



Ag Decision Maker

A Business Newsletter for Agriculture

Vol. 6, No. 3

January 2002



2002 Crop insurance update—Results from 2001

by William Edwards, extension economist, 515-294-6161, wedwards@iastate.edu

Declining corn and soybean prices from February 2001 to harvest time coupled with spotty yields and late planting in southeast Iowa resulted in significant crop indemnity payments to Iowa farmers in 2001. The ratio of indemnity payments to total premiums was 44 percent, the highest since 1998. After subtracting the federal share of crop insurance premiums, farmers received indemnities equal to 95 percent of the premiums they paid as shown in Figures 2 and 3.

Revenue Assurance policyholders actually received more dollars in indemnity payments than they paid in premiums, while CRC policies were slightly below breakeven. Note that Group Risk Plan (GRP) indemnities haven't been determined yet, pending estimation of county average yields.

Guarantee level	Corn	Soybeans
85 %	0 %	9 %
75 %	10 %	20 %
65 %	22 %	31 %

what percent of yield loss below the APH yield would have been required to receive an indemnity payment at other guarantee levels.

For 2002 the fall futures price used to calculate the actual revenue for corn will be the average of the December contract price during October instead of November.

continued on page 2

Handbook Updates

For those of you subscribing to the *Ag Decision Maker Handbook*, the following updates are included.

2002 Iowa Crop Production Cost Budgets — File A1-20 (13 pages)

Farmland Lease Contract— File C2-06 (2 pages)

Please add these files to your handbook and remove the out-of-date material

Revenue insurance

The February 2001 futures prices that were used to calculate the guarantees for Crop Revenue Coverage (CRC) and Revenue Assurance (RA) were \$2.46 for corn and \$4.67 for soybeans. The fall futures prices used to calculate the actual revenue in 2001 were \$2.05 for corn and \$4.37 for soybeans. Thus, the increasing coverage feature of CRC and RA-harvest price optional policies did not go into effect this year. Corn producers who purchased revenue insurance at the 85 percent level and achieved yields equal to their APH yield received a small payment based solely on the price decline. The table above shows

Inside . . .

Handling joint tenancy
at death Page 3

Building your brand..... Page 4

Applying the new capital
gains rules Page 6

2002 Crop insurance update—Results from 2001, continued from page 1

Actual Production History (yield) Insurance

APH indemnity prices for 2002 are not available yet. They likely will be close to the levels set for the past two years:

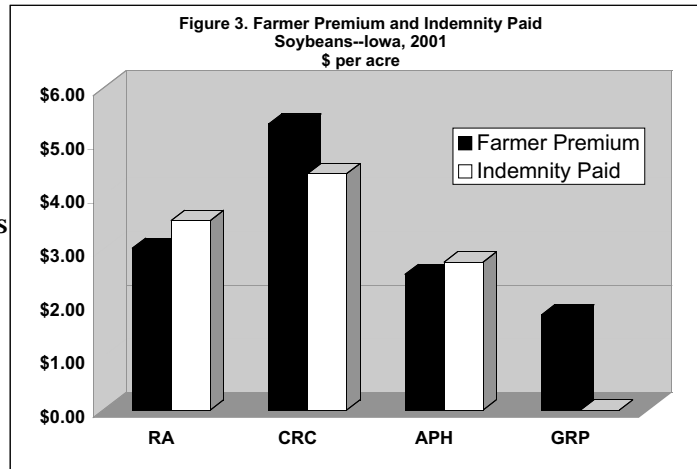
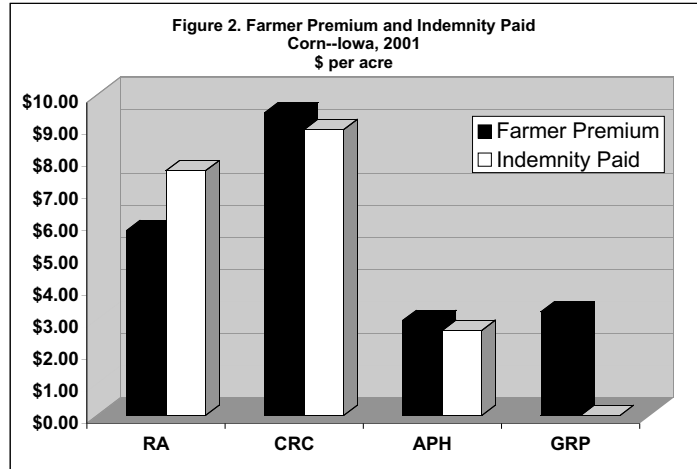
	Corn	Soybeans
2000	\$1.90	\$5.16
2001	\$2.05	\$5.26

Premiums

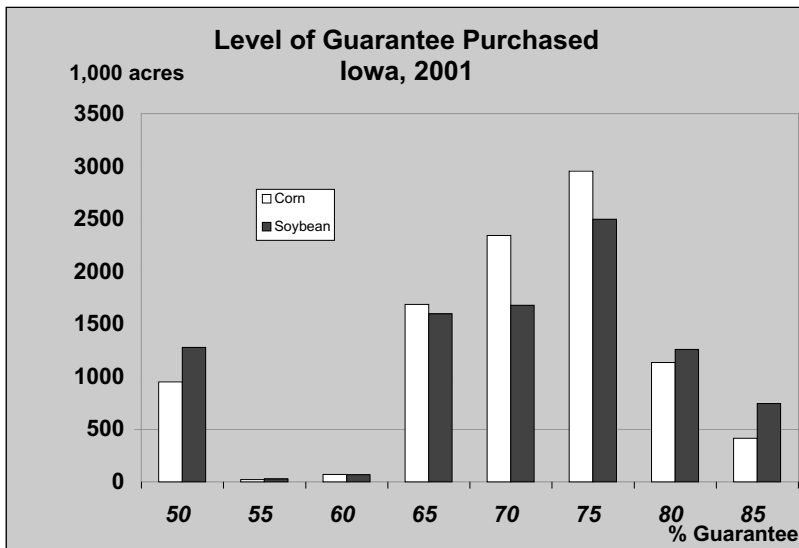
Higher coverage rates mean higher premiums. As a general rule, increasing the guarantee from 65 percent to 75 percent will about double the premiums, and increasing it from 75 percent to 85 percent will double it again. The federal subsidy (percent) is lower for higher levels of coverage. Figure 1 shows the coverage levels chosen by Iowa producers in 2001. The 50 percent coverage level was mostly from catastrophic policies.

Points worth remembering for 2002

- The USDA loan rate (LDP or marketing loan) sets a price floor near or above insurance rates, especially for soybeans.
- If yields are low and prices go up:
 - CRC or RA-optional give the most \$ coverage
 - MPCI is next
 - Standard RA gives the least protection
- If yields are average or better and prices don't rise, standard RA will give the same guarantee as optional RA or CRC, but often at a lower premium.



- The futures price for corn used to calculate RA and CRC guarantees has been above the APH indemnity price, but the futures price for soybeans has been considerably lower than the APH indemnity price. This makes APH insurance relatively more attractive for soybeans, and revenue insurance more attractive for corn.



- Producers who want to be in a position to aggressively pursue forward pricing opportunities in the event of a weather rally may prefer revenue insurance with the increasing coverage option, to protect against the possibility of yields falling below the level that is forward contracted. The same philosophy applies to producers who feed most of their corn and want to protect against having to buy supplemental bushels at a high price.



Handling joint tenancy at death *

by Neil E. Harl, Charles F. Curtiss Professor in Agriculture, professor of economics, 515-294-6354, harl@iastate.edu

It took nearly a decade, but the Internal Revenue Service has acknowledged the line of cases headed by *Gallenstein v. United States* and followed by five more cases holding that the so-called “consideration furnished” rule of federal estate taxation of jointly-owned property could be applied at the first death of a husband-wife joint tenancy to produce a higher income tax basis in the hands of the surviving joint tenant. IRS has now acquiesced in the Tax Court decision, *Hahn v. Commissioner*, which removes the remaining doubt as to whether application of the consideration furnished rule was acceptable in the case of husband-wife joint tenancies. In *Hahn v. Commissioner*, The Tax Court agreed that a surviving spouse could be entitled to a new income tax basis on 100 percent of the date of death value for property held in joint tenancy with a predeceased spouse.

Facts in *Hahn v. Commissioner*

In *Hahn v. Commissioner*, the husband, who was the first of the joint tenants to die, in 1972 had signed an agreement to purchase shares in a corporation representing an apartment. The shares were issued later to the husband and wife in joint tenancy. At the husband’s death, in 1991, the wife became the sole owner of the shares. The federal estate tax return included 100 percent of the value of the shares in the husband’s estate. That amount of course, was covered by the federal estate tax marital deduction. On later sale of the shares, the wife (as the surviving joint tenant) claimed an income tax basis of \$758,412. On audit, the Internal Revenue Service took the position that only 50 percent of the date of death value should have been included in the husband’s estate and, therefore, only that amount should have received a new basis at the husband’s death. The Tax Court disagreed.

History of the “consideration furnished” rule

Before 1977, the value of joint tenancy property was subject to federal estate tax in the estate of the first to die except to the extent it could be proved that the survivor contributed to its acquisition. This became known as the “consideration furnished” rule.

Before 1982, the creation of husband-wife joint interests in land was not subject to federal gift tax unless so reported on a gift tax return timely filed.

An important point in *Hahn v. Commissioner* is that whatever portion of asset value is included in the decedent’s gross estate also receives a new income tax basis at death. A surviving joint tenant is considered to have acquired property from the decedent only to the extent that the property was required to be included in the estate of the deceased joint tenant. Thus, the portion of the property not included in the decedent’s estate retains the survivor’s income tax basis.

The “fractional share” rule

In 1976, the joint tenancy rule was amended to create a special rule for joint tenants who were husbands and wives married to each other. Under that rule, one-half the value was included in the estate of the first to die without regard to which spouse furnished the consideration to acquire the jointly held property. Moreover, one-half the value received a new income tax basis at death.

Applicability of “consideration furnished” rule before 1982

The key question has been whether the “consideration furnished” rule continued to apply in the case of deaths after 1981. That question was first answered by *Gallenstein v. United States* in 1992 and confirmed by the other cases decided since 1992 including *Hahn v. Commissioner*. The *Gallenstein* case concluded that Congress had not repealed the “consideration furnished” rule for husband-wife joint tenancies either expressly or by implication. Indeed, in *Hahn v. Commissioner*, the court concluded that the “fractional share” rule “does not apply to spousal joint interests created before January 1, 1977.”

To what property does *Hahn* apply?

For federal gift tax purposes, by the general rule a gratuitous transfer of property by one person to that person and another as joint tenants is considered a gift of a proportionate part of the value. Before January 1, 1977, only three classes of property did not involve a gift when acquired by a husband and wife in joint tenancy—(1) the purchase of United States savings bonds registered as payable to the one providing the consideration “or” another did not

continued on page 4

* Reprinted with permission from the November 9, 2001 issue of Agricultural Law Digest, agricultural law press publication. Footnotes not included

Handling joint tenancy at death, continued from page 3

(and still does not) constitute a taxable gift until and unless the one not providing consideration redeems the bond during the lifetime of the other without any obligation to account for the proceeds to the other owner; (2) the transfer of funds into a joint bank account did not (and still does not) produce a taxable gift until and unless the one not providing funds withdraws amounts for his or her own benefit; and (3) through 1981, for a joint tenancy in real property created after December 31, 1954, in a husband and wife, by one of the spouses, a taxable gift did not result at the time of the transfer unless the donor elected to treat the transfer as a gift. Contribution was defined in terms of "money, other property or an interest in property."

Thus, these three types of categories of property appear eligible for application of the "consideration furnished" rule at the death of the first to die of a husband and wife joint tenancy, although only the land exception is of much interest. Of course, it is necessary for the spouse who provided the consideration to die first in order for the surviving spouse to benefit from a new basis for up to 100 percent of the value of the property. Note that if assets had declined in value, and death of the first to die would

result in a step-down in basis, the fractional share rule would result in a more advantageous result for the survivor. However, *Hahn v. Commissioner* states that "...section 2040(b)(1) [the "fractional share" rule] does not apply to spousal joint interests created before January 1, 1977."

Who can use *Hahn v. Commissioner*?

Obviously, in the estate of the first to die of a husband-wife joint tenancy, if the estate applied the "consideration furnished" rule (for acquisition of eligible property before 1977 when the first to die contributed the consideration), the rule of *Hahn v. Commissioner* can be applied. What if the estate of the first to die was not sufficiently large to file a federal estate tax return? In that case, it would appear that, so long as an inconsistent position was not taken after the first death (and the facts otherwise support application of the "consideration furnished" rule), the "consideration furnished" rule could be applied. An "inconsistent position" could possibly have been taken on a depreciation schedule as the schedule was adjusted after death of the first joint tenant to die or on a state inheritance tax return in a state with rules for joint tenancy taxation similar to the federal rules. These possibilities await further illumination in rulings or cases or both.

Building your brand

by Nancy Giddens, Agricultural Extension Marketing Specialist, Missouri Value-added Development Center, University of Missouri

Value-added products need a distinct identity - they need a brand. This article is the first of a five-part series and will examine what branding is, why it is important, and the necessary steps to brand your new product. Next month, we will discuss flanker branding.

What is branding?

Branding is one of the most important factors influencing an item's success or failure in today's marketplace. A brand is the combination of name, words, symbols or design that identifies the product and its company and differentiates it from competition.

Businesses use branding to market a new product, protect market position, broaden product offerings, and enter a new product category. Four types of branding are:

- **New product branding** — creating a new name for a new product in a category completely new to the company. Example: A Taste of the Kingdom jellies.

- **Flanker branding** — protect market position by marketing another brand in a category in which the firm already has a presence. Example: **HORMEL®** chili and its flanker brand, **STAGG®** chili.
- **Brand line extension** — use of the company's brand name in the firm's present product category. Example: PepsiCo's Pepsi and Diet Pepsi.
- **Brand leveraging (franchise extension)** — use of the existing brand name to enter a new product category is called leveraging. Example: Mr. Coffee (a coffee maker) and Mr. Coffee coffee.

Why is it important to develop a brand for your product?

A brand offers instant product recognition and identification. Consumers identify branded products

Building your brand, continued from page 4

and, as a result of effective advertising, have confidence in product quality. Retailers like branded products because they make the store profitable - shoppers attracted to branded products spend three to four times more on groceries than do private-label shoppers.

Branding is beneficial for four reasons:

- **Differentiate** — A brand provides a clear and definitive reason for customers to buy your product. If this reason does not exist, your product is a commodity and the only measure of value is price. Small, value-added businesses cannot compete on price successfully and need to incorporate some form of differentiation.
- **Conveys value** — Consumers perceive brand-name products as higher quality, more reliable, and a better value than non-branded products. The number one brand in a category can command a 10 percent price premium over the number two brand, and a 40 percent premium over the store brand. This price premium is known as a brand tax. Consumers understand that a strong brand can reduce getting stuck with disappointing or faulty products.
- **Builds brand loyalty** — Brand loyalty is the recurring stream of profit generated by repeat and referral sales of a specific brand. Repeat sales can be as much as 90 percent less expensive to a company than new customer development.
- **Builds pride** — Branded, recognizable products invoke a sense of pride in those associated with production, promotion, sale, and distribution of those products.

What is the process of branding a product?

A brand must be clear, specific, and unique to your product. For example, the Wheaties brand differentiates the cereal from its competition due to its association with health and "sports excellence." To achieve the same successes with your products, you need to execute the following steps to establish an effective brand:

- **Find a name.** Choose an appropriate name that is easily remembered and specific to the product. The name should be restricted to three

words or less - anything longer is difficult for customers to recall. This process may require legal screening to guarantee availability of the name and customer input to assess attractiveness and appropriateness of the name.

- **Develop a slogan.** The selected slogan needs to be two to three words, catchy, and easily remembered. To generate slogan ideas, you must stay focused on the buyer. Why should they buy the product? What will they like about the brand? How does competition compare? The slogan should take into account answers to these questions.
- **Create an appropriate symbol or logo.** It can be as simple as a geometric shape or as elaborate as a silhouette of a person or object. Use the name, slogan and symbol on every piece of correspondence related to the product- e-mails, invoices, letterhead, business cards, advertisements and promotions, etc. This system will eliminate inefficiencies in creative and production fees and extend the branding process throughout everything you do. In a sense, it will prevent "recreating the wheel" with each new media effort.

What are the challenges of building a brand?

The greatest challenge faced when developing and building a brand is creating just the right name, slogan, and symbol for the product. It will take a great deal of time and consideration. A thorough thought process and feedback from others will help to get past this obstacle.

It is often difficult to achieve initial customer recognition of a new product, regardless of branding. However, branded items are more recognizable and memorable. Effective advertising before and after the sale is key to overcoming this obstacle. Advertising and promotion before the sale are essential to obtain first purchases and follow-up advertisements after the sale will promote customer satisfaction and repeat purchases.

Repeat purchases are one of the primary objectives in brand development. Repeat purchases are critical to your business' long-term success and contribute to brand loyalty, which will be discussed in the final article of this series.

No endorsement of products or firms is intended nor is criticism implied of those not mentioned.



Applying the new capital gains rules *

by Neil E. Harl, Charles F. Curtiss Professor in Agriculture, professor of economics, 515-294-6354, harl@iastate.edu

In 1997, when Congress revamped the capital gains rules for eligible property, the maximum rate on net long-term capital gains for an individual was reduced from 28 percent to 20 percent. In addition, the rate for any net long-term capital gain, which would otherwise be taxed at 15 percent, was reduced to a 10 percent rate.

The 1997 Act also provided, beginning in 2001, for an 18 percent rate for long-term capital gains on eligible assets held for more than five years, 8 percent for those in the 15 percent tax bracket. That provision was made effective for property for which the holding period begins after December 31, 2000, *except for those in the 15 percent tax bracket*. Thus, for those in the 15 percent tax bracket, the holding period for the 8 percent rate could have begun before January 1, 2001. That is not the case for those in higher tax brackets.

Deemed sale

The 1997 Act further specified that taxpayers (other than corporations) and pass-through entities could elect to treat certain assets held on January 1, 2001, as having been sold and reacquired on the same date (often referred to as the market-to-market capital gains election). Any other capital asset or property used in a trade or business for which the election is made, is deemed to have been sold and reacquired on January 1, 2001, for its fair market value on that date. The purpose of the election is to make future gain on an asset eligible for the 18 percent rate (rather than the 20 percent rate). If the irrevocable election is made, any gain on the deemed sale is recognized on the 2001 income tax return; a loss from a deemed sale is not allowed in any tax year. To make the election, taxpayers are to report the deemed sale on a timely filed 2001 income tax return (with extensions).

If the deemed sale results in a loss, the taxpayer is to enter zero instead of the amount of the loss. The taxpayer should attach a statement to the return

stating that an election has been made under Section 311 of the Taxpayer Relief Act of 1997 and specify the assets for which the election is made.

Sale of residence

If an individual elects under the Taxpayer Relief Act of 1997 to treat the individual's principal residence as being both sold and reacquired on January 1, 2001, for an amount equal to its fair market value on that date, the individual cannot exclude from gross income under the \$250,000 residence exclusion (\$500,000 on a joint return) any of the gain resulting from the deemed sale. IRS has ruled to that effect on the grounds that the statute requires that gain be recognized "notwithstanding any other provision" of the Internal Revenue Code. Therefore, the gain on the deemed sale is not eligible for the exclusion on sale of the principal residence.

Property sold within one year of deemed election

In late 2000, Congress acted to assure that an election to make a "deemed sale" of assets and recognize gain does not apply to assets disposed of in a recognition transaction within one year of the date the election would otherwise have been effective. Therefore, if an asset is sold in 2001, no election may be made with respect to that asset. In addition, the deemed sale and repurchase by reason of the election is not to be taken into account in applying the "wash-sale" rules. The amendment is designed to prevent a taxpayer from generating a short-term capital loss, which could offset a short-term capital gain from other assets (such as corporate stock).

In conclusion

The changes made in 1997 and 2000 could have important implications for returns filed for the 2001 tax year.

** Reprinted with permission from the November 23, 2001 issue of Agricultural Law Digest, agricultural law press publication. Footnotes not included.*

... and justice for all

The U.S. Department of Agriculture (USDA) prohibits discrimination in all its programs and activities on the basis of race, color, national origin, gender, religion, age, disability, political beliefs, sexual orientation, and marital or family status. (Not all prohibited bases apply to all programs.) Many materials can be made available in alternative formats for ADA clients. To file a complaint of discrimination, write USDA,

Office of Civil Rights, Room 326-W, Whitten Building, 14th and Independence Avenue, SW, Washington, DC 20250-9410 or call 202-720-5964.

Issued in furtherance of Cooperative Extension work, Acts of May 8 and June 30, 1914, in cooperation with the U.S. Department of Agriculture. Stanley R. Johnson, director, Cooperative Extension Service, Iowa State University of Science and Technology, Ames, Iowa.

Permission to copy

Permission is given to reprint ISU Extension materials contained in this publication via copy machine or other copy technology, so long as the source (Ag Decision Maker Iowa State University Extension) is clearly identifiable and the appropriate author is properly credited.