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"Structured Sales" – A Different Twist from Installment Sales

-by Neil E. Harl*

Installment reporting for eligible property (including grain and livestock since 1980)[1] has been available for a very long time.[2] More recently, a concept referred to as "structured sales" has appeared on the scene with parallel features to installment sales (in fact relying on installment sales provisions)[3] and purporting to provide additional benefits to sellers of property. The concept has been used in some sectors but thus far has not played a significant role in the agricultural sector. This article addresses the features of "structured sales" and the obstacles encountered to date.

Features of a structured sale

With a structured sale, a property owner agrees to relinquish title to the property in return for a discounted sum available up front with a finance firm holding the title and making the advance payment to the seller of the property. The finance firm is compensated from the discounted transaction less the payment of the discounted value to the seller. One anticipated objection is that a seller who gives up title to the property is an unsecured party to the transaction if the finance firm holding the title defaults.

Experience with "9/11" payments

As has been fairly widely reported, the "structured sale" concept was reportedly used to defer income from the sizeable recoveries paid to victims and their families as a result of the 9/11 incident. That version was referred to as "structured settlements."[4] Documented abuses led to enactment in 2002 of the Victims of Terrorism Tax Relief Act[5] which imposed a tax equal to 40 percent of the "factoring discount" with respect to each transaction unless the transfer of structured settlement payment rights was approved in advance in a "qualified order."

Moreover, the states were encouraged to legislate on the abuse issue, also, and most states followed suit.[6] The object was to provide some protection against abuse as had been observed in some settings.

Another major concern

Another concern voiced with the concept, because of reliance on installment reporting rules,[7] has been a provision in the installment reporting statute[8] which can disqualify

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installment reporting if the evidence of indebtedness received by the seller of the property is "payable on demand" or is "readily tradable."[9] A Field Service Memorandum,[10] after analyzing whether a transaction similar to that of a "structured sale" would be tripped up by the readily tradable" restriction in the statute, opined that the Commissioner might well take that position. The conclusion of the author (or authors) of the Field Service Advice memorandum was that "we believe the Commissioner may argue that the LIBOR notes (used in that transaction) are not eligible for Section 453 installment treatment because they are readily tradable within the meaning of the statute.[11]

In light of the Field Service Advice Memorandum,[12] it would be prudent to request a private letter ruling, detailing the precise facts of a proposed sale before committing to such a transaction.

A final note

In general, sellers under installment contracts have retained title until all or a substantial proportion of the principal payments have been paid before giving up title to the property. That has provided a modicum of protection against default by the purchaser. In "structured sales" as described herein, there would be no such protection, creating a significant risk of non-payment under the obligation. The combined risks and uncertainties would suggest caution before entering into a "structured sales" transaction.

ENDNOTES

[1] See Installment Sales Revision Act of 1980, Pub. L. No. 96-471, 94 Stat. 2247 (1980). See also Senate Committee Report, 96-1000, 2d Sess. 1980-2 C.B. 494 (1980).

[2] See I.T. 2063, C.B. III-2, 108 (1931).

[3] I.R.C. § 453. See generally 6 Harl, *Agricultural Law* § 48.03 (2015); 1 Harl, *Farm Income Tax Manual* § 2.03 (2015 ed.); Harl, *Agricultural Law Manual* § 4.01[1][c] (2015).

[4] See I.R.C. § 5891(a).

[5] Pub. L. No. 107-134, § 115(a), (c), 115 Stat. 2427 (2002).

[6] E.g., Iowa Code Ch. 682, "Structured Settlement Protection."

[7] I.R.C. § 453.

[8] I.R.C. § 453(f)(4).

[9] I.R.C. § 453(f)(4)(A), (B).

[10] FSA 001968, Dec. 16, 1996, updated Jan. 31, 2004.

[11] I.R.C. § 453 (f)(4)(B).

[12] FSA 001968, Dec. 16, 1996, updated Jan. 31, 2004.

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr

BANKRUPTCY

CHAPTER 12

AVOIDABLE TRANSFERS. The debtor was a limited partnership which filed for Chapter 12. The debtor had granted a bank security interests in all livestock, equipment and crops owned by the debtor. The bank obtained relief from the automatic stay and began non-bankruptcy proceedings to obtain the collateral. However, instead of proceeding against the collateral, the bank allowed the debtor to sell equipment and livestock to a third party, with the proceeds used to pay off the debt secured by the property. The same process was used by another creditor. Both sets of sales were to the same person and neither sale was approved by the Bankruptcy Court. The debtor then sought to avoid the sales to the third party under Section 549 as unapproved post-petition sales. The purchaser filed for summary judgment, arguing that the debtor lacked standing to bring the action because the debtor was not injured by the sales in that the proceeds were used to pay off the debts secured by the collateral sold. The court denied the summary judgment because the purchaser failed to demonstrate conclusively that the sales were not injurious to the debtor or the bankruptcy estate. ***In re* David Johnsman Limited Partnership, 2015 Bankr. LEXIS 2702 (Bankr. N.D. Ohio 2015)**.

CONTRACTS

REMEDIES. The plaintiff contracted with the defendant to build a hog building on the plaintiff's farm. The building used trusses manufactured by the defendant. Six years later, the trusses failed and the roof collapsed, causing damage to the building and loss of hogs inside. The plaintiff sued for breach of implied warranty and sought damages for the cost of the building repair, loss of animals and loss of profits from use of the building. The defendant argued that no loss of profits could be recovered because the transaction was a commercial contract and the Uniform Commercial Code, Mich. Comp. Laws § 440.2725(2), applied to bar the case under its four year statute of limitations. The court looked to *Neibarger v. Universal Cooperatives, Inc., 486 N.W.2d 612, 618 (Mich. 1992)*, for application of the economic loss doctrine under Michigan law. The court interpreted *Neibarger* to hold that the economic loss doctrine prevented an action in tort "[w]here damage to other property was caused by the failure of a product purchased for commercial purposes to perform as expected, and this damage was within the contemplation of the parties to the agreement and the occurrence of such damage could have been the subject of negotiations between the parties." The plaintiffs argued that *Neibarger* did not apply to prohibit tort claims in this case because the defendant designed, manufactured and sold an