little decision making power, it is important to address the matter of compensation of individuals for their labor and management as well as their capital.

The hazards of delaying compensation adjustments, which is fairly common in family operations, are well known. It is important to compensate each individual fairly each year.[4] If cash compensation would strain the cash flow from the business, part of the compensation could be paid in increased equity in the business.

Valuing ownership interests

Especially for those unable to force dissolution and liquidation of the business, periodic valuation of ownership interests on a fair and equitable basis is a key part of protecting owners, particularly minority owners.[5] Several basic options are available including— (1) book value, (2) appraisal or (3) a periodically re-negotiated fixed price (set by the shareholders or directors annually based upon an inventory of all assets in the farm or ranch business).[6]

Protecting minority owners

In addition to providing for a fair and equitable valuation of ownership interests,[7] minority owners can be protected from the harshness of majority rule in other ways—

• Carefully drafted provisions for triggering first option and buy-sell agreements can be used to create a market for stock or other ownership interests.[8]

• The traditional decision-making rules can be modified in various ways to provide greater protection for the minority owners by providing for— (1) a greater than majority vote for decision making; (2) a below-majority vote (in some states); (3) key issues (such as an assured employment for a specified number of years or a designated minimum salary) to be predecided in a shareholders' agreement, voting trust or pooling agreement; (4) cumulative voting; or (5) pre-emptive rights.[9]

Phased retirement

The final element of a succession plan focuses on encouraging older individuals to retire and may include several components—

• An appropriate level of compensation should be assured during the retirement years.

• Access to retirement benefits should be assured and compensation arrangements should be compatible with receiving social security benefits, particularly for those under age 70.[10]

• Reduced-responsibility positions on the management team should be established for those approaching the retirement years.

In conclusion

In the final analysis, a successful plan of succession in the farm or ranch business depends heavily on the personal chemistry of the individuals involved. However, a carefully considered and thought-out succession plan can be helpful in shaping expectations and in providing a framework for implementing the steps needed for an efficient and tranquil transition.

FOOTNOTES

1 See generally 5 Harl, *Agricultural Law* § 41.02 (1997); Harl, *Agricultural Law Manual* § 5.01[3] (1997).

2 *Id*.

3 See 8 Harl, *Agricultural Law* ch. 58 (1997); Harl, *Agricultural Law Manual* § 7.02[5][a] (1997).

4 See 7 Harl, *Agricultural Law* § 57.04 (1997); Harl, *Agricultural Law Manual* § 7.02[4][d] (1997).

5 See 8 Harl, *Agricultural Law* §§ 58.03[6], 58.05 [1][a][D] (1997); Harl, *Agricultural Law Manual* § 7.02 [5][d] (1997).

6 *Id*.

7 See ns. 4-5 *supra* and accompanying text.

8 See 8 Harl, *Agricultural Law* § 58.05[1][a] (1997); Harl, *Agricultural Law Manual* § 7.02[5][d] (1997).

9 See 8 Harl, *Agricultural Law* § 58.05[1][a][iv] (1997), Harl, *Agricultural Law Manual* § 7.02[5][d] (1997).

10 See Harl, "Earnings After Retirement," 4 *Agric. Law Dig.* 37 (1993).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

BANKRUPTCY

GENERAL-*ALM* § 13.03.*

AUTOMATIC STAY. An attorney had performed legal services for the debtor in the bankruptcy case. The attorney was awarded legal fees from the Bankruptcy Court and the attorney had the award transferred to District Court for execution. The sheriff charged with executing the judgment against the debtor's tractor failed to execute the judgment and the attorney sued the sheriff for amercement, recovery, of the judgment amount. The attorney was awarded the judgment amount in state court. The sheriff sought to set aside the state court judgment as violating the automatic stay in the debtor's case. The court held that the automatic stay was not violated because the attorney did not seek or receive property from the debtor's estate. **Matter of McKeon, 210 B.R. 161 (Bankr. D. Neb. 1997)**.

FEDERAL TAXATION-*ALM* § 13.03[7].*

ADMINISTRATIVE EXPENSES. The debtor corporation had a June 1 taxable year and filed a Chapter 11 petition on December 27, 1989. The debtor paid the corporate income taxes for December 28, 1989 through May 30, 1990 and the IRS sought administrative expense status for the taxes for the June 1, 1989 through December 27, 1989 period, arguing that the taxes were assessable post-petition. The court held that the bankruptcy estate was not liable for the pre-petition taxes as an administrative expense. ***In re* Hillsborough Holdings Corp., 116 F.3d 1391 (11th Cir. 1997), *aff'g unrep. D. Ct. dec. aff'g*, 156 B.R. 318 (Bankr. M.D. Fla. 1993)**.

CLAIMS. The debtor filed for Chapter 11 and the IRS filed an unsecured priority tax claim for taxes owed by the debtor as a responsible person in a corporation which failed to pay employment taxes. The trustee objected to the claim for lack of substantiation. The IRS provided only a certificate of assessment and payment which showed the taxes owed by the debtor. The Bankruptcy Court had held that the IRS failed to substantiate the claim and disallowed the claim. The District Court reversed, holding that, under Bankr. Rule 3001(f), the filing of the tax claim was prima facie evidence of the validity of the claim and the burden of proof was shifted to the debtor to disprove the tax claim. ***In re* Pan, 209 B.R. 152 (D. Mass. 1997)**.

DISCHARGE. After losing a Tax Court case which held that the debtor owed taxes, the debtor married his long-time companion and executed an antenuptial agreement which transferred all of the assets of a corporation owned by the debtor to the debtor's spouse's corporation. In return, the spouse transferred to the debtor debts owed to her by the debtor. Neither set of assets had much value because the debtor's corporation had been incurring substantial losses. However, because the debtor's corporation owned the debtor's residence and vehicles, the antenuptial agreement effectively removed from the debtor's estate all assets against which the IRS could levy to satisfy the Tax Court judgment. The IRS petitioned for nondischarge of the debtor on the tax claims for willful and fraudulent attempt to evade taxes. The court held that the tax debt was nondischargeable because the intentional and voluntary transfer of the debtor's assets without adequate consideration to a family member was a willful and fraudulent attempt to evade taxes. ***In re* Griffith, 210 B.R. 216 (S.D. Fla. 1997), *aff'g*, 161 B.R. 727 (Bankr. S.D. Fla. 1993)**.

SETOFF. The debtor filed for Chapter 13 on January 29, 1997. After confirmation of the debtor's plan, the IRS set off the debtor's 1996 refund claim against 1991 taxes owed by the debtor. The debtor sought to recover the refund, arguing that the setoff violated the automatic stay. The court held that the refund was a pre-petition obligation of the IRS and was eligible for setoff against the 1991 pre-petition tax claim. The court held that the IRS did not intentionally violate the automatic stay because the debtor did not send notice of the bankruptcy case to the proper address for the IRS. **Matter of Okwukwu, 210 B.R. 194 (Bankr. N.D. Ala. 1997)**.

CONTRACTS

BREACH OF CONTRACT. The plaintiff was a fruit producer who contracted with the defendant cold storage company to store pears. The contract required the pears to be stored at a specific temperature and specific humidity. The plaintiff alleged that the defendant allowed the room temperature to exceed the contract temperature when "hot' pears were stored in the same room, causing some of the plaintiff's pears to mature and start spoilage. The defendant argued that the pears were already mature when placed in storage and were too warm to be cooled to the contract temperature. The defendant sought summary judgment on the causation issue, based on the plaintiff's lack of expert testimony as to the cause of the spoilage in opposition to the defendant's expert testimony. The court held that expert testimony from the plaintiff was not required to prove causation because the jury would have sufficient personal knowledge of the causes of fruit spoilage to ignore the defendant's expert testimony. The defendant also argued that it was excused from performance of the contract because the plaintiff delivered the fruit at such a high temperature that it was impossible for the defendant to store the fruit at the contract temperature. The court denied summary judgment on this issue because the defendant failed to reject the fruit when it was delivered and after the temperature of the delivered fruit was measured. **Dole Fresh Fruit Co. v. Delaware Cold Storage, 961 F. Supp. 676 (D. Del. 1997)**.

FEDERAL AGRICULTURAL PROGRAMS

DISASTER ASSISTANCE. The Commodity Credit Corporation has adopted as final regulations providing assistance under the Disaster Reserve Assistance Program (DRAP) for livestock producers whose production of livestock feed was adversely affected by severe winter disaster conditions. **62 Fed. Reg. 44391 (Aug. 21, 1997)**.

TOBACCO. The CCC has adopted as final regulations for the 1997 marketing quota ranges for tobacco:

Kind and Type	Million pounds
Virginia fire-cured(type 21)	2.395
Ky-Tenn. fire-cured(types 22-23)	43.4
Dark air-cured(types 35-36)	9.88
Virginia sun-cured(type 37)	0.156
Cigar filler & binder(types 42-44, 53-55)	8.4

The 1997 tobacco price support levels are as follows:

Kind and Type	Cents per pound
Virginia fire-cured(type 21)	149.8
Ky-Tenn. fire-cured(types 22-23)	162.3
Dark air-cured(types 35-36)	139.8
Virginia sun-cured(type 37)	132.6
Cigar filler & binder(types 42-44, 53-55)	116.9

62 Fed. Reg. 43917 (Aug. 18, 1997).

FEDERAL ESTATE AND GIFT TAX

DISCLAIMERS-*ALM* § 5.02[6].* The decedent's will provided for a marital trust and a residuary trust. The residuary trust had the surviving spouse and two children as beneficiaries. The children disclaimed a portion of the residuary trust sufficient to reduce to zero the federal estate tax on the decedent's estate, considering the available credits and deductions. Under the trust and will, the disclaimed portion passed to the surviving spouse's portion of the trust. The IRS ruled that the disclaimers were effective and the disclaimed portion was eligible QTIP. **Ltr. Rul. 9733006, May 15, 1997**.

The decedent and spouse had acquired a residence in 1965 as joint tenants. Under the decedent's will, the residence passed to the surviving spouse. Within nine months after the decedent's death, the surviving spouse disclaimed the decedent's interest in the residence which passed to the spouse. Under state law, the joint tenancy was unilaterally severable during life. The IRS ruled that the disclaimer was timely and effective. **Ltr. Rul. 9733008, May 15, 1997**.

MARITAL DEDUCTION-*ALM* § 5.04[3]. The decedent's will provided for a bequest to the surviving spouse in trust of shares of stock in a family corporation. The corporation elected to be taxed as an S corporation and the trust's ownership of the decedent's stock would have caused the termination of the S corporation election; therefore, the corporation redeemed the stock held by the trust for book value as allowed by the trust and will. The estate elected to treat the trust property as QTIP. The court held that the trust did not qualify as QTIP because the stock could be and was sold to the corporation for less than fair market value, decreasing the property passing to the surviving spouse. **Estate of Rinaldi v. U.S., 97-2 U.S. Tax Cas. (CCH) ¶ 60,281 (Fed. Cls. 1997)**.

The decedent's will bequeathed most of the estate to the decedent's surviving spouse and children. The children of the decedent's first spouse challenged the validity of the will for lack of testamentary capacity and undue influence. The two groups entered into extended negotiations and entered into a settlement, under which the surviving spouse received property in trust. The IRS ruled that the settlement proceeds passing to the spouse were eligible for the marital deduction. **Ltr. Rul. 9733017, May 20, 1997**.

VALUATION. The decedent owned a controlling interest in a family owned corporation. The stock in the corporation was subject to a buy-sell agreement which established the redemption price of the decedent's stock. The decedent owned a controlling interest in the corporation and had transferred several shares of stock as gifts, valuing the shares at fair market value, significantly above the buy-sell agreement price. The court held that the price established by the buy-sell agreement was not controlling for valuation for federal estate tax purposes because the agreement was not binding upon the decedent, whose controlling interest in the corporation would have allowed the decedent to revoke the agreement, and because the agreement was intended as a substitute for a testamentary distribution. **Bommer v. Comm'r, T.C. Memo. 1997-380**.

FEDERAL INCOME TAXATION

ALTERNATIVE MINIMUM TAX. The taxpayers, husband and wife, were grain farmers using the cash method of accounting. In October and November 1991, the taxpayers entered into deferred payment contracts with a grain warehouse, with title to the grain passing on November 22, 1991. The warehouse made payment on the contracts in January 1992, including payments on CCC loans owed by the taxpayers. Under I.R.C. § 56(a)(6), as interpreted by the IRS and prior to the Tax Relief Act of 1997, income from the installment sale of I.R.C. § 1221(1) property had to be included in AMT income without regard to the installment method of recognition of gain. The IRS position was that the sale of grain produced by a farmer was Section 1221(1) property and had to be included in 1991 AMT income. Under the TRA 1997, Section 56(a)(6) no longer applies to farm produce sold by installment sale, including all sales after December 31, 1987; therefore, the court held that the payments made under the deferred payment contracts were not included in 1991 AMT income. **Loomis v. Comm'r, T.C. Memo. 1997-381**.

BAD DEBT DEDUCTION. The taxpayer had established a wholly-owned S corporation to perform securities transactions solely for the taxpayer. The taxpayer contributed cash to the corporation which was used to purchase the securities. The contributions were not secured nor were any notes written or interest charged on the contributions. The corporation eventually became insolvent. The taxpayer claimed a bad debt deduction for the amounts contributed to the corporation; however, the court held that the contributions were not bona fide debt because no debtor-creditor relationship was established. **Boatner v. Comm'r, T.C. Memo. 1997-379**.

BUSINESS EXPENSES. The taxpayer was denied a business deduction for legal expenses incurred to appeal denial of admission to a state bar on moral character grounds. **Vannier v. Comm'r, T.C. Memo. 1997-370**.

CASUALTY LOSSES. The decedent's estate included two citrus tree groves. The groves were appraised for estate tax purposes based upon the income production capabilities of the groves. In the year following the decedent's death, the groves were severely damaged by frost. The groves were revalued using the same appraisal method, which resulted in some trees receiving a negative value because the trees would continue to be cultivated with the rest of the grove, yet the damaged trees would not produce income more than the cost of production. The IRS argued that the loss for each tree was limited to the pre-casualty value of the tree. The court allowed the deduction for casualty loss to be based upon the negative value of some trees. The court held that the post-casualty value was reasonable because the same valuation method was used both before and after the casualty and the groves would be treated as entire economic units by a producer. **Estate of Rinaldi v. U.S., 97-2 U.S. Tax Cas. (CCH) ¶ 60,281 (Fed. Cls. 1997)**.

CHARITABLE DEDUCTION. The taxpayer was a timber products corporation which owned 2 million acres of timber land. The corporation granted an easement to the State of Maine as part of a state initiative for environmental protection of watersheds. The easement provided, however, for the corporation to retain subsurface mineral rights, including the right to surface mine for gravel and stone. The court held that the easement was not qualified for a charitable deduction because the right to surface mine the land would destroy the purpose of the easement. **Great Northern Nekoosa Corp. v. U.S., 97-2 U.S. Tax Cas. (CCH) ¶ 50,591 (Fed. Cls. 1997)**.

COOPERATIVES. The taxpayer was a tax-exempt agricultural cooperative established to encourage the growth of agricultural education. The membership of the cooperative consisted of students and graduates of the state's agricultural schools. The taxpayer entered into a licensing agreement with one of the schools to use, develop, produce and distribute inbred seed lines, based on research produced by the school. The taxpayer would pay a royalty fee to the school and was required to provide the seed to all farmers and growers. The IRS ruled that the taxpayer did not recognize unrelated business income from the seed and that the taxpayer's tax exempt status was not adversely affected because the taxpayer's membership was a significant proportion of the interested agricultural community. **Ltr. Rul. 9732022, May 9, 1997**.

The taxpayer was a nonexempt agricultural cooperative formed for the purpose of administering the price-support program for members. The cooperative had made an election to treat CCC loans as income in the year received. When a member could not sell farm products for at least the price-support level, the cooperative would purchase the product using a nonrecourse loan from the CCC. The CCC loan would be paid with the proceeds of the cooperative's sale of the commodity. In order to protect the government from the losses on the CCC loans, the producers were assessed an amount based on their production and the assessments were collected by the cooperative. If the assessments exceeded the actual losses of the CCC in a year, the excess was to be returned to the cooperative. The assessments for 1982, 1983 and 1984 were returned to the cooperative by canceling the CCC loans for 1982, thus allowing the cooperative to retain all the proceeds of the sale of the commodities otherwise subject to the loans. Instead of returning the proceeds of the commodity sales to members, the cooperative retained the proceeds as a reserve to provide future price support. The IRS ruled that the undistributed income from the sale of the commodities would be subject to accumulated income tax if not demonstrated to be reasonable for the business needs of the cooperative. Because the cooperative recognized the CCC loan proceeds as income in the year received, the release of the CCC lien and subsequent sale of the commodities did not cause recognition of any additional income. **Ltr. Rul. 9734001, Jan. 9, 1997**.

COURT AWARDS AND SETTLEMENTS-*ALM* § 4.02[12]. The taxpayer was employed by a corporation and elected to participate in an early retirement program after learning that the taxpayer's further employment was in jeopardy because of age and health concerns by the employer. The taxpayer considered suing for age discrimination but signed a release of all claims in exchange for the early retirement benefit payment. The court held that the payment was included in income because the payment was intended as severance pay and as incentive for the taxpayer's early retirement and not as compensation for any personal injury to the taxpayer. **Phillips v. Comm'r, T.C. Memo. 1997-336**.

The taxpayer was one of a class of plaintiffs which sued their employer for violations of ERISA. The court held that the settlement payments received by the taxpayer were included in gross income because the settlement payment was for back wages and did not represent compensation for tort-like personal injuries. **Hemelt v. U.S., 97-2 U.S. Tax Cas. (CCH) ¶ 50,596 (4th Cir. 1997), *aff'g*, 96-2 U.S. Tax Cas. (CCH) ¶ 50,666 (D. Md. 1996)**.

HOME OFFICE. The taxpayer was an attorney who operated a law practice from the taxpayer's home. The court denied deductions relating to the office because the taxpayer used the area on nights and weekends for personal family activities. **Cook v. Comm'r, T.C. Memo. 1997-378**.

PARTNERSHIPS-*ALM* § 7.03[2].*

PARTNER'S DISTRIBUTIVE SHARE. The IRS has adopted as final regulations relating to the allocation of depreciation recapture among partners in a partnership. The 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. **62 Fed. Reg. 44214 (Aug. 20, 1996)**.

PREPRODUCTION EXPENSES. The IRS has issued new proposed and temporary regulations governing the special rules for preproduction expenses for property produced in the trade or business of farming, under I.R.C. § 263A.

The temporary regulations clarify that the special rules of section 263A(d) apply only to property produced in a farming business. The temporary regulations provide that, for purposes of section 263A, the term farming means the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity. Examples include the trade or business of operating a nursery or sod farm; the raising or harvesting of trees bearing fruit, nuts, or other crops; the raising of ornamental trees (other than evergreen trees that are more than six years old at the time they are severed from their roots); and the raising, shearing, feeding, caring for, training, and management of animals. The regulations clarify that for this purpose harvesting does not include contract harvesting of an agricultural or horticultural commodity grown or raised by another taxpayer. The temporary regulations clarify that the special rules of section 263A(d) do not apply to a taxpayer that merely buys and resells plants or animals grown or raised by another. In evaluating whether a taxpayer is engaged in the production, or merely the resale, of plants or animals, consideration will be given to factors including: the length of time between the taxpayer's acquisition of a plant or animal and the time the plant or animal is made available for sale to the taxpayer's customers, and, in the case of plants, whether plants acquired by the taxpayer are planted in the ground or kept in temporary containers.

The temporary regulations provide that a farming business does not include the processing of commodities or products beyond those activities that are incident to the growing, raising, or harvesting of such products.

The IRS and Treasury Department believe that, in general, section 263A does not change the rules regarding capitalization of costs during the preparatory period. Thus, the temporary regulations clarify that, as under prior law, taxpayers generally must capitalize preparatory expenditures, including the cost of seeds, seedlings, and animals; clearing, leveling and grading land; drilling and equipping wells; irrigation systems; and budding trees. However, because section 263A requires the capitalization of certain indirect costs as well as direct costs, the amount of preparatory expenditures capitalized may be greater under section 263A than under prior law.

The temporary regulations clarify that costs that were, in years prior to the enactment of section 263A, regarded as developmental are included in the category of preproductive period costs. Section 263A generally requires the capitalization of preproductive period costs including the costs of irrigating, fertilizing, spraying, cultivating, pruning, feeding, providing veterinary services, rent on land, and depreciation allowances on irrigation systems or structures. Preproductive period costs also include real estate taxes, interest, and soil and water conservation expenditures incurred during the preproductive period of a plant.

Taxpayers that are required by section 447 or 448(a)(3) to use an accrual method must capitalize all preproductive period costs of plants (without regard to the length of the preproductive period) and animals. Taxpayers that are not required by section 447 or 448(a)(3) to use an accrual method qualify for an exception to this general rule. Under this exception, taxpayers are not required to capitalize preproductive period costs incurred with respect to animals, or with respect to plants that have a preproductive period of 2 years or less. Thus, under this exception, taxpayers are required to capitalize only those preproductive period costs incurred with respect to plants that have a preproductive period in excess of 2 years. The temporary regulations clarify that, for purposes of determining whether a plant has a preproductive period in excess of 2 years, in the case of a plant grown in commercial quantities in the United States, the nationwide weighted average preproductive period of such plant is used.

The IRS and Treasury Department are considering the publication of guidance with respect to the length of the preproductive period of certain plants that will have more than one crop or yield. At the present time, the IRS and Treasury Department anticipate that such guidance would provide that plants producing the following crops or yields have a nationwide weighted average preproductive period in excess of 2 years: almonds, apples, apricots, avocados, blueberries, blackberries, cherries, chestnuts, coffee beans, currants, dates, figs, grapefruit, grapes, guavas, kiwifruit, kumquats, lemons, limes, macadamia nuts, mangoes, nectarines, olives, oranges, peaches, pears, pecans, persimmons, pistachio nuts, plums, pomegranates, prunes, raspberries, tangelos, tangerines, tangors, and walnuts.

Preproductive period costs (e.g., irrigating, fertilizing, real estate taxes, etc.) are capitalized during the preproductive period of a plant or animal. A taxpayer that grows a plant that will have more than one crop or yield is engaged in the production of two types of property, the plant and the crop or yield of the plant (e.g., the orange tree and the orange). The temporary regulations clarify the capitalization period for plants that will have more than one crop or yield, for crops or yields of plants that will have more than one crop or yield, and for other plants.

The temporary regulations clarify that the preproductive period of a plant generally begins when a taxpayer first incurs costs with respect to the plant, e.g., when the plant is acquired or the seed is planted. In the case of the crop or yield of a plant that has become productive in marketable quantities, the preproductive period of the crop or yield begins when the crop or yield first appears, whether in the form of a sprout, bloom, blossom, bud, etc.

In the case of a plant that will have more than one crop or yield, the preproductive period of the plant ends when the plant becomes productive in marketable quantities (i.e., when the plant is placed in service for purposes of depreciation). In the case of the crop or yield of a plant that has become productive in marketable quantities, the preproductive period of the crop or yield ends when the crop or yield is disposed of. Finally, in the case of other plants, the preproductive period ends when the plant is disposed of.

The temporary regulations provide that the preproductive period of an animal begins at the time of acquisition, breeding, or embryo implantation. The temporary regulations clarify that, in the case of an animal that will be used in the trade or business of farming, the preproductive period generally ends when the animal is placed in service for purposes of depreciation. However, in the case of an animal that will have more than one yield, the preproductive period ends when the animal produces (e.g., gives birth to) its first yield. In the case of any other animal, the preproductive period ends when the animal is sold or otherwise disposed of. The temporary regulations clarify that, in the case of an animal that will have more than one yield, the costs incurred after the beginning of the preproductive period of the first yield but before the end of the preproductive period of the animal must be allocated between the animal and the yield on a reasonable and consistent basis. Any depreciation allowance on the animal may be allocated entirely to the yield.

The temporary regulations provide that the costs required to be capitalized with respect to farming property may, if the taxpayer chooses, be determined using any reasonable inventory valuation method, such as the farm-price method of accounting (farm-price method) or the unit-livestock-price method of accounting (unit-livestock-price method). Under the temporary regulations, these inventory methods may be used by a taxpayer regardless of whether the farming property being produced is otherwise treated as inventory by the taxpayer, and regardless of whether the taxpayer is otherwise using the cash method or an accrual method.

The temporary regulations clarify that notwithstanding a taxpayer's use of the farm-price method with respect to farming property to which the provisions of section 263A apply, the taxpayer is not required, solely by such use, to use the same method of accounting with respect to farming property to which the provisions of section 263A do not apply.

The temporary regulations under section 263A modify the rule set forth in Sec. 1.471-6 providing that no increase in unit cost is required under the unit-livestock-price method with respect to the taxable year in which certain animals are purchased, if the purchases occur in the last 6 months of the taxable year. The temporary regulations provide that any taxpayer required to use an accrual method under section 448(a)(3) must include in inventory the annual standard unit price for all animals purchased during the taxable year, regardless of when in the taxable year the purchases are made. The temporary regulations further amend this rule and provide that all taxpayers using the unit-livestock-price method must modify the annual standard price to reasonably reflect the particular period in the taxable year in which purchases of livestock are made, if such modification is necessary in order to avoid significant distortions in income that would otherwise occur through operation of the unit-livestock-price method. The temporary regulations do not specify the particular modification that must be made to the annual standard price for any particular taxpayer, but rather allow any reasonable modification made by the taxpayer to the annual standard price to avoid significant distortions in income.

The temporary regulations clarify that farmers using the unit-livestock-price method are permitted to elect the simplified production method, as well as the simplified service cost method of accounting, under section 263A. In such a situation, section 471 costs are the costs taken into account by the taxpayer under the unit-livestock-price method using the taxpayer's standard unit price determined under these temporary and final regulations. The term “additional section 263A” costs includes all additional costs required to be capitalized under section 263A including costs that are required to be capitalized under section 263A that are not reflected in the standard unit prices (e.g., general and administrative costs and depreciation, including depreciation on a calf's mother).

Certain taxpayers, other than those required to use an accrual method by section 447 or 448(a)(3), may elect not to capitalize the preproductive period costs of certain plants even though such plants have a preproductive period in excess of 2 years and would otherwise be subject to the capitalization requirements of section 263A. Taxpayers making this election may continue to deduct (subject to other limitations of the Code) the preproductive period costs that were deductible under the rules in effect before the enactment of section 263A. The temporary regulations clarify that although a taxpayer producing a citrus or almond grove may make this election, the election does not apply to the preproductive period costs of a citrus or almond grove that are incurred before the close of the fourth taxable year beginning with the taxable year in which the trees were planted.

If a taxpayer makes this election with respect to any plant, the taxpayer must treat the plant as section 1245 property. In addition, the taxpayer, and any person related to the taxpayer, must use the alternative depreciation system of section 168(g)(2) for any property used predominantly in a farming business that is placed in service in a taxable year for which the election is in effect.

Section 263A(d) provides an exception from capitalization for preproductive period costs incurred with respect to plants that are replacing certain plants that were lost by reason of certain casualties. The temporary regulations clarify that this exception for preproductive period costs does not apply to preparatory expenditures or the costs of capital assets. In addition, the temporary regulations clarify that the casualty loss exception applies whether the plants are replanted on the same parcel of land as the plants destroyed by casualty or a parcel of land of the same acreage in the United States. The temporary regulations additionally clarify that the exception applies to all plants replanted on such acreage, even if the plants are replanted in greater density than the plants destroyed by the casualty.

The temporary regulations provide that, in the case of property that is not inventory in the hands of the taxpayer, the regulations are generally effective for costs incurred on or after August 22, 1997, in taxable years ending after such date. In the case of inventory property, the temporary regulations are generally effective for taxable years beginning after August 22, 1997. However, taxpayers in compliance with Sec. 1.263A-4T in effect prior to August 22, 1997, as modified by other administrative guidance, that continue to comply with Sec. 1.263A-4T in effect prior to August 22, 1997, as modified by other administrative guidance, will not be required to apply these new temporary rules until the notice of proposed rulemaking that cross-references these temporary regulations is finalized. The amendment to Sec. 1.471-6(f) is effective for taxable years beginning after August 22, 1997. **62 Fed. Reg. 44542 (Aug. 22, 1997), amending Temp. Treas. Reg. § 1.263A-4T**.

SAFE HARBOR INTEREST RATES
September 1997

	Annual	Semi-annual	Quarterly	Monthly
		Short-term		
AFR	5.81	5.73	5.69	5.66
110% AFR	6.40	6.30	6.25	6.22
120% AFR	7.00	6.88	6.82	6.78
		Mid-term		
AFR	6.23	6.14	6.09	6.06
110% AFR	6.86	6.75	6.69	6.66
120% AFR	7.51	7.37	7.30	7.26
		Long-term		
AFR	6.55	6.45	6.40	6.36
110% AFR	7.23	7.10	7.04	7.00
120% AFR	7.89	7.74	7.67	7.62

SELF-EMPLOYMENT INCOME. The IRS had issued proposed regulations which allow individuals to determine whether they are limited partners for purposes of the self-employment tax, I.R.C. § 1402(a)(13). 62 Fed. Reg. 1702 (Jan. 13, 1997), amending Treas. Reg. § 1.1402(a)-2., see p. 22, supra. The Taxpayer Relief Act of 1997, Section 935, prohibits the IRS from issuing final or temporary regulations on this issue until July 1, 1998. **Pub. L. No. 105-34, Sec. 935 (1997)**.

SECURED TRANSACTIONS

CONSERVATION RESERVE PROGRAM PAYMENTS. The debtor had enrolled farm land in the federal conservation reserve program (CRP) and was receiving payments for the land. The land was mortgaged to a bank and the bank obtained a foreclosure judgment and sale of the property. The issue was whether the CRP payment were conveyed with the land in the foreclosure sale. The original mortgage and deed contained language to include in the land all “incorporeal immovables.” The court held that the CRP payments did not pass with the land because the CRP payment rights were personal to the debtor and because the mortgage and deed involved only transfer of real property rights. **In re Havard, 209 B.R. 196 (W.D. La. 1997)**.

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