ADDITIONAL GUIDANCE ON THE 30 PERCENT DEPRECIATION ALLOWANCE  
— by Neil E. Harl

The legislation signed into law on March 9, 2002, the Job Creation and Worker Assistance Act of 2002, contained a highly important provision for farm and ranch (and other) taxpayers—an additional depreciation allowance of 30 percent of the adjusted income tax basis of qualifying property. In late April, the Internal Revenue Service issued needed guidance on how the depreciation allowance can be claimed and what should be done if the taxpayer does not wish to claim the 30 percent allowance.

General rules

Under Rev. Proc. 2002-33, the recently-issued guidance, a taxpayer may make an election to not deduct the 30 percent depreciation allowance. In the event that election is made (not to claim the 30 percent amount), the property is subject to AMT depreciation adjustments for its depreciation life. It is important to note that if an election is not made to not deduct the 30 percent depreciation allowance, it is assumed the 30 percent amount is claimed. Thus, the 30 percent amount is considered “allowed” or “allowable.”

In general, an election not to deduct the 30 percent depreciation allowance must be made by the due date (including extensions) of the federal income tax return for the year property is placed in service. An automatic extension of six months from the due date of the return (excluding extensions) is allowed for the election not to deduct the 30 percent depreciation amount if the return was timely filed.

Taxpayers who did not claim the allowance on the 2001 return—and want to claim the amount

Under the statute, for property to be eligible for the 30 percent allowance, the assets had to be acquired after September 10, 2001 (with no written contract to acquire the property before September 11, 2001) and before September 11, 2004, and placed in service before January 1, 2005 (except for certain property with longer production periods). That means many farm and ranch taxpayers had filed their 2001 returns before the statute was signed into law.

So how can taxpayers make the election to claim the 30 percent allowance for 2001? The recent guidance states that if an income tax return was filed before June 1, 2002, and did not claim the additional 30 percent depreciation allowance, if the taxpayer wishes to claim the depreciation amount, the taxpayer can either—

• File an amended return on or before the due date (excluding extensions) of the return for the next succeeding taxable year (that would be the due date for the 2002 return in

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most instances), in which case the amended return is to include the statement, “Filed Pursuant to Rev. Proc. 2002-33” at the top of the amended return, or

- File a Form 3115, Application for Change in Accounting Method, with the taxpayer’s federal tax return for the next succeeding taxable year (again, that would be the 2002 return in most instances). In that case, the Form 3115 is to be filed in accordance with the automatic change in method of accounting. The Form 3115 should include the statement, “Automatic ChangeFiled under Rev. Proc. 2002-33.” The deduction is claimed entirely in the year of change.

**Taxpayers who did not claim the allowance on the 2001 return and do not want to claim the amount**

For returns filed before June 1, 2002, the guidance states that the election not to deduct the 30 percent depreciation amount is considered made if—

- the taxpayer made the election by the due date of the return or within the six-months extension as required by the Form 4562 instructions (the Form 4562 instructions require a statement indicating the class of property for which the taxpayer is electing not to deduct the 30 percent depreciation allowance), or

- made the election by the due date of the return or within the six-month extension and attached a statement to the effect that the taxpayer is not deducting the 30 percent depreciation. A “deemed election” applies if the taxpayer did not claim the 30 percent depreciation deduction on the return and does not file an amended return to claim the 30 percent depreciation allowance.

Therefore, for returns filed before June 1, 2002, the taxpayer need do nothing if—(1) the 30 percent allowance was not claimed and (2) the taxpayer does not want to claim the amount.

**Returns filed on or after June 1, 2002**

For returns filed on or after June 1, 2002, taxpayers wanting to claim the 30 percent allowance do so on Form 4562. For taxpayers not wanting to claim the 30 percent depreciation deduction, an election must be made not to deduct the depreciation as required by the Form 4562 instructions (attach a statement to the return indicating the class of property for which the taxpayer is electing not to deduct the 30 percent depreciation amount). If the original return is timely filed, a taxpayer apparently is allowed an automatic extension of six months from the original due date to make the election (not to deduct the 30 percent depreciation allowance).

Thus, for returns filed on or after June 1, 2002, the taxpayer must either—

- Claim the 30 percent depreciation allowance on Form 4562, or

- Attach a statement to the income tax return that the taxpayer is electing not to claim the 30 percent depreciation allowance.

**Revoking elections not to deduct**

An election not to deduct the 30 percent depreciation allowance for a class of property is revocable only with the consent of the Commissioner.

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**Final note**

Remember, the 30 percent depreciation allowance is claimed after expense method depreciation has been claimed.

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**FOOTNOTES**

4 I.R.B. 2002-__.
5 Id.
6 Id., Sec. 3.01.
7 Id., Sec. 3.05.
8 See, e.g., Jakobowski v. United States, 2001-2 U.S. Tax Cas. (CCH) ¶ 50,594 (10th Cir. 2001) (unclaimed depreciation (over 14-years) had to reduce basis; sale produced additional gain).
9 Rev. Proc. 2002-33, Sec. 3.03, I.R.B. 2002-__.
10 Id., Sec. 3.03(2)(a).
12 See n. 1 supra and accompanying text.
13 Rev. Proc. 2002-33, Sec. 4.01(1), I.R.B. 2002-__.
14 Id.
15 Id., Sec. 4.01(2).
17 Id.
19 Rev. Proc. 2002-33, Sec. 4.02(1), I.R.B. 2002-__.
20 Id., Sec. 4.02(2).
21 Id., Sec. 3.03(3)(a).
22 Treas. Reg. § 301.9100-2(b).
23 Rev. Proc. 2002-33, Sec. 3.04, I.R.B. 2002-__.
24 Joint Committee on Taxation, Technical Explanation of the Job Creation and Worker Assistance Act of 2002, JCX-12.02, Sec. 1 (2002).

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**FARM ESTATE & BUSINESS PLANNING**

**15th EDITION**

By Neil E. Harl

THE PARSONAGE EXCLUSION - FIRST AMENDMENT CONCERNS?
— by Roger A. McEown

Overview

On May 16, 2000, the United States Tax Court, in Warren v. Comm’r, held that the parsonage exclusion for a minister is the actual amount used to provide a home, not the fair market rental value of the home. The petitioner, a “minister of the gospel” with significant outside income, and his wife purchased a home in 1992 for $360,000. The fair market rental value of the home was $58,061 in 1993, $58,004 in 1994, and $59,479 in 1995. As compensation, the petitioner’s church paid the petitioner $77,663, $86,175 and $99,653 for the years 1993, 1994 and 1995, respectively. For some of the years in question, the entire amount of compensation was designated as a housing allowance and entirely excluded from the petitioner’s gross income.

The petitioner spent a total of $77,663 in 1993, $76,309 in 1994 and $84,278 in 1995 for home expenditures including the mortgage, utilities, furnishings, repairs, maintenance, taxes and insurance. Based on these expenditures, the petitioner excluded all of the 1993 compensation and reported $9,866 in 1994 and $19,654 in 1995. The IRS, in accordance with Rev. Rul. 71-280, determined that the petitioner’s exclusion was limited to the fair market rental value of the home and increased the petitioner’s gross income by the difference between the compensation paid and the fair market rental value of the home for 1993, 1994 and 1995.

The I.R.C. § 107 Issue

The issue facing the Tax Court was whether the exclusion from gross income provided by I.R.C. § 107 was limited, as the IRS asserted, to the fair rental value of the “parsonage.”

I.R.C. § 107 provides:

“In the case of a minister of the gospel, gross income does not include

1. the rental value of a home furnished to him as part of his compensation or
2. the rental allowance paid to him as part of his compensation, to the extent used by him to rent or provide a home.”

The Tax Court, disagreeing with the contention of the IRS that the Congress, in enacting I.R.C. § 107, intended to impose a rental value limit on the exclusion, ruled that the exclusion is the amount actually used to provide a home not limited by the fair market rental value of the home. The IRS interpreted the exclusion to be the lesser of the amount used to provide a home or the fair market rental value of the home, and argued that permitting a greater exclusion would be contrary to both the “rental” language in the Code and the legislative history of concern for equality among ministers. The Tax Court noted that although I.R.C. § 107(1) limits the exclusion to the rental value of a home furnished as part of a minister’s compensation, there is no mention of rental value in I.R.C. § 107(2) or the regulations. The dissent stressed that the majority opinion ignored the modifier “rental” in I.R.C. § 107(2). The dissent concluded that the Congress intended that the exclusion be correlated to rental value, and that the majority’s opinion placed ministers or churches utilizing I.R.C. § 107(2) rather than I.R.C. § 107(1) in a more favorable position. The IRS appealed the Tax Court’s opinion to the U.S. Circuit Court of Appeals for the Ninth Circuit.

The Constitutional Issue

At the Tax Court level, neither the IRS nor the Tax Court raised a constitutional question. Indeed, at the Tax Court level, the issue was framed solely as a matter of statutory construction – whether a clergyman receiving a cash housing allowance from a religious employer can exclude from gross income the full amount of the allowance spent on housing or can only exclude up to the rental value of the home. On appeal, however, the Ninth Circuit asked the parties whether either wanted to frame the issue in constitutional terms. Both the IRS and the petitioner declined, but the three-judge panel hearing the case, over strong dissent, ordered the parties to brief both the constitutionality of I.R.C. § 107(2) and the propriety of the court reaching the issue on its own initiative. The panel, in ordering the briefing of the constitutional issue, specifically mentioned as relevant to the constitutional status of I.R.C. § 107(2) the opinion of the United States Supreme Court in Texas Monthly, Inc. v. Bullock, which struck on Establishment Clause grounds a Texas sales tax exemption limited to religious literature. However, the court failed to cite a 1970 Supreme Court opinion that focused more on Free Exercise concerns and suggested that tax provisions like I.R.C. § 107 properly accommodate the autonomy of sectarian entities and persons. Briefs on the matter were due on May 3, 2002.

The primary concern of the Ninth Circuit panel seems to be that I.R.C. § 107 provides a more generous rule for exclusion of employer-provided housing for “ministers of the gospel” than is provided under I.R.C. § 119 for those in secular employment. Section 119 excludes from an employee’s income employer-provided lodging, but only if the lodging is on the employer’s premises, is provided for the employer’s “convenience,” is required as a condition of employment, and is furnished in-kind rather than through a cash allowance. Section 119 applies irrespective of whether the employer is a secular organization or a sectarian entity. Section 107, on the other hand, is limited to “ministers of the gospel.” In addition, I.R.C. § 107 contains no convenience-of-the-employer test, does not require that the excluded housing be located on the employer’s premise or be a condition of employment, and extends tax-free treatment to cash allowances. Thus, from a constitutional standpoint, the potentially controversial situations are those arrangements by which religious employers provide housing assistance to clergy that fail the I.R.C. § 119 tests for excludability, but satisfy the more lenient standard of I.R.C. § 107. That is the precise situation presented in Warren.

In the event the constitutional issue is addressed by the court, one possible view is that I.R.C. § 107 actually helps disentangle the government from sectarian affairs by not requiring the IRS to undertake the detailed analysis that would be necessary if the minister’s lodging were provided pursuant to I.R.C. § 119. That approach is consistent with the rationale of Walz and the

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dissent in *Texas Monthly*, and suggests that I.R.C. § 107 is constitutional. Conversely, another view is that tax benefits extended to religious institutions are constitutional only if they are provided equally to nonreligious activities in accordance with a secular purpose. Under this view, I.R.C. § 107 is not constitutional, but I.R.C. § 119 is not at risk because it has broad application and is not designed to assist religion.

**Possible Outcomes**

In the event that the Ninth Circuit decides to rule on the constitutional matter and finds I.R.C. § 107 unconstitutional, the opinion would only be binding within the jurisdiction of the Ninth Circuit. The case would then proceed to the United States Supreme Court where, given the present make-up of the Court, it is unlikely that the Court (if it agrees to hear the case) would find the provision unconstitutional.

Even if I.R.C. § 107 were ultimately held unconstitutional, religious employers would still be able to provide tax-free lodging to ministers pursuant to the more restrictive rules of I.R.C. § 119 – the lodging would have to be on the employer’s premises, be provided for the employer’s “convenience,” be required as a condition of employment, and be furnished in-kind rather than through a cash allowance. In that setting, the Congress would likely act to preserve the tax preference for ministers.

Of course, the Ninth Circuit could refrain from ruling on the constitutional issue, but reverse the Tax Court’s opinion with the exclusion being limited to the rental value of the “parsonage” - the historic IRS position.

**Congressional Reaction**

The *Warren* case and the possibility of a federal court holding I.R.C. section 107 unconstitutional have moved the Congress. On April 16, 2002, the House passed legislation that would amend I.R.C. section 107(2) to provide specifically that the parsonage allowance is limited to an amount that “does not exceed the fair rental value of the home, including furnishings and appurtenances such as a garage, plus the cost of utilities.”

A similar bill was introduced in the Senate on April 18, 2002 and cleared the Senate on May 2, 2002. Interestingly, neither the House nor Senate bills, if enacted into law, will have any effect on the *Warren* litigation and, thus, neither bill will prevent the Ninth Circuit from potentially addressing the constitutional issue. Both bills apply prospectively to tax years after 2001, and do no apply to 1993-1995, the years at issue in *Warren*.

**Final Point**

The *Warren* case would never have arisen had the petitioner followed the long-standing IRS position and claimed as a housing exclusion only the amount representing the rental value of the “parsonage.” Obviously, the petitioner drew the attention of the IRS by claiming (in some years) his entire compensation as a non-taxable housing allowance. The case certainly illustrates the perils of taking an overly aggressive position on the tax return.

It is true in agriculture and often true in tax law – pigs get slaughtered. Unwittingly, Rev. Warren (whose gross income for the years in issue placed him in the top two percent of all individual taxpayers in the United States and who can certainly provide his own housing without the benefit of I.R.C. § 107) may have taken all “ministers of the gospel” (many of whom desperately depend on the I.R.C. § 107 exclusion) to the tax slaughterhouse with him.

**FOOTNOTES**

3. *Id.*
4. *Id.*
5. *Id.*
6. *Id.*
7. *Id.*
8. *Id.*
10. *Id.* The court also appointed Prof. Erwin Chemerinsky of the University of Southern California Law School to act as amicus curiae and brief both the constitutional issue and whether the court has the authority to raise the issue on its own.
11. It is not possible for the court to find I.R.C. § 107(2) unconstitutional, and uphold the balance of the provision. Either all of I.R.C. § 107 is unconstitutional or the entire provision is constitutional.
13. *Id.* There was no majority opinion in *Texas Monthly*. Rather, a plurality of three justices held that the state sales tax exemption at issue was a religious subsidy that entangled the state with religion in determining the bounds of the exemption. Three justices wrote a dissenting opinion (authored by Scalia), and the three swing justices who made up the plurality opinion issued two separate concurring opinions.
15. 114 T.C. 343 (2000). An important point that should not be overlooked is that the Ninth Circuit, even as it raised the issue of the constitutionality of I.R.C. § 107(2), also expressed reservations about the propriety of a court considering an issue advanced by neither litigant and indicated that it may, after all, decline to resolve the constitutional controversy. Thus, the matter may be purely an academic exercise.
19. Of the justices that authored the plurality opinion in *Texas Monthly*, only Justice Stevens presently remains on the court. Justice O’Connor also remains on the Court and concurred in the plurality opinion. All three of the dissenting justices – Scalia, Rehnquist and Kennedy, remain on the Court.
21. See n. 1 supra.
22. H.R. 4156, the Clergy Housing Allowance Clarification Act of 2002. The legislation passed 408-0, and would apply to
taxable years beginning after December 31, 2001. The bill is estimated to raise $33 million in revenue over the next decade.


25 Id. Both bills provide that “notwithstanding any prior regulation, revenue ruling, or other guidance issued by the Internal Revenue Service, no person shall be subject to the limitations added... before January 1, 2002.” The most likely interpretation of that language is that it does not render the Warren litigation moot. Instead, the Ninth Circuit would have to interpret I.R.C. § 107 without the benefit of Rev. Rul. 71-280, but would not be precluded from reaching the same result.

26 114 T.C. 343 (2000).


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**CASES, REGULATIONS AND STATUTES**

**BANKRUPTCY**

**FEDERAL TAX-ALM § 13.03[7].**

**DISCHARGE.** The debtor had failed to file returns for 1983 through 1986. The IRS made assessments based on substitute returns it created. The debtor made two offers in compromise which were rejected because the debtor had not filed returns. The debtor eventually filed the returns, claiming less tax due than the amount assessed by the IRS. The debtor sought to discharge the taxes because the returns were filed more than three years before the bankruptcy petition was filed. The court held that the debtor’s returns did not qualify as tax returns under Section 523(a)(1)(B) because the IRS had already created substitute returns and made an assessment and the debtors’ returns were not an honest attempt by the debtor to comply with the filing requirements. In re Rushing, 273 B.R. 223 (Bankr. D. Ariz. 2001).

**NET OPERATING LOSSES.** The debtor owned two S corporations and filed for Chapter 11, with the stock passing to the bankruptcy estate. The corporations had net operating losses for the period between the start of its tax year and the date of the debtor’s bankruptcy petition. The debtor claimed the losses as net operating losses and carried the losses forward to post-bankruptcy tax years. The debtor did not elect to bifurcate the debtor’s tax year in which the petition was filed. In a Chief Counsel Advice letter, the IRS ruled that the debtor could not claim the net operating losses because the losses passed to the bankruptcy estate with the stock. The net operating losses would then be used to decrease the basis of the stock to the extent of discharge of indebtedness which occurred as part of the bankruptcy case. If any net operating losses remained after the basis reduction, they passed to the debtor. After the bankruptcy case closed, the lowered basis of the stock also passed on to the debtor. CCA Ltr. Rul. 200217003, Dec. 14, 2001.

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**FEDERAL AGRICULTURAL PROGRAMS**

**FOOT AND MOUTH DISEASE.** The APHIS has issued proposed regulations amending the indemnity provisions pertaining to the control and eradication of foot-and-mouth disease and other serious diseases, including both cooperative programs and extraordinary emergencies. 67 Fed. Reg. 21933 (May 1, 2002).

**KARNAL BUNT.** The APHIS has issued interim regulations amending the Karnal bunt regulations to prohibit grain grown in a regulated area from being used as seed outside the regulated areas. The interim regulations also remove the requirement that wheat seed, durum wheat seed, and triticate seed that originates within a regulated area be treated with a fungicide before it may be planted within a regulated area. 67 Fed. Reg. 21159 (April 30, 2002).

The APHIS has issued interim regulations amending the Karnal bunt regulations to provide compensation for certain growers and handlers of grain and seed affected by Karnal bunt who are not currently eligible for compensation, and for certain wheat grown outside the regulated area that was commingled with wheat grown in regulated areas in Texas. 67 Fed. Reg. 21561 (May 1, 2002).

**MIGRANT WORKERS.** The plaintiffs were migrant and seasonal agricultural laborers who resided in Texas. The plaintiffs were recruited in Texas by a Texas farm-labor contractor hired by the defendant, a New York dairy, for work in New York. The employment contracts contained a provision that jurisdiction over the contracts was in New York. The defendant argued that the Texas District Court lacked personal jurisdiction over the defendant who had no contacts with the state. The court held that the forum selection clause was unenforceable as contrary to the provisions of MSAWPA which prohibited the waiver of rights granted by MSAWPA. The court also held that the court had personal jurisdiction over the defendant because the defendant had “purposefully directed” its activities at the residents of Texas by hiring the Texas farm-labor contractor to hire residents of Texas.
CHARITABLE DEDUCTION. The taxpayer owned shares of stock which were not publicly traded on a stock exchange market. The stock was issued by a bank holding company and was bought and sold through privately arranged sales. The taxpayer transferred the stock to a nonprofit family foundation and claimed a charitable deduction based on the fair-market value of the stock as determined by a subsequent sale of the stock to another bank corporation. The court held that the taxpayer could claim a deduction only for the taxpayer’s basis in the stock because the stock was not qualified appreciated stock, under Treas. Reg. § 1.170A-13(c)(7)(xi)(A), since it was not readily available on an established securities market. The court also noted that the taxpayer failed to meet the substantiation requirements to demonstrate the appreciated value of the stock when transferred. Todd v. Comm’r, 118 T.C. No. 19 (2002).

FEDERAL ESTATE AND GIFT TAX

CLAIMS. The decedent was killed in an automobile accident in which the other driver was also killed and the other driver’s spouse and child were injured. The spouse and child filed a claim against the decedent’s estate for the damages and also filed a lawsuit for damages, claiming that the decedent was at least partially at fault for the accident. The estate eventually settled with the spouse and child but claimed a deduction in excess of the amount paid, based upon the estimated liability of the estate on the decedent’s death. In a Chief Counsel Advice letter, the IRS ruled that the deduction was limited to the actual amount of the payments because the claim was too contingent at the decedent’s death. CCA Ltr. Rul. 200217022, Jan. 17, 2002.

FEDERAL INCOME TAXATION

PESTICIDES. The Federal Insecticide, Fungicide and Rodenticide Act (FIFRA), 7 U.S.C. § 136d(a)(2), requires pesticide registrants to report “factual information regarding unreasonable adverse effects on the environment” of a registered pesticide. The EPA issued a regulation, 40 C.F.R. § 159.158(a), which requires that this reporting include opinions of a registrant’s employees and agents. The plaintiff challenged the regulation as beyond the authority provided by the statute. The court held that the regulation was valid and not unreasonable or contrary to law. American Crop Protection Ass’n v. EPA, 182 F. Supp. 2d 89 (D. D.C. 2002).

WETLANDS. The USDA has issued proposed regulations setting out certain categorical minimal effect exemptions under the wetland conservation provisions of the Food Security Act of 1985, as amended. This proposed rule identifies five wetland conversion activities, which due to the type of wetlands or other criteria, would only have a minimal effect upon wetland functions and values, and thus would not render a producer ineligible for certain USDA program benefits. The five conservation activities would be (1) removal of woody vegetation, including stumps, from natural herbaceous wetlands; (2) removal of scattered woody vegetation, including stumps; (3) installation of grassed waterways for erosion control on non-highly erodible croplands; (4) terrace construction for erosion control on erodible cropland; and (5) control or removal of exotic invasive woody species, including stumps. 67 Fed. Reg. 19699 (April 23, 2002).

GIFTS. The decedent’s predeceased spouse had made over $800,000 in payments to the spouse’s personal secretary. The decedent’s estate sought a refund of gift taxes paid on the transfers, arguing that the transfers were compensation rather than gifts. The court held that the payments were gifts because the spouse maintained a close personal relationship with the secretary, had made numerous gifts over the years and filed gift tax returns for the transfers. Lane v. Comm’r, 2002-1 U.S. Tax Cas. (CCH) ¶ 60,437 (4th Cir. 2002), aff’g on point sub nom., Estate of Powell v. Comm’r, 2001-2 U.S. Tax Cas. (CCH) ¶ 60,416 (W.D. Va. 2001).

VALUATION. The decedent owned a 50 percent interest in five partnerships which owned and operated public assistance housing. Under contracts with HUD, the partnerships received guaranteed rents and subsidies for renting to low income and elderly tenants. The other 50 percent interests were owned by the decedent’s son who participated in the management of the business. The partnership agreement provided for the sale of the decedent’s interests to the son for $10,000 each and the estate claimed that amount as the value of each of the decedent’s interests. The court disregarded the buyout agreement price as based on a testamentary purpose. The court valued the partnerships using the value of the partnership assets and expected income. The court allowed a discount for the decedent’s interests for a lack of marketability, but did not allow a discount for a minority interest because (1) the HUD contracts provided a guaranteed income to both partners, (2) the partnership agreement required an annual distribution of net income to the partners, and (3) the partnership agreement required a vote of at least 75 percent of the interests to make any changes to the partnership agreement or to liquidate the partnership. Estate of Godley v. Comm’r, 2002-1 U.S. Tax Cas. (CCH) ¶ 60,436 (4th Cir. 2002).
CORPORATIONS-ALM § 7.02.*  
DEDUCTIONS. The taxpayer corporation was sued by its shareholders for improper reporting of annual income and expenses. The taxpayer settled the lawsuit by agreeing to pay the shareholders in cash and stock. The IRS ruled that the settlement payment could be claimed as a current business expense deduction. Ltr. Rul. 200216013, Jan. 16, 2002.

COURT AWARDS AND SETTLEMENTS. The taxpayer was a plaintiff in a personal injury lawsuit and received a jury verdict for compensatory and punitive damages. The parties then entered a settlement agreement which did not allocate the funds received for the various types of awards. The court held that the settlement proceeds had to be allocated in the same ratio as the damages were allocated by the jury. In re Valencia, 2002-1 U.S. Tax Cas. (CCH) ¶ 50,388 (Bankr. D. N.M. 2002).

DISASTER PAYMENTS. On April 4, 2002, the president determined that certain areas in Kentucky were eligible for assistance under the Disaster Relief and Emergency Assistance Act, 42 U.S.C. § 5121, as a result of severe storms and flooding on March 17-24, 2002. FEMA-1407-DR. On April 5, 2002, the president determined that certain areas in Tennessee were eligible for assistance under the Act as a result of severe storms and flooding on March 15-20, 2002. FEMA-1408-DR. On April 2, 2002, the president determined that certain areas in Virginia were eligible for assistance under the Act as a result of severe storms and flooding on March 17-20, 2002. FEMA-1406-DR. Accordingly, a taxpayer who sustained a loss attributable to these disasters may deduct the loss on his or her 2001 federal income tax return.

HOME OFFICE. The IRS has published a new brochure, “Home-Based Business Tax Avoidance Schemes . . . At A Glance.” The schemes described in the document claim that by setting up a bogus home-based business, individual taxpayers can deduct most, or all, of their personal expenses as business expenses. The brochure includes some examples of personal expenses that are not deductible but are commonly claimed as business expenses in home-based business tax avoidance schemes. The brochure explains that no matter how convincing the claims that are found in marketing materials for these schemes may appear, nondeductible personal living expenses cannot be transformed into deductible business expenses. The tax code firmly establishes that a clear business purpose and profit motive must exist in order to generate and claim allowable business expenses. Taxpayers who claimed such deductions on a past tax return should file an amended return as soon as possible to limit possible interest and penalties on top of any taxes they might owe. Ann. 2002-48, I.R.B. 2002—.

IRA. In Rev. Proc. 2002-10, I.R.B. 2002-4, 401, the IRS provided guidance to users of its model individual retirement arrangements (IRAs), simplified employee pensions (SEPs) and SIMPLE IRA plans regarding the adoption of revised plans. According to those guidelines, existing model IRAs, SEPs and SIMPLE IRA plans, which do not reflect law changes made by the Economic Growth and Tax Relief Reconciliation Act of 2001 and required minimum distribution regulations, cannot be used to establish new IRAs, SEPs and SIMPLE IRAs after June 1, 2002. The IRS has extended the June 1 deadline to October 1, 2002. Accordingly, financial institutions can use existing model IRAs to establish new IRAs for customers through October 1. Similarly, employers can use existing model SEPs or SIMPLE IRA plans to establish such plans through that date. The deadlines by which revised model forms must be adopted under Rev. Proc. 2002-10 remain unchanged. Ann. 2002-49, I.R.B. 2002—.

PENSION PLANS. For plans beginning in May 2002, the weighted average is 5.69 percent with the permissible range of 5.12 to 5.82 percent (90 to 106 percent permissible range) and 5.12 to 6.25 percent (90 to 110 percent permissible range) for purposes of determining the full funding limitation under I.R.C. § 412(c)(7). Notice 2002-32, I.R.B. 2002—.


STATE TAXATION

VALUATION. The plaintiff owned a farm on which the plaintiff had operated a hog farrowing facility since 1990. In 1999 the plaintiff built a house on the property a short distance from the farrowing facility. The plaintiff spent $328,000 in constructing the house but the county assessor valued the house at $540,000 for property tax purposes. The plaintiff challenged the valuation because it did not consider the negative effect of the proximity to the farrowing facility and the remoteness of the house from any road. The court held that the “external depreciation” caused by the proximity of the house to the farrowing facility was a valid factor in determining the value of the house and that this factor could not be ignored simply because the plaintiff chose the location of the house. Livingston v. Board of Equalization, 640 N.W.2d 426 (Neb. Ct. App. 2002).
ZONING

By Roger A. McEowen

MORATORIUM. This case arose as part of Lake Tahoe preservation efforts brought by the Tahoe Regional Planning Agency, a land use and planning organization. The Agency imposed a moratorium on development in Lake Tahoe from 1981 to 1984 to give the Agency adequate time to revise its land use plan for the lake and basin, areas that were threatened by rapid growth and the associated impact from a growing population. Authorities were concerned about the buildup of algae in the lake, which obscured the clarity of the water. An association of property owners who wanted to build single-family homes near Lake Tahoe brought a takings claim. The U.S. District Court found that a taking had occurred, but the Ninth Circuit reversed. The U.S. Supreme Court agreed to hear the case, and rejected the plaintiff’s argument that Lucas v. South Carolina Coastal Council, 505 U.S. 1003 (1992) required a finding that the moratorium was a categorical taking. The court said that Lucas only required analysis of regulatory taking claims as a categorical taking in the unusual case where there is a total prohibition on the beneficial economical use of property. The court reasoned that moratoria are essential land-use development tools and that the time it takes for a decision to be made should be protected. In addition, the court stated that fairness and justice could not be served if categorical rules are applied to numerous normal delays. The Chief Justice dissented, joined by justices Thomas and Scalia, and pointed out that the distinction between temporary and permanent prohibitions is tenuous and that the takings in the case lasted almost six years. A separate dissent, authored by justice Thomas and joined by Scalia, argued that regulations prohibiting all productive uses of property are subject to Lucas’ per se rule, regardless of whether the property involved retains theoretical useful life and value if, and when, the “temporary” moratorium is lifted. Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency, No. 00-1167, 2002 U. S. LEXIS 3028 (U.S. Sup. Ct. Apr. 23, 2002), aff’d, 216, F.3d 764 (9th Cir. 2000).

IN THE NEWS

2002 FARM BILL. The US House of Representatives by a vote of 280 to 141 approved the 2002 farm bill on May 2, 2002, despite a late bid to kill the plan by lawmakers who said the plan would encourage overproduction, fail to close loopholes for big farms and violate world trade rules. “First and foremost, this farm bill provides for a strong safety net for our agricultural producers,” said Charlie Stenholm, the Agriculture Committee’s Ranking Member. The bill, which would boost spending on crop and dairy subsidies by $31.2 billion through 2007, now goes to the Senate for a vote and the President has indicated that he will sign the legislation. @agriculture Online (www.agriculture.com).

CITATION UPDATES

Bachler v. United States, 281 F.3d 1078 (9th Cir. 2002), rev’g, 2000-2 U.S. Tax Cas. (CCH) ¶ 60,390 (N.D. Calif. 2000) (generation skipping transfers) see p. 43 supra.

In re Young, 122 S. Ct. 1036 (2002), aff’g, 233 F.3d 56 (1st Cir. 2000) (discharge) see p. 43 supra.