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Issue Contents

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Hiring Incentives to Restore Employment Act (HIRE), Pub. L. No. 111-147, Signed Into Law

-by Neil E. Harl*

Although public attention has been focused heavily on incentives in the legislation for hiring and retaining unemployed workers, the Hiring Incentives to Restore Employment Act,[1] which was signed into law on March 18, 2010, also contains several other significant provisions including continuing the 2008 and 2009 levels of expense method depreciation[2] for 2010;[3] several transportation-related provisions; a number of offset provisions that tighten the rules applicable to foreign accounts, foreign assets generally and disclosure provisions; and a provision increasing estimated tax payments for large corporations.

Expense method depreciation

The maximum allowable amount of expense method depreciation, which was scheduled to drop from $250,000 to $134,000 (inflation-adjusted up from $125,000) in 2010[4] was continued by the legislation for 2010 (for taxable years beginning before 2011) at the $250,000 level.[5] The phase-out amount was also continued at the 2008 and 2009 level of $800,000 through 2010.[6] The phase-out would otherwise have been in effect for 2010 at the $500,000 level. The new legislation also left in place the permanent level of phase-out of $200,000 but with an increase to $800,000 for 2007 through 2010.[7]

Further, the 2010 legislation repealed the provisions pertaining to inflation adjustments for expense method depreciation allowances.[8] That provision had been in federal tax law since 2002.[9] The repeal means that, if the expense method depreciation allowance drops to $25,000 in 2011,[10] as is now scheduled, there would be no inflation adjustment for 2011 or later years unless Congress amends the provision further. The legislation did not extend so-called "bonus" depreciation into 2010.[11] Off the shelf computer software was already eligible for expense method depreciation if placed in service before 2011.[12]

The amendments to Section 179 are effective for taxable years beginning after December 31, 2009 and before 2011.[13]

The legislation did not address the issue of late elections or late revocations for expense method depreciation purposes.[14] Late *revocations* can be made under current law through 2010 by the taxpayer with respect to any property without IRS consent provided the period for filing the amended return has not expired.[15] Once made, the election to revoke is irrevocable.[16] However, the situation with late *elections* is markedly different.[17] In 2005, the Department of the Treasury issued regulations confirming the right to elect (and to

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revoke) without Commissioner consent after 2005 and before 2008.[18] The right to elect on an amended return was not extended through 2010 as was done for revocations.[19] The statute clearly states that "such election shall be made in such manner as the Secretary may *by regulations* prescribe."[20] In late August of 2008, IRS issued a Revenue Procedure indicating that the Department of the Treasury "intended" to amend the regulations to allow late section 179 elections without Commissioner consent for taxable yearsafter 2007 and *before* 2010.[21] It is clear that the Congressional directive is that the Department of the Treasury (not IRS) can specify the manner in which elections may be made. Even the IRS guidance (which did not comport with the authority given the Treasury by the Congress) has expired. Therefore, it would appear that nothing which can be relied upon authorizes late elections in 2010 and the new legislation did nothing to change the situation.[22] Moreover, the Department of the Treasury has done nothing to issue regulations allowing late elections without Commissioner consent after 2007 and before 2011, either. As noted, except for the Congress, only the Department of the Treasury *in regulations* can authorize late elections without Commissioner consent. Therefore, late elections without Commissioner consent continue to be out of reach through 2010 unless regulations allowing such elections are promulgated or Congress amends the statute.[23]

Employment-related provisions

The legislation signed on March 18, 2010, as noted above, was driven heavily by a desire to encourage employers to add additional employees. One provision forgives payroll taxes for individuals employed after March 18, 2010, through December 31, 2010.[24] Eligible employees must have begun employment after February 3, 2010 and before January 1, 2011, have not been employed for more than 40 hours during the 60-day period ending on the date of employment and were not employed to replace another employee for the employer unless the other employee separated from employment voluntarily or for cause.[25] Most private sector employers are eligible (including colleges and universities) but governments at all levels are not considered eligible employers.[26]

The new legislation also contains a business credit for retention of newly-hired individuals in 2010.[27] The current year business credit is increased, for each retained worker, by the lesser of $1,000 or 6.2 percent of the wages paid by the taxpayer to the retained worker during the 52 consecutive week period.[28] A "retained worker" is any qualified individual who was employed by the taxpayer on any date during the taxable year, who was so employed for a period of not less than 52 consecutive weeks and whose wages for such employment during the last 26 weeks of the period equaled at least 80 percent of such wages for the first 26 weeks of the period.[29] Qualified individuals are defined in terms of the eligibility rules for forgiveness of payroll taxes.[30]

Payment of corporate estimated taxes

The 2010 legislation, in an effort to offset outlays elsewhere in the bill, increases the payment of estimated taxes by corporations with assets of not less than $1,000,000,000, determined as of the end of the preceding taxable year.[31]

ENDNOTES

[1] Pub. L. No. 111-147, 111th Cong., 2d Sess. (2010).

[2] I.R.C. § 179. See generally 4 Harl, *Agricultural Law* § 29.05[2][b] (2009); Harl, *Agricultural Law Manual* § 4.03[4][j] (2009); 1 Harl, *Farm Income Tax Manual* § 3.20[2] (2010 ed.). See also Harl, "Can Section 179 Elections Be Made on Amended Returns After 2007?" 18 *Agric. L. Dig*. 161 (2007); Harl, "IRS Says Amendments to Regulations Needed For Late Section 179 Elections on Amended Returns After 2007," 19 *Agric. L. Dig*. 141 (2008)..

[3] Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, § 201, 111th Cong., 2d Sess. (2010).

[4] I.R.C. § 179(b)(7), amended by Pub. L. No. 111-5, § 1202, 111th Cong., 1st Sess. 2009).

[5] Pub. L. No. 111-147, § 201(a)(1), 111th Cong., 2d Sess. (2010). Note that some states have not adopted the federal provision.

[6] I.R.C. § 179(b)(2).

[7] I.R.C. § 179(b)(2).

[8] I.R.C. § 179(b)(5), (7).

[9] Pub. L. No. 108-27, § 202(b).

[10] See I.R.C. § 179(b)(1).

[11] I.R.C. § 168(k).

[12] I.R.C. § 179(d)(1)(A)(ii), amended by the Small Business and Work Opportunity Tax Act of 2007, § 8212(a).

[13] Pub. L. No. 111-147, § 202(b), 111th Cong., 2d Sess. (2010).

[14] See I.R.C. § 179(c).

[15] I.R.C. § 179(c)(2).

[16] *Id*.

[17] See Harl, "Can Section 179 Elections Be Made on Amended Returns After 2007?" 18 *Agric. L. Dig*. 2007).

[18] Treas. Reg. § 1.179-5(c).

[19] Pub. L. No. 109-222, Sec. 101.

[20] I.R.C. § 179(c)(1) (emphasis added).

[21] Rev. Proc. 2008-54, 2008-2 C.B. 722 (the date of 2010 may have been in error inasmuch as the authority to revoke with Commissioner consent runs *through* 2010).

[22] See I.R.C. § 179(c)(1).

[23] I.R.C. § 179(c)(1).

[24] Pub. L. No. 111-147, § 101, 111th Cong., 2d Sess. 2010.

[25] *Id*., § 101(a), amending I.R.C. § 3111(d)(3).

[26] *Id*., § 101(a), amending I.R.C. § 3111(d)(2).

[27] Pub. L. No. 111-147, § 102, 111th Cong., 2d Sess. (2010).

[28] *Id*., § 102(a).

[29] *Id*., § 102(b).

[30] *Id*., § 102(b).

[31] Pub. L. No. 111-147, § 561, 111th Cong., 2d Sess. (2010).

Some Highlights from the Patient Protection and Affordable Care Act

-by Neil E. Harl

The Health Care and Education Reconciliation Act of 2010,[1] one of the most debated and discussed items of legislation in modern time, was set to become law as the *Agricultural Law Digest* went to press. The Patient Protection and Affordable Care Act[2] was passed by the House of Representatives on Sunday, March 21, 2010, along with H.R. 4872 which was drafted to make "fixes" to the main bill. The President signed the Patient Protection and Affordable Care Act on March 23. The Senate took up the Reconciliation Act provision on March 24 and stripped out two minor provisions (pertaining to technical corrections dealing with Pell Grants for low-income students) before that bill was passed. Because of the amendments, that bill had to return to the House where it was approved a second time by a 220 to 207 vote margin and sent on to the President for signature.

We anticipate an article in the next issue of the *Digest* on the new legislation with only a couple of provisions mentioned here.

Increase in the Medicare Hospital Insurance Tax

One of the revenue offsets in the bill is an increase in the Hospital Insurance (HI) tax on couples filing a joint return or a surviving spouse who earn more than $250,000 ($125,000 for married taxpayers filing separately) and $200,000 for other taxpayers.[3] The tax is imposed at a rate of 3.8 percent of the lesser of the taxpayer's "net investment income" or the excess (if any) over the modified adjusted gross income for the taxable year over the threshold amount.[4] The threshold amounts are the above figures based on filing status.

"Net investment income" is defined as the excess of the sum of gross income from interest, dividends, annuities, royalties and rents, other than such income derived in the ordinary course of a trade or business; other gross income derived from a trade or business which is a passive activity[5] or a trade or business of trading in financial instruments or commodities; and net gain attributable to the disposition of property other than property held in a trade or business which is not a passive activity or an activity.[6] The term also includes gain from the disposition of an interest in a partnership or S corporation but only to the extent of the net gain which would be taken into account by the transferor if all property of the partnership or S corporation were sold for fair market value immediately before the disposition of such interest.[7] The term "net investment income" does not include distributions from qualified plans.[8]

The new tax applies to trusts and estates at the same rate, based on the lesser of the undistributed net investment income for the taxable year or the excess of the adjusted gross income over the dollar amount at which the highest tax bracket begins for the taxable year.[9]

Effective date

The provision is effective for taxable years beginning after December 31, 2012.[10]

Student loan reform

The legislation makes major changes in the student loan program with termination of the authority of participating institutions to make or insure new loans.[11] Student loans will be made directly from the federal government with what has been calculated as producing a substantial saving.

Other provisions

The next issue of the *Digest* will discuss other major provisions of the massive legislation including additional tax provisions with coverage of credits for small business owners providing insurance coverage and other important features of the bill.

ENDNOTES

[1] H.R. 4872, 111th Cong., 2d Sess. (2010).

[2] Pub. L. No. 111-148, 111th Cong., 2d Sess. (2010).

[3] Health Care and Education Reconciliation Act of 2010, H.R. 4872, § 1411, 111th Cong., 2d Sess. (2010).

[4] *Id*., § 1411(a)(1).

[5] See I.R.C. § 469.

[6] H.R. 4872, § 1411(c), 111th Cong., 2d Sess. (2010).

[7] H.R. 4872, § 1411(c)(4), 111th Cong., 2d Sess. (2010).

[8] *Id*., § 1411(c)(5).

[9] *Id*., § 1411(a)(2).

[10] *Id*., § 1411(e)(4).

[11] H.R. 4872, §§ 2201, 2202, 111th Cong., 2d Sess. (2010).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr

FEDERAL ESTATE AND GIFT TAXATION

GENERATION SKIPPING TRANSFERS. The grantors had established three pre-September 25, 1985 trusts for three children. The trusts provided that, at the death of the last child, the trusts' assets were to be distributed to the remainder holders, the grandchildren. The trustee obtained court permission to separate and consolidate the trusts into trusts for each child and to change the distribution time to provide that, at the death of each child, the trust assets were to be distributed to the remainder holders. The IRS ruled that the separation and consolidation of the trusts and the change in distribution timing did not subject the trusts to GSTT. **Ltr. Rul. 201011002, Nov. 6, 2009; Ltr. Rul. 201011002, Nov. 6, 2009**.

GIFTS. The taxpayers, husband and wife, transferred partial interests in an LLC to their children. The LLC's principal asset was a parcel of undeveloped land. The LLC operating agreement provided for distributions of capital but only under the authority and discretion of a manager. The LLC members had a right to transfer their interests but subject to a right of first refusal by the

LLC and other restrictions. The taxpayers filed gift tax returns and claimed the federal gift tax annual exclusion. The IRS disallowed the annual exclusion on the basis that the transfers were not complete gifts of present interests in the LLC interests. The court agreed, holding that the LLC interests transferred were subject to conditions which prevented the children from currently enjoying the economic benefit of the LLC interests. **Fisher v. United States, 2010-1 U.S. Tax Cas. (CCH) ¶ 60,588 (S.D. Ind. 2010)**.

VALUATION. The decedent's estate included 20 percent of the common stock of a closely-held corporation. The stock had never been publicly traded and no sales of the stock had occurred in the 10 years prior to the decedent's death. In the six years preceding the decedent's death, the corporation profit dropped to almost zero. For estate tax purposes, the estate calculated the value of the decedent's share of the corporation at $1.75 million using the capitalization of income method, under which a company's value is calculated by (1) projecting the company's annual income, (2) determining a company-specific capitalization rate, (3) dividing the projected income by the capitalization rate, and (4) adding the value of non-operating assets. This yielded a valuation of $25.8 million for the company, of which the estate's share was $5.3 million, which was then further reduced by 40 percent to account for the decedent's minority ownership interest and by a further 45 percent to account for lack of marketability, to arrive at the final valuation of $1.75 million. The estate argues that this valuation reflects the company's grim profit prospects. The IRS valued the decedent's interest at $32 million, using two independent methods: the comparable public company method, which yielded a company value of $260 million, and the discounted cashflow method, which was performed twice (using different estimated future values) and which yielded company values of $212.6 million and $158.8 million. The IRS settled on $225 million, of which the estate's share was $46.3 million. That value was then discounted by 30 percent to account for lack of marketability, thus arriving at the final value of $32 million. The IRS valuation did not account for any lessening of profits from competition. The Tax Court disagreed with both valuations and used the capitalization of income method and added the value of non-operating assets. The decedent's share of the value of the company was reduced by a 15 percent minority interest discount and 30 percent for lack of marketability for a final value of $13.5 million. The appellate court held that the Tax Court properly ignored both the estate and IRS valuations as flawed and substituted its own valuation method. The IRS also sought an accuracy-based penalty which was denied by the Tax Court. The appellate court remanded the case back to the Tax Court for a finding whether the estate's reliance on its appraiser was reasonable. On remand, the Tax Court found that the reliance was reasonable and the appellate court affirmed. See also Thompson v. Comm'r, 499 F.3d 129 (2d Cir. 2007), *aff'g, vac'g and rem'g*, T.C. Memo. 2004-174. **Thompson v. Comm'r, 2010-1 U.S. Tax Cas. (CCH) ¶ 60,589 (2d Cir. 2010), *aff'g unrep*, Tax Court dec.**

FEDERAL INCOME TAXATION

CHARITABLE ORGANIZATIONS. The IRS has published a list of six things taxpayers should know about the tax treatment of tax-exempt organizations.

Annual returns are made available to the public. Exempt organizations generally must make their annual returns available for public inspection. This also includes the organization's application for exemption. In addition, an organization exempt under 501(c)(3) must make available any Form 990-T, Exempt Organization Business Income Tax Return. These documents must be made available to any individual who requests them, and must be made available immediately when the request is made in person. If the request is made in writing, an organization has 30 days to provide a copy of the information, unless it makes the information widely available.

Donor lists generally are not public information. The list of donors filed with Form 990, Return of Organization Exempt From Income Tax, is specifically excluded from the information required to be made available for public inspection by the exempt organization. There is an exception: private foundations and political organizations must make their donor list available to the public.

How to find tax-exempt organizations. The easiest way to find out whether an organization is qualified to receive deductible contributions is to ask them. You can ask to see an organization's exemption letter, which states the Code section that describes the organization and whether contributions made to the organization are deductible. You can also search for organizations qualified to accept deductible contributions in IRS Publication 78, Cumulative List of Organizations and its Addendum, available at IRS.gov. Taxpayers can also confirm an organization's status by calling the IRS at 877-829-5000.

Which organizations may accept charitable contributions. Not all exempt organizations are eligible to receive tax-deductible charitable contributions. Organizations that are eligible to receive deductible contributions include most charities described in section 501(c)(3) of the Internal Revenue Code and, in some circumstances, fraternal organizations described in section 501(c)(8) or section 501(c)(10), cemetery companies described in section 501(c)(13), volunteer fire departments described in section 501(c)(4), and veterans' organizations described in section 501(c)(4) or 501(c)(19).

Requirement for organizations not able to accept deductible contributions. If an exempt organization is ineligible to receive tax-deductible contributions, it must disclose that fact when soliciting contributions.

How to report inappropriate activities by an exempt organization. If a taxpayer believes that the activities or operations of a tax-exempt organization are inconsistent with its tax-exempt status, a taxpayer may file a complaint with the Exempt Organizations Examination Division by completing Form 13909, Tax-Exempt Organization Complaint (Referral) Form. The complaint should contain all relevant facts concerning the alleged violation of tax law. Form 13909 is available at IRS.gov or by calling 800-TAX-FORM (800-829-3676). See also IRS Publication 526, Charitable Contributions. **IRS Tax Tip 2010-59**.

CORPORATIONS

REORGANIZATIONS. In 2007 the IRS issued temporary regulations amending the signing date rule for nonrecognition of gain and loss from reorganization of corporations. ***72 Fed. Reg. 12974 (March 20, 2007).*** The temporary regulations were revisions of final regulations adopted in 2005, see 16 *Agric. L. Dig.* 141 (2005). The revisions include (1) the definition of fixed consideration under the signing date rule; (2) expansion of the definition of the contract modification rule; (3) expansion of the signing date rule to include contingent adjustments to the consideration received in the reorganization; and (4) provision for altering the signing date value of the issuing corporation's stock if the issuing corporation's capital structure is altered or the number of issuing shares is altered. The temporary regulations have expired under I.R.C. § 7805(e)(2) and the IRS has issued guidance which will apply until further guidance can be published. **Notice 2010-25, I.R.B. 2010-14**.

COURT AWARDS AND SETTLEMENTS. The taxpayer filed a suit against a former employer for gender, religion and race discrimination. The taxpayer settled for the amount of medical expenses after being told that the settlement would not be taxed. However, the settlement agreement made no mention of the purpose of the payment except to settle the lawsuit. The court held that the settlement payment was taxable income because the taxpayer failed to provide evidence that the payment was made in compensation for medical expenses. **Espinoza v. Comm'r, T.C. Memo. 2010-53**.

DEMUTUALIZATION. The following discussion of *Fisher v. United States, 2008-2 U.S. Tax Cas. (CCH) ¶ 50,481 (Fed. Cl. 2008)*, is from Harl, "Income Tax Consequences of Demutualization," 19 *Agric. L. Dig*. 133 (2008):

"The shift from member-owned, mutual insurance companies, to policyholder-owned firms, often publicly-traded, has produced a dramatic reordering of the insurance landscape in recent years. The move, facilitated by changes in state insurance laws, has involved an exchange of shares (or money) for the members' ownership rights in the company which included voting and distribution rights as well as contractual insurance rights. . . ."

"The key question, which is still not answered, is the amount of income tax basis for the shares issued in the exchange. On May 19, 2000, the Internal Revenue Service released a private letter ruling,' *Ltr. Rul. 200020048, Feb. 22, 2000*, which had been requested by the company, Sun Life Assurance Company. The ruling dealt with several aspects of the demutualization process as carried out by Sun Life. The ruling stated that the ownership rights at stake 'cannot be obtained by any purchase separate from an insurance contract. . .' issued by the company. Accordingly, IRS ruled that, based on [I.R.C. § 354(a)(1)], 'no gain or loss will be recognized by the Eligible Policyholders on the deemed exchange of their Ownership Rights solely for Company stock . . .' IRS further ruled that the '. . . basis of the Company stock deemed received by the eligible Policyholders in the exchange will be the same as the basis of the Ownership rights surrendered in exchange for such Company stock.' That amount was zero. . . ."

"The United States Court of Federal Claims, in deciding the case, stated that '. . . . the opinion rendered by plaintiff's valuation expert that the value of the ownership rights was not discernible' was supported by the record which led the court to conclude that this was an appropriate case for application of the 'open transaction' doctrine by which taxpayers could treat amounts received as return of basis until the basis was exhausted, with the remaining amounts subject to income tax. The problem with that outcome is that the court provided no guidance as to how the income tax basis amount should be determined."

The case has been affirmed in a decision designated as not for publication. **Fisher v. United States, 2010-1 U.S. Tax Cas. (CCH) § 50,289 (Fed. Cir. 2010), *aff'g*, 2008-2 U.S. Tax Cas. (CCH) ¶ 50,481 (Fed. Cl. 2008)**.

DOMESTIC PRODUCTION DEDUCTION. The taxpayer was a non-exempt farmer's marketing 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. 201010013, Nov. 24, 2009**.

EMPLOYER HIRING INCENTIVES. The IRS has published a discussion of two new tax benefits available to employers hiring workers who were previously unemployed or only working part time. These provisions are part of the Hiring Incentives to Restore Employment Act (HIRE), Pub. L. No. 111-147, enacted into law on March 18, 2010.

Employers who hire unemployed workers this year (after Feb. 3, 2010 and before Jan. 1, 2011) may qualify for a 6.2-percent payroll tax incentive, in effect exempting them from their share of Social Security taxes on wages paid to these workers after the date of enactment. This reduced tax withholding will have no effect on the employee's future Social Security benefits, and employers would still need to withhold the employee's 6.2-percent share of Social Security taxes, as well as income taxes. The employer and employee's shares of Medicare taxes would also still apply to these wages.

In addition, for each worker retained for at least a year, businesses may claim an additional general business tax credit, up to $1,000 per worker, when they file their 2011 income tax returns.

New hires filling existing positions also qualify but only if the workers they are replacing left voluntarily or for cause. Family members and other relatives do not qualify.

In addition, the new law requires that the employer get a statement from each eligible new hire certifying that he or she was unemployed during the 60 days before beginning work or, alternatively, worked fewer than a total of 40 hours for someone else during the 60-day period. The IRS is currently developing a form employees can use to make the required statement.

Businesses, agricultural employers, tax-exempt organizations and public colleges and universities all qualify to claim the payroll tax benefit for eligible newly-hired employees. Household employers cannot claim this new tax benefit.

Employers claim the payroll tax benefit on the federal employment tax return they file, usually quarterly, with the IRS. Eligible employers will be able to claim the new tax incentive on their revised employment tax form for the second quarter of 2010. Revised forms and further details on these two new tax provisions will be posted on IRS.gov during the next few weeks. **IR-2010-33**. See article by Neil Harl on the HIRE Act developments, p. 49 *supra*.

EXPENSE METHOD DEPRECIAITON. The Hiring Incentives to Restore Employment Act (HIRE), Pub. L. No. 111-147, extended I.R.C. § 179 expense method depreciation through

2010 at the $250,000. See article by Neil Harl on the HIRE Act developments, p. 49 *supra*.

FARM INCOME AND DEDUCTIONS. The IRS has issued a summary of ten items of farm income and deductions.

Crop Insurance Proceeds. Taxpayers must include in income any crop insurance proceeds received as the result of crop damage. A taxpayer generally includes them in the year they were received. [**Ed. Note**: However, taxpayers may be eligible to elect to defer the amounts to the year following the year of destruction or damage to the crops.]

Sales Caused by Weather-Related Conditions. If a taxpayer sells more livestock, including poultry, than the taxpayer normally would in a year because of weather-related conditions, the taxpayer may be able to choose to postpone reporting the gain from selling the additional animals due to the weather until the next year. [**Ed. Note**: Taxpayers may be eligible, for draft, dairy or breeding livestock, to reinvest the proceeds within four years in similar livestock and, in special situations, in other farm property.]

Farm Income Averaging. Taxpayers may be able to average all or some of a current year's farm income by allocating it to the three prior years. This may lower the current year tax if current year income from farming is high, and taxable income from one or more of the three prior years was low. This method does not change a prior year tax, it only uses the prior year information to determine the current year tax.

Deductible Farm Expenses. The ordinary and necessary costs of operating a farm for profit are deductible business expenses. An ordinary expense is an expense that is common and accepted in the farming business. A necessary expense is one that is appropriate for the business.

Employees and hired help. A taxpayer can deduct reasonable wages paid for labor hired to perform farming operations. This includes full-time employees as well as part-time workers.

Items Purchased for Resale. Taxpayers may be able to deduct the cost of livestock and other items purchased for resale *in the year of sale*. [**Ed. Note**: not necessarily the year of purchase.] This cost includes freight charges for transporting the livestock to the farm.

Net Operating Losses. If a taxpayer's deductible expenses from operating the farm are more than other income for the year, a taxpayer may have a net operating loss. If a taxpayer has a net operating loss this year, the taxpayer can carry it back five years and then forward to other years and deduct it. A taxpayer may be able to get a refund of part or all of the income tax paid for past years or may be able to reduce taxes in future years.

Repayment of loans. Taxpayers cannot deduct the repayment of a loan if the loan proceeds are used for personal expenses. However, if the proceeds of the loan are used for a farming business, taxpayers can deduct the interest that paid on the loan.

Fuel and Road Use. Taxpayers may be eligible to claim a credit or refund of federal excise taxes on fuel used on a farm for farming purposes.

Farmers Tax Guide. More information about farm income and deductions can be found in IRS Publication 225, Farmer's Tax Guide which is available at www.IRS.gov or by calling the IRS at 800-TAX-FORM (800-829-3676). **IRS Tax Tip 2010-56**.

GAMBLING LOSSES. The taxpayer filed a Schedule C as a professional gambler and claimed gambling losses in excess of gambling income and deductions for meals and entertainment and for promotional activities. The court held that I.R.C. § 165(d) limits any deduction for gambling losses in excess of gambling income. The promotion activities expenses were disallowed because the taxpayer failed to prove that the expenses were ordinary and necessary for the gambling activity. **Crawford v. Comm'r, T.C. Memo. 2010-54**.

HEALTH COVERAGE TAX CREDIT. The IRS has published a discussion of the health coverage tax credit. The health coverage tax credit pays 80 percent of health insurance premiums for eligible taxpayers and their qualified family members. The HCTC pays 80 percent of an eligible taxpayer's health insurance premiums. The HCTC is a refundable credit, which means it not only reduces a taxpayer's tax liability but also may result in cash back at the end of the year. Taxpayers can receive the HCTC monthly—when their health plan premiums are due—or as a yearly tax credit. A taxpayer may be eligible for the HCTC if the taxpayer receives Trade Readjustment Allowances—or unemployment insurance in lieu of TRA—through one of the Trade Adjustment Assistance programs. A taxpayer also may be eligible for the HCTC if the taxpayer is a Pension Benefit Guaranty Corporation payee and is 55 years old or older. The most common types of health plans that qualify for the HCTC include COBRA, state-qualified health plans, and spousal coverage. In some cases, non-group/individual plans and health plans associated with Voluntary Employee Benefit Associations established in lieu of COBRA plans also qualify. HCTC candidates receive the HCTC Program Kit by mail. The Kit explains the tax credit and provides a simple checklist to determine eligibility. Also included in the Kit is the HCTC Registration Form. For more information on the HCTC and how it may benefit you, call the HCTC Customer Contact Center toll free at 1-866-628-HCTC (4282). **IRS Tax Tip 2010-54**.

HEALTH INSURANCE. The IRS has announced that it has de-coordinated its coordinated issue paper "All Industries Coordinated Issue on Health Insurance Deductibility for Self-employed Individuals" See **http://www.irs.gov/businesses/article/0,,id=96445,00.html**

INNOCENT SPOUSE. The Tax Court, in *Lantz v. Comm'r, 132 T.C. No. 8 (April 7, 2009)*, held that the two-year limitation on bringing an innocent spouse relief claim was invalid. The IRS has rejected the holding in *Lantz* and will continue to litigate the issue. The IRS has announced that, while the litigation and appeal continues on the *Lantz* issue, the IRS will respond to new innocent spouse claims filed beyond the two-year limit with two choices for the claimants: (1) the claimant may elect to suspend consideration of the claim pending resolution of the *Lantz* issue by appeal; or (2) the claimant may elect to receive a final determination letter rejecting the claim, making the issue eligible for appeal to the Tax Court. If election (1) is chosen, collection efforts will be suspended, the collection statute of limitations will be suspended, and any underpayment interest will continue to accrue. **Chief Counsel Notice CC-2010-005, March 18, 2010**.

During the tax year involved, the taxpayer's spouse was employed and received wage income. The taxpayer was aware of the wages and the wages were used to pay household expenses. The wages were not reported on a joint return and the taxpayer sought innocent spouse relief from the assessed deficiency on the grounds that the spouse controlled the household finances. The court held that the taxpayer was not entitled to statutory innocent spouse relief because the taxpayer was aware of the wages. The court also held that the taxpayer was not entitled to equitable relief because the taxpayer benefited from the unreported income and failed to demonstrate that the spouse had agreed to be solely responsible for the taxes and that the payment of the taxes would be a financial hardship on the taxpayer. **Stewart v. Comm'r, T.C. Summary Op. 2010-31**.

IRA. The taxpayer owned an IRA and was diagnosed with multiple sclerosis. The disease forced the taxpayer to quit working and the taxpayer received social security disability benefits. The taxpayer received unequal, non-periodic payments from the IRA before reaching age 59 1/2. The IRS ruled that, under I.R.C. § 72(t)(2), the distributions were not subject to the 10 percent tax on early distributions. **Ltr. Rul. 201011036, Dec. 14, 2009**.

LEGAL FEES. The taxpayers, husband and wife, sold a rental property and used some of the proceeds to pay off a lien against the property which was filed by their attorney who had obtained a judgment against the taxpayers. The taxpayer claimed that the amount paid to the attorney reduced the gain on the sale of the property because the lien prevented them from transferring clear title. The court held that the judgment arose out of a case against the taxpayers; therefore, the judgment was a personal non-deductible expense which could not reduce the gain from the sale of the property. **Chow v. Comm'r, T.C. Memo. 2010-48**.

PENALITES. The IRS has published a discussion of return filing penalties. If a taxpayer does not file by the deadline, the taxpayer might face a failure-to-file penalty. If a taxpayer does not pay by the due date, the taxpayer could face a failure-to-pay penalty. The failure-to-file penalty is generally more than the failure-to-pay penalty. So if the taxpayer cannot pay all the taxes owed, the taxpayer should still file the tax return and explore other payment options in the meantime. The penalty for filing late is usually 5 percent of the unpaid taxes for each month or part of a month that a return is late. This penalty will not exceed 25 percent of unpaid taxes. If a taxpayer files a return more than 60 days after the due date or extended due date, the minimum penalty is the smaller of $135 or 100 percent of the unpaid tax. The taxpayer will have to pay a failure-to-pay penalty of ½ of 1 percent of unpaid taxes for each month or part of a month after the due date that the taxes are not paid. This penalty can be as much as 25 percent of unpaid taxes. If a taxpayer filed an extension and paid at least 90 percent of the actual tax liability by the due date, the taxpayer will not be faced with a failure-to-pay penalty if the remaining balance is paid by the extended due date. If both the failure-to-file penalty and the failure-to-pay penalty apply in any month, the 5 percent failure-to-file penalty is reduced by the failure-to-pay penalty. However, if a taxpayer files a return more than 60 days after the due date or extended due date, the minimum penalty is the smaller of $135 or 100% of the unpaid tax. The taxpayer will not have to pay a failure-to-file or failure-to-pay penalty if the taxpayer can show that the taxpayer failed to file or pay on time because of reasonable cause and not because of willful neglect. **IRS Tax Tip 2010-51**.

PARTNERSHIPS

ELECTION TO ADJUST PARTNERSHIP BASIS. A partner in the taxpayer partnership died during the tax year and the tax return preparer hired by the partnership failed to include the election to adjust the basis of partnership assets. The IRS granted the taxpayer an extension of time to file an amended return with the election. **Ltr. Rul. 201011004, Nov. 23, 2009**.

SAFE HARBOR INTEREST RATES

April 2010

	Annual	Semi-annual	Quarterly	Monthly
		Short-term		
AFR	0.67	0.67	0.67	0.67
110 percent AFR	0.74	0.74	0.74	0.74
120 percent AFR	0.80	0.80	0.80	0.80
		Mid-term		
AFR	2.70	2.68	2.67	2.67
110 percent AFR	2.97	2.95	2.94	2.93
120 percent AFR	3.25	3.22	3.21	3.20
		Long-term		
AFR	4.40	4.35	4.33	4.31
110 percent AFR	4.85	4.79	4.76	4.74
120 percent AFR	5.29	5.22	5.19	5.16

Rev. Rul. 2010-11, I.R.B. 2010-14.

S CORPORATION

SHAREHOLDER BASIS. The taxpayer was the sole shareholder of an S corporation which operated the taxpayer's law practice. The taxpayer had personally guaranteed a loan made to the corporation used to fund the business operations. The taxpayer claimed a share of the corporation's losses based on an increase in the taxpayer's basis in the taxpayer's stock in the corporation. In a later tax year, the taxpayer paid off the corporation's loan with personal funds. The court held that the mere guaranty of the corporation's loan was insufficient investment in the corporation to increase the taxpayer's basis in the taxpayer's stock; therefore, the loss was properly disallowed because the taxpayer did not prove any basis in the stock. **Weisberg v. Comm'r, T.C. Memo. 2010-55**.

TAX RETURN PREPARERS. The IRS has issued proposed regulations governing the identifying numbers to be used by tax return preparers on tax returns prepared for other taxpayers. Tax return preparers will need to apply and pay for a preparer tax identification number (PTIN) which may not be the preparer's social security number. In keeping with the announced program to register all tax return preparers who are not attorneys, CPAs, or enrolled agents, only those individuals and registered tax return preparers will be given PTINs. **75 Fed. Reg. 14539 (March 26, 2010**.

IN THE NEWS

AGRICULTURAL CREDIT. On March 18, 2010, the U.S. House of Representatives passed H.R. 3509, the Agricultural Credit Act of 2009. The legislation amends the Agricultural Credit Act of 1987 to authorize appropriations through 2015 for the state agricultural loan mediation programs. The programs, which are used in 32 states, provide grants to state mediation programs to help producers, creditors and other agencies address disputes involving various stakeholders in agricultural lending and credit. **The United State Agricultural & Food Law and Policy Blog, http://www.agandfoodlaw.com**.

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AGRICULTURAL TAX SEMINARS

by Neil E. Harl

May 4-5, 2010

I-80 Quality Inn (formerly the Holiday Inn), Grand Island, NE

Join us for expert and practical seminars on the essential aspects of agricultural tax law. Gain insight and understanding from one of the country's foremost authorities on agricultural tax law.

The seminars will be held on Tuesday and Wednesday from 8:00 am to 5:00 pm. Registrants may attend one or both days, with separate pricing for each combination. On Tuesday, Dr. Harl will speak about farm and ranch income tax. On Wednesday, Dr. Harl will cover farm and ranch estate and business planning. Your registration fee includes written comprehensive annotated seminar materials for the days attended and lunch. **E-mail robert@agrilawpress.com for a brochure.**

The topics include:

Tuesday, May 4, 2010

FARM INCOME TAX

New Legislation

Reporting Farm Income

Leasing land to family entity
Constructive receipt of income
Deferred payment and installment payment arrangements for grain and livestock sales
Payments from contract production
Items purchased for resale
Items raised for sale
Crop insurance proceeds
Weather-related livestock sales
Sales of diseased livestock
Reporting federal disaster assistance benefits
Gains and losses from commodity futures

Claiming Farm Deductions

Soil and water conservation expenditures
Fertilizer deduction election
Farm lease deductions
Prepaid expenses
Preproductive period expense provisions
Paying rental to a spouse
Paying wages in kind
Section 105 plans

Sale of Property

Income in respect of decedent
Sale of farm residence
Installment sale including related party rules
Private annuity
Self-canceling installment notes
Sale and gift combined.

Like-Kind Exchanges

Requirements for like-kind exchanges
"Reverse Starker" exchanges
What is "like-kind" for realty
Like-kind guidelines for personal property
Partitioning property
Exchanging partnership assets

Taxation of Debt

Turnover of property to creditors
Discharge of indebtedness
Taxation in bankruptcy.

Wednesday, May 5, 2010

FARM ESTATE AND BUSINESS PLANNING

The Liquidity Problem

Property Held in Co-ownership

Federal estate tax treatment of joint tenancy
Severing joint tenancies
Joint tenancy and probate avoidance
Joint tenancy ownership of personal property
Other problems of property ownership

Federal Estate Tax

The gross estate
Special Use Valuation
Family-owned business deduction recapture
Property included in the gross estate
Claiming deductions from the gross estate
Marital and charitable deductions
Taxable estate
The unified credit and other credits
Unified estate and gift tax rates
Generation skipping transfer tax
Federal estate tax liens
Undervaluations of property
Reopening an examination

Gifts

Use of the Trust

The General Partnership

Limited Partnerships

Limited Liability Companies

The Closely-Held Corporation -

State anti-corporate farming restrictions
Developing the capitalization structure
Tax-free exchanges
Would incorporation trigger a gift because of severance of land held in joint tenancy?
"Section 1244" stock

Status of the Corporation as a Farmer

The regular method of income taxation
The Subchapter S method of taxation

Financing, Estate Planning Aspects and Dissolution of Corporations

Corporate stock as a major estate asset
Valuation discounts
Dissolution and liquidation
Reorganization

Social Security

In-kind wages paid to agricultural labor

The seminar registration fees for *current subscribers* to the *Agricultural Law Digest*, the *Agricultural Law Manual*, or *Principles of Agricultural Law* (and for each one of multiple registrations from one firm) are $200 (one day) and $370 (two days).

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