

To: abc@abclaw.com  
Subject: FLP Implications of Kimbell v. U.S. 5th US Appeals' Court decision of 5/24/04.  
From: "J.L. Pierson, ASA" <jlp@NYNJCT-BV.COM>  
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Dear Attorney ABC:

The U.S. 5th Circuit has provided some hope for shocked estates as the IRS had been winning quite a few battles on the subject of including FLP-transferred decedend's assets in his/her estate pursuant to IRC section 2036. The decision - Kimbell v. United States, US Court of Appeals for the 5th Circuit, filed May 2, 2004 - could stop the IRS along its line of reasoning. By providing a new "definition" of 2036 and remanding the case to the US District Court, the decision could lead to a more logical interperatation of the law.

The Court of Appeals' opinion is at:  
<ftp://opinions.ca5.uscourts.gov/pub/03/03-10529-CV0.wpd.pdf>

and, just in case.. it is attached to this e-mail. I have no faith in technology; if you need to, e-mail me and I will send you what I have.

By broadly interpreting the "bona fide sale" exemption, the appeals court reviewed the reasoning of the other courts and found it lacking; it substituted a more logical interpretation.

WITH THE PROVISIO THAT I AM NOT A LAWYER, here is my spin on this.

In order to qualify for the 'bona fide sale for adequate and full value of money and money's worth' exemption to IRC 2036 - without which the assets revert to the estate in full - previous courts have directed that the asset transfer can not be "a mere recycling of value," which they construed to exist if the relationship between the decedent and the assets remains largely unchanged after the transfer to the entity. The Appeal Court here replaced this No Recycling of Value prerequisite with **Business Purpose**.

Specifically, the 5th Circuit determined that the bona fide sale exemption is a two-part test: it must be **"arms' length"** and there must be **"adequate and full consideration"**.

The "adequate and full consideration" test is further divided into 3 parts:

**Is each interest credited to each partner proportionally to to the fair market value of the assets contributed by each partner ?**

**Are the assets properly credited to the partners' respective capital accounts ?**

**Are the partners on termination entitled to distribution in amounts equal to their respective capital accounts ?**

The decision clarifies 2036 (a) (2) which states that the assets are pulled back into the estate if the decedend has retained the right, either alone or in conjunction with another person, to designate who shall possess or enjoy the property and its concome. The 5th Circuit thus decided that the previous application was incorrect, and ignored the "in conjunction with any person" portion of 2036(a)(2).

An **important** decision, don't you think ? Regards.

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