

# Olson Ag Law Update

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**This issue of Olson Ag Law Update looks at tax saving IC-DISC corporations and crop insurance “good farming practices” appeals.**



## **IC-DISC CORPORATIONS SAVE TAXES**

**In Georgia, farmers now export a significant percentage of their cotton and pecan crops. Any producer growing these or any other export crops should consider using an IC-DISC corporation to reduce the federal income tax owed on these sales.**

**The Internal Revenue Code permits a farmer (or anyone who sells virtually any type of goods abroad) to set up an IC-DISC (Interest Charged – Domestic International Sales) corporation. Use of the corporation permits a farmer to pay taxes on approximately one-half of the farmer’s export sales at the federal qualified dividend rate rather than at higher ordinary income rates.**

**This can result in substantial savings. Under the tax law enacted in December, taxpayers in the 25% through 35% ordinary income tax brackets continue to pay only 15% on qualified dividends. Taxpayers in the new 39.6% ordinary income bracket pay 20% on dividends.**

**As an example, if a farmer in the 35% bracket has a \$200,000 profit on export sales, the farmer will pay roughly \$70,000 in tax if the entire amount is treated as ordinary income. However, by using an IC-DISC corporation, \$100,000 of the profit will be taxed at 15% and \$100,000 at 35%, for a total tax of \$50,000, thus saving the farmer \$20,000.00.**

**Mechanically it works this way. The farmer pays the IC-DISC corporation a commission for acting as the farmer’s “broker” of the export crops – usually 50% of the profits on the export sales. The corporation then distributes the commission back to the farmer as a dividend. The corporation pays no tax on the commission received, and the farmer pays the dividend rate on the dividend the farmer receives from the corporation. The corporation does not have to perform any actual brokerage activities. The corporation is used simply as an accounting mechanism. The farmer sells his or her crop in the same manner and using the same brokers as the farmer always has.**

**The farmer does not have to sell the crops directly to a foreign buyer. They may pass through any number of intermediaries as long as they eventually end up overseas. It is important, however, that the farmer be able to document where the crops were finally delivered.**

**The Code and IRS regulations set forth a number of requirements that the corporation must satisfy to qualify as an IC-DISC corporation. These include a minimum capitalization and the filing of an election to be treated as an IC-DISC corporation on IRS form 4876.**

**The corporation must be created, and the minimum capital deposited in its bank account, before crop sales will qualify for IC-DISC treatment. Crops may be contracted to be sold prior to setting up the corporation, but the corporation must be in existence prior to the contract being filled and the crops shipped from the warehouse. Farmers who wait**

until the end of the year to set up an IC-DISC corporation will not be able to take advantage of its benefits for crops sold in that year.

Please note that the ownership of the IC-DISC corporation should be the same as the ownership of the underlying farming operation to avoid losing farm program payments.

The IRS IC-DISC regulations are found at 26 C.F.R. § 1.991-1, Treas. Reg. § 1.991-1.

### **WHEN CROP INSURANCE CLAIMS GO BAD** **CROP INSURANCE GOOD FARMING PRACTICES APPEALS**

Crop insurance provides a crucial risk management tool for most farm operations today. It is likely to become even more important in the future as other farm subsidies are cut back or eliminated.

But, bad farming practices, real or perceived, can scuttle a crop insurance claim, leaving a farmer with no compensation for lost yields and revenues. Your crops may have endured the worst drought in history or washed away in an antediluvian flood, but if the crop insurance company or USDA's Risk Management Agency finds that you failed to follow "good farming practices," you may not be paid.

And, bad farming practices may not always be what they seem. They certainly include failing to use enough seed or fertilizer, not putting enough water on irrigated crops, and allowing weeds to take over your fields. They may also include, in the eyes of the company or RMA, farming practices that you have used successfully for years or innovative practices that are not fully known or accepted in the agricultural community. Not only "insurance farmers" can be tagged with a "bad farming practices" label. Legitimate farmers can be as well.

"Good farming practices" are defined in crop insurance policies as:

The production methods utilized to produce the insured crop and allow it to make normal progress toward maturity and produce at least the yield used to determine the production guarantee or amount of insurance, including any adjustments for late planted acreage, which are: (1) for conventional and sustainable farming practices, those generally recognized by agricultural experts for the area; or (2) for organic farming practices, those generally recognized by the organic agricultural industry for the area or contained in the organic plan.

If you can't find an expert to say you followed good farming practices, or if the company or RMA prefers their expert's opinion over your expert's opinion, your claim may be denied. If your claim is denied, you have certain appeal rights, but the appeal must



**be handled correctly if you are to have any chance of overturning the bad farming practices decision.**

**The denial usually comes in the form of a letter from your crop insurance company. The letter will often describe how the company consulted with RMA in making the decision and then will give you your appeal rights. Even if the letter does not set out appeal rights, you still have them under the terms of the policy and RMA regulations. Frequently the company will have discussed the bad farming practice issue with you prior to sending the letter.**

**Your appeal rights are as follows. First, you must ask RMA to review the company's bad farming practices decision. This review is conducted by the RMA Regional Office based on written information that you submit and other information that RMA obtains from the company and its own experts. No hearing is held.**

**If the RMA Regional Office upholds the company's decision, you may request reconsideration of the RMA decision by the Federal Crop Insurance Corporation in Washington. Again, reconsideration is based on written submissions only with no opportunity for a hearing.**

**If FCIC upholds the Regional Office, you may then appeal the decision to the Federal District Court for the district in which your farm is located. But here is the rub. The appeal to the District Court is a record review only. The Court looks at the written record developed by RMA to support its bad farming decision, including information that you submitted to RMA and FCIC. The Court will not hear any oral testimony or receive additional written reports. It can only receive legal arguments based on the written record submitted by RMA. There is no jury trial.**

**It is thus very important that you submit all the evidence and expert reports that you have supporting your use of good farming practices to RMA and FCIC as part of the review and reconsideration process. You will not have a chance to add to the record later. Furthermore, the reports must come from recognized experts.**

**Agricultural experts accepted by RMA include persons employed by the Cooperative Extension System, the agricultural departments of States and of universities, and persons certified by the American Society of Agronomy, the National Alliance of Independent Crop Consultants, or the American Society for Horticultural Sciences. RMA will not consider the opinions of other farmers. You should get reports from as many qualified experts as possible. You should get these reports as soon as you have any indication of a possible bad farming practices issue. The longer you wait the harder it will be for an expert to evaluate your farming practices. You also risk having RMA consult that expert first.**

**RMA review must be requested in writing. The regulations do not set a specific time limit for requesting review, but RMA guidance documents require that such request be**

**made no later than 30 days after receiving the bad farming practices denial letter from the insurance company. Wait too long and your appeal may be rejected.**

**Reconsideration by FCIC must be requested in writing no more than 30 days following the RMA bad farming practices determination. This deadline is in the regulations. However, while RMA review is a prerequisite for filing suit later in Federal Court, FCIC reconsideration is optional.**

**Suit must be filed in the Federal District Court no later than one year after the RMA determination or the FCIC reconsideration, whichever is later. This deadline is mandatory. If you miss it, the appeal will be dismissed, and the denial will stand.**

**In Federal Court, the farmer must prove that the RMA and FCIC decisions were “arbitrary and capricious.” This is a tough standard, but it can sometimes be met if you have submitted good expert opinions to RMA. Representing yourself in these appeals is not recommended. Competent counsel should be hired not only for the Federal District Court action but for the RMA review and FCIC reconsideration process as well.**

**Farmers would also be well advised to consult with their crop insurance companies whenever they think a particular farming practice might be questioned in the event of a crop loss. You should request that the company document in writing its approval of your use of that practice. Don’t rely on the agent’s or adjuster’s oral statement that such practice is OK. Avoiding a bad farming practices issue is almost always easier and less costly than fighting one after the fact.**

### **OLSON AG LAW PRACTICE AREAS**

**Most of you know that I do a lot of work on farm program matters including payment limitations planning, USDA administrative appeals and federal litigation. You may not know that my practice also includes the following:**

- Water Law**
- Crop insurance arbitration and litigation.**
- Conservation easement planning and drafting.**
- Perishable Agricultural Commodities Act litigation.**
- Farm finance planning and litigation.**
- Chapter 12 farm bankruptcies.**
- Farm transition (estate) planning.**

- **Representation of farmers in commercial disputes including landlord tenant matters.**
- **Advice and representation on other specialized areas of agricultural law.**

**Please give me a call if you think I may be able to help you with any of these matters.**

**Disclaimer: All of the information provided in this Update is of a general nature and may not be applicable to your farming operation, transaction or dispute. This information should not be substituted for advice from a competent attorney who is familiar with the specific facts of your case, transaction or situation.**