Williamson v. Commissioner, 97 T. C. 250 (1991)

Cash leasing of specially valued property to a family member triggers the recapture tax under Section 2032A.

Summary

In Williamson v. Commissioner, the court addressed whether cash leasing farm property to a family member constituted a cessation of qualified use under Section 2032A, triggering the recapture tax. Beryl Williamson inherited farm property from his mother, which was subject to special use valuation. He leased it to his nephew for cash, leading to a dispute over whether this constituted a cessation of qualified use. The court ruled that cash leasing, even to a family member, was not a qualified use, thus imposing the recapture tax. The decision emphasized the distinction between active use and passive rental, clarifying that only the qualified heir's active use qualifies, not passive income from leasing.

Facts

Elizabeth R. Williamson devised farm property to her son, Beryl P. Williamson, upon her death in 1983. The estate elected special use valuation under Section 2032A, valuing the property based on its use as a farm rather than its highest and best use. Initially, the property was leased to Harvey Williamson, Beryl's nephew, under a crop-share lease. Later, Beryl executed a cash lease with Harvey for the period from March 1, 1985, to February 28, 1989. The IRS determined that this cash lease constituted a cessation of qualified use, triggering a recapture tax against Beryl.

Procedural History

The IRS issued a notice of deficiency to Beryl Williamson, asserting a recapture tax due to the cessation of qualified use when the property was leased for cash. Beryl petitioned the Tax Court for a redetermination of the deficiency. The Tax Court heard the case and issued its opinion, ruling in favor of the Commissioner and upholding the recapture tax.

Issue(s)

1. Whether cash leasing of specially valued property to a family member constitutes a cessation of qualified use under Section 2032A(c)(1)(B), triggering the recapture tax?

Holding

1. Yes, because cash leasing, even to a family member, is considered a passive rental activity and not a qualified use under Section 2032A(c)(6)(A).

Court's Reasoning

The court interpreted Section 2032A(c)(1)(B) and its amplifying provision, Section 2032A(c)(6)(A), to require active use of the property by the qualified heir for it to remain a qualified use. The court emphasized that cash leasing is a passive rental activity, which does not satisfy the qualified use requirement. The legislative history and subsequent amendments, such as those in 1981 and 1988, reinforced the court's interpretation that cash leasing to anyone, including family members, triggers the recapture tax unless specifically exempted. The court rejected Beryl's argument that leasing to a family member should be considered a disposition to a family member under Section 2032A(c)(1)(A), clarifying that a lease does not constitute a disposition of an interest in property but rather a use of the property. The court relied on prior cases like Martin v. Commissioner to support its stance on the distinction between active farming and passive rental income.

Practical Implications

The Williamson decision has significant implications for estates electing special use valuation under Section 2032A. It underscores the importance of active use by the qualified heir to avoid the recapture tax, even if the property is leased to a family member. Legal practitioners must advise clients to ensure that qualified heirs actively participate in farming or business activities on the property, rather than relying on passive income from cash leases. The ruling also highlights the need to monitor legislative changes, as exceptions like those for surviving spouses can affect estate planning strategies. Subsequent cases have continued to apply this principle, emphasizing the need for material participation in the qualified use to maintain the special valuation benefits.

