taxpayer is a member of a family with ties to farming[25] (which certainly does not apply to a corporation).

The court's view that a corporation could have a principal occupation of farming meant that Golden Rod could be a "qualified farm-related taxpayer" and could, therefore, sidestep the rules on farming syndicates. Thus, the prepaid expenses were deductible in the year paid, 1987, rather than in the next year when used.

The decision opens up the statute and its exceptions to bona fide farm operations regardless of how organized.

FOOTNOTES

1 See generally, 4 Harl, *Agricultural Law* § 28.05[5] (1997); Harl, *Agricultural Law Manual* § 4.03[8] (1997).
2 4 Harl, *supra* n. 1, § 28.05[5] [b].
3 Rev. Rul. 79-229, 1979-2 C.B. 210; Rev. Rul. 75-152, 1975-1 C.B. 144, superseded by Rev. Rul. 79-229, 1979-2 C.B. 210.
4 1979-2 C.B. 210.
5 Rev. Rul. 79-229, 1979-2 C.B. 210.
6 I.R.C. § 464(a).
7 I.R.C. § 464(c)(1).
8 Prop. Treas. Reg. § 1.464-2(a)(1). See Estate of Wallace v. Comm'r, 95 T.C. 525 (1990), *aff'd*, 965 F.2d 1038 (11th Cir. 1992) (medical doctor who owned cattle-feeding business was limited entrepreneur who did not actively participate in cattle feeding business and profit motive was irrelevant; only feed actually consumed during year deductible).
9 I.R.C. § 464(f)(4)(A), added by Pub. L. 99-514, Sec. 404(a), 100 Stat. 2223 (1986).
10 I.R.C. § 464(f)(4)(A), (B).
11 I.R.C. § 464(f)(4)(A).
12 *Id*.
13 I.R.C. § 464(f)(2)(B).
14 I.R.C. § 464(f)(2)(C).
15 I.R.C. § 464(f)(3)(A)(ii).
16 I.R.C. § 464(f)(3)(A)(i).
17 I.R.C. § 464(f)(3)(A).
18 I.R.C. § 464(f)(3)(B)(i).
19 I.R.C. § 464(f)(3)(B)(ii).
20 I.R.C. § 464(f)(3)(B)(iii).
21 I.R.C. §§ 464(f)(3)(B), 464(f)(3)(A).
22 97-2 U.S.T.C. ¶ 50,507 (11th Cir. 1997).
23 I.R.C. § 464(f)(3)(B)(ii). See n. 19 *supra*.
24 I.R.C. § 464(f)(3)(B)(i). See n. 18 *supra*.
25 I.R.C. § 464(f)(3)(B)(iii). See n. 20 *supra*.

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

BANKRUPTCY

Chapter 11-*ALM* § 13.03.*

ELIGIBILITY. The debtor, a tomato farmer, filed a previous Chapter 11 case and had achieved a confirmed plan. The debtor, under the plan, executed a new note on a loan secured by the farm land and made a few payments to other creditors before defaulting on plan payments. The case was voluntarily dismissed by the debtor. Another creditor obtained a judgment against the debtor, the current crop of tomatoes failed, and the land mortgagee was about to foreclose when the debtor filed the current Chapter 11 case. The mortgagee argued that the new filing was not allowed because the debtor had substantially consummated the previous plan. The court held that the execution of the new note and some payments to creditors did not amount to substantial consummation of the plan. In addition, the court held that the debtor had sufficient change in circumstances after the dismissal of the first case to file the second, especially where there was no other evidence of bad faith in filing the second case. The court noted that the debtor had little chance of presenting a confirmable plan, but held that the debtor should at least have the chance to try. ***In re* Woodson, 213 B.R. 404 (Bankr. M.D. Fla. 1997)**.

Chapter 12-*ALM* § 13.03[8].*

PLAN. The debtors had purchased a cattle ranch on installments and filed for bankruptcy after defaulting on one of the annual payments. The debtors had owned the ranch for only one year so the court looked to the historical business performance of the ranch under the previous owners as well as during the time of the debtors' ownership. The debtors' plan was attacked by creditors as not feasible because the income projections exceeded the historical income from the property and the plan required negative amortization of the real property installment contract. The court reviewed the Bankruptcy Court's ruling that the plan was feasible and held that the ruling was not clearly erroneous. The court noted that, although the ranch did not have historical income to fund the plan, the debtors were experienced ranchers and had instituted several management improvements which could increase income from the ranch. The court also held that the lower court's ruling was supported by evidence that cattle prices would improve. Further, the court held that the negative amortization of the real property installment contract for two years was allowed. The court examined the plan under the ten factors enumerated in *Great Western Bank v. Sierra Woods Group, 953 F.2d 1174 (9th Cir. 1992)*. The court found that the debtors had 30 percent equity in the property, the plan was feasible, and the creditors were adequately protected during those years if the plan income did not exceed historical income. ***In re* Nauman, 213 B.R. 355 (Bankr. 9th Cir. 1997)**.

FEDERAL TAXATION-*ALM* § 13.03[7].*

CLAIM. The IRS filed a timely claim for $5,000 in 1994 corporate income taxes, and FICA and FUTA taxes. The claim included language that the claim was an estimate because of a continuing investigation. The IRS later withdrew the entire claim, although the IRS had not made a final determination as to the income taxes. Thirteen months after the claims bar date, the IRS concluded an audit of the debtor and filed new claims for over $350,000 in taxes for 1993 and 1994. The debtor agreed to allow reinstatement of the $5,000 income tax claim but argued that the remainder of the new claim was time barred. The court held that the tax claim for 1993 was barred because it was a new claim since it involved a tax year different from the original claim. The court also barred the 1994 tax claim because 13 months had passed after the claims bar date, allowance of the claim would prejudice other creditors who relied on the IRS withdrawal of the original claim and the IRS failed to seek a continuance of the claims bar date even though the IRS had a continuing audit of the debtor's taxes. ***In re* Limited Gaming of America, Inc., 213 B.R. 369 (Bankr. N.D. Okla. 1997)**.

DEBTOR-IN-POSSESSION. The debtor filed for Chapter 11 for the debtor's sole proprietorship manufacturing business. The debtor operated the business as debtor-in-possession and incurred employment taxes for wages earned pre-petition and post-petition. For the pre-petition wages, the taxes were due post-petition. The debtor argued that, because the taxes were all due post-petition, the debtor was not personally liable for the taxes. The court held that taxes on pre-petition wages were incurred when the wages were paid, not when the tax payment was due. However, the court held that the post-petition taxes due on wages paid post-petition were the obligation of the debtor-in-possession and the bankruptcy estate and were not the personal liability of the debtor. **Bellus v. U.S., 125 F.3d 821 (9th Cir. 1997), *aff'g in part and rev'g in part,* 198 B.R. 792 (N.D. Calif. 1996)**.

DISCHARGE. The U.S. Supreme Court has denied certiorari in the following case. The debtor first filed a Chapter 13 case in 1988 which was eventually dismissed in 1991. Three months later, the debtor filed for Chapter 7 and received a discharge. The debtor had timely filed a return for 1987 taxes but without payment of those taxes. The debtor argued that the 1987 taxes were discharged in the Chapter 7 case because the return was timely filed more than three years before the petition. The IRS argued that the three year period of Section 507(a)(8)(A)(i) was tolled during the previous bankruptcy filing. The court agreed with the IRS and the majority of reported cases that the three year period was tolled. ***In re* Waugh, 109 F.3d 489 (8th Cir. 1997), *cert. denied*, 118 S. Ct. 80 (1997)**.

FEDERAL AGRICULTURAL PROGRAMS

BRUCELLOSIS. The APHIS has adopted as final regulations changing the classification of Kentucky from a Class A to Class Free state. **62 Fed. Reg. 65596 (Dec. 15, 1997)**.

CROP INSURANCE-*ALM* § 13.04.* The FCIC has adopted as final regulations which include the Hybrid Sorghum Seed Endorsement in the Common Crop Insurance Policy and restrict the endorsement provisions to 1997 and earlier crop years. **62 Fed. Reg. 65313 (Dec. 12, 1997)**.

The FCIC has adopted as final regulations which include the Potato Endorsement in the Common Crop Insurance Policy and restrict the endorsement provisions to 1997 and earlier crop years for counties in which the Northern Potato Crop Provisions will be used and to the 1998 and prior crop years in all other states. **62 Fed. Reg. 65321 (Dec. 12, 1997)**.

The FCIC has adopted as final regulations which amend the Sweet Corn Endorsement in the Common Crop Insurance Policy and restrict the endorsement provisions to 1997 and earlier crop years. **62 Fed. Reg. 65338 (Dec. 12, 1997)**.

The FCIC has adopted as final regulations which include the Dry Peas Endorsement in the Common Crop Insurance Policy and restrict the endorsement provisions to 1997 and earlier crop years. **62 Fed. Reg. 65741 (Dec. 16, 1997)**.

The FCIC has adopted as final regulations which include the Canola and Rapeseed Endorsement as a permanent provision in the Common Crop Insurance Policy. **62 Fed. Reg. 65991 (Dec. 17, 1997)**.

FARM CREDIT ADMINISTRATION. The FCA has issued a direct final rule amending its regulations concerning interest rates and charges. The FCA stated that the action was consistent with the FCA's continuing efforts to reduce regulatory burden and unnecessary prior approval requirements whenever possible. The amendments eliminate the prior approval requirement for changes in interest rate policies at banks for cooperatives (BCs), eliminate unnecessary or duplicative regulatory requirements and clarify existing requirements that are retained. The effect of the amendments is to enable BCs to revise rate policies for discounting negotiable paper without prior FCA approval, to eliminate the requirement that fees charged by an association are subject to bank approval, and to clarify that, in all Farm Credit System banks and direct lender institutions, the board of directors is responsible for setting interest rates and annually reviewing interest rate plans in conjunction with the review and approval of the institution's annual business plan. **62 Fed. Reg. 66816 (Dec. 22, 1997)**.

GRAIN STANDARDS. The Federal Grain Inspection Service of the Grain Inspection, Packers and Stockyards Administration has issued proposed regulations revising the United States Standards for Rye to certificate dockage to the nearest tenth of a percent. The current method of dockage certification rounds the actual dockage percentage down to the nearest whole percent. This method may result in understating the level of dockage up to 0.99 percent on the certificate. The FGIS noted that identification of dockage to the nearest tenth of a percent was more precise than the current method and should enhance the marketability of U.S. rye traded in the domestic and export markets. This change would also require the establishment of new inspection tolerances or breakpoints, as appropriate. **62 Fed. Reg. 66036 (Dec. 17, 1997)**.

ORGANIC FARMING. The Agricultural Marketing Service has issued proposed regulations which establish a National Organic Program (NOP). The program is proposed under the Organic Foods Production Act of 1990 (OFPA), which requires the establishment of national standards governing the marketing of certain agricultural products as organically produced to facilitate commerce in fresh and processed food that is organically produced and to assure consumers that such products meet consistent standards. This program would establish national standards for the organic production and handling of agricultural products, which would include a national list of synthetic substances approved for use in the production and handling of organically produced products. It also would establish an accreditation program for state officials and private persons who want to be accredited to certify farm, wild crop harvesting, and handling operations that comply with the program's requirements, and a certification program for farm, wild crop harvesting, and handling operations that want to be certified as meeting the program's requirements. The program additionally would include labeling requirements for organic products and products containing organic ingredients, and enforcement provisions. Further, the proposed rule provides for the approval of state organic programs and the importation into the United States of organic agricultural products from foreign programs determined to have equivalent requirements. **62 Fed. Reg. 65849 (Dec. 16, 1997), adding 7 C.F.R. Part 205.**.

PSEUDORABIES. The APHIS has issued proposed regulations amending the pseudorabies regulations by adding the glycoprotein I Particle Concentration Fluorescence Immunoassay test to the list of official pseudorabies tests and allowing its use as an approved differential test. The proposed regulations are based on a finding that the sensitivity and specificity of the glycoprotein I Particle Concentration Fluorescence Immunoassay test are equivalent to those of official tests for the diagnosis of pseudorabies. The proposed change would allow the glycoprotein I Particle Concentration Fluorescence Immunoassay test to be used as an official pseudorabies test to qualify certain pseudorabies vaccinated swine for interstate movement to destinations other than slaughter or a quarantined herd or quarantined feedlot. The addition of the glycoprotein I Particle Concentration Fluorescence Immunoassay test to the list of official pseudorabies tests also allows its use for the testing of nonvaccinated swine. **62 Fed. Reg. 65630 (Dec. 15, 1997)**.

VACCINE. See summary under Product Liability *infra*. **Symens v. Smithkline Beecham Corp., Civ. 94-1036 (D. S.D. Oct. 7, 1997)**.

FEDERAL ESTATE AND GIFT TAX

DISCLAIMERS-*ALM* § 5.02[6].* The IRS has adopted as final regulations concerning the requirement that a qualified disclaimer occur within nine months after creation of the interest disclaimed. The IRS noted in the comments, that in *United States v. Irvine, 981 F.2d 991 (8th Cir. 1992), rev'd on another point, 114 S. Ct. 1473 (1994)*, a disclaimer of a pre-gift tax transfer was not subject to the nine-month rule because no taxable transfer had occurred. The regulations provide that the nine-month rule applies to inter vivos or testamentary transfers, whether or not any gift or estate tax is imposed on the transfer. The same applies to interests passing as a result of an exercise, release or lapse of a general power of appointment, whether or not the event is subject to gift or estate tax. The regulations clarify this rule by changing the prior regulations use of the term “taxable transfer” to the statutory term “transfer creating the interest.” **Treas. Reg. §§ 20.2041-3(d)(6); 20.2046-1(a); 20.2056(d)-2(a),(b); 25.2511-1(c); 25.2514-3(c); 25.2518-1; 25.2518-2(c)(3)**.

The IRS also noted that the regulations governing the disclaimer of a survivorship interest in joint tenancy property were held invalid in several cases (see, e.g., *Kennedy v. Commissioner, 804 F.2d 1332 (7th Cir. 1986)*). The amendments revise the regulations to provide that a surviving joint tenant may disclaim the one-half survivorship interest in property held in joint tenancy with right of survivorship within 9 months of the death of the first joint tenant to die, even if the surviving joint tenant provided some or all of the consideration for the creation of the tenancy. The proposed regulations had provided that the rule did not apply to unseverable tenancies (tenancies by the entirety) but that rule was removed in the final regulations. **Treas. Reg. § 25.2518-2(c)(4)**.

The regulations provide that the 9-month period for making the qualified disclaimer commences on the death of the first joint tenant of a jointly held bank account, brokerage account or mutual fund. The regulations also clarify that a surviving joint tenant cannot disclaim any portion of the account attributable to that survivor's contribution to the account. Further, the regulations clarify that this rule applies even if only one-half of the property is included in the decedent's gross estate under I.R.C. § 2040(b) because the joint tenants are married. **Treas. Reg. § 25.2518-2(c)(4)(iv)**.

The regulations also clarify the estate tax treatment of a disclaimed interest in a joint bank account. State law generally deems a disclaimant to have predeceased the decedent with respect to the disclaimed interest. The disclaimed interest in a joint bank account (the creation of which is treated as an incomplete gift under the gift tax law), would lose its character as joint property and pass through the decedent's probate estate. Accordingly, under such circumstances, the interest disclaimed is subject to inclusion in the decedent's gross estate under I.R.C. § 2033, rather than I.R.C. § 2040(a) (providing for inclusion based on the contribution of each tenant) or I.R.C. § 2040(b) (providing for inclusion of one-half the property in the case of certain joint tenancies between spouses). The balance of the account not subject to the disclaimer retains its character as joint property and is includible in the decedent's gross estate under either I.R.C. § 2040(a) or I.R.C. § 2040(b). **Treas. Reg. § 25.2518-2(c)(5), Examples 13, 14, 15**. **62 Fed. Reg. 68183 (Dec. 31, 1997)**. Dr. Harl will publish an article on these regulations in the next issue of the *Digest*.

PRESENT INTEREST. The taxpayer donated limited partnership interests to children and grandchildren. The general partner of the partnership was a corporation controlled by the taxpayer. The partnership agreement gave the general partner the power to retain partnership income “for any reason whatever” and prohibited the sale or assignment of limited partnership interests without the consent of the general partner. The IRS ruled that the limited

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partnership interests were not present interests which qualified for the annual exclusion. **Ltr. Rul. 9751003, Aug. 28, 1997**.

VALUATION. The taxpayer established an irrevocable trust for two of the taxpayer's children and funded the trust with stock. The remainder of the stock was given to or acquired by a third child. The taxpayer was a co-trustee with an independent third party, but both trustees were directors of the corporation. The trust prevented the co-trustees from disposing of trust principal at less than fair market value; however, the co-trustees and the third child as directors caused the corporation to recapitalize and exchange the common stock held by the trust for lower value preferred stock. The exchange was made without permission from a court and without the knowledge of the trust beneficiaries, who were minors. The court first held that the exchange was a violation of the co-trustees' duty to the beneficiaries and created a constructive trust in favor of the beneficiaries.; therefore, the value of the beneficiaries' ownership interest in the corporation could include the value of the constructive trust interest. The Tax Court had used a subsequent sale of the stock as determining the value of the stock for gift tax purposes at the time of the exchange. The appellate court held that, because there was no finding that the subsequent sale was not foreseeable or compelled at the time of the exchange, the subsequent sale could not be used to value the stock at the time of the exchange. **Saltzman v. Comm'r, 97-2 U.S. Tax Cas. (CCH) ¶ 60,295 (2d Cir. 1997**.

The IRS has adopted as final regulations permitting the reformation of a personal residence trust or a qualified personal residence trust in order to comply with the applicable requirements for such trusts. *The regulations also provide that the trust governing instruments must prohibit the sale of a residence held in the trust to the grantor, the grantor's spouse or an entity controlled by the grantor or the grantor's spouse.* The regulations allow the disposition of the residence upon the termination of the trust to a grantor trust for the original grantor or the grantor's spouse or directly to the grantor's spouse. **62 Fed. Reg. 66987 (Dec. 23, 1997)**.

FEDERAL INCOME TAXATION

CASUALTY LOSS. The taxpayer purchases agricultural land with the intent to develop the land as residential properties. The land was zoned for agricultural use only and the taxpayer planned to seek rezoning of the land in order to develop the land. In 1989, much of the land was ruled to be wetlands under the Clean Water Act and the taxpayer was required to obtain a permit from the U.S. Corps of Engineers. The taxpayer claimed a loss based on the denial of a rezoning request and the designation of the land as wetlands. The court held that no casualty or other loss deduction was allowed because no definable event occurred which caused a loss of the property and because the taxpayer did not abandon the property. The court noted that the taxpayer did not argue that there was any partial regulatory taking, there was no condemnation by a governmental unit and there was no involuntary conversion of the property. The court also noted that the mere diminution of property value was not sufficient to give rise to a deductible loss. **Lakewood Associates v. Comm'r, 109 T.C. No. 21 (1997)**.

CORPORATIONS-*ALM* § 7.02[3][c].*

SMALL BUSINESS STOCK. The IRS has adopted as final regulations which permit a corporation to redeem a de minimis amount of small business stock without violating the anti-evasion rules of I.R.C. § 1202(c). The rules also allow redemptions which are unlikely to result in evasion of the original issue requirement, such as redemptions upon termination of the shareholder's employment or upon the shareholder's death, disability or mental incompetency. The rules allow redemptions where the shareholder sells stock to an employee. **62 Fed. Reg. 68165 (Dec. 31, 1997)**.

COST SHARING PAYMENTS. The IRS has ruled that cost-share payments received under the Wetlands Reserve Program, Environmental Quality Incentives Program and the Wildlife Habitat Incentives Program are eligible for exclusion from gross income under I.R.C. § 126. **Rev. Rul. 97-55, I.R.B. 1997-__, __**.

DEMOLITION. I.R.C. § 280B requires any costs or losses incurred on account of the demolition of any structure to be capitalized into the land upon which the demolished structure was located. The IRS has adopted as final regulations defining what ``structure'' means for purposes of Section 280B. The regulations define the term ``structure'' for purposes of Section 280B as a building and its structural components as those terms are defined in Treas. Reg. § 1.48-1(e). Thus, under section 280B, a structure will include only a building and its structural components and not other inherently permanent structures such as oil and gas storage tanks, blast furnaces, and coke ovens. **62 Fed. Reg. 67725 (Dec. 30, 1997)**.

DISCHARGE OF INDEBTEDNESS. The taxpayers were partners in a partnership which had discharge of indebtedness income from a renegotiation of a loan. The taxpayers did not include their share of the discharge of indebtedness income because the taxpayers claimed they were insolvent at the time of the discharge. The taxpayers included in their personal debts a guarantee of the partnership debt. However, the court found that at the time of the discharge, it was more likely than not that the taxpayers would not have to pay on the guarantee. Therefore, the court held that the guarantee was not includible in the taxpayers' debts since the guarantee was only a contingent debt. **Merkel v. Comm'r, 109 T.C. No. 22 (1997)**.

HOBBY LOSSES. The taxpayers were employed full-time as a secretary and framing contractor. The taxpayers lived on a one acre rural parcel of land neighboring two acres owned by one of the taxpayer's parents. The taxpayers used the two acres for training and raising race horses. The court stated that the standard was whether the taxpayers' "primary" motive in the business was profit. The court then reviewed the factors of Treas. Reg. § 1.183-2(b): (1) the taxpayers maintained accurate and separate books for the business but did not develop a pre-operation business plan based on expert advice nor did they seek a new business plan when the business produced nothing but losses; (2) the taxpayers had some experience at raising horses and sought professional advice; (3) the taxpayers devoted only spare time to the business; (4) the expected appreciation of the horses was not sufficient to offset the losses accumulated over the 16 years of operation; (5) the business had only annual losses over the entire 16 years of existence; (6) although the taxpayers did not have significant income from other sources, the business losses did offset much of the income; (7) the court found that the taxpayers' principal purpose in the activity was their personal pleasure in attending horse races, betting on their horses, and watching their horses race. The court held that the taxpayers did not operate the business primarily for profit. **Taras v. Comm'r, T.C. Memo. 1997-553**.

INTEREST. The taxpayers, husband and wife, purchased a residence through the husband's brother. The brother obtained the title and mortgage loan because the taxpayers could not qualify for the loan, but the taxpayers made all payments on the loan. The brother testified that the brother would hold the taxpayers liable if any payments were not made. The brother issued a quitclaim deed to the taxpayers but the deed was not recorded. The court held that, because the taxpayers held the equitable and beneficial interests in the property, the taxpayers could deduct the interest paid on the loan as qualified personal residence interest. **Uslu v. Comm'r, T.C. Memo. 1997-551**.

LODGING. The taxpayer was hired as a headmistress of a school and was required to live within a short distance from the school. The taxpayer received compensation for the lodging and acquired lodging not on the school premises. The taxpayer was required to be near the school to respond to emergencies and was required to use her residence for school social functions but not for teaching or administrative duties. The IRS ruled that the compensation received for the residence was includible in income because (1) the lodging was not furnished in-kind by the employer, the lodging was not on the employer's premises and was not required for employment. **Ltr. Rul. 9801023, Sept. 30, 1997**.

MILEAGE DEDUCTION. The standard mileage rate for 1998 is 32.5 cents per mile for business use, 14 cents per mile for charitable use and 10 cents per mile for medical and moving expense purposes. **Rev. Proc. 97-58, I.R.B. 1997-__**.

PENALTIES. The IRS has issued revised guidance for disclosure on returns required to avoid the understatement of tax penalty, the understatement of tax component of the accuracy-related penalty, and the return preparer penalty. **Rev. Proc. 97-56, I.R.B. 1997-__, __, updating Rev. Proc. 96-58, 1996-2 C.B. 390**.

PENSION PLANS. The IRS has announced amendments to proposed regulations under I.R.C. § 3121(v)(2), relating to when amounts deferred under or paid from certain nonqualified deferred compensation plans are taken into account as ``wages'' for purposes of the taxes imposed by the Federal Insurance Contributions Act (FICA). The amendments extend the proposed general effective date of the regulations to January 1, 1998. The extension also applies to the proposed regulations under I.R.C. § 3306(r)(2), relating to when amounts deferred under or paid from certain nonqualified deferred compensation plans are taken into account as ``wages'' for purposes of the taxes imposed by the Federal Unemployment Tax Act, due to the cross-reference therein to the provisions of the proposed regulations under section 3121(v)(2). **62 Fed. Reg 67304 (Dec. 24, 1997)**.

The IRS has issued guidance concerning the simplified method for determining the tax-free and taxable portions of certain annuity payments made from qualified plans under I.R.C. § 401(a), employee annuities under I.R.C. § 403(a), and annuity contracts under I.R.C. § 403(b). The rules apply to annuities with starting dates after Nov. 18, 1996. **Notice 98-2, I.R.B. 1998-__, __**.

QUALIFIED DEBT INSTRUMENTS. The IRS has announced the 1998 inflation adjusted amounts of debt instruments which qualify for the 9 percent discount rate limitation under I.R.C. §§ 483 and 1274:

Year of Sale or Exchange	1274A(b) Amount	1274A(c)(2)(A) Amount
1998	$3,823,100	$2,730,800

The $3,723,800 figure is the dividing line for 1998 below which (in terms of seller financing) the minimum interest rate is the lesser of 9 percent or the Applicable Federal Rate. Where the amount of seller financing exceeds the $3,823,100 figure, the imputed rate is 100 percent of the AFR except in cases of sale-leaseback transactions, where the imputed rate is 110 percent of AFR. If the amount of seller financing is $2,730,800 or less (for 1998), both parties may elect to account for the interest under the cash method of accounting. **Rev. Rul. 97-56, I.R.B. 1997-__, _**.

RESEARCH AND DEVELOPMENT EXPENSES. The taxpayers were members of partnerships formed for the purpose of investing in possible jojoba growing businesses. The partnerships were on the accrual method of accounting. Near the end of a tax year, the partnerships entered into contract with a corporation for the investigation of whether it would be feasible to grow jojoba plants in a certain area in Arizona. The corporation was controlled by members of the partnership who did not have experience in agricultural research. The farms attempted to grow jojoba in the area but conducted no scientific tests or evaluation of the growing attempts. The court found that the corporation was formed in order to characterize investments in the partnership as research expenses which were actually contributions used to develop the farm land. **Utah Jojoba 1 Research v. Comm'r, T.C. Memo. 1997-504**.

RETURNS. The IRS has issued changes in the procedures for participants in the Form 1040 ELF Program. **Rev. Proc. 97-60, I.R.B. 1997-__**.

The IRS has issued changes in the procedures for participants in the On-Line Filing Program. **Rev. Proc. 97-61, I.R.B. 1997-__**.

S CORPORATIONS-*ALM* § 7.02[3][c].*

ELECTION. The taxpayers filed an S corporation election Form 2553, apparently with traced or forged signatures. The IRS claimed that the signatures did not appear to be forged and were authorized by the shareholders.

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The court denied summary judgment for the taxpayers because an issue of fact remained as to whether the forged signatures were authorized by the shareholders. **Johnson v. Comm'r, T.C. Memo. 1997-558**.

SAFE HARBOR INTEREST RATES
January 1998

	Annual	Semi-annual	Quarterly	Monthly
		Short-term		
AFR	5.70	5.62	5.58	5.56
110% AFR	6.28	6.18	6.13	6.10
120% AFR	6.85	6.74	6.68	6.65
		Mid-term		
AFR	5.93	5.84	5.80	5.77
110% AFR	6.52	6.42	6.37	6.34
120% AFR	7.13	7.01	6.95	6.91
		Long-term		
AFR	6.13	6.04	6.00	5.97
110% AFR	6.75	6.64	6.59	6.55
120% AFR	7.38	7.25	7.19	7.14

SELF-EMPLOYMENT INCOME. The taxpayer owned interests in three separate farming operations: a sole proprietorship in which the taxpayer actively participated, a general partnership interest in which the taxpayer did not actively participate, and a S corporation interest in which the taxpayer did not actively participate. The sole proprietorship and S corporation had net income for the tax year involved but the partnership had current and carryover net passive activity losses. The taxpayer had a total net passive activity loss for the tax year involved. The IRS ruled that the current allowed net passive activity losses would be included in determining self-employment income and that the allowed carryover net passive activity losses would also be included in determining self-employment income. However, the IRS ruled that the inclusion was limited to the losses attributable to tax deductions otherwise includible in determining self-employment income. **Ltr. Rul. 9750001, Aug. 15, 1997**.

TAX RATES. The standard deductions for 1998 are $7,100 for joint filers, $6,250 for heads of households, $4,250 for single filers and $3,550 for married individuals who file separately. The personal exemption is $2,700. The income limit for the maximum earned income tax credit is $4,460 for taxpayers with no children, $6,680 for taxpayers with one child, and $9,390 for taxpayers with two or more children. The IRS also announced the inflation adjusted tax tables and other inflation adjusted figures for 1998. **Rev. Proc. 97-57, I.R.B. 1997-__, __**.

PRODUCT LIABILITY

VACCINE. The plaintiffs operated a feedlot and vaccinated their cattle with a vaccine manufactured by the defendant. The plaintiffs alleged that the vaccine was defective and failed to prevent the cattle from contracting disease which caused weight loss and death in their cattle and cattle owned by others in the feedlot. The plaintiffs brought actions for breach of implied warranties of fitness for a particular purpose and merchantabilty, failure to warn about foreseeable dangers, and supplying false information to the USDA in application for a vaccine license. The defendant argued that all of the claims were preempted by the regulations promulgated under the Virus-Serum-Toxin Act, 21 U.S.C. §§ 151-159. The court held that the statute contained no specific preemption provision and that only the regulations attempt to preempt state regulation of vaccines. The court also held that the regulations have no provisions specifically preempting state court tort actions. Instead, the court found that the regulations specifically prohibit vaccines from disclaiming merchantability, fitness for the purpose offered or manufacturer responsibility for the product. The court refused to allow broad preemption by the regulations where the statute did not contain any preemption provision and held that the plaintiffs' causes of action were not preempted by the regulations or statute. **Symens v. Smithkline Beecham Corp., Civ. 94-1036 (D. S.D. Oct. 7, 1997)**.

SECURED TRANSACTIONS

PERFECTION BY POSSESSION. The debtor had granted a bank a security interest in all present and after-acquired inventory. The debtor had subsequently purchased an interest in cattle held by a feedlot business. The agreement provided that the feedlot retained a security interest in the cattle to secure the cost of purchasing the cattle. The feedlot did not file a financing statement but the cattle never left the feedlot. After the debtor filed for bankruptcy, the trustee sought a determination as to the priority of the security interests as to the cattle in the possession of the feedlot. Under Kan. U.C.C. § 9-312(3), a purchase money security interest has priority over prior security interests if the purchase money security interest is perfected when the debtor receives possession of the collateral and the holder of the purchase money security interest notifies the other security interest holder within five years before the debtor receives possession of the collateral. The court held that because the debtor never had possession of the collateral and the purchase money security interest was perfected by possession of the purchase money security interest holder, notification of the other security interest holder was not necessary to perfect the purchase money security interest. The bank also argued that the cattle were not in the possession of the feedlot for perfection purposes but for their feed and care; therefore the possession exception did not apply. The court held that the cattle were held under the agreement which stated that the cattle were security for the price of the cattle; therefore, one of the purposes of the possession was for security for the cost of the cattle. The court noted that the facts also indicated that the debtor may not have acquired enough rights in the cattle for the bank's security interest to attach, since the debtor did not have sufficient control over the care or selling of the cattle. The appellate court affirmed except that it held that the debtor had sufficient interest in the cattle for the banlk's security interest to attach. **Kunkel v. Sprague Nat'l Bank, 128 F.3d 636 (8th Cir. 1997), *aff'g*, 198 B.R. 734 (D. Minn. 1996)**.

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