

## T&E - Tax Alert October 13, 2008

Gross v. Commissioner of Internal Revenue, 120 T.C. No. 221 filed Sept. 29, 2008.

For the second time in the space of 3 months, the U.S. Tax Court has considered a challenge to an FLP under IRC section 2511 as an indirect gift. The Service however went into this litigation with presumed high confidence that it would win on that issue because it stipulated with the taxpayer that it would accept a combined lack-of-minority and marketability discount of 35% *if* it could be shown that the 11 days between the transfer of funds by the founder to the FLP and the creation of limited partnership interests did not make it an indirect gift. Since the partnership was invested in a portfolio of blue chip equities, the combined stipulated discount appears generous. In fact, the partners did not execute a partnership agreement until after the transfer was completed. Six months earlier, the FLP had complied with all other filing and notice requirements under New York state law. The service, in fact, claimed that the partnership did not formally exist until execution of the agreement, thus conveniently telescoping formation, funding and interest distribution into a single day.

The case was decided by the same Judge who heard Holman [May 27, 2008, T.C. 2008-12] in which the Court decided that 6 days between funding and interests distribution was sufficient to disqualify the transfer as an indirect gift and also threw out the “step transaction doctrine” or treating a series of intertwined events as one for tax purposes. In this matter, the Court could not see any difference in facts, particularly since under New York law, a general partnership is in existence when the certificate is filed with the secretary of state. Making it a limited partnership later has no bearing on the issue. Accordingly, the taxpayer “won” and the Court adopted the 35% combined discount.

Curiously, the Service in Gross did not raise IRC 2036, as it did successfully in Holman. It is possible, however, that those issues will continue to be raised in estate cases.

The decision is at: <http://www.ustaxcourt.gov/InOpHistoric/Gr9oss.TCM.WPD.pdf>. A copy has been placed on my practice's website at <http://www.NYNJCT-BV.com/Gr9oss.pdf> Please do not hesitate to call or e-mail to discuss this or any other valuation issue.

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