D.C. Circuit rules on District Court jurisdiction Over USDA NAD appeals

The D.C. Circuit has ruled that 7 U.S.C. § 6999 places jurisdiction for the review of final USDA National Appeals Division (USDA NAD) determinations solely in the federal district courts. *Deaf Smith County Grain Processors v. Glickman*, 162 F.3d 1206 (D.C. Cir. 1998). The ruling is significant because, prior to the creation of the USDA NAD in 1994, the government had routinely argued that actions for the review of farm program determinations could be brought only in the United States Court of Federal Claims pursuant to the Tucker Act, 28 U.S.C. § 1491, if the amount of the program payments in dispute exceeded $10,000.

The importance of the ruling in *Deaf Smith County Grain Processors* is best illustrated by a brief review of a jurisdictional issue that has long plagued farm program litigation. The review necessarily begins with the fact that the federal government is immune from suit unless it waives its sovereign immunity. Confronted with this immunity, farm program participants seeking judicial review of adverse determinations traditionally have relied on the waiver of sovereign immunity found in the Administrative Procedure Act (APA), 5 U.S.C. §§ 701-706, specifically, 5 U.S.C. § 702. Though, with some exceptions, the APA waives sovereign immunity, it does not confer jurisdiction. However, because the district courts possess general federal question jurisdiction under 28 U.S.C. § 1331, most farm program litigation in the federal district courts has been premised on both the APA and general federal question jurisdiction. As to the sope of review, APA § 706 provided the standards. *See* 5 U.S.C. § 706.

Premising an action in a district court on the APA's waiver of sovereign immunity and general federal question jurisdiction has not been trouble-free, however. Two difficulties have arisen. First, if the complaint expressly sought an award of the program payments allegedly improperly denied, the government routinely moved to dismiss the action or to transfer it to the Court of Federal Claims (formerly the Court of Claims) if the payments exceeded $10,000. Under the so-called "Big" Tucker Act, 28 U.S.C. § 1491, which both confers jurisdiction and waives the federal government's sovereign immunity, the Court of Federal Claims has exclusive jurisdiction over claims based in contract where the amount of monetary relief sought exceeds $10,000. Under the so-called "Little" Tucker Act, 28 U.S.C. § 1346(a)(2), the district

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Report on the Unified National Strategy for Animal Feeding Operations

On March 9, 1999, the U.S. Department of Agriculture and the Environmental Protection Agency set forth their Unified National Strategy for Animal Feeding Operations (Strategy) aimed at addressing water pollution and public health impacts from animal feeding operations (AFOs). This Strategy announces a set of guiding principles suggesting further government activity with mandatory and voluntary programs regarding AFOs. While the Strategy does not delineate a federal regulation or serve as a substitute for existing regulations, it sets the stage for appropriate actions to reduce environmental degradation from AFOs.

A perusal of the guiding principles of this Strategy identifies priorities and areas of possible governmental involvement.

1. The government seeks to minimize water quality and public health impacts from AFOs, with a focus on AFOs that represent the greatest risks to the environment and public health.

2. The government seeks to make appropriate use of diverse tools including voluntary, regulatory, and incentive-based approaches that complement the long-

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Solicitation of articles: All AALA members are invited to submit articles to the Update. Please include copies of decisions and legislation with the article. To avoid duplication of effort, please notify the Editor of your proposed article.

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- The Biosafety Protocol and the Cartegena Negotiations

courts possess concurrent jurisdiction with the Court of Federal Claims over such actions only if the monetary award sought does not exceed $10,000. Given the costs of litigation, very few actions seeking less than $10,000 have been brought in district court, and when the complaint has sought more than $10,000 the government usually has been successful in dismissing or transferring the case. *See Divine Farms, Inc. v. Block*, 679 F. Supp. 867 (S.D. Ind. 1988).

Second, even if the complaint did not seek a monetary award but instead sought only a declaratory judgment pursuant to 28 U.S.C. §§ 2201 and 2202 declaring that the plaintiff was eligible or entitled to the payments sought, the government often moved to dismiss or to transfer the action. In such cases the government contended that, in effect, the action was for money damages in excess of $10,000 since compliance with the judgment would require payment. *See, e.g., Justice v. Lyng*, 716 F. Supp. 1570 (D. Ariz. 1989). In other words, if the payments in dispute exceeded $10,000, the government often maintained that district court jurisdiction was lacking, even if the complaint did not expressly seek payment in the form of "money damages."

Whether in fact or in effect a complaint seeks "money damages" is significant because the APA § 702 does not waive sovereign immunity for actions seeking "money damages." *See* 5 U.S.C. § 702. In addition, APA § 704 contains another exception that applies to claims for which an "adequate remedy" exists elsewhere. *See* 5 U.S.C. § 704. In *Bowen v. Massachusetts*, 487 U.S. 879 (1988), however, the Supreme Court held that an action for "money damages" does not include a declaratory judgment and injunction action challenging the denial of federal entitlement payments, specifically, Medicaid reimbursements to a Medicaid provider. It also ruled that such an action was not barred by APA § 704 because the Tucker Act did not provide an "adequate remedy," in part because it authorizes only very limited injunctive relief. The rationale in *Bowen* was subsequently applied to federal farm program payments by the D.C. Circuit in *Esch v. Yeutter*, 876 F.2d 976 (D.C. Cir. 1989). Nonetheless, following the *Bowen* and *Esch* decisions, the government persisted in seeking the dismissal or transfer of declaratory judgment actions in which the payments in dispute exceeded $10,000.

In 1994, Congress authorized the Secretary to create the USDA NAD. The statutory authorization for the USDA NAD provided as follows:

> A final determination of the [National Appeals] Division shall be reviewable and enforceable by any United States district court of competent jurisdiction in accordance with chapter 7 of Title 5.

7 U.S.C. § 6999. The meaning of this provision, § 6999, was at issue in *Deaf Smith County Grain Processors* decision.

The plaintiff in *Deaf Smith County Grain Processors* commenced an action in district court expressly seeking approximately $95,000 in acreage reduction program and disaster program payments that it claimed had been improperly denied to it. The final administrative determination had been made by the USDA NAD, thus § 6999 applied. Though the district court granted summary judgment on the merits in the Secretary's favor, an issue on appeal was whether the district court possessed jurisdiction over the action. More broadly stated, the issue was whether Congress intended by enacting § 6999 to end the litigation over the proper forum for the judicial resolution of farm program disputes.

Characterizing § 6999 as a waiver of sovereign immunity, the D.C. Circuit thus had to decide the extent of its waiver. More specifically, it had to decide whether the waiver was broad enough to encompass the plaintiff's express demand for an award of approximately $95,000 in program payments.

For the D.C. Circuit, the issue turned on the meaning of the phrase "in accordance with chapter 7 of Title 5," a reference to the APA. Noting that the APA contains both limits on reviewability (e.g., §§ 702 and 704) and scope of review standards (§ 706), the court found that this language in § 6999, standing alone, allowed at least three plausible interpretations:

> To say, as § 6999 does, that final determinations of the NAD are reviewable by the district court "in accordance with" the judicial review provisions of the APA is to say one of three things: (i) that the NAD determinations are reviewable to the extent allowed by §§ 702 and 704 of the APA; (ii) that NAD determinations are reviewable under the procedures set forth in § 706 of the APA; or (iii) that NAD determinations are reviewable pursuant to all of the judicial review provisions of the APA.

162 F.3d at 1211.

Faced with an ambiguous statute, the court found little guidance in the legislative history of § 6999 as to its intent. In fact, it concluded that the legislative history was as ambiguous as the statute itself because the committee report accompanying the bill contained only the following explanation of § 6999:

> This section provides that a final determination of the [National Appeals] Division can be appealed to a U.S. District Court. Analysis of which issues are subject to judicial review shall conform with provisions of the Administrative Procedure Act (APA).

Id. at 1212 (quoting S. Rep. No. 103-241, at 15 (1994). Though it found the first sentence "quite straightforward," the court could not find a clearly discernable expression in the report's second sentence as to whether the APA's limit on review found in § 704, for example, was applicable.

Faced with both an ambiguous statute and ambiguous legislative history, the court then examined the recent history of farm program litigation, focusing on the "numerous 'thorny and frustrating' jurisdictional disputes" over whether such actions should be brought in the district courts under the APA's waiver of sovereign immunity or in the Court of Federal Claims pursuant to the Tucker Act's waiver of sovereign immunity. It concluded that it was "[a]gainst this back-

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AALA Editor..........................Linda Grim McCormick
Rt. 2, Box 292A, 2816 C.R. 163
Alvin, TX 77511
Phone: (281) 388-0155
FAX: (281) 388-0155
E-mail: lgmccormick@teacher.esc4.com

Contributing Editors: Terence J. Centner, The University of Georgia, Athens, GA; Susan A. Schneider, University of Arkansas, Fayetteville, AR; Christopher R. Kelley, University of Arkansas, Fayetteville, AR; Roger A. McEowen, Kansas State University; Drew L. Kershen, Norman, OK.

For AALA membership information, contact William P. Babione, Office of the Executive Director, Robert A. Leflar Law Center, University of Arkansas, Fayetteville, AR 72701.

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term sustainability of livestock production in the United States.

3. Through regulations, the government proposes to establish a national goal and environmental performance expectation for all AFOs.

4. The government seeks to focus technical and financial assistance to support AFOs in meeting the national performance expectation established in this Strategy.

A national performance expectation that all AFOs should implement an economically feasible Comprehensive Nutrient Management Plan (CNMP) is the underlying basis for the Strategy. A CNMP identifies actions or priorities that will be followed to meet clearly defined nutrient management goals at an agricultural operation.

CNMPs are expected to address feed management, manure handling and storage, land application of manure, land management, record keeping, and management of other utilization options. They will be site-specific, written to address the goals and needs of the individual owner/operator, and revised whenever a facility increases in size or changes its method of manure management. After considering the pertinent factual information, a CNMP can embody a schedule to implement management practices that protect water quality and public health.

CNMPs are expected to be mandatory for less than five percent of AFOs, those subject to an National Pollutant Discharge Elimination System permit under the Clean Water Act, and voluntary for other AFOs. The development and implementation of a CNMP are the responsibilities of the AFO operator, with assistance as needed from government agency specialists, private consultants and other qualified vendors.

The Natural Resources Conservation Service Field Office Technical Guide is the primary technical reference for the development of CNMPs for AFOs. This Technical Guide contains technical information about utilization and conservation of soil, water, air, plant, and animal resources, and is localized to consider particular characteristics for the geographic area for which it is prepared. It is intended that CNMPs encourage and facilitate technical innovation and new approaches to manure and nutrient management.

—Terence J. Centner, The University of Georgia, Athens, GA

Short term Chapter 12 extension — again

On March 30, 1999, Congress once again passed a short term extension to the provisions of Chapter 12 of the Bankruptcy Code, 11 U.S.C. §§ 1201-1231. Extension of Reenactment of Chapter 12, Family Farmers Indebtedness, Pub. L. No. 106-5, 113 Stat. 9 (1999). This extension provides that Chapter 12 will remain available to eligible family farmers until October 1, 1999.

Chapter 12, *Adjustment of Debts of a Family Farmer with Regular Annual Income*, was first enacted in October 1986. Bankruptcy Judges, United States Trustees and Family Farmer Bankruptcy Act of 1986, Pub. L. No. 99-554, tit. II, § 255, 100 Stat. 3088, 3105-3113 (1986) (codified at 11 U.S.C. §§ 1201 - 1231). Originally, it had a sunset provision that provided for repeal on October 1, 1993. Pub. L. No. 99-554, tit. III, § 302(f), 100 Stat. 3088, 3124 (1986). On August 6, 1993, Chapter 12 was extended for another five years. Pub. L. No. 103-65, 107 Stat. 311 (1993). Chapter 12 officially sunset on October 1, 1998, but it was resurrected with a six month retroactive extension as part of an omnibus appropriations bill passed later in October. Omnibus Consolidated and Emergency Supplemental Appropriations Act, Pub. L. 105-277, div. C, tit. 1, § 149, 112 Stat. 2681, 2681-610-11 (1999). This extension was set to expire on April 1, 1999.

There appears to be substantial support in Congress for legislation that would make Chapter 12 a permanent part of the Bankruptcy Code. *See* 145 Cong. Rec. H1033-36 (daily ed. Mar. 9, 1999) (statements of Rep. Gekas, Rep. Baldwin, Rep. Bereuter, Rep. Etheridge, Rep. Smith, Rep. Nadler, Rep. Jackson-Lee). This legislation, however, has become mired in the controversial bankruptcy reform issue. Proponents of pending reform legislation have sought to tie the permancy of Chapter 12 to this reform.

—Susan A. Schneider, Assistant Professor of Law, University of Arkansas

NAD Appeals/*Cont. from page 2*

drop" that Congress created the "'new'" NAD in 1994, replacing its predecessor, the ASCS NAD. *Id*. at 1213. The court then reasoned that Congress probably intended to remedy the jurisdictional confusion "that reigned prior to the creation of the new NAD...." *Id*. That is, in the court's words, "although the evidence is not overwhelming and the language of the statute is far from unambiguous, it appears that the purpose of § 6999 was to simplify appeals from the NAD by placing jurisdiction over them solely in the district court." *Id*. Accordingly, the court held that the district court had jurisdiction over the case. On the merits, however, the court affirmed the district court.

If followed in the other circuits, the *Deaf Smith County Grain Processors* decision will have closed a chapter in federal farm program litigation. The only forum for the review of USDA NAD determinations, by choice or otherwise, will be the federal district courts, even if the complaint expressly seeks the program payments allegedly improperly denied. However, as the decision makes evident, the intent of § 6999 is not altogether clear.

—Christopher R. Kelley, Assistant Professor, University of Arkansas School of Law. Of Counsel, Vann Law Firm, Camilla, GA

Minimum interest rules and installment sales of farmland among family members—what is a fair market rate of interest for gift tax purposes?

By Roger A. McEowen

Overview of the problem

It is believed that a large amount of farm and ranch assets will change hands in the next decade. Undoubtedly, some of the transfers will involve sales and other types of dispositions among family members. Several options exist for the transfer of agricultural real estate during life. For instance, the land could be transferred under a private annuity arrangement,[1] by means of a self-canceling installment note, by virtue of a cash transaction with the proceeds then reinvested in other assets, or the land could be sold in a transaction qualifying for installment reporting of gain.[2] If the residence is sold with the land, the gain on sale attributable to the residence may be eligible for exclusion.[3]

While there are numerous factors to consider when selling farm or ranch land during life,[4] one factor that may be overlooked is the gift tax implication upon installment sale of the farmland to family members if the interest rate specified in the contract is deemed by the Internal Revenue Service (Service) to be inadequate. A recent decision of the Federal District Court for the Northern District of New York[5] has again raised the question of what rate of interest in such contracts avoids the creation of a gift.

Interest rate sensitivity

The interest rate selected for installment sale obligations is important to both sellers and buyers. Sellers generally prefer a lower interest rate coupled with a higher sale price. Interest is taxable as ordinary income, but the additional gain from the higher sales price is taxable as capital gain.[6] Buyers, on the other hand, tend to prefer higher interest rates and a lower selling price. Interest is income tax deductible, but principal payments are nondeductible except to the extent the principal payments represent depreciable or depletable property. Thus, in situations where the seller's objectives dominate the negotiation process (which may be likely in situations where both the seller and the buyer are family members), the Congress has specified minimal limits on interest rates for installment sale obligations to prevent sellers from converting what would otherwise be ordinary income into capital gain.

Minimum interest rules and the I.R.C. § 483 safe harbor

If the minimum interest rules are triggered and the sale results in capital gain to the seller, a part of each principal payment is treated as interest rather than principal and the total sales price is correspondingly reduced.[7] Section 483(e) fixes imputed rates for qualified intrafamily installment sales of real estate at six percent. The six percent rate may be used for sales of less than $500,000 in one calendar year between related parties.[8] If the sale produces ordinary income only, the minimum interest rules do not apply,[9] and the purchaser is entitled to deduct a portion of each payment as interest and no interest amount is imputed to the seller.[10] The purchaser must reduce the income tax basis in the asset by the total amount allocated to interest during the term of the obligation.[11] However, if the gain on sale is capital gain, the minimum interest rules apply,[12] and a portion of each payment is treated as additional interest with a corresponding reduction in principal.[13] In that event, the additional interest amount is a deduction for the purchaser, and the purchaser's income tax basis in the asset is reduced by the amount considered to be interest expense.[14]

Gift tax implications of I.R.C. § 483?

A significant question is whether the minimum interest rules of I.R.C. § 483 apply for gift tax as well as income tax purposes. The federal gift tax is imposed on outright gifts made during life.[15] For example, an option for purchase of land at less than fair market value that is enforceable under state law is a gift at the time the option is transferred.[16] Likewise, the gratuitous transfer of a legally binding promissory note is a completed gift.[17] Even interest-free loans payable on demand to family members have been held to be subject to federal gift tax.[18] The value of a gift is the difference between the fair market value of the property transferred and the consideration received.[19] For installment contracts, the computation of the gift, if any, requires discounting the value of the compensation the seller receives over the contract term by the interest rate established in the contract.

Before legislation enacted in 1984, the Service announced that, for interest-free demand loans made before 1984, donors could compute the value of the gifts by using the I.R.C. § 6621 rate or the average annual rate for three-month Treasury Bills.[20] For term loans made after June 6, 1984, and demand loans outstanding on June 6, 1984 (except for demand loans repaid within 60 days after July 18, 1984), low-interest and no-interest loans are treated as arm's length transactions.[21] Interest-free and low-interest demand gift loans outstanding after June 6, 1984, are subject to the rules of I.R.C. § 7872. The rules apply to gift loans, compensation-related loans, corporate-shareholder loans, tax avoidance loans and other types of loans with interest charged below the applicable federal interest rate.[22] For gift loans, where the interest foregone is in the nature of a gift, uncharged interest on interest-free or below market interest rate loans represents a transfer by gift to which federal gift tax provisions apply. In essence, the maker of a demand loan is deemed to have made an annual gift of the uncharged interest up to the statutory federal rate. The maker of a term loan is considered to have made a gift on the date of the loan equal to the excess of the loan amount over the present value of all payments required to be made under the terms of the loan. Uncharged interest is imputed as income to the lender and as a deductible expense to the borrower.[23] For gift tax purposes, a term loan is deemed to be a demand loan. Historically, I.R.C. § 483 has provided a safe harbor at a lower discount than the I.R.C. § 7872 rates. While I.R.C. § 7872 generally applies to the income, gift and estate tax treatment of loans, it expressly does not on its face apply to transactions covered by I.R.C. § 483 and to installment sale contracts subject to I.R.C. § 1274.[24]

Caselaw developments

In a case arising before the 1984 legislation creating I.R.C. § 7872, the seller entered into a contract with the seller's three children with the contract providing that the children would each receive a one-third interest in her 286-acre farm.[25] The farm's fair market value was

Roger A. McEowen is Associate Professor of Agricultural Law at Kansas State University.

$582,000. The contract specified a $386,000 selling price and a six percent interest rate. The seller filed a gift tax return reporting a gift of the difference between the fair market value of the farm and the face value of the consideration the seller was to receive from the children under the contract. The seller covered the resulting gift tax with unified credit and reported zero gift taxes due. The Service issued a notice of deficiency, determining that the discounted value of the consideration the seller was to receive under the contract was only $134,298.20 because the market rate of interest was 18% rather than the six percent contract rate.[26] Thus, the Service argued that the difference between the market value of the property and the discounted value of the contract at 18% represented an actual gift of $437,701.80 to the children.

In the Tax Court, the seller argued that I.R.C. § 483 provided a "safe harbor" permitting the use of a six percent rate of interest on the contract without either income or gift tax consequences.[27] The Service disagreed, contending instead that I.R.C. § 483 applied only to income taxes. The Tax Court agreed with the Service, but the Seventh Circuit reversed on appeal.[28] The Seventh Circuit based its reversal upon the use of the language in I.R.C. § 483(a) stating that the section applied "for purposes of this title" The court construed the word "title" as a reference to *all* provisions of the Internal Revenue Code (title 26 of the U.S. Code). Thus, any qualified sale satisfying the requirements of I.R.C. § 483 could utilize the six percent safe harbor rate of I.R.C. § 483(e)(1) for both income and gift tax purposes.[29]

In another case involving a tax year before enactment of I.R.C. § 7872, a Minnesota farm couple transferred land to their sons by means of a contract for deed.[30] The contract provided for a purchase price of $400,000, an interest rate of six percent and thirty annual payments of $29,060. The parents, relying on the Seventh Circuit's opinion in *Ballard,*[31] argued that even if I.R.C. § 483 did not apply, that the Service had incorrectly used an eleven percent interest rate to determine the 1981 present value of the contract because a six percent rate was consistent with rates for similar types of transactions at the time. The Tax Court disagreed with the parents on both point[32] In addition, the Tax Court expressly refused to follow the Seventh Circuit's opinion in *Ballard*, determining that *Ballard* was wrongly decided and noting that the present case was not appealable to the Seventh Circuit. On appeal, the Eighth Circuit Court of Appeals affirmed the Tax Court, noting that I.R.C. § 483 operates to recharacterize certain amounts of installment or deferred payments as interest and was irrelevant for gift tax valuation purposes[33] The Eighth Circuit affirmed, noting that the Service may rely on rates for similar transactions and that the rate at the Minnesota office of the Federal Land Bank at the time was 10.75 percent[34] Also, neither the Seventh Circuit in *Ballard* or the Eighth Circuit in *Krabbenhoft* took into account the legislative history of I.R.C. § 483 indicating congressional intent that the I.R.C. § 483(e) safe harbor should apply for estate and gift tax as well as income tax purposes.[35]

In *Frazee v. Commissioner*[36] a case involving a tax year after enactment of I.R.C. § 7872, the taxpayers sold 12.2 acres of improved real property to their children for a note bearing six percent interest and payable in twenty annual installments.[37] The Tax Court stressed that in valuing the contract for gift tax purposes, the appropriate discount rate is supplied by I.R.C. § 7872 rather than I.R.C. § 483 or I.R.C. § 1274. The court noted that I.R.C. § 7872 applied specifically to gifts and that both I.R.C. § 483 and I.R.C. § 1274 applied only to income tax issues. While the court noted that the Service's proposed regulations under I.R.C. § 483 specifically allowed the six percent safe harbor interest rate for gift tax purposes[38] the court stated that it considered proposed regulations as no more than a litigation position and that the Service had later abandoned the position that it had taken in the proposed regulations in a General Counsel's Memorandum[39] Accordingly, the Tax Court held that the value of promissory note had to be recomputed using the federal rate for long-term loans compounded semi-annually, with quarterly payments at the time the taxpayers conveyed the property to their children.[40] At the time, the applicable federal rate was substantially higher than six percent.

In *Schusterman v. United States*[41] another case involving a transaction entered into before the enactment of I.R.C. § 7872, the Tenth Circuit followed the Eighth Circuit's opinion in *Krabbenhoft* and held that donors may not rely on the I.R.C. § 483 safe harbor for gift tax purposes. The case involved the valuation of gifts resulting from transfers of stock to trusts in exchange for promissory notes. The *Schusterman* court determined that such gifts are demand loans and utilized the IRS rate of 11.5% in accordance with Rev. Proc. 85-46.[42]

In the most recent case involving the issue[43] the taxpayer, in 1979, sold 6,894 shares of common capital stock for a purchase price of slightly over $1 million to an irrevocable trust created for the benefit of her lineal descendants. Pursuant to the sale agreement, the trust was to pay the purchase price in eighty equal quarterly installments, and to pay interest with each quarterly installment on the unpaid balance of the purchase price at six percent per annum. The prevailing market rate for a twenty-year note at the time of sale was 8.8 percent. The Service concluded that the installment sale at the lower rate constituted a taxable gift, and the court agreed.

Estate planning implications

It appears that there is little room to argue (outside the Seventh Circuit) that the six percent safe harbor rate of I.R.C. § 483 applies for gift tax valuation of an installment contract. Thus, a market rate of interest must be utilized to avoid the creation of a gift upon execution of the contract, with the rate tied to the Applicable Federal Rate as specified monthly in accordance with I.R.C. § 7872. When market rates in the economy again rise significantly above the six percent level, an incentive may be present to utilize a below-market rate of interest, especially in contracts involving family members. In that event, one option may be to utilize a variable rate of interest tied to an index such that a market rate comparable to the Service's rate is assured. Indeed, this may be the only way for taxpayers engaging in long-term installment sales during periods of high rates to complete a transaction in a manner that is both affordable for the buyer and safe from gift tax assessment.

In any event, installment sales should be routinely reviewed for potential gift tax exposure and the related reduction in the seller's unified credit. Also, estate tax consequences should be considered. In the Seventh Circuit, arguably the full face value of the contract is taxable for estate tax purposes without discount for the difference between the six percent rate and the prevailing market rate at the time the contract was entered into. Elsewhere, it appears that installment contracts will be valued at fair market value for both estate and gift tax purposes.

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[1] See generally 7 Harl, *Agricultural Law*, Ch. 49 (1998).

[2] I.R.C. section 453.

[3] I.R.C. section 121. Legislation has been proposed that would broaden the scope of I.R.C. § 121 to provide an exclusion for gain attributable to the sale of farmland. "Qualified farm property" is defined as any real property located in the United States that the taxpayer or

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member of the family used as a farm for farming purposes and the taxpayer or family member materially participated in the farm's operation for at least three out of five years immediately preceding the date of sale. H.R. 1503, 106th Cong. 1st Sess. ___ (1999).

[4] These factors include the projected income tax liability upon sale, the potential effects of inflation (or deflation) on income and principal from the sale, the desirability of "freezing" the landowner's estate, the landowner's willingness to manage the property, and the qualification requirements for post-mortem planning techniques as well as certain other noneconomic factors.

[5] *Lundquist v. United States*, No. 1:96-CV-0725, 1999 U.S. Dist. LEXIS 3042 (N.D. N.Y. Feb. 23, 1999).

[6] For sales after May 6, 1997 and before July 29, 1997, for property held more than one year, individuals in the 15% marginal income tax bracket are subject to a 10% capital gain rate while those in higher brackets are subject to a 20% rate. For sales after July 28, 1997 and before January 1, 1998, involving property held more than one year, but eighteen months or less, the capital gain tax rate is 15% for those in the 15% tax bracket and 28% for those in higher brackets. For property held more than eighteen months, the capital gain tax rate is 10% for those persons in the 15% tax bracket and 20% for those in higher brackets. For sales after December 31, 1997, for individuals in the 15% marginal income tax bracket and for property that has been held more than one year, the applicable long-term capital gain tax rate is 10%. For those individuals in higher marginal brackets, the applicable long-term capital gain tax rate is 20%.

[7] I.R.C. § 483.

[8] I.R.C. § 483(e).

[9] I.R.C. § 483(f)3). See also Rev. Rul. 82-124, 1982-1 C.B. 89.

[10] Treas. Reg. § 1.483-2(b)(3)(ii).

[11] Rev. Rul. 82-124, 1982-1 C.B. 89.

[12] Treas. Reg. § 1.483.

[13] See Rev. Rul. 82-124, 1982-1 C.B. 89.

[14] *Id.*

[15] See, e.g., *Warda v. Commissioner*, T.C. Memo. 1992-43, *aff'd*, 15 F.3d 533 (6th Cir. 1994), *cert. denied*, 513 U.S. 808 (1994)(gifts at time deeds to farmland executed and recorded rather than on earlier execution of contract; but gift occurred on execution of contract for one parcel because of indication donor intended to then give up dominion and control).

[16] Rev. Rul. 80-186, 1980-2 C.B. 280.

[17] Rev. Rul. 84-25, 1984-1 C.B. 191.

[18] See *Dickman v. Commissioner*, 465 U.S. 330 (1984).

[19] Because gift taxation seeks to avoid untaxed depletion of the donor's estate, transfers for inadequate consideration constitute gifts for gift tax purposes. See, e.g., *Commissioner v. Wemyss*, 324 U.S. 303 (1945); *Merrill v. Fahs*, 324 U.S. 308 (1945).

[20] I.R. 84-60, May 11, 1984.

[21] Tax Reform Act of 1984, Sec. 172, 98th Cong., 2d Sess. (1984).

[22] See, e.g., Kta-Tator, Inc., 108 T.C. 100 (1997)(demand loans made by closely-held corporation to sole shareholders to build facilities to be leased to corporation; each advance treated as separate loan and subject to below-market interest rate.

[23] There is an exclusion for loans if the aggregate outstanding amount of all loans from the lender to the borrower does not exceed $10,000 and if the proceeds of the loan are not used to buy incomd producing assets. I.R.C. § 7872(c)(2).

[24] Section 7872(f)(8); Prop. Treas. Reg. § 1.7872-2(a)(2)(ii).

[25] *Ballard v. Commissioner*, 854 F.2d 185 (7th Cir. 1988).

[26] Because the Service determined that the market rate of interest was 18%, the Service discounted the $386,000 selling price to reflect an 18% interest rate. As a result, the discounted value of the consideration the mother was to receive under the contract was $134,298.20.

[27] T.C. Memo. 1987-128.

[28] 854 F.2d 185 (7th Cir. 1988).

[29] I.R.C. section 483(e)(2) specifies that a qualified sale is any sale or exchange of land by an individual to a member of such individual's family.

[30] *Krabbenhoft v. Commissioner*, 939 F.2d 529 (8th Cir. 1991).

[31] 854 F.2d 185 (7th Cir. 1998).

[32] *Krabbenhoft v. Commissioner*, 94 T.C. 887 (1990).

[33] *Krabbenhoft v. Commissioner*, 939 F.2d 529 (8th Cir. 1991).

[34] Interestingly, the Eighth Circuit in *Krabbenhoft* did not consider the issue of whether the gift under the contract was "up front" and was a present interest or was a future interest. However, in *Deal v. Commissioner*, 29 T.C. 730 (1958), an installment sale with forgiveness of all payments was deemed to be a gift ab initio and was a future interest.

[35] See Conf. Rep. to ERTA and H.R. Rep. No. 215, 97th Cong., 1st Sess. 281 (1981).

[36] 98 T.C. 554 (1992).

[37] The sellers had been growers and worldwide distributors of flower bulbs for more than 50 years and wished to retire from the flower farming business.

[38] Treas. Reg. § 1.483-(b)(2).

[39] G.C.M. 39,566 (Oct. 23, 1986)(taxpayer conveyed farm to children in 1981 in a part sale, part gift transaction receiving a note payable over a fixed term of years with interest at six percent.

[40] See I.R.C. § 7872(f)(2)(A).

[41] 63 F.3d 986 (10th Cir. 1995).

[42] 1985-2 C.B. 508. Under Rev. Proc. 85-46, a taxpayer may value the gift resulting from an interest-free loan by multiplying the average outstanding loan balance for the calendar period by the difference between the rate of interest on the loan and the interest rate for the applicable year provided in the table.

[43] *Lundquist v. United States*, No. 1:96-CV-0725, 1999 U.S. Dist. LEXIS 3042 (N.D. N.Y. Feb. 23, 1999).

UCC Articles 7 & 9 versus the Federal Warehouse Receipt Act

In 1997, Thomas Hendrix of Statesboro, Georgia grew his cotton using a loan from Agricredit Acceptance LLC. In making the loan, Agricredit took a perfected security interest against the cotton. [Ga. Stat. §§ 11-9-203 and 11-9-401.] Agricredit also filed direct notice with Sea Island Cotton Trading Company to protect its security interest in the Hendrix cotton against buyers, commission merchants, and selling agents. [7 U.S.C. § 1631.]

When Hendrix harvested his cotton, warehouses stored the cotton under electronic warehouse receipts as authorized by federal law. [7 U.S.C. §259.] Sea Island purported to sell the Hendrix cotton to various cotton merchants. Shortly thereafter, Sea Island Cotton went bankrupt.

Agricredit filed a law suit seeking to foreclose against the Hendrix cotton, to enjoin the transfer of the Hendrix cotton from the warehouses to the cotton merchants, and for conversion and damages for any Hendrix cotton that the cotton merchants had already received from the warehouses.

In response to the Agricredit law suit, the cotton merchants sought a summary judgment claiming that the United States Federal Warehouse Act provision authorizing electronic warehouse receipts preempted Agricredit's claims under Article 9 of the Georgia Uniform Commercial Code. The cotton merchants argued that 7 U.S. C. § 259 provided the only method for determining possessory rights in cotton.

In *Agricredit Acceptance, LLC v. Hendrix*, 1998 U.S. Dist. LEXIS 20595, 1998 WL 928547 (S.D. Ga.), the District Court ruled against the cotton merchants. Judge John Nangle ruled that Congress did not intend to preempt the UCC when it passed 7 U.S.C. § 259 authorizing

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—Drew L. Kershen, Professor of Law, The University of Oklahoma, Norman, OK

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federal and state warehouses to use electronic warehouse receipts. Judge Nangle interpreted the 1992 amendments to the Federal Warehouse Act to allow state UCC law to control the priority between competing claims to cotton under electronic warehouse receipts. He determined that 7 U.S.C. § 259 places electronic warehouse receipts on a parity with paper receipts and that the Georgia UCC governs for purposes of priority.

As for how the Georgia UCC resolves the dispute between Agricredit's Article 9 security interest and the cotton merchants' claim to the cotton based on the electronic warehouse receipts, Judge Nagle ruled that the record before the court provided insufficient evidence to resolve issues of due negotiability under Ga. Stat. §§ 11-7-501 and 11-7-503.

—Drew L. Kershen, University of Oklahoma, Norman, OK