Agricultural Law Press
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Agricultural Law Digest

Volume 20, No. 23 December 4, 2009 ISSN 1051-2780

Warning to Grandparents and Others: Bankruptcy Filing by A Section 529 Account Owner Can Result in Loss of a Contribution Within Last 720 Days

-by Neil E. Harl*

A recent Bankruptcy Court decision[1] interpreting an amendment in the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act[2] has confirmed that the 2005 amendment poses a substantial risk where the account owner files bankruptcy within 720 days or less of contributions made to a Section 529 plan. Part or all of the contributions within that period became property of the bankruptcy estate (the debtor had a legal interest in the account as of the petition date) and the contributions are not fully excluded under 11 U.S.C. § 541(c)(2).[3] That poses a risk that many had not anticipated when contributions were made to the account.

What is a Section 529 Plan?

"Section 529 Plans" or "Section 529 Accounts" are tax advantaged plans developed to encourage saving for future college costs and were first authorized in 1996 in the Small Business Job Protection Act of 1996,[4] by providing that a qualified state tuition program is exempt from all federal income taxation except for unrelated business income tax of a charitable organization. Amendments since enactment have shaped the concept into a widely accepted vehicle for funding higher education expenses. Technically known as "qualified tuition program,"[5] the plans enable a person to purchase tuition credits or certificates on behalf of a designated beneficiary entitling the beneficiary to a waiver or payment of qualified higher education expenses (essentially pre-paid tuition plans)[6] or a college savings plan.[7]

The pre-paid tuition plans can be set up and maintained by a state or state agency or by educational institutions; the college savings plans must be set up and maintained by a state or state agency.[8] All 50 states and the District of Columbia sponsor at least one type of Section 529 plan. College savings plans typically permit an account holder to establish an account for a student or potential student (the beneficiary) for the purpose of paying the beneficiary's higher education expenses. The account holder can usually choose among several investment options for the contributions.[9] Withdrawals can generally be used at any college or university.

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Agricultural Law Digest is published by the Agricultural Law Press, P.O. Box 835, Brownsville, OR 97327 (ph 541-466-5544), bimonthly except June and December. Annual subscription $120 ($90 by e-mail). Copyright 2009 by Robert P. Achenbach, Jr. and Neil E. Harl. No part of this newsletter may be reproduced or transmitted in any form or by any means, electronic or mechanical, including photocopying, recording or by any information storage or retrieval system, without prior permission in writing from the publisher. http://www.agrilawpress.com Printed on recycled paper.

In re Bourguignon

In the 2009 Bankruptcy Court case, *In re Bourguignon*,[10] the debtor had set up a Section 529 plan for a daughter on March 10, 2009, and deposited $14,500 into the account. The debtor's mother later added $40,000 to the account. On March 27, 2009, just over two weeks after the Section 529 account was opened, the debtor filed a petition in Chapter 7 bankruptcy. The debtor's "Statement of Financial Affairs" disclosed a "529 college fund for children" as property owned by another person that debtor holds or controls." The debtor did not list the 529 account on Schedule B nor did the debtor claim an exemption for the account on Schedule C.[11]

The Bankruptcy Court found that the debtor had a legal interest in the account as of the petition date and that it was the property of the bankruptcy estate.[12] Moreover, the court found that the account was not excluded under 11 U.S.C. § 541(c)(2) which deals with restrictions on the transfer of a "beneficial interest under a trust." As the court pointed out, the debtor was not the "beneficiary" of the account; rather the debtor was the owner of the account.

The court then turned to the debtors' primary argument, that the account was excluded under 11 U.S.C. § 541(b)(6) which had been added in the 2005 amendments. That subsection states that property of the bankruptcy estate does not include --

> ". . . funds used to purchase a tuition credit or certificate or contributed to an account in accordance with section 529(a)(1)(A) of the Internal Revenue Code of 1986 under a qualified State tuition program (as defined in section 529(b)(1) of such Code) not later than 365 days before the date of the filing of the petition in a case under this title, but --
>
> "(A) only if the designated beneficiary of the amounts paid or contributed to such tuition program was a child, stepchild, grandchild, or stepgrandchild of the debtor for the taxable year for which the funds were paid or contributed;
>
> "(B) with respect to the aggregate amount paid or contributed to such program having the same designated beneficiary, only so much of such amount as does not exceed the total contributions permitted under section 529(b)(7) of such Code with respect to such beneficiary. . . ; and
>
> "(C) in the case of funds paid or contributed to such program having the same designated beneficiary not earlier than 720 days nor later than 365 days before such date, only so much of such funds as does not exceed $5,475."

The court concluded that the above language meant— (1) contributions to a Section 529 account more than 720 days prior to bankruptcy are fully excluded from property of the estate; (2) contributions made between 365 and 720 days prior to bankruptcy are excluded from property of the estate to the extent below $5,475; (3) contributions over $5,475 in that same time frame remain fully property of the estate and (4) amounts contributed within a year of bankruptcy filing are not excluded at all from being property of the bankruptcy estate. As the court concluded, it is only funds contributed more than 720 days before bankruptcy filing that are fully excluded from the bankruptcy estate without a monetary limit. As for the $40,000 contribution by the debtor's mother, the court held that was treated the same as the debtors' contribution -- the Bankruptcy Code makes no distinction based on the source of the contributions.[13]

ENDNOTES

[1] *In re* Bourguignon, 2009-2 U.S. Tax Cas. (CCH) ¶ 50,717 (Bankr. D. Idaho 2009).

[2] Pub. L. No. 109-8, 119 Stat. 23 (2005).

[3] *In re* Bourguignon, 2009-2 U.S. Tax Cas. (CCH) ¶ 50,717 (Bankr. D. Idaho 2009).

[4] Pub. L. 104-188, § 1806(c)(2), 110 Stat. 1755 (1996).

[5] I.R.C. § 529(b)(1).

[6] I.R.C. § 529(b)(1)(A)(i).

[7] I.R.C. § 529(b)(1)(A)(ii).

[8] I.R.C. § 529(b)(1).

[9] See Securities and Exchange Commission, "An Introduction to 529 Plans," http://sec.gov/investor/pubs/intro529.htm.

[10] 2009-2 U.S. Tax Cas. (CCH) ¶ 50,717 (Bankr. D. Idaho 2009).

[11] 11 U.S.C. § 521(c), added by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, requires debtors to "file with the court a record of any interest that a debtor has . . . under a qualified State tuition program" as defined in § 529(b)(1) of the Internal Revenue Code.

[12] *In re* Bourguignon, 2009-2 U.S. Tax Cas. (CCH) ¶ 50,717 (Bankr. D. Idaho 2009).

[13] *In re* Bourguignon, 2009-2 U.S. Tax Cas. (CCH) ¶ 50,717 (Bankr. D. Idaho 2009).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr

ADVERSE POSSESSION

BOUNDARY FENCE. The parties owned adjoining properties and disputed a portion of their boundary which was determined by a survey to be on the plaintiff's side of an old fence line. The original fence was constructed as part of a livestock corral but had not been used for some time. The plaintiff had used the property up to the fence to plant crops. The defendant argued that the fence did not qualify as a boundary fence because it was used as part of a limited livestock corral, was no longer used, and was obscured by a stand of trees. The trial court ruled that the fence was a boundary fence because it started at the proper property line, was mostly straight and was used to keep livestock. The appellate court affirmed, noting that the plaintiff had made continuous use of the disputed property to raise crops, treating the fence as the limit of the property. **Crosby v. Park, 2009 Mich. App. LEXIS 2411 (Mich. Ct. App. 2009)**.

FEDERAL FARM PROGRAMS

WHEAT. The GIPSA is reviewing the United States Standards for Wheat under the United States Grain Standards Act. The GIPSA stated that, since the standards were last revised, numerous changes have occurred in the breeding and production practices of wheat; the technology used to harvest, process, and test wheat; and also wheat marketing. To ensure that standards and official grading practices remain relevant, GIPSA has invited interested parties to comment on whether the current wheat standards and grading practices need to be changed. **74 Fed. Reg. 62257 (Nov. 27, 2009)**.

FEDERAL ESTATE AND GIFT TAXATION

ABATEMENT OF INTEREST AND PENALTIES. The decedent had obtained a deferral of recognition of gain from an involuntary sale of condemned property by purchasing similar property. The replacement property was sold and the decedent recognized gain just before the decedent passed away. The estate filed a tax return reporting the gain from the sale but did not pay any taxes. The IRS sent six letters requesting payment but no payment was made. The estate sold several real properties after obtaining a discharge of any estate tax lien and eventually paid the tax owed. The estate requested that the IRS abate the interest and penalties on the tax and the IRS abated the penalties but not the interest. The estate sued to have the IRS abate the penalties, arguing that the IRS caused the delay in payment of the taxes by not pursuing payment vigorously enough. The court noted that the IRS had sent six letters requesting payment of the taxes soon after the estate income tax return was filed. The court held that the IRS was not grossly unfair in failing to abate the interest on the taxes because the interest accrued primarily because of the delays caused by the estate. **Estate of Ball v. Comm'r, T.C. Memo. 2009-262**.

MARITAL DEDUCTION. The decedent's estate included a marital trust which passed to the surviving spouse and for which a reverse QTIP election was made. Subsequent to the filing of decedent's Form 706, Treas. Reg. § 26.2652-2(c) was issued which provided a transitional rule that allows certain trusts subject to a reverse QTIP election, to which GST exemption had been allocated, to be treated as two separate trusts, so that only a portion of the trust would be treated as subject to the reverse QTIP election, and that portion would be treated as having a zero inclusion ratio. The deadline for making the election set forth in the transitional rule was June 24, 1996. The IRS granted the estate an extension of time to file the election by completing the statement required in Treas. Reg. § 26.2652-2(c) and submitting the election, a copy of the return on which the reverse QTIP election was made under I.R.C. § 2652(a)(3), and a copy of the letter ruling, to the IRS. **Ltr. Rul. 200946027, Aug. 10, 2009**.

FEDERAL INCOME TAXATION

C CORPORATIONS

ACCOUNTING METHOD. The taxpayer was a U.S. corporation which wholly-owned a foreign partnership taxed as a corporation. The foreign corporation wanted to change the currency used to conduct transactions and the taxpayer filed Form 3115 with its Form 1120 but failed to send a signed copy to the IRS national office. The IRS granted an extension of time to file the signed copy of the From 3115. **Ltr. Rul. 200946031, Aug. 5, 2009**.

COOPERATIVES. The taxpayer was a rural electric cooperative. The taxpayer purchased an electric and natural gas distribution system from another utility. The taxpayer amended its bylaws to make all of the new electric and natural gas customers members of the cooperative. The IRS ruled that the new business was a like organization under I.R.C. § 501(c)(12)(A) and would

not terminate the taxpayer's status as a cooperative under I.R.C. § 501(c)(12). **Ltr. Rul. 200946057, Aug. 18, 2009**.

DISCHARGE OF INDEBTEDNESS. The taxpayer's residence was foreclosed upon and sold for less than the amount owed on the mortgage. The lender did not mail a confirmation of the foreclosure sale but only sent a notice to the taxpayer that the difference between the loan and the sale proceeds was forgiven. The taxpayer did not include the loan forgiveness amount in income. The taxpayer argued that the lender's failure to provide documentation of judicial confirmation of the foreclosure sale prohibited the lender from pursuing any deficiency; therefore, the lender could not have collected on the amount forgiven and therefore no discharge of indebtedness occurred. The court held that the failure of the lender to issue the confirmation of foreclosure was only part of the lender's decision not to pursue collection of the deficiency and still resulted in forgiveness of the deficiency amount. The forgiven deficiency was discharge of indebtedness to the taxpayer. ***In re* Godfrey, 2009-2 U.S. Tax Cas. (CCH) ¶ 50,754 (Bankr. N.D. Ga. 2009)**.

DEPRECIATION. The taxpayer was a partnership formed to purchase and develop four buildings, three of which were mixed commercial and residential rental properties and one was a garage. The four buildings were developed as a single complex. The IRS ruled that the four buildings could be treated as a single building for depreciation purposes as either residential or nonresidential real property. The IRS ruled that, if the properties qualified as a single nonresidential building, the partnership would be a qualified business for purposes of the new markets credit under I.R.C. § 45D(d)(3). **Ltr. Rul. 200947004, Aug. 14, 2009; Ltr. Rul. 200947005, Aug. 14, 2009**.

The taxpayer owned and operated a studio recording business. While the taxpayer was employed at another job, the taxpayer began purchasing equipment for the studio during 2002, 2003 and 2004 but only tested some of the equipment before fully assembling the studio in 2004. The taxpayer claimed depreciation deductions for the equipment on the taxpayer's 2004 tax return but the IRS disallowed the deduction because the equipment was placed in service in 2002 and 2003. The court held that the equipment was placed in service in 2004 because the studio could not be operated until all the equipment was connected together. **Brown v. Comm'r, T.C. Summary Op. 2009-171**.

DOMESTIC PRODUCTION DEDUCTION. The taxpayer was a farmer-owned agricultural cooperative. The cooperative made payments to members which were qualified per-unit retain allocations because they were (1) distributed with respect to the crops that the cooperative stored, processed and marketed for its patrons; (2) determined without reference to the cooperative's net earnings; and (3) paid pursuant to a contract with the patrons establishing the necessary pre-existing agreement and obligation, and within the payment period of I.R.C. § 1382(d). The IRS ruled that the cooperative was allowed to add back these amounts paid to members as net proceeds in calculating its qualified production activities income under I.R.C. § 199(d)(3)(C). **Ltr. Rul. 200946021, Aug. 12, 2009**.

The taxpayer was a corporation which produced a product from 1996 through 2004 and an improved version of the same product from 2005 through 2008. The taxpayer incurred direct and indirect costs that were includible in inventory costs under I.R.C. § 263A. Some of the costs incurred and capitalizable in the tax year were attributable to events that occurred prior to the effective date of I.R.C. § 199. Sales of the inventory items generated domestic production gross receipts (DGPR). The taxpayer sought a ruling as to whether Treas. Reg. § 1.199-4(b)(2)(ii)(B) required or permitted the taxpayer to allocate some of the pre-Section 199 cost of goods sold (CGS) to non-domestic production gross receipts. In a Chief Counsel Advice letter, the IRS ruled that I.R.C. § 1.199-4(b)(2)(ii)(B) does not require or permit taxpayers to allocate part of the CGS of an inventory item to non-DPGR when the gross receipts from the sale of that item are treated as DPGR. Because the costs at issue are properly capitalizable to current year's production pursuant to I.R.C. § 263A, they must be included in determining the CGS allocable to DPGR for the taxable year in which the costs are incurred, and allocated to DPGR using a "reasonable method" pursuant to Treas. Reg. § 1.199-4(b)(2)(i). Application of a reasonable method results in the entire amount of the costs at issue being allocated to DPGR. **CCA Ltr. Rul. 200946037, Oct. 26, 2009**.

EMPLOYEE EXPENSES. The taxpayer was employed as a veterinarian at an animal hospital and claimed employee business expenses. The taxpayer provided no written records to support the deductions claimed and no testimony as to the employer's requirement for any of the expenses. The deductions were denied as unsubstantiated. **Young v. Comm'r, T,C. Summary Op. 2009-173**.

ENERGY CREDIT. The taxpayer was a manufacturer of knitwear clothing which installed a rooftop photovoltaic solar generation system. The system included a reflective roof surface which directed sunlight to the solar generation system. The IRS ruled that the reflective surface was solar energy property, under Treas. Reg. § 1.48-9(d)(3), eligible for the energy credit under I.R.C. § 48. **Ltr. Rul. 200947027, Aug. 11, 2009**.

FIRST-TIME HOMEBUYER CREDIT. The IRS has issued a press release noting changes made to the First-Time Homebuyer Credit made by the Worker, Homeownership, and Business Assistance Act of 2009 (Pub. L. No. 111-92). Taxpayers who claim the credit on their 2009 returns will not be able to file electronically, but will have to file a paper return. An IRS video on YouTube discusses various rules related to the credit. http://www.youtube.com/watch?v=GkzB03uuGlg. **IR-2009-108**.

Here are the top 10 things the IRS wants you to know about the expanded credit and the qualifications you must meet in order to qualify for it.

- You must buy – or enter into a binding contract to buy a

principal residence – on or before April 30, 2010.

• If you enter into a binding contract by April 30, 2010 you must close on the home on or before June 30, 2010.

• For qualifying purchases in 2010, you will have the option of claiming the credit on either your 2009 or 2010 return.

• A long-time resident of the same home can now qualify for a reduced credit. You can qualify for the credit if you've lived in the same principal residence for any five-consecutive year period during the eight-year period that ended on the date the new home is purchased and the settlement date is after November 6, 2009.

• The maximum credit for long-time residents is $6,500. However, married individuals filing separately are limited to $3,250.

• People with higher incomes can now qualify for the credit. The new law raises the income limits for homes purchased after November 6, 2009. The full credit is available to taxpayers with modified adjusted gross incomes up to $125,000 or $225,000 for joint filers.

• The IRS will issue a December 2009 revision of Form 5405 to claim this credit. The December 2009 form must be used for homes purchased after November 6, 2009 – whether the credit is claimed for 2008 or for 2009 – and for all home purchases that are claimed on 2009 returns.

• No credit is available if the purchase price of the home exceeds $800,000.

• The purchaser must be at least 18 years old on the date of purchase. For a married couple, only one spouse must meet this age requirement.

• A dependent is not eligible to claim the credit.

For more information about the expanded First-Time Home Buyer Credit, see www.IRS.gov/recovery. See also Harl, "Worker, Homeownership, and Business Assistance Act of 2009," 20 *Agric. L. Dig.* 169 (2009).

IRA. In early 2004, the taxpayer received a Notice of Intent to Levy from the IRS which stated that the IRS intended to levy against any state tax refunds owed to the taxpayer. The taxpayer received an early distribution in 2004 which the taxpayer used to pay pre-2004 federal taxes and other debts and expenses. The taxpayer claimed the distribution as income but did not include any payment of the 10 percent additional tax for early distributions. The taxpayer argued that the exception in I.R.C. § 72(t)(2)(A)(vii) applied because the of the Notice of Levy filed in early 2004. The court held that the exception in I.R.C. § 72(t)(2)(A)(vii) did not apply because the Notice of Intent to Levy did not constitute a levy against the taxpayer's retirement account since there were administrative appeals and other procedures to occur before a levy would be made. In addition, the notice mentioned only that the levy would be against any state tax refunds and did not indicate any intent to levy against the taxpayer's retirement plan. **Willhite v. Comm'r, T.C. Memo. 2009-263**.

The taxpayer incurred substantial credit card and mortgage debt during a period of unemployment. After the taxpayer became employed again, the taxpayer withdrew funds from an IRA to pay off the credit card debt and for taxes. The taxpayer was 48 at the time of the withdrawal. The taxpayer also provided funds to a daughter who was attending college. The funds were not paid directly for college tuition but used for rent and personal expenses. The taxpayer reported the withdrawal as income but did not pay the 10 percent additional tax for early withdrawals. The taxpayer argued that the withdrawal should be excepted from the additional tax because of the taxpayer's unemployment and because of the higher education expenses exception. The court held that there was no exception for financial difficulties and allowed an exclusion for the higher education expenses equal to the amount of room and board charges included in the cost of the college education by the college. **Venet v. Comm'r, T.C. Memo. 2009-268**.

INFORMATION RETURNS. The IRS has created a pilot program allowing filers of information returns to truncate an individual payee's nine-digit identifying number on paper payee statements for calendar years 2009 and 2010 if the filers meet the requirements set forth in this notice. The IRS will treat a filer as having satisfied any requirement in Treasury and IRS guidance, whether in a regulation, form, or form instructions, to include a payee's identifying number on a payee statement if the following requirements are met: (1) the identifying number is a social security number, IRS individual taxpayer identification number, or IRS adoption taxpayer identification number; (2) the identifying number is truncated by replacing the first five digits of the nine-digit number with asterisks or Xs (for example, a social security number 123-45-6789 would appear on the paper payee statement as ***-**-6789 or XXX-XX-6789); and (3) the truncated identifying number appears on a paper payee statement (including substitute and composite substitute statements) in the Form 1098 series, Form 1099 series, or Form 5498 series for calendar year 2009 or 2010. **Notice 2009-93, I.R.B. 2009-51**.

The IRS has issued proposed regulations under a new statute requiring that, starting with transactions in calendar year 2011, the gross amount of payment card and third-party network transactions be reported annually to participating merchants and the IRS. The provision was enacted as part of the Housing Assistance Tax Act of 2008 and is designed to improve voluntary tax compliance by business taxpayers and help the IRS determine whether their tax returns are correct and complete. The proposed regulations propose rules to implement reporting of credit card, debit card and similar transactions, as well as transactions settled through third-party payment networks, such as third-party organizations that settle online transactions. The IRS also published a draft version of new Form 1099K, Merchant Card and Third-Party Payments, which will be used to make these reports. The new law requires banks and other payment settlement entities to report payment card and third-party network transactions with their participating merchants. The IRS emphasized that individual cardholders are unaffected by this requirement, and none of the cardholder's personal information will be shared with the IRS. The IRS has created Form 1099-K, which is similar to the existing Forms 1099 used to report interest, dividends and other payments. The first information return covering calendar year 2011 must be filed with the IRS and furnished to participating merchants in early 2012.

Among other things, the proposed regulations describe who is required to file a return and which payment card and third-party network transactions are subject to the reporting requirement. The proposed regulations also provide numerous examples. **74 Fed. Reg. 61294 (Nov. 24, 2009)**.

INTEREST RATE. The IRS has announced that, for the period January 1, 2010 through March 31, 2010, the interest rate paid on tax overpayments remains at 4 percent (3 percent in the case of a corporation) and for underpayments remains at 4 percent. The interest rate for underpayments by large corporations remains at 6 percent. The overpayment rate for the portion of a corporate overpayment exceeding $10,000 remains at 1.5 percent. **Rev. Rul. 2009-37, I.R.B. 2009-52.**

INVOLUNTARY CONVERSION. The taxpayer was a family limited partnership holding investments for the benefit of the partners. The original assets of the taxpayer were in the form of corporate stock in a corporation which was acquired by a second corporation which distributed its stock to the first corporation's shareholders. The transaction was structured by the second corporation so that approximately 75 percent of its stock was distributed directly to the shareholders upon surrender of their certificates, and two escrow accounts were set up holding back the remaining approximately 25 percent of second corporation's stock for each shareholder. One escrow was distributed after approximately one year. The taxpayer never received the distribution from the second escrow. Prior to the second escrow release, the original trustee of the taxpayer died. When a new trustee was appointed, the existence of the stock in the escrow account was unknown to that new trustee. Apparently, any attempted communication or delivery by the escrow agent to the deceased former trustee was returned to the escrow agent. At a subsequent unknown date, the escrow agent transferred the shares remaining in the escrow account owed to the taxpayer to the state in accordance with the state's unclaimed property law. The state sold the shares and retained control of the cash proceeds, publishing its holding of the funds as unclaimed property. The trustee was made aware by a third party of the state's holding of the unclaimed property, and the trustee placed a claim for it with state. The state subsequently transferred the proceeds to the taxpayer's brokerage account. The taxpayer sought a ruling that the stock was involuntarily converted by the state and entitled the taxpayer to defer any gain on the sale of the stock by obtaining replacement stock within two years after receiving the funds from the state. The IRS agreed and ruled that the conversion of the stock to money was an involuntary conversion by the state and that the two year replacement rule began when the taxpayer received the funds from the state. **Ltr. Rul. 200946006, July 29, 2009**.

LEVY. The taxpayer was incarcerated and owned a residence in which the taxpayer had resided during two of the past five years. The residence was rented to unrelated parties during the incarceration and the taxpayer received all mail at the prison. An IRS revenue officer sought an opinion as to whether the officer had to acquire a judge's approval before seizing the residence as part of a levy for unpaid taxes. In a Chief Counsel Advice letter, the IRS ruled that the officer did not need approval from a judge under I.R.C. § 6334(e) because the residence was no longer the taxpayer's principal residence. The IRS ruled that the two-out-of-five-years residency test, used in I.R.C. § 121 for exclusion of gain from a sale, did not apply to I.R.C. § 6334(e). **CCA Ltr. Rul. 200947036, Aug. 17, 2009**.

LIMITED LIABILITY COMPANY. The taxpayer was the sole owner of a limited liability company (LLC) which had incurred employment taxes when the LLC was owned by more than one person. In a Chief Counsel Advice letter, the IRS ruled that the taxpayer was not personally liable for the employment taxes incurred while the LLC was owned by more than one person. **CCA Ltr. Rul. 200946050, July 17, 2009**.

MILEAGE EXPENSES. The taxpayer operated a medication transcription service and claimed mileage expenses for a vehicle used in that business. The taxpayer's income tax return originally claimed a $3000 actual vehicle expense deduction but the taxpayer changed the deduction to $14,000 using the standard mileage deduction method. The taxpayer presented mileage logs of the vehicle use constructed after the filing of the return. The IRS argued that the mileage deduction should be limited to the accepted $3,000 amount because the mileage log was inaccurate in that it conflicted with other written evidence. The taxpayer claimed that the mileage log was accurate and that the inconsistencies were due to another person using the car on some days. The court held that a sufficient issue of fact had been raised as to the sufficiency of the mileage log to meet the substantiation requirements for the mileage deduction; therefore, a summary judgment on the issue requested by the IRS would be denied. **United States v. Norlem, 2009-2 U.S. Tax Cas. (CCH) ¶ 50,748 (D. Minn. 2009)**.

NET OPERATING LOSSES. IRS has issued guidance describing when and how taxpayers can elect to carry back applicable net operating losses (NOLs) under relief provided by section 13 of the Worker, Homeownership, and Business Assistance Act of 2009 (Pub. L. No. 111-92). Section 13 of the Act amended I.R.C. § 172(b)(1)(H) to allow taxpayers to elect to carry back applicable NOLs for a period of three, four or five years, or a loss from operation for four or five years, to offset taxable income in those previous years. In addition, section 13 amended I.R.C. § 810(b) to allow losses from the operations of life insurance companies to be treated in the same manner as NOLs. Any NOL or loss from operations carried back five years can only offset a maximum of 50 percent of the taxpayer's taxable income for that fifth preceding year. This relief is available to all taxpayers with business losses except those that received payments under the Troubled Asset Relief Program (if the federal government acquired or had the right to acquire an equity interest in the firm), and applies to taxpayers that incurred NOLs or losses from operations in tax years ending after December 31, 2007, and before January 1, 2010. See Harl, "Worker, Homeownership, and Business Assistance Act of 2009," 20 *Agric. L. Dig.* 169 (2009). **Rev. Proc. 2009-52, I.R.B. 2009-49**.

PASSIVE ACTIVITY LOSSES. The taxpayers were married and conducted a real property business which qualified under

I.R.C. § 469. The taxpayers claimed to be qualified under I.R.C. § 469(c)(7)(B) to make the election to treat all interests in rental real estate as a single rental real estate activity. The taxpayers filed their income tax return without the statement required under Treas. Reg. § 1.469-9(g)(3) and sought an extension of time to properly file the statement and meet the requirements of the Section 469 election. The IRS granted the extension to file the statement with an amended return. **Ltr. Rul. 200947017, Aug. 10, 2009**.

The taxpayer claimed to be qualified under I.R.C. § 469(c)(7)(B) to make the election to treat all interests in rental real estate as a single rental real estate activity. The taxpayer filed an income tax return without the statement required under Treas. Reg. § 1.469-9(g)(3) and sought an extension of time to properly file the statement and meet the requirements of the Section 469 election. The IRS granted the extension to file the statement with an amended return. **Ltr. Rul. 200946011, Aug. 11, 2009**.

PENSION PLANS. The IRS has published the cost-of-living adjustments (COLAs), effective on Jan. 1, 2010, applicable to dollar limitations on benefits paid under qualified retirement plans and to other provisions affecting such plans. The maximum limitation for the I.R.C. § 415(b)(1)(A) annual benefit for defined benefit plans remains unchanged at $195,000 and the I.R.C. § 415(c)(1)(A) limitation for defined contribution plans remains unchanged at $49,000. The annual compensation limit under I.R.C. §§ 401(a)(17), 404(l), 408(k)(3)(C) and 408(k)(6)(D)(ii) remains unchanged at $245,000. The annual compensation limitation under I.R.C. § 401(a)(17) for eligible participants in certain governmental plans that, under the plan as in effect on July 1, 1993, allowed COLAs to the compensation limitation under the plan to be taken into account, remains unchanged at $360,000. The compensation amounts under Treas. Reg. § 1.61-21(f)(5)(i) concerning the definition of "control employee" for fringe benefit valuation purposes remaines at $95,000. **Notice 2009-94, I.R.B. 2009-50**.

SAFE HARBOR INTEREST RATES

December 2009

	Annual	Semi-annual	Quarterly	Monthly
		Short-term		
AFR	0.69	0.69	0.69	0.69
110 percent AFR	0.76	0.76	0.76	0.76
120 percent AFR	0.83	0.83	0.83	0.83
		Mid-term		
AFR	2.64	2.62	2.61	2.61
110 percent AFR	2.90	2.88	2.87	2.86
120 percent AFR	3.16	3.14	3.13	3.12
		Long-term		
AFR	4.17	4.13	4.11	4.09
110 percent AFR	4.59	4.54	4.51	4.50
120 percent AFR	5.02	4.96	4.93	4.91

Rev. Rul. 2009-38, I.R.B. 2009-49.

SALE OF RESIDENCE. The taxpayer was a member of the armed services and had purchased a personal residence. During 25 years of ownership, the taxpayer used the residence as a personal residence for 23 months during the 25 years, renting the property to unrelated persons when not personally using the property. The property was sold when the taxpayer received orders to live in government quarters. The IRS allowed a partial exclusion, based on the ratio of personal use and rental of the property, of gain from the sale of the property because the assignment to government quarters was an unanticipated circumstance. The exclusion ratio did not include any time the taxpayer chose to live in government quarters instead of the residence. In addition, the exclusion would not apply to any gain from depreciation taken on the residence as part of the rental use of the property. **Ltr. Rul. 200947024, Aug. 13, 2009**.

WITHHOLDING TAXES. The IRS has amended the rules, originally set in *Notice 2005-76, 2005-2 C.B. 947*, for determining the amount an employer should withhold from wages paid to nonresident alien employees. The amended rules reflect changes made in the withholding tables as a result of the enactment of I.R.C. § 36A (the "Making Work Pay Tax Credit") in the American Recovery and Reinvestment Act of 2009 (Pub. L. No. 111-5). Nonresident alien individuals are not eligible for the Making Work Pay Tax Credit under I.R.C. § 36A. The modified rules provide for withholding on the wages of nonresident alien employees that more closely approximates their income tax liability. **Notice 2009-91, I.R.B. 2009-48**.

LABOR

AGRICULTURAL LABOR. The plaintiff was originally employed as a worker on a fruit packers' loading dock, loading and unloading trucks. The plaintiff was promoted to shipping supervisor and changed from an hourly to salaried employee without overtime pay. The plaintiff's employment was terminated and the plaintiff sued for back overtime pay. The employer argued that the plaintiff was an agricultural laborer exempt from the overtime requirement under the Washington Minimum Wage Act, Rev. Code Wash. § 49.46.130(2)(g)(ii). which exempts from overtime pay any person employed "in packing, packaging, grading, storing or delivering to storage, or to market or to a carrier for transportation to market, any agricultural or horticultural commodity." The court held that the statute was clear and unambiguous and clearly excluded the plaintiff from overtime pay rules. **Elliott v. Custom Apple Packers, Inc., 2009 Wash App. LEXIS 2820 (Wash. Ct. App. 2009)**.

PARTNERSHIP

DEFINITION. The plaintiff had entered into a contract to sell dairy cattle to the defendant husband. The plaintiff sought to include the defendant wife as liable on the contract as a partner in the dairy operation. The court held that no partnership existed because the plaintiff failed to show that (1) the wife had any ownership in the dairy; (2) the wife shared in the gross returns from the dairy; and (3) the defendants never held themselves out to be a partnership in general or as to the contract to purchase the cattle. **McGregor v. Crumley, 2009 S.D. LEXIS 171 (S.D. 2009)**.

Agricultural Law Press
P.O. Box 835 Brownsville, OR 97327

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