South Dakota Amendment E Ruled Unconstitutional – Is There A Future For Legislative Involvement In Shaping The Structure Of Agriculture?
— by Roger A. McEowen* and Neil E. Harl**

In *South Dakota Farm Bureau, Inc. et. al v. Hazeltine*,¹ the U.S. Court of Appeals for the Eighth Circuit upheld the Federal District Court for the District of South Dakota and ruled the South Dakota anti-corporate farming law unconstitutional on “dormant commerce clause” grounds. The opinion is viewed as critical to the future viability of anti-corporate farming restrictions in other states² and, more generally, to the ability of state legislatures to shape the structure of agriculture within their borders.

**Ante-Corporate Farming Restrictions**

Presently, nine states prohibit corporations from engaging in agriculture to various degrees.² Recently, consolidation in almost every aspect of the farm economy has further threatened the continued viability of a vibrant, independently owned and widely dispersed farm production sector with the specter of being vertically integrated (largely through contractual arrangements) in the production, processing and marketing functions. Thus, as concentration of agricultural production has accelerated in recent years, legislatures in many of these same states have attempted to legislate protections for the economic autonomy of individual farmers and the environmental health and safety of both the rural and non-rural sectors.

**The South Dakota Provision**

The South Dakota restriction dates from 1974, and in 1998 South Dakota voters amended the state constitution (known as “Amendment E”) to prohibit corporations and syndicates from owning an interest in farmland (with numerous exceptions).⁴ Section 21 states: “[n]o corporation or syndicate may acquire, or otherwise obtain an interest, whether legal, beneficial, or otherwise, in any real estate used for farming in this state, or engage in farming.”

Section 22 exempts “family farm corporations” or “family farm syndicates” as follows: “a corporation or syndicate engaged in farming or the ownership of agricultural land, in which a majority of the partnership interests, shares, stock, or other ownership interests are held by members of a family or a trust created for the benefit of a member of that family. The term, family, means natural persons related to one another within the fourth degree of kinship according to civil law, or their spouses. At least one of the family members in a family farm corporation or syndicate shall reside on or be actively engaged in the day-to-day labor and management of the farm. Day-to-day

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labor and management shall require both daily or routine substantial physical exertion and administration.”

The plaintiffs, a collection of farm groups, South Dakota feedlots, public utilities and other farm organizations, challenged Amendment E on the basis that it would prevent the continuation of their existing farming enterprises unless those enterprises changed organizationally to come within a statutory exemption. Specifically, several of the plaintiffs feed livestock in their South Dakota feedlots under contracts with out-of-state firms and claimed that Amendment E would apply to their out-of-state contracting parties and hurt economically their South Dakota livestock feeding businesses.5

The “Dormant Commerce Clause”

The Commerce Clause of the U.S. Constitution (Article I, § 8, Clause 3) forbids discrimination against commerce, which repeatedly has been held to mean that states and localities may not discriminate against the transactions of out-of-state actors in interstate markets even when the Congress has not legislated on the subject.6 The overriding rationale of the commerce clause was to create and foster the development of a common market among the states and to eradicate internal trade barriers. Thus, a state may not enact rules or regulations requiring out-of-state commerce to be conducted according to the enacting state’s terms.7

Historically, dormant commerce clause analysis has attempted to balance national market principles with federalism, and was never intended to eliminate the state’s power to regulate local activity, even though it is incidentally related to interstate commerce.8 Indeed, if state action also involves an exercise of the state’s police power, the impact of the action on interstate commerce is largely ignored.9 Absent an exercise of a state’s police power, the courts evaluate dormant commerce clause claims under a two-tiered approach. If the state has been motivated by a discriminatory purpose, the state bears the burden to show that it is pursuing a legitimate purpose that cannot be achieved with a nondiscriminatory alternative.10 However, if the state regulates without a discriminatory purpose but with a legitimate purpose, the provision will be upheld unless the burden on interstate commerce is clearly excessive in relation to the benefits that the state derives from the regulation.11 In essence, a state may regulate transactions that occur within its borders,12 but not those that occur elsewhere.13

“Dormant Commerce Clause” Precedent in the Eighth Circuit

In Hampton Feedlot, et al. v. Nixon,14 the court upheld against a dormant commerce clause challenge provisions of the Missouri Livestock Marketing Law that the state legislature passed in 1999 preventing livestock packers that purchase livestock in Missouri from discriminating against producers in purchasing livestock except for reasons of quality, transportation costs or special delivery times.15 The law requires any differential pricing to be published.16 The trial court held the law to be unconstitutional, but the Eighth Circuit reversed. While the court noted that the Act closely resembled an earlier South Dakota law that had been found unconstitutional,17 the court noted that the Missouri provision did not eliminate any method of sale – it simply requires price disclosure. More importantly, however, the court noted that the Missouri statute, unlike the South Dakota provision, only regulates the sale of livestock sold in Missouri. As such, the extraterritorial reach that the court found fatal to the South Dakota statute was not present in the Missouri statute. The court reasoned that the statute was indifferent to livestock sales occurring outside Missouri and had no chilling effect on interstate commerce because packers could easily purchase livestock other than in Missouri to avoid the Missouri provision. The court also noted that the Missouri legislature had legitimate reasons for enacting a price discrimination statute, including preservation of the family farm and Missouri’s rural economy, and an improvement in the quality of livestock marketed in Missouri.18 Specifically, the court opined that the Missouri legislature had the authority to determine the course of its farming economy and that the legislation was a constitutional means of doing so.

The Hazeltine Court’s Rationale

In a discussion involving the issue of the plaintiffs’ standing, the court in Hazeltine cited an Ohio statute that charged out-of-state natural gas vendors at a higher sales tax rate than certain in-state vendors.19 The court reasoned that the South Dakota livestock feeders contracting with out-of-state firms that were not within an exemption under the South Dakota law were similarly disaffected because of the imminent loss of business if Amendment E were to be enforced. However, the court did not discuss the obvious difference between the Ohio statute and Amendment E. The Ohio statute treated out-of-state natural gas vendors differently from in-state vendors. Amendment E treats all businesses operating in South Dakota under the same set of rules, regardless of whether the business is a South Dakota business or an out-of-state enterprise.

Under the Hampton10 rationale, the test is whether Amendment E has an extraterritorial reach requiring business transactions conducted in states other than South Dakota to be governed in accordance with South Dakota law, not whether South Dakota businesses are financially injured because of business relations with companies not coming within an exemption to the law. While the court was addressing legal standing on this point, the court was also framing the dormant commerce clause issue. Unbelievably, the court did not even make a single reference to its prior opinion in Hampton Feedlot.21

The court also provided no analysis on the issue of what entity is actually performing farming operations under the contract feeding arrangements. If the South Dakota feeding operations are making the relevant production decisions under the contracts and are the ones rendering material participation, then it seems highly unlikely that the out-of-state contracting parties could be found to be engaged in farming in South Dakota in a manner that Amendment E prohibits.22 The court, again without discussing the matter, simply assumed that Amendment E would apply to the contract feeding situations in the case.23

Without any analysis of the actual language of Amendment E, the court determined that South Dakota voters had acted with a discriminatory purpose in enacting Amendment E. The court noted that the record contained a substantial amount of evidence on the point.24 The court also found relevant on the discrimination issue statements of drafters, as well as a statement of a co-chairman of the Amendment E promotional organization that Amendment E was motivated in part by the environmental problems caused by large-scale hog operations in other states.25 The court called this statement “blatant” discrimination.26 The court also found indirect evidence of discrimination in that the drafters and supporters of Amendment E had no evidence that a ban on corporate farming
would preserve family farms or protect the environment, and that no economic studies had been undertaken to determine the economic impact of “shutting out corporate entities from farming in South Dakota.”27 Because the court found that Amendment E was enacted with a discriminatory purpose, the state bore the burden to show that it had no other way to advance legitimate state interests. The court held that the state failed to meet its burden.

Implications of the Decision

If left standing, the Hazeltine court’s opinion raises serious concerns about the analysis of future dormant commerce clause cases in the Eighth Circuit, the doctrine of stare decisis, the theory of separation of powers and the ability of states to regulate business conduct within their borders.28 The court’s willingness to ignore its prior opinion in Hampton Feedlot29 and not evaluate the actual language of Amendment E on dormant commerce clause grounds poses difficulty for other states defending against either current or future challenges to anti-corporate farming laws.30 It would appear at this time, however, that the court is not favorably disposed to anti-corporate farming laws in general, and may also strike down other laws designed to deal with the structural conditions presently facing family farming and ranching operations. The court’s opinion represents a complete shift from its opinion in Hampton Feedlot,31 and the court appears to have adopted the modern economic theory of free trade as its framework for evaluating commerce clause cases involving state regulation of business activity.32 Unfortunately, the court failed to note that the types of production contract arrangements involved in the case have been used in other settings to provide vertically integrated firms with market power and to exclude producers from competitive market outlets for their products.33

It is hoped that the Eighth Circuit will reconsider its decision in Hazeltine and continue the judicial path laid down in Hampton Feedlot.34

FOOTNOTES


2 The opinion takes on even greater significance because many of the states with the major restrictions on corporate involvement in agriculture are located in the Eighth Circuit. See, e.g., Minn. Stat. § 500.24; Mo. Ann. Stat. Ch. 350; Neb. Const. Art. XII, § 1; Iowa Code § 9H; N.D. Cent. Code § 10-06-01.


5 Two of the plaintiffs feed cattle under contract with out of state firms, one plaintiff raises contract hogs and another raises contract lambs.

6 See, e.g., Dean Milk Co. v. Madison, 340 U.S. 349 (1951) (holding as unconstitutional a city ordinance prohibiting sale of milk in city unless bottled at approved plant within five miles of city); Hunt v. Washington State Apple Advertising Commission, 432 U.S. 333 (1977) (state statute requiring all closed containers of apples sold or shipped into state to bear “no grade other than applicable U.S. grade or standard” held unconstitutional discrimination against commerce).


8 See, e.g., Huron Cement Co. v. Detroit, 362 U.S. 440 (1960) (state legislation designed to maintain clean air constituted legitimate exercise of police power allowing state to act in many areas of interstate commerce).

9 Id. A strong argument can be made that Amendment E was also enacted according to the state’s police power to protect South Dakotans from adverse health and environmental effects of large-scale, vertically integrated livestock operations. In that event, the impact of the law on interstate commerce would be less of a concern.

10 See, e.g., Hughes v. Oklahoma, 441 U.S. 322 (1979). But, the plaintiff bears the initial burden of proving discriminatory purpose. Id.

11 See, e.g., Pike v. Bruce Church, Inc., 397 U.S. 137 (1970) (state law prohibiting interstate shipment of cantaloupes not packed in compact arrangements in closed containers, even though furthering legitimate state interest, held unconstitutional due to substantial burden on interstate commerce).

12 Milk Control Board v. Eisenberg Farm Products, 306 U.S. 346 (1936) (court upheld Pennsylvania price control statute as applied to purchasers of milk in Pennsylvania by a dealer who intended to ship all the milk out of state; Court stated that purpose of statute was “to reach a domestic situation” and that the activity regulated was “essentially local”).


14 249 F.3d 814 (8th Cir. 2001).


17 S.D. Codified Laws § 40-15B et. seq.

18 The court found persuasive the testimony of a witness for the state that by providing an incentive for packers to buy livestock on the basis of quality through the grade and yield method, producers would make better genetic decisions, raise better quality animals and earn a better price. The court also noted that, under the current system, larger producers receive premiums for their livestock, giving them an economic advantage over smaller farmers.

19 An Ohio manufacturing facility purchased nearly all of its natural gas from out-of-state suppliers subject to the higher sales
The plaintiffs operated a dairy farm and had purchased feed from the debtor under the recommendation of a nutritionist employed by the debtor. The plaintiff filed a lawsuit for damages to the cows resulting from improper formulation of the feed by the nutritionist. While the lawsuit was pending, the debtor filed for Chapter 11. There was some dispute as to whether the plaintiffs received proper notice of the bankruptcy proceedings, the issue would have remained as to whether Amendment E discriminated against these businesses by treating them in a more disadvantageous manner than in-state businesses.

For example, the court noted that the “pro” Amendment E statements compiled by the Attorney General informed voters that without passage of Amendment E, “[d]esperately needed profits will be skimmed out of local economies and into pockets of distant corporations,” and “Amendment E gives South Dakota the opportunity to decide whether control of our state’s agriculture should remain in the hands of family farmers and ranchers or fall into the grasp of a few, large corporations.” The court claimed that these statements were “brimming with protectionist rhetoric.” Why the court found statements of intent relevant to the discrimination issue without examining the content of the language of Amendment E is not explained.

However, state legislation designed to maintain clean air has been held to constitute a legitimate exercise of the state’s police power allowing the state to act in many areas of interstate commerce. See, e.g., Huron Cement Co. v. Detroit, 362 U.S. 440 (1960).

The court failed to mention the numerous exemptions under the South Dakota provision.

It is noted that South Dakota is expected to file a petition for rehearing with the court.

The state of Iowa presently has an appeal pending with the Eighth Circuit involving the state’s ban on packer ownership of livestock. Smithfield Foods, Inc. et. al. v. Miller, 241 F. Supp.2d 978 (S.D. Iowa 2003). Most of the states with major anti-corporate farming laws are located within the Eighth Circuit.

Indeed, the court cited H.P. Hood & Sons v. DuMond, 336 U.S. 525 (1949), where the Court stated that “the vision of the Framers was that every farmer . . . shall be encouraged to produce by the certainty that he will have free access to every market in the Nation.”

For a discussion of these issues see, McEowen, Carstensen and Harl, note 22 supra; Stumo and O’Brien, Antitrust Unfairness vs. Equitable Unfairness in Farmer/Meat Packer Relationships, 8 Drake J. of Ag. L. 91 (2003); and Carstensen, Concentration and the Destruction of Competition in Agricultural Markets: The Case for Change in Public Policy, 2000 Wis. L. Rev. 531 (2000).

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34 249 F.3d 814 (8th Cir. 2001).
share to the brother. The creditor sought to have the loan declared nondischargeable under Section 523(a)(6) for willful and malicious injury by the debtor to the creditor’s property and under Section 523(a)(2)(A) for obtaining the loan by false pretenses. The court held that the loan was not nondischargeable under Section 523(a)(6) because, although reckless in failing to properly distinguish corporate property from jointly owned property, the debtor’s actions were not malicious. The court also held that the loan was not nondischargeable under Section 523(a)(2)(A) because the debtor did not make any oral statements that misrepresented the true nature of the equipment ownership with the intent to deceive the creditor. In re Mau, 293 B.R. 919 (Bankr. C.D. Ill. 2003).

The debtor had granted a security interest in 100 cattle and two trailers for a loan from a creditor. The security agreement also required the debtor to use a specific auction to sell the cattle. Beginning nine days after the execution of the loan until the creditor obtained possession of the cattle after the bankruptcy petition, the debtor sold many of the cattle at other auctions and did not use the proceeds for the loan. The debtor claimed that the sales were made at other auctions in order to maximize the price received and the proceeds were used for the farm operation, including the feeding and care of the remaining cattle. The creditor sought a declaration that the loan was nondischargeable under Section 523(a)(6) for willful and malicious injury to the creditor’s property. The court held that, although the debtor’s actions were willful, the creditor failed to prove that the sales were made with a malicious intent to harm the creditor; therefore, the loan was not nondischargeable under Section 523(a)(6). In re Logue, 294 B.R. 59 (Bankr. 8th Cir. 2003).

FEDERAL TAX

DISCHARGE. The debtor did not file returns or pay taxes for 1993, 1994 and 1995. The IRS prepared substitute returns and issued a notice of deficiency and assessments based on those returns. The debtor received a discharge in a Chapter 7 case but the discharge order did not specifically mention the income taxes owed. When the IRS sought to levy on the debtor’s property for those taxes, the debtor sought a ruling that the taxes were discharged. The court held that the taxes were not discharged because the debtor did not timely file income tax returns and the substitute returns prepared by the IRS did not constitute returns for purposes of Section 523(a)(1)(B). Swanson v. Comm’r, 121 T.C. No. 7 (2003).

TAX REFUNDS. The debtor’s plan provided for payment of any federal income tax refunds directly to the Chapter 13 trustee and the trustee sought an order requiring the IRS to send the refunds directly to the trustee. The IRS objected on three grounds: (1) the refunds were not “projected disposable income,” (2) such an order would violate the Assignment of Claims Act, and (3) the order would place an unfair administrative burden on the IRS. The court held that, (1) because the debtor agreed to have the refunds included in the plan income, the refunds were included in disposable income; (2) the Assignment of Claims Act does not bar voluntary payments under bankruptcy plans; and (3) because income deduction orders in bankruptcy cases have proved to be essential in successful reorganizations, the benefit outweighed the burden on the IRS. The IRS was ordered to pay the refunds directly to the trustee. In re Knapp, 294 B.R. 334 (W.D. Wash. 2003), aff’g, 285 B.R. 480 (Bankr. W.D. Wash. 2002).

CONTRACTS

HEDGE-TO-ARRIVE CONTRACTS. The Chapter 12 debtor was a farmer who had entered into several hedge-to-arrive contracts which provided for delivery of grain but allowed the debtor to rollover the delivery of the grain to subsequent years. The contracts also contained clauses which required all disputes involving the contracts to be arbitrated under the National Grain and Feed Association arbitration rules. After the debtor defaulted on the contracts, the buyer obtained a state court judgment to enforce the arbitration provisions and the parties submitted the dispute to arbitration. The arbitration panel ruled that the hedge-to-arrive contracts were enforceable and not illegal off-exchange futures contracts because actual delivery of the grain was intended. The buyer filed a claim in the bankruptcy case based on the arbitration award. The debtor sought to challenge the claim on the basis that the arbitration award was improper because of industry bias of the arbitration panel and because the hedge-to-arrive contracts were illegal off-exchange futures contracts. The court held that the debtor failed to prove that the arbitration panel was biased or exceeded its authority and also upheld the panel’s ruling that the contracts were enforceable. A petition for rehearing was denied. In re Robinson, 330 F.3d 834 (6th Cir. 2003), denying rehearing for, 326 F.3d 767 (6th Cir. 2003), aff’g, 265 B.R. 722 (Bankr. 6th Cir. 2001).

FEDERAL AGRICULTURAL PROGRAMS

FEDERAL FARM LOANS. The FSA has issued proposed regulations revising the regulations governing the guaranteed farm loan program to allow guaranteed loans to be rescheduled with a balloon payment under certain circumstances. The proposed regulations also (1) allow low-risk subordinations to be approved by the appropriate agency personnel at the field level rather than the national office, (2) allow lenders to make debt installment payments in accordance with lien priorities, payment due dates and cash flow projections, (3) clarify that packager and consultant fees for servicing of guaranteed loans are not covered by the guarantee, and (4) clarify the amount a lender can bid at a foreclosure sale. 68 Fed. Reg. 49723 (Aug. 19, 2003).

SHARED APPRECIATION AGREEMENTS. The plaintiffs had entered into shared appreciation agreements with the USDA in exchange for a write-down of their federal farm loans. The plaintiffs did not sell or otherwise transfer their property during the agreements and claimed that the USDA county supervisors had told them that if the loan was not paid, the property was not
sold and the plaintiffs continued farming the land, nothing would be owed under the shared appreciation agreements. The District Court had held that the Agriculture Credit Act, 7 U.S.C. Sec. 2001(b)(4), unambiguously requires recapture of 50 percent of the appreciated value of the property securing the loan upon the expiration date of a shared appreciation agreement. The appellate court affirmed, holding that the plaintiffs’ action for a declaratory judgment asserting a different construction of the Act and the agreement was properly dismissed. Stahl v. USDA, 327 F.3d 697 (8th Cir. 2003), aff’d, 2002 U.S. Dist. LEXIS 9534 (D. N.D. 2002).

SUGAR BEETS. The CCC has adopted as final regulations implementing provisions of the Agricultural Assistance Act of 2003 related to the Sugar Beet Disaster Program. This program will assist sugar beet producers who suffered production losses for either the 2001 or 2002 crop year due to weather related disasters which resulted in the prevention of planting or the reduction of quantity or quality while the beets were in the field. 68 Fed. Reg. 49329 (Aug. 18, 2003).

### FEDERAL ESTATE AND GIFT TAXATION

**DISCLAIMER.** The taxpayer was a minor when the taxpayer’s parent died. The decedent’s will provided for bequests to the taxpayer and the taxpayer executed a written disclaimer of a portion of the bequests within nine months after reaching age 21 and before receiving any of the estate assets. The IRS ruled that the disclaimer was effective. Ltr. Rul. 200333023, May 8, 2003.

**UNIFIED CREDIT.** The taxpayer was the beneficiary of a QTIP marital trust established under a decedent spouse’s will. The marital trust was funded with stock in exchange for money from the decedent’s children. The taxpayer assigned the taxpayer’s entire interest in the trust to the children resulting in the stock being held in the names of the children and not by the trust. The assignment to the children was reported as gifts and a gift tax return was filed. The gifts used up the taxpayer’s unified credit. The taxpayer filed a lawsuit to negate the assignment of the stock as invalid under the spendthrift clause of the trust. A state court ruled that the assignments were null and void and the assets reverted back to the trust. The IRS ruled that the state court ruling complied with state law; therefore, the gift did not occur and the unified credit was restored to the taxpayer. Ltr. Rul. 200334020, May 13, 2003.

**VALUATION.** The decedent had won a state lottery and, as of the date of the decedent’s death, was eligible for 18 annual installment payments of the prize. Although the estate acknowledged that the remaining prize payments were included in the decedent’s estate, the estate argued that the installments should be valued under a fair market test. The IRS agreed that under standard fair market valuation, the value of the remaining installments would be highly discounted because of the restrictions on assignment of the annual installments. The Tax Court held that the installments were an annuity for federal estate tax purposes and had to be valued using the actuarial tables of I.R.C. § 7520. The appellate court reversed, holding that the second part of the holding was contrary to the holding of Estate of Shackleford v. United States, 262 F.3d 1028 (9th Cir. 2001), aff’d, 99-2 U.S. Tax Cas. (CCH) ¶ 60,356 (E.D. Cal. 1999). The appellate court held that the use of the valuation tables would produce an unrealistic and unreasonable result, given the restrictions on transfers or assignment of annual installments under the state lottery rules. Estate of Gribauskas v. Comm’r, 2003-2 U.S. Tax Cas. (CCH) ¶ 60,466 (2d Cir. 2003), rev’g and rem’g, 116 T.C. 142 (2001).

### FEDERAL INCOME TAXATION

**CORPORATIONS**

**ESTIMATED TAXES.** The IRS has issued a reminder that corporations making estimated tax payments are permitted to postpone payment of 25 percent of the September 15 estimated installment until October 1, 2003, notwithstanding I.R.C. § 6655, which imposes a penalty for nonpayment of estimated tax, pursuant to Section 501 of the Jobs and Growth Tax Relief Reconciliation Act of 2003 (P.L. 108-27). IR-2003-105.

**DEPRECIATION.** The taxpayer constructed and operated wind turbine electric generators (WTGs). The turbines had reached a state of service where (1) all necessary permits and licenses had been obtained; (2) the WTGs were synchronized to the power grid generating electricity for production of income; (3) the critical tests for the various components of the WTGs had been completed; (4) the WTGs were placed in the control of taxpayer by the building contractor; and (5) taxpayer had sold some electricity. However, a substation operated by a the taxpayer had to be upgraded in order for the full generating capacity of the WTGs to be used. The IRS ruled that the WTGs had been placed in service and were eligible for depreciation on the date the above factors had been established. Ltr. Rul. 200334031, May 19, 2003.

The taxpayer claimed a deduction for computer equipment purchased in one tax year; however, the taxpayer did not file Form 4562 to claim expense method depreciation, under I.R.C. § 179, for the computer equipment. The court held that, because the taxpayer did not make the Section 179 election for the computer equipment, the taxpayer was not entitled to a current
deduction for the cost of the computer equipment but had to 

EARNED INCOME CREDIT. The taxpayer had two 
children by a previous marriage. The divorce decree was not 
placed in evidence and there was no evidence of either parent’s 
right to custody of the children. The evidence of where the 
children lived during the tax year at issue was contradictory 
and the court held that the taxpayer failed to prove that the 
children lived with the taxpayer more than one-half of the tax 
year and was not entitled to claim the earned income tax credit 
2003-121.

HOME OFFICE. The taxpayer was self-employed as an 
interior designer and claimed a deduction for a portion of the 
rent paid by the taxpayer for an apartment which was also used 
as the taxpayer’s residence. The total of home office deductions 
exceeded the gross income from the interior design business 
and the IRS disallowed the portion of the expenses in excess of 
the income, as provided by I.R.C. § 280A(c)(5). The taxpayer 
argued that the Section 280A(c)(5) limitation did not apply to 
rent expense. The court disagreed, holding that the Section 
280A(c)(5) limitation applied to expenses associated with a 
residence and the taxpayer’s apartment was used by the taxpayer 
as a residence. The court noted that the amount of disallowed 
expense could be carried over to the next tax year. Visin v. 
Comm’r, T.C. Memo. 2003-246.

IRA. The taxpayer was a trust beneficiary of a trust which 
was funded by a decedent’s interest in an IRA. The beneficiary 
of the trust requested a distribution from the IRA to the taxpayer 
under the erroneous advice of a third party. The error was not 
discovered until more than 60 days after the distribution. The 
IRS ruled that the erroneous distribution could not be returned 
to the IRA and that the distribution was included in the taxpayer’s 

MILEAGE EXPENSES. The taxpayer claimed to operate a 
travel service and claimed mileage expenses for trips to pick up 
tickets for clients. The taxpayer had no written contemporaneous 
logs of the trips or other written records. The court disallowed 
the mileage deductions to the extent not approved by the IRS. 

OFFERS IN COMPROMISE. The IRS has released a 
revenue procedure that explains procedures for submission and 
processing of offers to compromise a tax liability. The procedures 
reflect changes to the law made by the IRS Restructuring and 
Reform Act of 1998 (P.L. 105-206). The revenue procedure 
applies to all offers to compromise a civil or criminal liability 
under I.R.C. § 7122, except for those offers submitted directly 
to the Office of Appeals. The procedures do not apply to offers 
to compromise a tax liability after a case involving a civil or 
criminal liability has been referred to the Department of Justice 
36.

The IRS has posted Form 656-A, Offer in Compromise 
Application Fee Instructions and Certification, to its website, 
The document is available at no charge and can be obtained (1) 
by calling the IRS’s toll-free telephone number, 1-800-TAX-
FORM (1-800-829-3676); (2) through FedWorld on the Internet; 
or (3) by directly accessing the Internal Revenue Information 
Services bulletin board at (703) 321-8020. The IRS has 
announced that, beginning November 1, 2003, it will charge a 
$150 application fee for the processing of many offers in 
compromise (OICs), in order to offset the cost of the service and 

PENSION PLANS. The taxpayer received distributions from 
two pension plans and did not include the amounts in taxable 
income. The taxpayer claimed that the amounts were transferred 
to IRAs but failed to provide sufficient evidence of the location 
of the funds. The court held that the funds were included in 
taxable income for lack of evidence of a qualifying rollover 

REVENUE RULINGS. The IRS has published a list of 
revenue rulings, revenue procedures, and notices that, although 
not specifically revoked or superseded, are obsolete. Rev. Rul. 

SAFE HARBOR INTEREST RATES

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<td>5.60</td>
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<tr>
<td>100 percent</td>
<td>6.11</td>
</tr>
<tr>
<td></td>
<td>5.95</td>
</tr>
</tbody>
</table>


SAVINGS BONDS. The taxpayer cashed two U.S. Savings 
Bonds but did not report the interest accrued on the bonds as 
tax income. The taxpayer claimed that the proceeds of the bonds 
were used to pay for education expenses but did not provide any 
documentation of the taxpayer’s education status or expenses 
during the tax year in which the bonds were cashed. The court 
held that, without such evidence, the interest was taxable income. 

CITATION UPDATES

Scott v. United States, 328 F.3d 132 (4th Cir. 2003), aff’g, 
2002-1 U.S. Tax Cas. (CCH) ¶ 50,364 (E.D. Va. 2002) (trusts) 
see p. 78 supra.
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