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Thomas H. Holman, Jr. and Kim D.L. Holman v. Commissioner of Internal Revenue, 120 T.C. No. 12 filed May 27, 2008.

Mr. Holman had accumulated a sizeable bloc of Dell stock. After his retirement, he and his wife formed a family limited partnership, funded with the Dell stock; large limited interests were then gifted to trusts for their daughters in 1999, 2000 and 2001. The FLP was formed in response to the Holmans' concern that regular trust accounts did not address their concerns about maintaining the wealth of the children, i.e. possible dissipation, did not provide for the long term and did not involve them in the management process.

The Service argued that the first large transfer was an indirect gift of Dell shares, as opposed to a gift of FLP units. The Service also argued that any discount would be limited under IRC 2703 (a) (2.) Finally, the Service disagreed with the application of discounts. The Service lost its first argument but prevailed on IRC 2703 (a) (2) and on discounts.

In view of the strict adherence to the partnership formalities, the Court saw no reason to consider the indirect gift argument, particularly as contributions were properly allocated, unlike in Shepherd and Senda which involved assets of static values.

On IRC 2703 (a) (2) the Court found that, because the Holmans' motives were personal and thus not entirely business-related, the transfer restrictions were not bona fide business arrangements and were a mere testamentary device. Despite legal expert testimony, the Court declined to rule on the "terms similar to arm's length transactions" because the other two conditions were not met. Accordingly, the transfer restrictions were ignored in computing the discounts.

Closed-end investment funds were used by both experts to support Lack-of-Control discounts, but the Service's expert prevailed by not adding industry-specific equity funds to the mix, and by refraining from making unsupported adjustments in an attempt to mimic the FLP' unique investment strategy [hold only Dell stock.] In the end, the Court determined its LOC discount from net asset vale at 11%,14% and 4% for each of the transfers, respectively.

On the issue of the Lack-of-Marketability discount, the Court rejected one expert's reliance on the restricted stock studies [SEC rule 144] and espoused the other's more controversial idea that it should be limited to 12% because most of discounts observed in the restricted stock studies involve both a lack of liquidity or lack of market access, and an irrelevant holding period component.

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

J. L. PIERSON, ASA
Business Valuation
mailto:jlp@NYNJCT-BV.COM
http://www.NYNJCT-BV.COM
(203) 325-2703 Office
(203) 504-7925 Fax
(203) 434-4648 Cell
P.O. Box 2392 Darien CT 06820-0392