

The IRS Attack List and How to Defend Against It

Salt Lake City Estate Planning
Council
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I. Overview

1. Gift Tax Cases

- Indirect gifts
- Annual exclusion gifts
- Defined value transactions
- Installment sales/Promissory notes
 - FMV of interest sold
 - FMV of consideration/note received
- GRATs
- BDITs
- Adequate Disclosure

I. Overview (cont'd)

Statistics on Gifts

Year/Tax Collected	709s Filed	709s Examined	% Audited	\$ Collected After Audit
2017/\$2.0B	244,974	1,886	0.8%	\$440M
2016/\$2.5B	249,302	1,843	0.8%	\$303M
2015/\$2.1B	238,324	2,539	0.9%	\$286M
2014/\$2.6B	267,600	3,098	0.8%	\$1.3B
2013/\$5.8B	371,747	2,775	1.1%	\$1.2B
2012/\$2.1B	260,426	3,164	1.4%	\$351M
2011/\$6.6B	223,090	2,623	1.2%	\$301M
2010/\$2.8B	226,241	1,777	0.7%	\$203M

I. Overview (cont'd)

2. Estate Tax Cases

- § 2036
- Marital Deduction Mismatch
- *Graegin* Loans

See, e.g., *Estate of Black v. Comm'r*, 133 T.C. 15 (2009), *supp. by* 103 T.C.M. (CCH) 1302 (2012);
See *Estate of Shurtz v. Comm'r*, 99 T.C.M. (CCH) 1096 (2010).

I. Overview (cont'd)

Statistics on Estates

Year/Tax Collected	706s Filed	706s Examined	% Audited	\$ Collected After Audit
2017/\$21.8B	35,042	2,876	8.2%	\$799M
2016/\$19.9B	35,592	3,187	8.8%	\$790M
2015/\$18.0B	36,130	2,770	7.8%	\$428M
2014/\$17.6B	35,619	2,853	8.5%	\$775M
2013/\$14.1B	33,719	3,250	11.6%	\$3.3B
2012/\$12.3B	28,061	3,762	29.9%	\$1.2B
2011/\$2.5B	12,582	4,195	18.2%	\$1.6B
2010/\$16.9B	23,014	4,288	10.1%	\$1.4B

I. Overview (cont'd)

3. General Issues

- Valuation
- S corporation (tax affecting)
- Unrealized capital gains
- Chapter 14
 - § 2701
 - § 2702
 - § 2703
 - Safe harbors (meet all 3)
 - Bona fide business arrangement
 - Not testamentary device (paraphrased)
 - Comparable to 3rd party arrangements
 - § 2704
- Undervaluation Penalties

I.R.C. §§ 6662(g), (h).

II. Consider Appropriateness of Partnership

1. Keep your potential future audience in mind
 - Consider what you write – email, memo to file regarding reasons for partnership formation, time records (for attorneys/accountants), letters, etc.
 - The IRS, a judge, or even a jury may eventually be reviewing documents written during the planning stages
 - Consider and document all substantive non-transfer tax reasons that fit the situation
 - Best evidence of formation rationale often comes from correspondence prepared in connection with transaction
 - Suggest that clients avoid template laundry list in partnership agreement

E.g., Estate of Jorgensen v. Comm'r, 97 T.C.M. (CCH) 1328 (2009) ("Guess we have to be real straight on who borrowed what etc. so the partnership looks very legit."); *Linton v. United States*, 638 F. Supp. 2d 1277 (W.D. Wash. 2009) ("[Y]ou have to get the assets into the LLC first so it's the owner of the assets before you start making transfers."), *rev'd in part and remanded*, 630 F.3d 1211 (9th Cir. 2011); *Estate of Purdue v. Comm'r*, 110 T.C.M. (CCH) 627 (2015).

I.R.C. §§ 721, 351, 368.

II. Consider Appropriateness of Partnership (cont'd)

2. Consider whether clients are ready for a partnership
 - Sophistication of clients
 - Willingness to comply with Partnership Agreement's terms
 - Willingness to pay professional fees over time

II. Consider Appropriateness of Partnership (cont'd)

3. Evaluate potential assets

- Refrain from contributing personal use assets
- Retain enough assets outside Partnership to support lifestyle (and annual gifting program)

See, e.g., Estate of Bigelow v. Comm'r, 503 F.3d 955 (9th Cir. 2007);
Estate of Korby v. Comm'r, 471 F.3d 848 (8th Cir. 2006);
Estate of Strangi v. Comm'r, 85 T.C.M. (CCH) 1331 (2003), *aff'd*, 417 F.3d 468 (5th Cir. 2005);
Estate of Harper v. Comm'r, 83 T.C.M. (CCH) 1641 (2002);
Estate of Strangi v. Comm'r, 115 T.C. 478 (2000), *aff'd in part, rev'd in part*, 293 F.3d 279 (5th Cir. 2002);
Estate of Reichardt v. Comm'r, 114 T.C. 144 (2000).

See, e.g., Estate of Jorgensen v. Comm'r, 97 T.C.M. (CCH) 1328 (2009);
Estate of Beyer v. Comm'r, 112 T.C.M. (CCH) 356;
Estate of Miller v. Comm'r, 98 T.C.M. (CCH) 159 (2009);
Estate of Purdue v. Comm'r, 110 T.C.M. (CCH) 627 (2015).

See, e.g., Estate of Hurford v. Comm'r, 96 T.C.M. (CCH) 422 (2008);
Estate of Rector v. Comm'r, 94 T.C.M. (CCH) 567 (2007);
Estate of Stone v. Comm'r, 86 T.C.M. (CCH) 551 (2003);
Estate of Thompson v. Comm'r, 84 T.C.M. (CCH) 374 (2002).

But see Estate of Mirowski v. Comm'r, 95 T.C.M. (CCH) 1277 (2008).

II. Consider Appropriateness of Partnership (cont'd)

3. Evaluate potential assets (cont'd)
 - Review transfer restrictions on assets to be contributed; obtain appropriate consents, if necessary
 - Ensure sufficient cash is contributed to the Partnership to fund maintenance of Partnership's real estate or other non-liquid assets
 - Consider income tax issues related to contribution of assets subject to debt (margin debt, mortgages, etc.)
 - Analyze investment company rules

See *Estate of Bigelow v. Comm'r*, 89 T.C.M. (CCH) 954 (2005), *aff'd*, 503 F.3d 955 (9th Cir. 2007); *Estate of Beyer v. Comm'r*, 112 T.C.M. (CCH) 356 (2016) .

I.R.C. §§ 721, 351, 368; PLR 200931042.

II. Consider Appropriateness of Partnership (cont'd)

4. Evaluate potential partners
 - Consider whom to involve
 - Consider health of partners
 - Beware use of power of attorney
 - Encourage meaningful contributions by partners

See, e.g., Estate of Miller v. Comm'r, 98 T.C.M. (CCH) 159 (2009) (stable health; steep decline for second contribution);
Estate of Mirowski v. Comm'r, 95 T.C.M. (CCH) 1277 (2008) (stable health);
Estate of Erickson v. Comm'r, 93 T.C.M. (CCH) 1175 (2007) (bad health, agent formed);
Estate of Purdue v. Comm'r, 110 T.C.M. (CCH) 627 (2015) (good health);
Estate of Rector v. Comm'r, 94 T.C.M. (CCH) 567 (2007) (bad health);
Estate of Rosen v. Comm'r, 91 T.C.M. (CCH) 1220 (2006) (bad health, agent formed);
Estate of Strangi v. Comm'r, 85 T.C.M. (CCH) 1331 (2003), *aff'd*, 417 F.3d 468 (5th Cir. 2005) (bad health, agent formed);
Estate of Stone v. Comm'r, 86 T.C.M. (CCH) 551 (2003) (good health).

Estate of Harper v. Comm'r, 83 T.C.M. (CCH) 1641 (2002).
But see Estate of Bongard v. Comm'r, 124 T.C. 95 (2005).

II. Consider Appropriateness of Partnership (cont'd)

5. Avoid gift planning until Partnership is up and running

Compare

Pierre v. Comm'r, 133 T.C. 24 (2009), *supp. by* 99 T.C.M. (CCH) 1436 (2010);

Holman v. Comm'r, 130 T.C. 170 (2008), *aff'd*, 601 F.3d 763 (8th Cir. 2010);

Gross v. Comm'r, 96 T.C.M. (CCH) 187 (2008);

Estate of Strangi v. Comm'r, 85 T.C.M. (CCH) 1331 (2003), *aff'd*, 417 F.3d 468 (5th Cir. 2005);

Estate of Jones v. Comm'r, 116 U.S. 212 (2001);

Estate of Strangi v. Comm'r, 115 T.C. 478 (2000), *aff'd in part and rev'd in part*, 293 F.3d 279 (5th Cir. 2002);

with

Linton v. United States, 638 F. Supp. 2d 1277 (W.D. Wash. 2009), *rev'd in part and remanded*, 630 F.3d 1211 (9th Cir. 2011);

Heckerman v. United States, 2009 WL 2240326 (W.D. Wash. Jul. 27, 2009);

Senda v. Comm'r, 88 T.C.M. (CCH) 8 (2004), *aff'd*, 433 F.3d 1044 (8th Cir. 2006);

Shepherd v. Comm'r, 115 T.C. 376 (2000), *aff'd*, 283 F.3d 1258 (11th Cir. 2002).

III. Partnership Formation

1. Consider separate counsel for some (or all) participants
 - Leads to review of terms of Partnership Agreement,
 - Which then leads to discussion,
 - Which may lead to better understanding,
 - And almost certainly leads to proposed edits.

See, e.g., Estate of Jorgensen v. Comm'r, 97 T.C.M. (CCH) 1328 (2009);
Estate of Beyer v. Comm'r, 112 T.C.M. (CCH) 356 (2016);
Estate of Erickson v. Comm'r, 93 T.C.M. (CCH) 1175 (2007);
Estate of Rector v. Comm'r, 94 T.C. M. (CCH) 567 (2007);
Estate of Rosen v. Comm'r, 91 T.C.M. (CCH) 1220 (2006);
Estate of Stone v. Comm'r, 86 T.C.M. (CCH) 551 (2003).

III. Partnership Formation (cont'd)

2. Engage/consult with advisors who have experience in this area
 - Involve attorney/accountant sooner rather than later
 - Avoid "kit partnerships"

See, e.g., Estate of Strangi v. Comm'r, 85 T.C.M. (CCH) 1331 (2003), *aff'd*, 417 F.3d 468 (5th Cir. 2005); *Estate of Thompson v. Comm'r*, 84 T.C.M. (CCH) 374 (2002); *aff'd*, 382 F.3d 367 (3rd Cir. 2004); *Estate of Strangi v. Comm'r*, 115 T.C. 478 (2000), *aff'd in part and rev'd in part*, 293 F.3d 279 (5th Cir. 2002).

III. Partnership Formation (cont'd)

3. Counsel Partners to discuss partnership terms
 - Management structure
 - Compensation to be paid to managers
 - Investment policy
 - Expected distributions
 - Transfer restrictions on partnership interests
 - Term of Partnership

See, e.g., Estate of Rector v. Comm'r, 94 T.C.M. (CCH) 567 (2007) (formation without discussion);
Estate of Strangi v. Comm'r, 417 F.3d 468 (5th Cir. 2005);
Estate of Harper v. Comm'r, 83 T.C.M. (CCH) 1641 (2002) (formation without discussion);
Estate of Thompson v. Comm'r, 84 T.C.M. (CCH) 374 (2002), *aff'd*, 382 F.3d 367 (3rd Cir. 2004).

Estate of Beyer v. Comm'r, 112 T.C.M. (CCH) 356 (2016);
Estate of Miller v. Comm'r, 98 T.C.M. (CCH) 159 (2009);
Holman v. Comm'r, 601 F.3d. 763, No. 08-3774, 2010 WL 1331270 (8th Cir. Apr 07, 2010), *aff'g* 130 T.C. 170 (2008).

Estate of Jorgensen v. Comm'r, 97 T.C.M. (CCH) 1328 (2009).
Holman v. Comm'r, 601 F.3d. 763, No. 08-3774, 2010 WL 1331270 (8th Cir. Apr 07, 2010), *aff'g* 130 T.C. 170 (2008).

III. Partnership Formation (cont'd)

4. Counsel Partners to discuss purposes of formation
 - Joint enterprise for profit
 - Centralized management
 - Furtherance of family investment strategies
 - Division of control, financial benefits among children
 - Marriage protection
 - Bankruptcy protection
 - Creditor protection

See Estate of Stone v. Comm'r, 86 T.C.M. (CCH) 551 (2003).

Estate of Miller v. Comm'r, 98 T.C.M. (CCH) 159 (2009);

Estate of Schutt v. Comm'r, 89 T.C.M. (CCH) 1353 (2005).

Estate of Murphy v. United States, 2009 WL 3366099 (W.D. Ark. Oct. 2, 2009).

Estate of Purdue v. Comm'r, 110 T.C.M. (CCH) 627 (2015).

III. Partnership Formation (cont'd)

5. Ensure that schedules to Partnership Agreement are complete
 - Partnership Agreement should accurately set forth assets contributed to Partnership and ownership interests in Partnership

III. Partnership Formation (cont'd)

6. Ensure that partners receive interests in the Partnership in proportion to the fair market value of the assets contributed by each to the Partnership
 - Correctly reflect the fair market value of the assets contributed in the respective partner's capital account

Compare

Holman v. Comm'r, 130 T.C. 170 (2008), *aff'd*, 601 F.3d 763 (8th Cir. 2010);

Gross v. Comm'r, 96 T.C.M. (CCH) 187 (2008);

Estate of Strangi v. Comm'r, 85 T.C.M. (CCH) 1331 (2003), *aff'd*, 417 F.3d 468 (5th Cir. 2005);

Estate of Strangi v. Comm'r, 115 T.C. 478 (2000), *aff'd in part and rev'd in part*, 293 F.3d 279 (5th Cir. 2002);

Estate of Jones v. Comm'r, 116 T.C. 121 (2001);

with

Linton v. United States, 638 F. Supp. 2d 1277 (W.D. Wash. 2009), *rev'd in part and remanded*, 630 F.3d 1211 (9th Cir. 2011);

Heckerman v. United States, 2009 WL 2240326 (W.D. Wash. Jul. 27, 2009);

Shepherd v. Comm'r, 115 T.C. 376 (2000), *aff'd*, 283 F.3d 1258 (11th Cir. 2002).

III. Partnership Formation (cont'd)

7. Consider preparation of deeds and transfer documents prior to formation date
 - Have parties sign transfer documents at the same time as Partnership Agreement and related formation documents
 - Ensures transfer of title of all assets to Partnership
 - Ensures that transfer restrictions on assets are complied with
 - Ensures that partners own assets to be contributed before Partnership is created

See, e.g., Estate of Hurford v. Comm'r, 96 T.C.M. (CCH) 422 (2008);
Estate of Erickson v. Comm'r, 93 T.C.M. (CCH) 1175 (2007);
Estate of Purdue v. Comm'r, 110 T.C.M. (CCH) 627 (2015);
Estate of Rector v. Comm'r, 94 T.C.M. (CCH) 567 (2007);
Estate of Rosen v. Comm'r, 91 T.C.M. (CCH) 1220 (2006);
Senda v. Comm'r, 88 T.C.M. (CCH) 8 (2004), *aff'd*, 433 F.3d 1044 (8th Cir. 2006);
Estate of Hillgren v. Comm'r, 87 T.C.M. (CCH) 1008 (2004);
Shepherd v. Comm'r, 115 T.C. 376 (2000), *aff'd*, 283 F.3d 1258 (11th Cir. 2002).

III. Partnership Formation (cont'd)

8. Promptly file for Employer Identification Number (EIN)
 - Upon receipt of Certificate of Formation

See Estate of Thompson v. Comm'r, 84 T.C.M. (CCH) 374 (2002), *aff'd*, 382 F.3d 367 (3rd Cir. 2004).

But see Estate of Miller v. Comm'r, 98 T.C.M. (CCH) 159 (2009) (24 days not too delayed).

III. Partnership Formation (cont'd)

9. Create Partnership bank/brokerage accounts in a timely manner
 - Upon receipt of EIN

See, e.g., Estate of Beyer v. Comm'r, 112 T.C.M. (CCH) 356 (2016);
Estate of Rector v. Comm'r, 94 T.C.M. (CCH) 567 (2007);
Estate of Thompson v. Comm'r, 84 T.C.M. (CCH) 374 (2002), *aff'd*, 382 F.3d 367 (3rd Cir. 2004).

III. Partnership Formation (cont'd)

10. Involve an accountant specializing in partnership matters

– Factors to consider

- Understanding of when changes in ownership interests occur
- Understanding of when (and whether) to consider Section 754 elections
- Understanding of when and how to file protective claims
- Understanding of audit procedures
- Experience negotiating with IRS
- Number of partnership returns per year
- Documentation of capital accounts in addition to Form 1065/1120

See *Estate of Jorgensen v. Comm'r*, 97 T.C.M. (CCH) 1328 (2009).

See *Linton v. United States*, 638 F. Supp. 2d 1277 (W.D. Wash. 2009) ("The tax return itself . . . does not constitute contemporaneously prepared evidence as to the sequence of transactions resulting in the capital account balances."), *rev'd in part remanded*, 630 F.3d 1211 (9th Cir. 2011).

III. Partnership Formation (cont'd)

11. Consider amortizing partnership set-up fees
 - Invoices directed to Partnership, rather than founding family member
 - Reimbursement to partner who initially paid

See Estate of Jorgensen v. Comm'r, 97 T.C.M. (CCH) 1328 (2009).

III. Partnership Formation (cont'd)

12. If necessary, amend Partnership percentages as quickly as possible after formation

III. Partnership Formation (cont'd)

13. Consider establishing Partnership office
 - Partnership telephone number
 - Phonebook listing
 - Physical office space

IV. Partnership Maintenance

1. File annual filings
 - Partnership returns for each year in existence
 - Annual/bi-annual registration statements required by relevant state authorities

IV. Partnership Maintenance (cont'd)

2. Comply with terms of Partnership Agreement

- Are periodic meetings required? At any meeting, consider taking minutes, even if not required by Partnership Agreement
- Are annual statements (other than tax returns) required?
- Are annual distributions required?
- Are payments on preferred interests required?

See *Estate of Bigelow v. Comm'r*, 89 T.C.M. (CCH) 954 (2005), *aff'd*, 503 F.3d 955 (9th Cir. 2007).

See *Estate of Jorgensen v. Comm'r*, 97 T.C.M. (CCH) 1328 (2009);
Estate of Purdue v. Comm'r, 110 T.C.M. (CCH) 627 (2015).

IV. Partnership Maintenance (cont'd)

3. Comply with loan terms, if loans are made
 - Generally, beware lending from the Partnership to family members
 - Any loans made by the Partnership should comply with the terms of the Partnership Agreement
 - Any loans should be properly documented
 - Loan terms should be reasonable
 - Payments should be made timely

See, e.g., Estate of Jorgensen v. Comm'r, 97 T.C.M. (CCH) 1328 (2009);
Estate of Thompson v. Comm'r, 84 T.C.M. (CCH) 374 (2002), *aff'd*, 382 F.3d 367 (3rd Cir. 2004).

IV. Partnership Maintenance (cont'd)

4. Make any distributions pro rata (pursuant to Agreement)
 - Ensure that all distributions are pro rata (proportionate to percentage interests in the Partnership), if Partnership Agreement requires pro rata
 - If you discover a prohibited non-pro rata distribution, consider a "make-up" distribution, perhaps with interest

See *Estate of Jorgensen v. Comm'r*, 97 T.C.M. (CCH) 1328 (2009).

See *Estate of Thompson v. Comm'r*, 84 T.C.M. (CCH) 374 (2002), *aff'd*, 382 F.3d 367 (3rd Cir. 2004).

IV. Partnership Maintenance (cont'd)

5. Refrain from use of Partnership assets for Partners' personal obligations
 - Personal use assets
 - Partners' expenses
 - Estate's needs

See, e.g., Estate of Beyer v. Comm'r, 112 T.C.M. (CCH) 356 (2016);
Estate of Hurford v. Comm'r, 96 T.C.M. (CCH) 422 (2008);
Estate of Rector v. Comm'r, 94 T.C.M. (CCH) 567 (2007);
Estate of Bigelow v. Comm'r, 89 T.C.M. (CCH) 954 (2005), *aff'd*, 503 F.3d 955 (9th Cir. 2007);
Estate of Strangi v. Comm'r, 85 T.C.M. (CCH) 1331 (2003), *aff'd*, 417 F.3d 468 (5th Cir. 2005).

See, e.g., Estate of Miller v. Comm'r, 98 T.C.M. (CCH) 159 (2009) (margin debt payoff is not personal expense);
Estate of Jorgensen v. Comm'r, 97 T.C.M. (CCH) 1328 (2009).

But see Estate of Mirowski v. Comm'r, 95 T.C.M. (CCH) 1277 (2008);
Estate of Graegin v. Comm'r, 56 T.C.M. (CCH) 387 (1988).

IV. Partnership Maintenance (cont'd)

6. Counsel partners to refrain from paying Partnership obligations

See Estate of Jorgensen v. Comm'r, 97 T.C.M. (CCH) 1328 (2009).

IV. Partnership Maintenance (cont'd)

7. Encourage Partners to maintain current and accurate books and records

See Estate of Jorgensen v. Comm'r, 97 T.C.M. (CCH) 1328 (2009).

IV. Partnership Maintenance (cont'd)

8. Avoid multiple transactions between partners and Partnership
 - Loans
 - Redemptions
 - Non-regular distributions
 - Non-pro rata distributions

Estate of Beyer v. Comm'r, 112 T.C.M. (CCH) 356 (2016).

IV. Partnership Maintenance (cont'd)

9. Review non-tax reasons stated for forming Partnership and follow them
 - Involvement of family members
 - Asset management

See Estate of Beyer v. Comm'r, 112 T.C.M. (CCH) 356 (2016);
Estate of Jorgensen v. Comm'r, 97 T.C.M. (CCH) 1328 (2009).

V. Transfers of Entity Interests

1. Generally

- Ensure books and records of Entity are in order
- Review Partnership Agreement, Bylaws, Buy-Sell Agreement to ensure transfer complies with terms or triggers any rights of first refusal
- Keep track of changes in ownership interests
 - Restate schedule to Partnership Agreement indicating ownership interests
 - Consider keeping historical spreadsheet showing changes at each transaction
 - Update stock transfer ledger, issue stock certificates
- Consider whether to make §754 election
 - If made, use stepped-up basis for future transactions

See *Estate of Jorgensen v. Comm'r*, 97 T.C.M. (CCH) 1328 (2009).

V. Transfers of Entity Interests (cont'd)

1. Generally (cont'd)

- Document the transfer, to be executed by transferor and transferee
- Date the transfer document – effective date vs. date signed
 - Ask partners to fill in date signed
- Review Partnership Agreement to determine how interest is to be valued
- Ensure that changes in percentage interests are reflected in all books and records of Partnership
- Ensure that the Certificate of Limited Partnership is amended, if necessary
- Ensure that K-1s conform to ownership changes
- Ensure that distributions conform to ownership changes

Linton v. United States, 638 F. Supp. 2d 1277 (W.D. Wash. 2009);
Holman v. Comm'r, 130 T.C. 170 (2008), *appeal docketed*, No. 08-3774 (8th Cir. Dec. 12, 2008).

V. Transfers of Entity Interests (cont'd)

2. By Gift or Sale

- For gifts: Refrain from gift planning until Partnership is formed and operating
- For sales: Consider income tax issues

Compare

Linton v. United States, 630 F.3d 1211 (9th Cir. 2011);

Pierre v. Comm'r, 133 T.C. 24 (2009), *supp. by*, 99 T.C.M. (CCH) 1436, (2010);

Holman v. Comm'r, 130 T.C. 170 (2008), *aff'd*, 601 F.3d 763 (8th Cir. 2010);

Gross v. Comm'r, 96 T.C.M. (CCH) 187 (2008);

Estate of Strangi v. Comm'r, 85 T.C.M. (CCH) 1331 (2003), *aff'd*, 417 F.3d 468 (5th Cir. 2005);

Estate of Jones v. Comm'r, 116 U.S. 212 (2001);

Estate of Strangi v. Comm'r, 115 T.C. 478 (2000), *aff'd in part and rev'd in part*, 293 F.3d 279 (5th Cir. 2002);

with

Heckerman v. United States, 2009 WL 2240326 (W.D. Wash. Jul. 27, 2009);

Senda v. Comm'r, 88 T.C.M. (CCH) 8 (2004), *aff'd*, 433 F.3d 1044 (8th Cir. 2006);

Shepherd v. Comm'r, 115 T.C. 376 (2000), *aff'd*, 283 F.3d 1258 (11th Cir. 2002).

V. Transfers of Entity Interests (cont'd)

3. At Death

- Review transfer to determine whether lapse occurs under Chapter 14
- Consider maintaining interest in hands of Executor, subject to estate administration, until closing letter is received from the IRS
- Once IRS closing letter is received, document transfer, to be executed by executor and beneficiary

V. Transfers of Entity Interests (cont'd)

4. By Redemption

- Review Partnership Agreement or corporate documents to ensure that entity is not prohibited from redeeming the interest
- Document the redemption, to be executed by management and the transferring owner
- Ensure that books and records of Partnership reflect decrease to transferring partner's interest and corresponding proportionate increase to all remaining partners' interests

VI. Transfer Tax Reporting

1. Obtain independent appraisal from qualified appraiser
 - Appraiser should be engaged by attorney, not taxpayer

Kohler v. Comm'r, 92 T.C.M 55 (2006).

VI. Transfer Tax Reporting (cont'd)

2. Encourage communication among appraiser, client, and advisors
 - A good appraisal reflects a high level of communication
 - Bad legal facts + Good appraisal = Bad result
 - Good legal facts + Bad appraisal = Bad result
 - Both scenarios = Unhappy client

VI. Transfer Tax Reporting (cont'd)

3. Confirm with appraiser interest to be valued

VI. Transfer Tax Reporting (cont'd)

4. Consider whether to aggregate interests
 - Interests held in marital trust may be valued separately

See, e.g., Estate of Nowell v. Comm'r, 77 T.C.M. (CCH) 1239 (1999);
Estate of Lopes v. Comm'r, 78 T.C.M. (CCH) 46 (1999);
Ahmanson Foundation v. United States, 674 F.2d 761 (9th Cir. 1981).

See, e.g., Estate of Mellinger v. Comm'r, 112 T.C. 26 (1999);
Estate of Bonner v. United States, 84 F.3d 196 (5th Cir. 1996);
Estate of Bright v. U.S., 658 F.2d 999 (5th Cir. 1981).

VI. Transfer Tax Reporting (cont'd)

5. Consider whether tiered discounts might be appropriate

See Astleford v. Comm'r, 95 T.C.M (CCH) 1497 (2008).

VI. Transfer Tax Reporting (cont'd)

6. Promote defensibility of valuation reports
 - Clients should be realistic about projections
 - Appraiser should
 - conduct thorough due diligence – be sure appraiser fully understands the nature, characteristics of business
 - have clear understanding of empirical data
 - apply relevant comparative factors
 - Appraisal should be
 - well documented
 - readily understood

VI. Transfer Tax Reporting (cont'd)

7. Review appraisal closely for facts
 - Distribution policy
 - Partnership terms
 - Assets
 - Cash flow
 - Buy-Sell and other restrictive agreements

See Kohler v. Comm'r, 92 T.C.M. (CCH) 48 (2006) (declining to rely on IRS appraisal where expert “did not understand Kohler’s business”).

VI. Transfer Tax Reporting (cont'd)

8. Encourage taxpayer to live by factual information provided to appraiser
 - Cash flow, distribution policy, etc.

VI. Transfer Tax Reporting (cont'd)

9. Beware of rounding on appraisals and tax returns

VI. Transfer Tax Reporting (cont'd)

10. Consider IRS Settlement Guidelines

- Goal: Consistency across different jurisdictions
- Issues addressed:
 - Discounts expected for various asset classes
 - Inclusion of assets under I.R.C. Section 2036 or 2038 transfers in gross estate
 - Determination of indirect gifts of assets
 - Applicability of accuracy-related penalties

07 No. 020 BNA Taxcore 25; http://www.irs.gov/pub/irs-utl/asg_penalties_family_limited_pships_finalredacted10_20_06.pdf.

See, e.g., Estate of Murphy v. United States, 104 A.F.T.R.2d 7703 (W.D. Ark. 2009);
Astleford v. Comm'r, 95 T.C.M. (CCH) 1497 (2008);
McCord v. Comm'r, 120 T.C. 358 (2003), *rev'd*, 461 F.3d 614 (5th Cir. 2006);
Temple v. United States, 423 F. Supp. 2d 605 (E.D. Tex. 2006);
Peracchio v. Comm'r, 86 T.C.M. (CCH) 412 (2003);
Lappo v. Comm'r, 86 T.C.M. (CCH) 333 (2003);
Estate of Beyer v. Comm'r, 112 T.C.M. (CCH) 356 (2016);
Estate of Dailey v. Comm'r, 82 T.C.M. (CCH) 710 (2001);
Estate of Deputy v. Comm'r, 85 T.C.M. (CCH) 1497 (2003).

VII. Audit

1. How are transfer tax returns selected for Audit?

- Initial screening and review at Cincinnati Service Center
- Preparer's reputation can impact selection process
- Location of taxpayer does not drive location of Examining Agent
- Second review may be performed by local manager
- Valuation issues may be referred to IRS Engineering & Valuation Division
 - Appraisals versus Commentary/Rebuttal

VII. Audit (cont'd)

2. Determine whether document destruction policy exists; if so, suspend

See, e.g., Qualcomm Inc. v. Broadcom Corp., 2008 WL 66932 (S.D. Cal. Jan. 7, 2008);
Phoenix Four, Inc. v. Strategic Re. Corp., 2006 WL 1409413 (S.D.N.Y. May 23, 2006).

VII. Audit (cont'd)

3. Consider burden of proof

- Burden shifts to IRS if taxpayer:
 - complies with reasonable requests for documents, information, and interviews
 - maintains required records
 - is not a partnership, corporation, or trust

I.R.C. § 7491.

VII. Audit (cont'd)

4. Consider impact of privileges

- Attorney-client privilege
 - Relation to email?
- Work-product doctrine
- Tax Practitioner's Privilege
- Waiver, generally
- Subject matter waiver

See Scott v. Beth Israel Medical Center, Inc., 847 N.Y.S.2d 436 (N.Y. Sup. 2007);
Sims v. Lakeside Sch., 2007 WL 2745367 (W.D. Wash. September 30, 2007).

See Schaeffler v. United States, 806 F.3d 34 (2nd Cir. 2015);
United States v. Frederick, 182 F.3d 496 (7th Cir. 1999);
United States v. Adlman, 68 F.3d 1495 (2^d Cir. 1995).

But see United States v. Textron, 507 F. Supp. 2d 138 (D.R.I. 2007), *aff'd in part, vacated in part, and remanded*, 553 F.3d 87 (1st Cir. 2009).

I.R.C. § 7525.

VII. Audit (cont'd)

5. Consider whether production of privileged information may support taxpayer's case
 - Beware subject matter waiver
 - Beware inadvertent waiver

See Fed. R. Evid. 502.

VII. Audit (cont'd)

6. Provide responses that are true and correct, to best of taxpayer's knowledge
 - How much information to volunteer?

VII. Audit (cont'd)

7. Consider right to conference with manager

VII. Audit (cont'd)

8. Anything stated or written can be treated as admission
 - Anything written to any expert is discoverable
 - Educate your appraiser
 - Beware spoliation of evidence

VII. Audit (cont'd)

9. Produce responsive documents in taxpayer's possession, custody, or control

VII. Audit (cont'd)

10. Keep careful track of every document and electronic file produced to IRS
 - Bates-label documents
 - Keep copy

VII. Audit (cont'd)

11. Understand IRS's broad summons power

- May examine or summon laundry list of items and people
- For purpose of “ascertaining the correctness of any return, making a return where none has been made, or determining the liability of any person for any internal revenue tax”
- Subpoena power is subject to privileges

I.R.C. § 7602(a).

Cavallaro v. United States, 284 F.3d 236 (1st Cir. 2002);
United States v. Richey, 632 F.3d 559 (9th Cir. 2011).

VII. Audit (cont'd)

12. File protective claims if necessary
 - Variance doctrine

I.R.C. §§ 6031(A), 6222-6231.

VII. Audit (cont'd)

13. Keep Partnership in place

See Estate of Bigelow v. Comm'r, 89 T.C.M. (CCH) 954 (2005), *aff'd*, 503 F.3d 955 (9th Cir. 2007).

VII. Audit (cont'd)

14. If you're in an audit of an estate . . .

- Refrain from distributing Partnership interests held in estate to beneficiaries
- Save any estate audit expenses for deduction at conclusion of matter
 - on Form 4421
 - consider not taking expenses as deductions on estate's 1041s
 - advise Executor to consider keeping track of time spent on estate matters

I.R.C. § 6324;
31 U.S.C. § 3713;
I.R.C. § 2204.

VII. Audit (cont'd)

15. Treat informal interviews as depositions
 - Prepare witnesses as if for a deposition
 - Conduct interview at advisor's office, rather than client's office

Relevant Cites

<u>Topic(s)</u>	<u>Citation</u>
2036:	<i>Estate of Abraham v. Comm'r</i> , 87 T.C.M. (CCH) 975 (2004), <i>aff'd</i> , 408 F.3d 26 (1 st Cir. 2005)
Valuation:	<i>Adams v. United States</i> , 83 A.F.T.R.2d 1887 (N.D. Tex. Mar. 17, 1999), <i>rev'd</i> , 218 F.3d 383 (5 th Cir. 2000)
Valuation:	<i>Adams v. United States</i> , 218 F.3d 383 (5 th Cir. 2000), <i>entered by</i> 88 A.F.T.R.2d 6057 (N.D. Tex. 2001)
Burden of Proof:	<i>Estate of Adell v. Comm'r</i> , 108 T.C.M. (CCH) 107 (2014)
Aggregation:	<i>Estate of Adler v. Comm'r</i> , 101 T.C.M. (CCH) 1118 (2011)
Work Product Doctrine:	<i>United States v. Adlman</i> , 68 F.3d 1495 (2 ^d Cir. 1995)
Aggregation:	<i>Ahmanson Foundation v. United States</i> , 674 F.2d 761 (9 th Cir. 1981)
Valuation:	<i>Estate of Amlie v. Comm'r</i> , 91 T.C.M. (CCH) 1071 (2006)
Post-Event Facts:	<i>Estate of Andrews v. United States</i> , 850 F. Supp. 1279 (E.D. Va. 1994)
Valuation:	<i>Astleford v. Comm'r</i> , 95 T.C.M. (CCH) 1497 (2008)
Valuation:	<i>Estate of Baird v. Comm'r</i> , 82 T.C.M. (CCH) 666 (2001), <i>rev'd and remanded</i> , 416 F.3d 442 (5 th Cir. 2005)
2036:	<i>Estate of Beyer v. Comm'r</i> , 112 T.C.M. (CCH) 356 (2016)
Indirect Gift:	<i>Estate of Bies v. Comm'r</i> , 80 T.C.M. (CCH) 628 (2000)
2036:	<i>Estate of Bigelow v. Comm'r</i> , 89 T.C.M. (CCH) 954 (2005), <i>aff'd</i> , 503 F.3d 955 (9 th Cir. 2007)
2036:	<i>Estate of Bischoff v. Comm'r</i> , 69 U.S. 32 (1977)
2036, Promissory Notes, Marital Deduction Mismatch:	<i>Estate of Black v. Comm'r</i> , 133 T.C. 340 (2009), <i>supp. by</i> 103 T.C.M. (CCH) 1302 (2012)
2036:	<i>Estate of Bongard v. Comm'r</i> , 124 T.C. 95 (2005)
Aggregation:	<i>Estate of Bonner v. United States</i> , 84 F.3d 196 (5 th Cir. 1996)

Relevant Cites (cont'd)

<u>Topic(s)</u>	<u>Citation</u>
Indirect Gift:	<i>Estate of Bosca v. Comm'r</i> , 76 T.C.M. (CCH) 62 (1998)
2036:	<i>Estate of Boykin v. Comm'r</i> , 53 T.C.M. (CCH) 345 (1987)
Aggregation:	<i>Estate of Bright v. United States</i> , 658 F.2d 999 (5 th Cir. 1981)
2036:	<i>United States v. Byrum</i> , 408 U.S. 125 (1972)
Privileges:	<i>Cavallaro v. United States</i> , 153 F. Supp. 2d 52 (Mass. 2001), <i>aff'd</i> , 284 F.3d 236 (1 st Cir. 2002)
Burden of Proof, Valuation:	<i>Cavallaro v. Comm'r</i> , 108 T.C.M. (CCH) 287 (2014), <i>aff'd in part, rev'd in part, remanded</i> , 842 F.3d 16 (1 st Cir. 2016)
Aggregation:	<i>Estate of Chenowith v. Commissioner</i> , 88 T.C. 1577 (1987)
Defined Value:	<i>Estate of Christiansen v. Comm'r</i> , 130 T.C. 1 (2008), <i>aff'd</i> , 586 F.3d 1061 (8 th Cir. 2009)
2703, Gift on Formation, Valuation:	<i>Church v. United States</i> , 85 A.F.T.R.2d 804 (W.D. Texas 2000), <i>aff'd</i> , 268 F.3d 1063 (5 th Cir. 2001)
2036:	<i>Comm'r v. Church's Estate</i> , 335 U.S. 632 (1949)
Aggregation:	<i>Estate of Clarke v. Comm'r</i> , 35 T.C.M. (CCH) 1482 (1976)
2036:	<i>Estate of Cohen v. Comm'r</i> , 79 T.C. 1015 (1982)
Aggregation:	<i>Estate of Curry v. United States</i> , 706 F.2d 1424 (7 th Cir. 1983)
Valuation:	<i>Estate of Dailey v. Comm'r</i> , 82 T.C.M. (CCH) 710 (2001)
Valuation:	<i>Estate of Davis v. Comm'r</i> , 110 U.S. 530 (1998)
Valuation:	<i>Estate of Deputy v. Comm'r</i> , 85 T.C.M. (CCH) 1497 (2003)
Aggregation:	<i>Estate of Dieringer v. Comm'r</i> , 146 T.C. 117 (2016)
2036:	<i>Estate of Disbrow v. Comm'r</i> , 91 T.C.M. (CCH) 794 (2006)
Promissory Notes:	<i>Estate of Duncan v. Comm'r</i> , 102 T.C.M. (CCH) 421 (2011)
Valuation (built-in gains):	<i>Estate of Dunn v. Comm'r</i> , 301 F.3d 339 (5 th Cir. 2002)
Valuation:	<i>Eisenberg v. Comm'r</i> , 155 F.3d 50 (2d Cir. 1998)
2703:	<i>Estate of Elkins v. Comm'r</i> , 140 T.C. 86 (2013)
2036:	<i>Estate of Erickson v. Comm'r</i> , 93 T.C.M. (CCH) 1175 (2007)

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<u>Topic(s)</u>	<u>Citation</u>
Valuation:	<i>Evenchik v. Comm'r</i> , 105 T.C.M. (CCH) 1231 (2013)
Annual Exclusion:	<i>Fisher v. United States</i> , 105 A.F.T.R.2d 1347 (S.D. Ind. 2010)
2703:	<i>Fisher v. United States</i> , 106 A.F.T.R.2d 6144 (S.D. Ind. 2010)
Post-Event Facts:	<i>Estate of Foster v. Comm'r</i> , 101 T.C.M. (CCH) 1444 (2011)
Work Product Doctrine:	<i>United States v. Frederick</i> , 182 F.3d 496 (7 th Cir. 1999)
Valuation:	<i>Estate of Gallagher v. Comm'r</i> , 101 T.C.M. (CCH) 1702 (2011)
Promissory Notes:	<i>Estate of Gilman v. Comm'r</i> , 88 T.C.M. (CCH) 627 (2004)
Valuation:	<i>Estate of Gimbel v. Comm'r</i> , 92 T.C.M. (CCH) 504 (2006)
Valuation:	<i>Estate of Giovacchini v. Comm'r</i> , 105 T.C.M. (CCH) 1179 (2013)
Valuation:	<i>Estate of Giustina v. Comm'r</i> , 101 T.C.M. (CCH) 1676 (2011), <i>rev'd, remanded</i> , 586 Fed. Appx. 417 (9 th Cir. 2014)
2036:	<i>Estate of Gore v. Comm'r</i> , 93 T.C.M. (CCH) 1436 (2007)
2053; Promissory Notes:	<i>Estate of Graegin v. Comm'r</i> , 56 T.C.M. (CCH) 387 (1988)
Valuation:	<i>Estate of Green v. Comm'r</i> , 86 T.C.M. (CCH) 758 (2003)
Valuation:	<i>Estate of Gribauskas v. Comm'r</i> , 116 T.C. 142 (2001), <i>rev'd</i> , 342 F.3d 85 (2d Cir. 2003)
Indirect Gift:	<i>Gross v. Comm'r</i> , 96 T.C.M. (CCH) 187 (2008)
2503, Annual Exclusion Gifts:	<i>Hack'l v. Comm'r</i> , 118 T.C. 279 (2002), <i>aff'd</i> , 335 F.3d 664 (7 th Cir. 2003)
2036, Recycling of Value:	<i>Estate of Harper v. Comm'r</i> , 83 T.C.M. (CCH) 1641 (2002)
2036, Aggregation:	<i>Estate of Harrison v. Comm'r</i> , 52 T.C.M. (CCH) 1306 (1987)
Indirect Gift:	<i>Heckerman v. United States</i> , 104 A.F.T.R.2d 5551 (W.D. Wash. 2009)
Defined Value:	<i>Hendrix v. Comm'r</i> , 101 T.C.M. (CCH) 1642 (2011)
2036:	<i>Estate of Hillgren v. Comm'r</i> , 87 T.C.M. (CCH) 1008 (2004)
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2703, Indirect Gift, Valuation:	<i>Holman v. Comm'r</i> , 130 T.C. 170 (2008), <i>aff'd</i> , 601 F.3d 763 (8 th Cir. 2010)
2036:	<i>Estate of Hurford v. Comm'r</i> , 96 T.C.M. (CCH) 422 (2008)
2036:	<i>Hutchens v. Comm'r</i> , 66 T.C.M. (CCH) 1599 (1993)
Valuation (built-in gains) Constitutionality:	<i>Estate of Jameson v. Comm'r</i> , 267 F.3d 366 (5 th Cir. 2001), <i>vacating, remanding</i> 77 T.C.M. (CCH) 1383 (1999)
Valuation (built-in gains):	<i>Estate of Jelke v. Comm'r</i> , 507 F.3d 1317 (11 th Cir. 2007), <i>vacating, remanding</i> 89 T.C.M. (CCH) 1397 (2005)
Valuation (built-in gains):	<i>Estate of Jensen v. Comm'r</i> , 100 T.C.M. (CCH) 138 (2010)
Indirect Gift, Valuation:	<i>Jones v. Comm'r</i> , 116 T.C. 121 (2001)
2036, Equitable Recoupment:	<i>Estate of Jorgensen v. Comm'r</i> , 97 T.C.M. (CCH) 1328 (2009), <i>aff'd</i> , 431 Fed. Appx. 544 (9 th Cir. 2011)
Valuation:	<i>Estate of Jung v. Comm'r</i> , 101 T.C. 412 (1993)
2701:	<i>Estate of Karmazin v. Comm'r</i> , T.C. Docket No. 2127-03 (settled prior to disposition)
2036, Promissory Notes, Valuation:	<i>Keller v. United States</i> , 104 A.F.T.R.2d 6015 (S.D. Tex. 2009), <i>aff'd</i> , 697 F.3d 238 (5 th Cir. 2012)
Valuation:	<i>Estate of Kelley v. Comm'r</i> , 90 T.C.M. (CCH) 369 (2005)
2036:	<i>Estate of Kelly v. Comm'r</i> , 103 T.C.M. (CCH) 1393 (2012)
2704:	<i>Kerr v. Comm'r</i> , 113 T.C. 449 (1999), <i>aff'd</i> , 292 F.3d 490 (5 th Cir. 2002)
2036:	<i>Kimbell v. United States</i> , 244 F. Supp. 2d 700 (N.D. Tex. 2003), <i>vacated, remanded</i> , 371 F.3d 257 (5 th Cir. 2004)
2036:	<i>Estate of King v. Comm'r</i> , 37 T.C. 973 (1962)
Valuation:	<i>In the Matter of King</i> , 424 F. Supp. 117 (D.C. Colo. Jan. 28, 1975), <i>aff'd</i> , 545 F.2d 700 (10 th Cir. 1976)
2519:	<i>Estate of Kite v. Comm'r</i> , 105 T.C.M. (CCH) 1277 (2013)

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<u>Topic(s)</u>	<u>Citation</u>
2036, Valuation:	<i>Estate of Knepp v. United States</i> , 358 F. Supp. 2d 421 (M.D. Pa. 2004)
2704, Valuation:	<i>Knight v. Comm'r</i> , 115 T.C. 506 (2000)
2031, 2032, 2512, Valuation:	<i>Kohler v. Comm'r</i> , 92 T.C.M. (CCH) 48 (2006)
Promissory Notes, Valuation:	<i>Koons v. Comm'r</i> , 105 T.C.M. (CCH) 1567 (2013)
2036:	<i>Estate of Korby v. Comm'r</i> , 89 T.C.M. (CCH) 1150 (2005), <i>aff'd</i> , 471 F.3d 848 (8 th Cir. 2006)
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Valuation:	<i>United States v. Land</i> , 303 F.2d 170 (5 th Cir. 1962)
Valuation:	<i>Lappo v. Comm'r</i> , 86 T.C.M. (CCH) 333 (2003)
2053:	<i>Estate of Lasarzig v. Comm'r</i> , 78 T.C.M. (CCH) 448 (1999)
Aggregation:	<i>Estate of Lehmann v. Comm'r</i> , 74 T.C.M. (CCH) 415 (1997)
Valuation:	<i>Levy v. United States</i> , No. A-07-CA-339-LY (W.D. Tex. Nov. 26, 2008), <i>aff'd</i> , 402 Fed. Appx. 979 (5 th Cir. 2010)
2036:	<i>Estate of Liljestrand v. Comm'r</i> , 102 T.C.M. (CCH) 440 (2011)
Indirect Gift:	<i>Linton v. United States</i> , 638 F. Supp. 2d 1277 (W.D. Wash. 2009), <i>rev'd in part, remanded</i> , 630 F.3d 1211 (9 th Cir. 2011)
Valuation:	<i>Litman v. United States</i> , 78 Fed. Cl. 90 (2007)
2036:	<i>Estate of Lockett v. Comm'r</i> , 103 T.C.M. (CCH) 1671 (2012)
Aggregation:	<i>Estate of Lopes v. Comm'r</i> , 78 T.C.M. (CCH) 46 (1999)
Valuation, Undivided Interest:	<i>Ludwick v. Comm'r</i> , 99 T.C.M. (CCH) 1424 (2010)
2036, Indirect Gift:	<i>Estate of Malkin v. Comm'r</i> , 98 T.C.M. (CCH) 57938 (2009)
Valuation:	<i>Mandelbaum v. Comm'r</i> , 69 T.C.M. (CCH) 2852 (1995)

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<u>Topic(s)</u>	<u>Citation</u>
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Valuation:	<i>Estate of McFarland v. Comm'r</i> , 72 T.C.M. (CCH) 673 (1996)
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2036:	<i>Estate of McNichols v. Comm'r</i> , 265 F.2d 667 (3d Cir. 1959)
Aggregation:	<i>Estate of Mellinger v. Comm'r</i> , 112 T.C. 26 (1999)
2036:	<i>Estate of Miller v. Comm'r</i> , 97 T.C.M. (CCH) 1602 (2009)
2036:	<i>Estate of Mirowski v. Comm'r</i> , 95 T.C.M. (CCH) 1277 (2008)
2036, Promissory Notes:	<i>Estate of Murphy v. United States</i> , 104 A.F.T.R.2d 7703 (W.D. Ark. 2009)
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Valuation:	<i>Peracchio v. Comm'r</i> , 86 T.C.M. (CCH) 412 (2003)
Defined Value:	<i>Petter v. Comm'r</i> , 98 T.C.M. (CCH) 534 (2009), <i>aff'd</i> , 653 F.3d 1012 (9 th Cir. 2011)
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2036:	<i>Estate of Powell v. Comm'r</i> , 148 T.C. ____ (2017)
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2036:	<i>Estate of Reichardt v. Comm'r</i> , 114 T.C. 144 (2000)
2036:	<i>Reinecke v. Northern Trust Co.</i> , 278 U.S. 339 (1929)
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Indirect Gift:	<i>Senda v. Comm'r</i> , 88 T.C.M. (CCH) 8 (2004), <i>aff'd</i> , 433 F.3d 1044 (8 th Cir. 2006)
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Topic(s)	Citation
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Privileges:	<i>Sims v. Lakeside School</i> , No. 06cv1412 (RSM) (W.D. Wash. Sept. 20, 2007)
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<u>Topic(s)</u>	<u>Citation</u>
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IRS Settlement Guidelines:	07 No. 020 BNA Taxcore 25; http://www.irs.gov/pub/irs-utl/asq_penalties_family_limited_pships_finalredacted_10_20_06.pdf
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Investment Company Rules:	I.R.C. § 368
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