendant who continued to live on land adjacent to the plaintiff's. A survey done at the time of sale showed that the boundary between the properties ran straight and did not follow a fence which was located a few feet onto the defendant's land. In 2011 the parties were involved in a water drainage dispute and in the course of that litigation, the parties affirmed the boundary as set forth in the survey. In 2015, the plaintiff filed a lawsuit in which the plaintiff claimed the portion of land on the plaintiff's side of the fence under adverse possession. The plaintiff claimed to have used the property for pasturing horses and cattle, mowed and hayed the land, and maintained the fence. The defendant claimed to have given the plaintiff permission to use the land on the plaintiff's side of the fence within the surveyed boundary. The trial ruled in favor of the defendant, concluding that the plaintiff had failed to establish

(1) that the plaintiff had exclusive and continuous possession for at least 15 years and (2) that the plaintiff had occupied the property under a belief that the plaintiff owned it. On appeal, the appellate court affirmed, holding that the plaintiff failed to prove that the plaintiff had exclusive and continuous possession of the disputed property. The court pointed to evidence by the defendant that the defendant had entered the disputed property for hunting, maintaining pastures and to inspect the fence. **Bradford v. Parlett, 2015 Kan. App. LEXIS 1031 (Kan. Ct. App. 2015).**

ANIMALS

ANIMAL CRUELTY. The defendant appealed a conviction of animal cruelty under Alaska Stat. § 11.61.140(a). The defendant co-owned three horses with the defendant's partner and kept the horses on the partner's father's farm. The horses were found starving and one had to be euthanized. The defendant argued that the statute was unconstitutionally vague in that it did not define which persons had