The courts allowing the exclusion on sale of a principal residence by the bankruptcy estate have reasoned that the Bankruptcy Tax Act of 1980[14] provides that—

> "Except as otherwise provided by this section,[15] the taxable income of the [bankruptcy] estate shall be computed in the same manner as for an individual. The tax shall be computed on such taxable income and shall be paid by the trustee."[16]

Moreover, the transfer of property to the bankruptcy estate is not to be treated as a disposition of the property "…and the estate shall be treated as the debtor would be with respect to such asset."[17]

Two of the recent decisions allowing the exclusion[18] noted that the Bankruptcy Tax Act of 1980[19] also specifies that the bankruptcy estate takes over from the debtor various tax attributes including the holding period and the "character" of the asset "it had in the hands of the debtor.'[20] The court in the case of *In re Kerr*[21] concluded that to allow the exclusion (which the court did) was consistent with *In the Matter of Kochell*[22] which stated that once the debtor files bankruptcy, the estate is thereafter treated as the debtor. Thus, in that case, the bankruptcy estate was liable for the penalty for premature withdrawal of funds from the debtor's IRA.[23]

Ownership by estate

Typically, the new income tax basis received at death[24] or up to six months after death[25] largely eliminates the gain on post-death sale of the principal residence. However, if the decedent's principal residence is sold after death with gain on the transaction, the question is whether that gain is eligible for the exclusion provided the ownership and use requirements are met and the debtor had not used the exclusion within the last two years.[26]

The repeal of the age requirement in 1997 eliminated one barrier to an estate claiming the exclusion to date. No case or ruling has considered the eligibility of an estate for the exclusion but it would appear that an estate should not be prevented from claiming the exclusion if the various requirements are met.

FOOTNOTES

1 I.R.C. § 121. See generally 6 Harl, *Agricultural Law* § 48.02[3] (1999); Harl, *Agricultural Law Manual* § 6.03[2][a] (1999).

2 I.R.C. § 121(b)(1), (2), enacted by Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788 (1997).

3 I.R.C. § 121(a).

4 See Rev. Rul. 75-62, 1975-1 C.B. 188 (no exclusive rule for determining when partnership is viewed as an entity or an aggregate).

5 Ltr. Rul. 8741066, July 16, 1987.

6 Allied Marine Systems, Inc. v. Comm'r, T.C. Memo. 1997-101.

7 Ltr. Rul. 8007050, Nov. 23, 1979; Ltr. Rul. 8313025, Dec. 23, 1982.

8 *Id.*

9 Ltr. Rul. 8239055, June 29, 1982.

10 See *In re* Barden, 105 F.3d 821 (2d Cir. 1997) (chapter 7 bankruptcy); *In re* Manfred Mehr, 153 Bkrpcy. Rep. 430 (Bankr. D. N.J. 1993) (chapter 7 bankruptcy); *In re* Winch, 226 Bkrpcy. Rep. 591 (Bankr. S.D. Ohio 1998).

11 *Id.*

12 In re Kerr, 99-1 U.S.T.C. ¶ 50,310 (W.D. Wash. 1999) (Chapter 7 bankruptcy).

13 *In re* Popa, 98-1 U.S. Tax Cas. (CCH) ¶ 50,276 (Bankr. N.D. Ill. 1998), *appeal pending*, U.S. District Court, N.D. Ill.; *In re* Munster, 226 Bkrpcy. Rep. 632 (Bankr. E.D. Mo. 1998); *In re* Bradley, 1998 WL 400737, *appeal pending*, U.S. District Court, M.D. Tenn.; *In re* Godwin, 99-1 U.S. Tax Cas. (CCH) ¶ 50,287 (Bankr. S.D. Ohio 1999).

14 I.R.C. § 1398(c)(1).

15 I.R.C. § 1398.

16 *Id.*

17 I.R.C. § 1398(f)(1).

18 *In re* Popa, 98-1 U.S. Tax Cas. (CCH) ¶ 50,276 (Bankr. N.D. Ill. 1998); *In re* Bradley, 1998 WL 400737, *appeal pending*, U.S. District Court, M.D. Tenn.

19 See note 13 *supra*.

20 I.R.C. § 1398(g)(6).

21 99-1 U.S. Tax Cas. (CCH) ¶ 50,310 (W.D. Wash. 1999).

22 804 F.2d 84 (7th Cir. 1986).

23 *Id.*

24 I.R.C. § 1014(a)(1).

25 I.R.C. § 1014(a)(2).

26 I.R.C. § 121(b).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

BANKRUPTCY

GENERAL-*ALM* § 13.03.*

EXEMPTIONS

EARNED INCOME CREDIT. The debtor claimed an income tax refund due to earned income credit as exempt, under Okla. Stat. tit. 31, § 1.1, earnings from personal services. The court held that the earned income credit was not exempt as wages but was nonexempt return of overpayment of taxes. ***In re* Dickerson, 227 B.R. 742 (Bankr. 10th Cir. 1998)**.

CHAPTER 12-*ALM* § 13.03[8].*

PLAN. The IRS had filed a claim for administrative expenses resulting from unpaid post-petition employment taxes. The debtor's Chapter 12 plan provided for payment of the taxes over three years, along with other installment payments of other claims. The IRS argued that, under Section 1226(b),

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administrative expense claims had to be paid in full with the first payments to other creditors. The court held that Section 1226(b) allowed installment payments of administrative claims over the life of the plan. ***In re* Ryan, 228 B.R. 746 (Bankr. D. Or. 1999)**.

FEDERAL TAXATION-*ALM* § 13.03[7].*

DISCHARGE. The debtor had timely, with extensions, filed the 1989 return in October 1990. The debtor filed a Chapter 7 case in August 1992 which was dismissed in December 1992. In both cases the IRS filed a claim for the unpaid 1989 taxes. The debtor filed the current case in July 1993 and received a discharge in November 1993. The issue was whether the first case tolled the three-year limitation period of Section 523. The court held that the taxes were nondischargeable because the first Chapter 7 case tolled the three-year period in Section 523. The case is designated as not for publication. ***In re* Brustman, 99-1 U.S. Tax Cas. (CCH) ¶ 50,348 (Bankr. 9th Cir. 1998)**.

The debtor had filed three previous bankruptcy cases and agreed that the three-year limitation of Section 523 was tolled during the cases. However, more than three years had elapsed on several tax claims even with the tolled periods. The IRS argued that, under I.R.C. § 6503(h), each tolled period included an additional six months after the end of each bankruptcy case. The court agreed and included an additional 180 days of tolled time to each prior bankruptcy case, resulting in a total of less than three years of untolled time between the filing of the tax returns and the filing of the current bankruptcy petition. Thus, the tax claims were nondischargeable. ***In re* Daniel, 227 B.R. 675 (Bankr. N.D. Ind. 1998)**.

CONTRACTS

HEDGE-TO-ARRIVE CONTRACTS. The plaintiff was a grain farmer who entered into cash forward grain contracts with the defendants who included an agricultural consultant firm, a grain elevator and commodity trading advisor. The contracts required a certain amount of grain to be delivered, based on the estimated entire yield of the plaintiff. If the year's production fell short of the required contract amount, the deficit was carried over to the following year. The agricultural consultants were also supposed to acquire sufficient hedges on the futures market to offset any price deficiencies but failed to accomplish that goal. The plaintiff's crops were short each year and the hedges failed to offset the price differences, resulting in the plaintiff owing over $300,000 on the contracts. The plaintiff alleged that the contracts were illegal off-exchange futures contracts. The court held that the contracts were standard cash forward contracts under which a producer was expected to deliver grain. The court held that the rollover provisions were insufficient to make the contracts futures contracts under the Commodity Exchange Act. **Lachmund v. ADM Investor Services, Inc., 26 F. Supp. 3d 1107 (N.D. Ind. 1998)**.

CORPORATIONS

LOANS TO SHAREHOLDERS. The plaintiff and defendant were 50 percent shareholders and sole directors in a corporation formed to purchase and operate a ranch. Because the corporation had no other assets, livestock, employees and equipment were leased or bartered from another corporation owned by the defendant. The corporation's books recorded all of these transactions as loans from the defendant or the defendant's corporation. When the corporation was terminated the loans were paid first from the liquidation proceeds. The plaintiff argued that the loans were not bona fide corporate debts because the loans were not ratified by all of the directors, the plaintiff and defendant, as required by the bylaws. The court found that the bylaws required a majority vote of directors to ratify any corporate contract with a shareholder, an impossibility for a corporation with only two directors/shareholders. The court also found that the bylaws provided that a corporate contract with a shareholder was not invalidated by the ratification provision if the contract otherwise complied with state law. The court held that state law permitted corporate-shareholder contracts if the contract was fair to the corporation. The court held that the contract was fair to the corporation because the employees, livestock and other borrowed assets were essential to the operation of the ranch. In addition, the court held that the plaintiff had impliedly ratified the loans because the plaintiff had knowledge of the use of the assets, had signed financial statements to lenders which listed the loans as corporate liabilities, and had resigned as director and refused to participate in the operation of the ranch. **Lahnston v. Second Chance Ranch Co., 968 P.2d 32 (Wyo. 1998)**.

FEDERAL AGRICULTURAL PROGRAMS

LIVESTOCK ASSISTANCE. The CCC has adopted as final regulations governing a new livestock disaster assistance program authorized by the Agriculture, Rural Development, Food and Drug Administration, and Related Agencies Appropriations Act, 1999 (Pub. L. 105-277) (1999 Act). As provided in the 1999 Act, livestock producers who suffered livestock feed losses as a result of natural disaster may apply for benefits to compensate for losses which occurred in calendar year 1998. Benefits will be provided to eligible livestock producers only in those counties where a severe natural disaster occurred, and that were subsequently approved by the Deputy Administrator for Farm Programs. A county must have suffered a 40 percent or greater grazing loss for three consecutive months during the 1998 calendar year, as a result of damage due to a natural disaster in order to be eligible; livestock producers in counties contiguous to an approved county are not eligible. A livestock producer in an approved county must have suffered at least a 40 percent loss of normal grazing for the producer's eligible livestock for a minimum of three consecutive months. Losses will only be compensable up to 80 percent of the total grazing available and the compensable loss will also not exceed a county maximum set by the local county committee. The program will be administered through the Deputy Administrator for Farm Programs of the Farm Service Agency. Payments will be made according to a formula subject to funding and other limitations, including a per person payment limitation and a provision which precludes participation for persons whose gross revenue exceeds a specified amount. A final payment shall not exceed 50 percent

of the eligible loss amount determined prior to applying a national factor, if applicable. The regulations provide that the rules of 7 CFR Part 1400 will be used to make "person" determinations for these purposes. **64 Fed. Reg. 13497 (March 19, 1999), adding 7 CFR §§ 1439.101 *et seqs*.**

NOXIOUS WEEDS. The APHIS has adopted as final amendments to the noxious weeds regulations which add Solanum Tampicense Dunal (wetland nightshade) and Caulerpa Taxifolia (Mediterranean clone) to the list of aquatic weeds and remove Ipomoea Triloba Linnaeus from the list of terrestrial weeds. **64 Fed. Reg. 12881 (March 16, 1999)**.

PERISHABLE AGRICULTURAL COMMODITIES ACT. The defendant was a medical doctor who owned all of the stock of a PACA-licensed produce dealer corporation. The corporation purchased produce from the plaintiffs but did not pay for all of it. The corporation did not have enough assets, after liquidation of all accounts and property, to pay for the produce. The plaintiffs sought recovery from the defendant personally liable for the PACA trust fund shortfall of the corporation. The plaintiffs cited *Morris Okun, Inc. v. Harry Zimmerman, Inc., 814 F. Supp. 346 (S.D. N.Y. 1993)* as authority for the defendant's personal liability for the PACA trust. The defendant argued that the defendant merely owned the company as an investor and did not take part in any of the management of the business; therefore, the defendant should not be held liable for the corporation's failure to pay for the produce. The court cited *Sunkist Growers, Inc. v. Fisher, 104 F.3d 280 (9th Cir. 1997)* in support of its holding that a 100 percent shareholder was in the position to control PACA trust assets held by the corporation. The court held that the defendant breached a fiduciary duty toward the PACA trust assets and was personally liable for the failure of the corporation to preserve PACA trust assets. The court noted that the PACA was a "tough law" and that the defendant should have known that it was the defendant's personal responsibility to ensure that the corporation preserved the PACA trust for produce sellers. **Golman-Hayden Co., Inc. v. Fresh Source Produce, Inc., 27 F. Supp.2d 723 (N.D. Tex. 1998)**.

FEDERAL ESTATE AND GIFT TAX

ADMINISTRATIVE EXPENSES. The decedent's estate was assessed the fraud penalty for willful failure to disclose assets of the estate on the estate tax return. The estate sought to deduct the interest on the penalty as an administrative expense. The IRS ruled that the interest on the fraud penalty actually paid or accrued was deductible provided it was allowable as an expense of the estate under local law and the expense was incurred for the benefit of the estate. **FSA 199910003, Nov. 19, 1998**.

CHARITABLE DEDUCTION. The IRS has provided guidance on the ordering and taxation of distributions under I.R.C. § 664(b)(2) from a Charitable Remainder Trust (CRT) to reflect changes made to I.R.C. § 1(h) by the Taxpayer Relief Act of 1997 (TRA 1997). TRA 1997 amended I.R.C. § 1(h) to provide for new capital gain tax rates for noncorporate taxpayers. A CRT's long-term capital gains (LTCGs) and losses fall into three separate tax rate groups: (1) the 28-percent group, (2) the 25-percent group, and (3) the 20-percent group. Grouping of LTCGs properly taken into account by a CRT is necessary in order to determine the treatment of distributions by the CRT. The LTCGs properly taken into account by a CRT from January 1, 1997, through May 6, 1997, are treated as LTCGs in the 28-percent group. **Notice 99-17, I.R.B. 1999-__, __**.

DEDUCTIONS. The decedent had redeemed stock received from the estate of a predeceased spouse. The decedent realized gain on the redemption, based on the basis in the stock established by the predeceased spouse's estate for federal estate tax purposes. The decedent's estate tax return claimed a deduction for the federal income tax paid on the stock redemption. The predeceased spouse's estate tax return was audited and the value of the stock was increased, thus increasing the decedent's basis in the stock and decreasing the income tax liability. The decedent's estate filed for a refund which was allowed. The IRS then assessed a deficiency against the decedent's estate tax because of a decrease in the deduction for federal income tax. The estate argued that post-death events should not be considered in determining the amount of a deduction which was valid on the date of the decedent's death. The estate cited *Propstra v. United States, 680 F.2d 1248 (9th Cir. 1982)* and *Estate of Sachs v. Comm'r, 88 T.C. 769 (1987), rev'd, 856 F.2d 1158 (8th Cir. 1988)* which did not allow changes based on post-death events. The court distinguished the current case on the basis that the estate here had requested the refund of income taxes, demonstrating that the income tax liability was contingent as of the decedent's death. The court held that the income tax deduction for estate tax purposes had to be decreased by the amount of the refund. The court also held that the deduction for state income taxes was also decreased since the state tax liability was dependent upon the estate's income tax liability. **Est. of McMorris v. Comm'r, T.C. Memo. 1999-82**.

SPECIAL USE VALUATION-*ALM* § 5.03[2].* The decedent died owning an interest in a general partnership, a ranching partnership, for which an election under I.R.C. § 2032A could be made. On the federal estate tax return, the estate did not make an election under I.R.C. § 2032A to specially value the ranch property. The executors of the estate requested an extension of time under I.R.C. § 301.9100-1 to make an election under I.R.C. § 2032A with respect to the ranch property. An extension was granted. **Ltr. Rul. 9911030, Dec. 17, 1998**.

VALUATION OF STOCK. The decedent owned 18 of the outstanding 76.445 shares of the voting stock and 3,942.048 of the outstanding 141,288.584 shares of the nonvoting stock of a private, family-owned corporation. The remaining shares of outstanding voting stock were owned by the decedent's three siblings. The voting stock was subject to a 360-day restriction on transferability or hypothecation. Both classes of stock were entitled to the same dividends on a per-share basis, if and when dividends were declared. Holders of the nonvoting stock were entitled to a liquidating preference. The court valued the stock by calculating the equity value of the corporation, adding a premium for voting privileges, and applying a 35-percent marketability discount to the voting stock and a 40-percent marketability discount to the nonvoting stock. **Est. of Simplot v. Comm'r, 112 T.C. No. 13 (1999)**.

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FEDERAL INCOME TAXATION

CAPITAL ASSETS. Legislation has been intriduced to reduce the holding period for horses from 24 months to 12 months for purposes of determining whether horses are capital assets under I.R.C. § 1231. **H.R. 1174, 106th Cong., 1st Sess. (1999)**.

CASUALTY LOSSES. The taxpayers owned a home near to the home owned by O.J. Simpson. The taxpayers claimed a $400,000 casualty loss deduction for loss of value of their home, resulting from the publicity surrounding the O.J. Simpson trial which caused buyers to be less likely to pay the full fair market value for the property. The court disallowed the deduction because the taxpayers did not allege any physical damage to their property from either the murders or the media coverage. **Caan v. United States, 99-1 U.S. Tax Cas. (CCH) ¶ 50,349 (C.D. Calif. 1999)**.

CORPORATIONS-*ALM* § 7.02.*

COSTS OF GOODS SOLD. The taxpayer was a corporation with one shareholder. The shareholder owned two unimproved lots and the taxpayer constructed two single-family houses on the shareholder's lots. In calculating the taxpayer's gross income, the taxpayer subtracted the construction expenditures as cost of goods sold. The shareholder formed a second corporation of which the shareholder was president and 50-percent shareholder. The shareholder transferred the improved lots to the second corporation which sold both properties and reported the income from the sale of the properties. The court held that the taxpayer could not claim the costs of the construction as cost of goods sold because the expense was personal to the shareholder. **Jim Wood Land Clearing Co., Inc., T.C. Memo. 1999-90**.

ELECTION. The taxpayer purchased 100 percent of an entity considered a per se corporation under Treas. Reg. § 301.7701-2(b)(8). The entity was converted to an entity eligible to elect its classification for federal tax purposes. The purpose of the conversion was to elect that the entity be treated as an entity that is disregarded as an entity separate from its owner for federal tax purposes. However, the election was not timely filed. The IRS allowed an extension of time to file the election. **Ltr. Rul. 9910051, Dec. 7, 1998**.

EMPLOYEE COMPENSATION. The taxpayer was a publicly-held corporation and a calendar year taxpayer. Several of the taxpayer's corporate officers had resigned their positions as officers and all of their duties as such. These individuals could continue to perform services as the taxpayer's employees for the remainder of the year of resignation and possibly in future years, but it was not their or the taxpayer's intent that these individuals resume their duties as officers at any time in the foreseeable future. These officers, however, could be listed pursuant to the executive compensation disclosure rules under the Securities Exchange Act as chief executive officer or one of the highest compensated officers of the taxpayer for the year of resignation. The IRS ruled that the resigned officers would not be covered employees for the year of resignation and no compensation paid to them with respect to that year would be subject to the I.R.C. § 162(m) deduction limitation. **Ltr. Rul. 9910011, Dec. 4, 1998**.

COURT AWARDS AND SETTLEMENTS. As part of a staff reduction plan, the taxpayer's employer offered employees the chance to participate in an early termination program. The taxpayer elected to participate and in exchange for a lump-sum payment the taxpayer signed a general release form releasing the employer for all liability in contract, tort or any other type of claim. The taxpayer did not file any type of claim against the employer. The court held that the payments were included in the taxpayer's gross income because the payments were not received in compensation for personal injuries. **Primozic v. Comm'r, T.C. Memo. 1999-95**.

EMPLOYEE EXPENSES. The taxpayer was employed by two employers during the tax year involved and submitted employee expense statements to those employers. The employers reimbursed the taxpayer for those expenses. The taxpayer, however, claimed additional expenses on the taxpayer's income tax return. The taxpayer provided no explanation of why those expenses were not included in the expense statements. The court held that no deduction was allowed for those expenses because the taxpayer did not demonstrate that those expenses were not reimbursable by the employers. In addition, the taxpayer was denied deductions for travel, lodging and meal expenses because the taxpayer did not provide corroborating evidence of the time and place of the travel and the business purpose of the expense. **Gomez v. Comm'r, T.C. Memo. 1999-94**.

EXPENSE METHOD DEPRECIATION. The taxpayer was a partner in an LLC which started a new business. The LLC was taxed as a partnership and had a net loss for the first tax year. In addition to the loss, the LLC claimed $17,000 in expense method depreciation deduction for new equipment. The taxpayer claimed a share of the net loss and expense method depreciation on the taxpayer's personal income tax return. The court held that the eligibility for the expense method depreciation deduction had to be determined at the partnership level. Because the partnership did not have any taxable income, no expense method depreciation deduction could be taken. The taxpayer argued that the regulation involved, Treas. Reg. § 1.179-2(c)(2), was invalid. The taxpayer contended that, since for purposes of the I.R.C. § 179(b)(3)(A) limitation, the taxpayer could aggregate taxable incomes from different trades or businesses, the taxpayer should be able to aggregate the taxpayer's taxable income with the income of the partnership under I.R.C. § 179(d)(8) to determine the partnership's taxable income. The taxpayer also argued that I.R.C. § 179(b)(3)(A) applied only to the taxable income *of the taxpayer* derived from the trade or business *by the taxpayer*. The taxpayer contended that, under I.R.C. § 701, a partnership is not a taxpayer; therefore, that section cannot apply to a partnership. The taxable income limitation in I.R.C. § 179(b)(3)(A) was, therefore, meaningless when applied to a partnership, and Treas. Reg. § 1.179-2(c)(2) was accordingly invalid. The court noted that a partnership is often considered a taxpayer under the I.R.C. and held that the regulation was valid. **Hayden v. Comm'r, 112 T.C. No. 11 (1999)**.

FARM AND RANCH RISK MANAGEMENT ACCOUNTS. Legislation has been introduced in the U.S. Senate to create a deduction for contributions made to a "farm or ranch risk management account" (FARRM account). The

deduction would be limited to 20 percent of the taxpayer's taxable income from an eligible farming business. An eligible farming business is defined as "any farming business (as defined in [I.R.C.] section 263A(e)(4)) which is not a passive activity (within the meaning of [I.R.C.] section 469(c)) of the taxpayer." The contributions are to be invested in cash or other interest bearing obligations with trust income taxable to the trust. The FARRM account is to be a grantor trust for the benefit of the taxpayer and contributions are to be redistributed to the grantor within five years, with distributions included in income. **S. 642, 106th Cong., 1st Sess. (1999)**.

FARMING SYNDICATES. The IRS has announced that it is withdrawing proposed regulations §§ 1.278–2, 1.464–1, 1.464–2. **I.R.B. 1999-12, 34**.

HOBBY LOSSES. The taxpayer raised, bred and trained horses for 12 years. The court reviewed the factors of Treas. Reg. § 1.183-2(b) and held that the activity was not engaged in with the intent to make a profit: (1) the activity was not carried on in a business-like manner because the taxpayer (a) did not seriously investigate the activity's potential for profit, (b) did not formulate a business plan, (c) did not prepare budgets and other financial statements to gauge the profitability of the activity, (d) did not have a separate business bank account, and (e) did not change the business operation to make it more profitable; (2) the taxpayer had no expertise at operating a horse breeding business and did not obtain expert advice on operating the business; (3) the taxpayer did not present evidence that the horses would appreciate in value; (4) the taxpayer had not profitably operated any similar business; (5) the business never made a profit; (6) the activity had substantial losses which did not occur from unforeseen circumstances; (7) the losses offset income from other sources; and (8) the taxpayer received much personal pleasure from the activity. **Lundquist v. Comm'r, T.C. Memo. 1999-83**.

The taxpayer owned a manufacturing company and also operated a horse breeding and racing operation over many years. The court reviewed the factors of Treas. Reg. § 1.183-2(b) to hold that the activity was not engaged in with the intent to make a profit: (1) the activity was not carried on in a business-like manner because the taxpayer (a) did not change the method of operation to make it profitable and (b) did not seek expert advice on how to make the business profitable; (2) the taxpayer had no expertise at operating a horse breeding business and did not obtain expert advice on operating the business; (3) the taxpayer did not present evidence that the horses would appreciate in value; (4) although the taxpayer was successful at manufacturing, there was no evidence that this ability was applied to horse breeding; (5) the business never made a profit; (6) the activity had substantial losses which did not occur from unforeseen circumstances; and (7) the losses offset income from other sources. **Filios v. Comm'r, T.C. Memo. 1999-92**.

In addition to regular employment, the taxpayer raised and bred Pomeranian dogs for four years. The court reviewed the factors of Treas. Reg. § 1.183-2(b) to hold that the activity was not engaged in with the intent to make a profit: (1) the taxpayer did not have a business plan; (2) did not maintain sufficient records to analyze the profit making capability of the activity; (3) only five of 28 dogs generated any income; (4) the taxpayer derived much personal pleasure from the activity; and (5) the activity produced no profitable years and had substantial tax losses. **Spranger v. Comm'r, T.C. Memo. 1999-93**.

INCENTIVE AWARDS. The taxpayer was a manufacturer. The taxpayer awarded prizes of trips worth more than $600 to dealers for successfully carrying a certain amount of the taxpayer's products in inventory. The individuals who took the trips could not compete in the taxpayer's incentive program. Only dealers could meet the criteria and be awarded prizes, and they were the recipients of the trips awarded by the taxpayer. Thus, each trip was a "prize or award" includible in the recipient dealer's gross income under I.R.C. § 74 and constituted a payment of fixed or determinable income under I.R.C. § 6041. However, the dealers which were corporations that received trip awards were not the kind of corporations payments to which were subject to the information reporting requirements of I.R.C. § 6041. The dealers, whether they were proprietorships, partnerships, or corporations, were subject to information reporting requirements when they designated the individuals who would take the trips. The IRS ruled that the taxpayer was required to file information returns under I.R.C. § 6041 for the trips it awarded to noncorporate dealers if the fair market value of a trip awarded was $600 or more in any taxable year. The IRS also ruled that the taxpayer was not required to file information returns with respect to the individuals designated by the dealers to take the trip. **Ltr. Rul. 9911053, Dec. 18, 1998**.

IRA-ROTH. The IRS has announced supplemental instructions for the proper completion of Form 8606, Nondeductible IRAs, for Roth IRA conversions and recharacterizations. The announcement also clarified the proper computation of the 10 percent additional tax for early distributions in the case of Roth IRA conversions and subsequent withdrawals from Roth IRA accounts. Finally, it corrects the computation of modified AGI for purposes of Roth IRAs on page 2 and the Ed IRA Contribution Worksheet on page 3 in the separate instructions for Form 8606. **Ann. 99-18, I.R.B. 1999-__, __**.

INTEREST RATE. The IRS has announced that, for the period April 1, 1999 through June 30, 1999, the interest rate paid on tax overpayments is 8 percent (7 percent in the case of a corporation) and for underpayments is 8 percent. The interest rate for underpayments by large corporations is 10 percent. The overpayment rate for the portion of a corporate overpayment exceeding $10,000 is 5.5 percent. **Rev. Rul. 99-16, I.R.B. 1999-__, __**.

INVOLUNTARY CONVERSIONS. The taxpayer had entered into timber cutting contracts with a federal agency. Congress enacted legislation which unilaterally changed provisions in the contracts, including the price paid for stumpage. The taxpayer sued the government for compensation and received a settlement. The taxpayer also exchanged the federal contracts for other contracts to cut timber on other land owned by related and unrelated parties. The IRS ruled that the legislation was an involuntary conversion of the timber contracts and that the exchange of the contracts was eligible for like-kind exchange treatment. **Ltr. Rul. 9911048, Dec. 15, 1998**.

LIKE-KIND EXCHANGES-*ALM* § 4.02[16].* The taxpayer owned a grantor trust which owned real property. The trust sold the property by transferring the sales contract to a

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qualified intermediary. The intermediary identified replacement property which was to be acquired with a loan. The lender required the title to be held by a "bankruptcy remote entity" so the trust formed an LLC which elected not to be taxed as a separate entity. The IRS ruled that the LLC would be disregarded for purposes of the like-kind exchange rules such that the trust would be treated as having acquired the replacement property. **Ltr. Rul. 9911033, Dec. 18, 1998**.

PENSION PLANS. For plans beginning in March 1999, the weighted average is 6.15 percent with the permissible range of 5.54 to 6.46 percent (90 to 106 percent permissible range) and 5.54 to 6.77 percent (90 to 110 percent permissible range) for purposes of determining the full funding limitation under I.R.C. § 412(c)(7). **Notice 99-15, I.R.B. 1999-12, 20**.

The taxpayer received a lump-sum distribution from a pension plan and rolled the distribution over to an IRA. However, because the taxpayer failed to file Form 4972 as required by Treas. Reg. § 1.402(e)(4)(B)-1, the court held that the rollover was not entitled to tax-free treatment. **Smith v. United States, 99-1 U.S. Tax Cas. (CCH) ¶ 50,357 (D. Md. 1999)**.

SAFE HARBOR INTEREST RATES
April 1999

	Annual	Semi-annual	Quarterly	Monthly
		Short-term		
AFR	4.99	4.93	4.90	4.88
110% AFR	5.49	5.42	5.38	5.35
120% AFR	6.01	5.92	5.88	5.85
		Mid-term		
AFR	5.28	5.21	5.18	5.15
110% AFR	5.81	5.73	5.69	5.66
120% AFR	6.35	6.25	6.20	6.17
		Long-term		
AFR	5.67	5.59	5.55	5.53
110% AFR	6.24	6.15	6.10	6.07
120% AFR	6.82	6.71	6.65	6.62

PROPERTY

FRAUDULENT TRANSFER. The plaintiff purchased a ranch with a partnership as tenants in common. The ranch incurred financial difficulty and the partnership asked the plaintiff to execute a quitclaim deed to the partnership of the plaintiff's interest so that the partnership could obtain a loan. The deed was not supposed to be recorded but the partnership did so without the plaintiff's permission or knowledge. The partnership then sold the ranch to a third party. The plaintiff sought to set aside the transfer and to recover the plaintiff's interest in the ranch. The court held that the third parties received an absolute conveyance of the property according to recorded documents and were bona fide purchasers for value and without notice; therefore, the transfer could not be set aside. The court noted that the plaintiff took on the risk of the loss when the plaintiff executed a document which transferred the plaintiff's interest without reservation. **Vanderwerf v. Kirwan, 586 N.W.2d 858 (S.D. 1998)**.

SECURED TRANSACTIONS

ATTACHMENT. The defendant was the spouse of a cattle buyer who had established a corporation in the defendant's name to purchase cattle because the spouse could not make the purchases. The cattle were purchased on an account of third parties and sold to the defendant's corporation. That corporation then resold the cattle. The defendant's corporation had a security agreement with the plaintiff for all livestock. The spouse purchased many cattle without reimbursing the sellers or the third party buyers. The sellers and third party buyers argued that the plaintiff's security interest did not attach to the cattle because the defendant was merely a front for the spouse who was the real owner and manager of the corporation. The court found that the defendant had a substantial involvement in the financial operation of the corporation and was sufficiently aware of the transactions to be considered a bona fide officer of the corporation; therefore, the defendant had sufficient rights in the cattle for the security interest of the plaintiff to attach to the cattle. The court rejected the seller's and third party's argument that the plaintiff was estopped from claiming a security interest because of the wrong-doing of the spouse and the defendant. The court found that the seller and third party had not taken any steps to protect themselves, even after notice that the spouse was not making payments for the cattle; therefore, the seller and third party could not invoke the doctrine of equitable estoppel to defeat the plaintiff's security interest. **Continental Grain Co. v. Brandenburg, 587 N.W.2d 196 (S.D. 1998)**.

STATE REGULATION OF AGRICULTURE

LIVESTOCK CONFINEMENT FACILITIES. The defendant counties had passed ordinances regulating the location of concentrated livestock facilities. The plaintiff wanted to construct a livestock confinement facility on the plaintiff's land which would violate the ordinances. The plaintiff alleged that the ordinances were preempted by state law and regulations of the Mississippi Department of Environmental Quality. The regulations involved the distances between concentrated livestock facilities and adjacent property. The defendant sought a preliminary injunction against enforcement of the ordinances pending trial. The court granted the injunction, holding that the defendants were likely to prevail on the preemption issue and on the claims that the ordinances violated substantive due process in that the distance requirements were unduly oppressive. **Prestage Farms v. Bd. of Supervisors of Noxubee Co., 23 F. Supp.3d 663 (N.D. Miss. 1998)**.

CITATION UPDATES

***In re* Scott Cable Comm., Inc., 227 B.R. 596 (Bankr. D. Conn. 1998)** (bankruptcy administrative expenses), see p. 43 *supra*.

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In the next issue: Information about the date and location of the Seminar in Paradise

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