Section 1

Valuation Issues for Estate and Gift Taxes

Hypothetical #1: Valuation Issues

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Hypothetical #1
Valuation

Mr. H dies, age 89, January 15, 2003, having survived his wife, Mrs. H, by several years. In addition to his homestead and inconsequential personalty, he owns the following as of date of death:

1. A 50% undivided interest in the family ranch. The property is about 1,200 acres of picturesque timberland in the old East Texas Oil Field. Mineral rights associated with the land were transferred to the Family Limited Partnership (FLP) (discussed below) some six years prior to date of death. There is some oil production, both working interest and royalty interest, and several old, unreclaimed well sites. The standing timber is marketable but harvesting would substantially reduce the aesthetic value of the property.

2. The FLP was formed prior to his spouse's death, the original partners being Mr. H and Mrs. H, each owning 49.5% as limited partners with a 1% corporate general partner owned 50-50. The FLP's original assets were cash and cash equivalents contributed by Mr. and Mrs. H from community property. The FLP has continued to invest in similar property. The original equity interests were distributed in proportion to the value of the contributions. Within the first year of the partnership's existence, Mr. and Mrs. H made annual gifts of fractional limited partnership interests to each of their five adult children; a pattern that has continued in each subsequent year. In the second year of the FLP, after the first round of gifting, Mr. and Mrs. H contributed the mineral rights described above; without a valuation study and without changing either capital accounts or partnership percentages. No gift tax returns have ever been filed. As of the date of death, Mr. H owned 34% limited partnership interest and continued to own his 50% interest in the corporate GP; the balances of both the LP and GP interests were split evenly among the five children.

Several months prior to his death, Mr. H was persuaded to place the bulk of his personal funds in a dubious investment. That scheme obliged him to make additional investments periodically, some of which were unpaid at date of death. Upon review, it appears the scheme was fraudulent and Mr. H may have a cause of action against the promoters. However, that cause of action is imperiled by Mr. H's unavailability to testify and the precarious financial condition of the potential defendants.

All told, Mr. H's assets, under any valuation scenario, exceed the minimum reporting requirements and a 706 will have to be filed.

VALUATION ISSUES FOR ESTATE AND GIFT TAXES

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VALUATION ISSUES FOR ESTATE AND GIFT TAXES

I. GUERILLA WARFARE, BUILT-IN GAINS TAX AND VALUATION METHODOLOGY - THE FIFTH CIRCUIT REVERSES THE TAX COURT AGAIN

AGAIN. *Estate of Dunn v. Commissioner*, 2002 U.S.T.C. ¶ 60,446 (5th Cir. 2002), *rev'g and remanding* 83 T.C.M. (CCH) 1337 (2000).

A. General Facts. The Decedent owned a 62.96% common stock interest in a Texas C corporation that was in the heavy equipment leasing business. The corporation had been in business for 42 years and had been unable to raise its rental rates for more than 10 years due to competition. Since the Decedent owned less than two-thirds (2/3) of the stock, she could not compel a liquidation of the corporation or a sale of all or substantially all of its assets.

The Decedent died in June 1991. The Tax Court trial did not occur until June 1996. Thereafter, it took the Tax Court approximately 3 ½ years to issue its opinion.

Prior to trial, the IRS amended its answer to roughly double the value of Decedent's stock. The Estate had valued the stock in the Federal estate tax return at $1,635,465 and subsequently obtained an appraisal reducing the value to $1,582,185. The notice of deficiency asserted a value of $2,229,043, and the amended answer asserted a value of $4,430,238. Nevertheless, the IRS did not have a valuation expert at trial. It only used an accounting expert to "snipe" at the methodology of the Estate's valuation expert.

The Tax Court valued the corporation by assigning a weight of 35% to its earnings based valuation of $1,321,740 and 65% to its asset based value of $7,922,892. In calculating the asset based or liquidation value, the court reduced the value of the assets by only a 5% built-in gains tax as it viewed liquidation as unlikely. The court also allowed a 15% lack of marketability discount and a 7.5% lack of super-majority control discount, for a total discount of 22.5%. Based on these conclusions, the Tax Court found the value of Decedent's stock to be $2,738,558.

On appeal, the Estate contested the weighting of the two valuation approaches and the magnitude of the built-in gains tax. Otherwise, the valuations and the discounts were not appealed.

B. Holding. Reversed and remanded.

1. **Standard for Review**. The determination of fair market value is a mixed question of fact and law for which the factual premises are subject to review on a clearly erroneous standard, and the legal conclusions are subject to *de novo* review. The mathematical computation of fair market value is an issue of fact, but determination of the appropriate valuation method is an issue of law to be reviewed *de novo*.

2. **Built-In Gains Tax**. As a matter of law, the 34% built-in gains tax liability of a C corporation is a dollar-for-dollar reduction when calculating the asset-based value of the corporation.

3. **Weighting of the Two Valuation Approaches**. The proper method of valuing the stock of the corporation, under all the relevant circumstances and discrete facts (not the least of which is the "unlikelihood" of liquidation of its assets), requires assigning a weight to its earnings-based value somewhere between 75% and 90%, and to its asset-based value somewhere between 10% and 25%. Within these ranges, the court selected 85% for the earnings-based weight and 15% for the asset-based weight, producing an 85:15 weighting ratio.

C. Highlights of the Fifth Court's Analysis.

1. **The Guerilla Warfare**. The court was highly critical of the IRS' actions through the Tax Court trial. The court's comments included the following:

> The Commissioner's posture on appeal is a stark departure from his pre-trial and trial position: amending his answer to quadruple the Estate's tax deficiency as originally assessed, urging the Tax Court to disregard totally the built-in tax liability of the Corporation's assets, insisting that the Corporation be valued solely on asset values, and urging that no consideration whatsoever be given the earnings or cash-flow based approach to valuation. Indeed, at trial, the Commissioner did not favor the Tax Court with testimony of an expert appraiser, even though the Commissioner had affirmatively proposed his own, geometrically higher value for the Decedent's block of stock ---- values that

> started out higher than the ones reported on the estate tax return and that were then multiplied, by virtue of the Commissioner's amended answer, to almost four times the Estate's figures. Yet, instead of supporting his own higher values (for which he had the burden of proof) by proffering professional expert valuation testimony during the trial, the Commissioner merely engaged in guerrilla warfare, presenting only an *accounting* expert to snipe at the methodology of the Estate's *valuation* expert. The use of such trial tactics might be legitimate when merely contesting values proposed by the party opposite, but they can never suffice as support for a higher value affirmatively asserted by the party employing such a trial strategy. This is particularly true when, as here, that party is the Commissioner, who has the burden of proving the expanded value asserted in his amended answer.
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> Using such tactics remains the prerogative of the Commissioner and his trial counsel, at least up to a point. But when his choice of tactics is viewed in the framework of the substantive valuation methodology urged by the Commissioner in the Tax Court, his posture at trial is seen to be so extreme and so far removed from reality as to be totally lacking in probative value.

2. **<u>The Realities of the Built-In Gains Tax</u>**. In concluding that all of the potential built-in gains tax liability should be deducted in computing a C corporation's asset based value, the court reasoned as follows:

> The Tax Court's fundamental error . . . is reflected in its statement that ---- for purposes of an asset-based analysis of corporate value ---- a fully-informed willing buyer of *corporate shares* (as distinguished from the Corporation's assemblage of assets) constituting an operational-control majority would *not* seek a substantial price reduction for built-in tax liability, absent that buyer's intention to

liquidate. This is simply wrong: It is inconceivable that, since the abolition of the *General Utilities* doctrine and the attendant repeal of relevant I.R.C. sections, such as §§333 and 337, any reasonably informed, fully taxable buyer (1) of an operational-control majority block of stock in a corporation (2) *for the purpose of acquiring its assets,* has not insisted that all (or essentially all) of the latent tax liability of assets held in corporate solution be reflected in the purchase price of such stock.

We are satisfied that the hypothetical willing buyer of the Decedent's block of . . . stock would demand a reduction in price for the built-in gains tax liability of the Corporation's assets at essentially 100 cents on the dollar, regardless of his subjective desires or intentions regarding use or disposition of the assets. Here, that reduction would be 34%. This is true "in spades" when, for purposes of computing the *asset*-based value of the Corporation, we assume (as we must) that the willing buyer is purchasing the stock to get the assets, whether in or out of corporate solution.
. . .
. . .

In other words, when one facet of the valuation process requires a sub-determination based on the value of the company's assets, that value must be tested in the same willing buyer/willing seller crucible as is the stock itself, which presupposes that the property being valued is in fact bought and sold. It is axiomatic that an asset-based valuation starts with the gross market (sales) value of the underlying assets themselves, and, as observed, the Tax Court's finding in that regard is unchallenged on appeal: When the starting point is the assumption of sale, the "likelihood" is 100%!

(footnote omitted)

See also Estate of Jameson v. Commissioner, 267 F.3d 366, 372 (5th Cir. 2001).

3. **<u>The Weighting</u>**. Based on factual stipulations and findings in the Tax Court trial, there was little likelihood that the corporation would be liquidated. Even though the Estate's valuation expert had proposed a 50:50 weighting, the court found the much more favorable weight of 85:15 for the Estate, reasoning as follows:

> Given the stipulated or agreed facts, the additional facts found by the Tax Court, and the correct determination by that court that the likelihood of liquidation was minimal, our expectation would be that if the court elected to assign unequal weight to the two approaches, it would accord a minority (or even a nominal) weight to the asset-based value of the Corporation, and a majority (or even a super-majority) weight to the net cash flow or earnings-based value. Without explanation, however, the Tax Court baldly ---- and, to us, astonishingly ---- did just the opposite, assigning a substantial majority of the weight to the *asset-based* value. The court allocated almost two-thirds of the weight (65%) to the results of the asset-based approach and only slightly more than one-third (35%) to the results of the earnings-based approach. We view this as a legal, logical, and economic non sequitur, inconsistent with all findings and expressions of the court leading up to its announcement of this step in its methodology. We also note that the Tax Court's ratio roughly splits the difference between the 50:50 ratio advanced by the Estate and the 100:0 ratio advocated by the Commissioner.
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> . . .
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> When we review the objective, factual record in this case ---- which is all that remained for the Tax Court to rely on after it disregarded most expert testimony ---- we are left with the definite impression that an error was committed at the weighting step of the method employed here. This review also mandates

> that something between zero and a small percentage of weight be assigned to the Corporation's asset-based value, and that the remainder of the weight be assigned to its earnings-based value. Under different circumstances, we might be inclined to remand for the Tax Court to make another try at assigning relative weights and constructing a reasonable ratio. Given the state of the record and the seven-plus years that this case has languished in the courts (over a year now in ours), such a remand, coupled with its potential for yet another appeal, militates against sending this particular issue back to the Tax Court. After all, the record of this case, free as it is of credibility calls and genuine disputes of material fact between the parties (other than as to their experts) places us in exactly the same methodological vantage point as the Tax Court when it comes to assigning relative weights to the results of the valuation approaches employed. This is true regardless of whether that assignment be labeled a question of law or a mixed question of fact and law.

D. **Remand**. On remand, the court instructed to the Tax Court to do the following:

1. **Calculation**. The Tax Court was given precise instructions as to how to calculate the value of the Decedent's stock in light of the court's holding, leaving in it no discretion whatsoever.

2. **Attorney Fees and Costs**. Given the IRS' delays in issuing the notice of deficiency and its extreme and unjustifiable trial position in advocating a valuation based entirely on asset value (with no reduction for built-in tax liability and no weight given to income-based value), exacerbated by its failure to adduce expert appraisal testimony in support of its exorbitant proposed value, the court directed the Tax Court to entertain any claim that the Estate might elect to assert under Section 7430 of the Code, if the re-valuation of the Decedent's block of stock should reduce the net worth of the Estate to a sum below the 2 million cap on entitlement to relief under that section.

E. **Comments**.

1. **Standard for Review**. The most important aspect of this case is its holding that the appropriate valuation methodology is an issue of law. This will make the appeal of Tax Court valuation cases dramatically easier when the Tax Court ignores accepted appraisal methodology and attempts to characterize everything as a finding of fact subject to appellate review under the higher standard of clearly erroneous.

2. **3% of the Built-In Gains Tax Was Missed**. The correct rate for the built-in gains tax for a Texas C corporation is 37%. This consists of the 34% Federal rate and the 3% effective rate of the 4.5% Texas Franchise tax rate, taking into account the federal income tax deductibility of the Texas franchise tax (.66 x 4.5% = 2.97%).

II. DISCOUNTING THE ESTATE BY DEDUCTING PRE-DEATH IRS CLAIMS.

Estate of O'Neal v. United States, 2002-2 U.S.T.C. ¶ 60,448 (N.D. Ala. 2002), *on remand from* 258 F.3d 1265 (11th Cir. 2001), *aff'g in part, vacating in part and remanding* 1999-2 U.S.T.C. ¶ 60,365 (N.D. Ala. 1999).

A. **Facts**. The Decedent died owning assets valued at $5,303,744 and debts of $13,124. There was also a claim against her estate by her children and grandchildren for transferee tax liability allegedly owed by them because of gifts made by the Decedent to them.

The purported transferee liability involved gift and generation skipping transfer taxes and penalties and interest attributable to the revaluation of certain gifts of stock in a closely held corporation by the Decedent to her children and grandchildren. The Decedent reported the value of the gifted stock in her timely filed gift tax return at $54 per non-voting common share and $61 per voting common share, and the statute of limitations had expired on the gift tax return. Nevertheless, the IRS increased the value of the stock to $375 per non-voting common share and to $415 per voting share. Since the IRS was barred from assessing the asserted deficiency of approximately $7,000,000 against the Decedent, the IRS asserted transferee liability against the children and grandchildren for that amount at the time of the Decedent's death.

The children and grandchildren contested the asserted transferee liability. The grandchildren settled their liability in a Tax Court proceeding more than 9 months after the Decedent's date of death. This settlement was followed in a related Federal district court proceeding filed by the children. The combined settlement of the transferee liability totaled $563,314.

In the original Federal district court proceeding, the district court used hindsight and held that the Decedent's estate could only deduct the $563,314 settlement amount ultimately paid by the Estate to the children and grandchildren for their settled transferee liability. On appeal, the Eleventh Circuit of Appeals reversed, relying in large part on *Estate of Smith v. Commissioner*, 198 F.3d 515 (5th Cir. 1999). As in *Estate of Smith*, the Eleventh Circuit held that the value of a claim must be determined as of the date of a Decedent's death, without consideration of post-death events. Therefore, it instructed the district court on remand to neither admit nor consider evidence of post-death occurrences in determining the date of death value of the children's and grandchildren's claims against the Decedent's estate.

On remand, the Estate presented two expert reports valuing the claim, the first by a retired Federal District Judge with special expertise in tax cases and the second by a practicing attorney specializing in tax matters. The government chose not to offer an expert and only put on testimony regarding the underlying audit that offered no evidence of the value of the claim.

B. **Holding**.

1. **Value of Claim**. The opinion of the Estate's first expert was accepted, and the claim was valued at $5,835,000 as of the date of the Decedent's death.

2. **Deductible Claim**. Since Section 2053(c)(2) limits the deduction of a claim to the value as of a decedent's death of the property subject to claims, the deductible claim is limited to $5,303,744. Since this reduced the Decedent's taxable estate to zero, the full amount of the estate taxes paid by the Estate were ordered refunded, together with interest.

C. **Overview of the Estate's Primary Expert's Valuation Methodology**. Valuing a claim, either as an asset or as a liability, is uncertain at best. Probabilities and educated guesses are an inherit part of the valuation process. In valuing the potential transferee tax liability, the retired Federal District Judge summarized his calculations as follows:

- a 20% to 30% chance of a per-share value at or near $54

  .25 x $54 = $ 13.50

- a 20% to 30% chance of a per-share value at or near $178

  .25 x $178 = $44.50

- a 20% to 30% chance of a per-share value at or near $375

  .25 x $375 = $ 93.75

- a 20% to 30% chance of a per-share value at or near the intermediate point between $54 and $375

  .25 x $214.50 = $ 53.63

- composite per-share value expectancy $205.38

The per-share value of $205.38 resulted in an expected transferee liability, with penalties and interest, of approximately $7,780,000.00. Then, this potential amount was multiplied by 75% to reflect the uncertainties regarding the enforceability of the claim against the Decedent's estate under Alabama law. This resulted in the reduced $5,835,000 value of the claim accepted by the court.

D. Comments.

1. **The IRS and Hindsight**. The IRS has and will continue to use hindsight when it is to the advantage of the IRS. Nevertheless, the law is clear – assets and liabilities must be valued as of the applicable valuation date without regard to subsequent occurrences.

2. **Poetic Justice**. This is another example of "guerilla warfare" by the IRS. This time it paid a high price. A more than $5,000,000 taxable estate was zeroed out as a result of the apparently unsupportable position taken by the IRS in the valuation of the gifted stock.

3. **The Estate Knew How to Pick an Expert**. The retired Federal District Judge whose opinion was accepted had recently retired as Chief Judge of the United States District

Court for the Northern District of Alabama, having served for 29 ½ years. Surprisingly, this case was before the same court.

III. **<u>THE TAX COURT RECYCLES ANOTHER FLP CASE VIA SECTION 2036</u>**. *Estate of Thompson v. Commissioner*, T.C.M. (CCH) 2002-246.

A. **<u>General Facts</u>**. The Decedent was born in 1898, was wealthy and lived in an assisted care facility for approximately ten years preceding his death in 1995. Approximately two years prior to his death, he created two "Fortress" family limited partnerships, one with his son and one with his daughter. On formation, he owned 49% of each of the corporate general partners and a 95.4% limited partnership interest in one of the partnerships and a 62.27% limited partnership interest in the other partnership. The bulk of his assets were transferred to the two limited partnerships and consisted of liquid investments. A combined discount of 40% was claimed for lack of control and lack of marketability in the estate tax return for the Decedent's interests in the entities.

B. **<u>Holdings</u>**.

1. **<u>Burden of Proof</u>**. The IRS had the burden of proof as to its lack of economic substance and business purpose argument and as to Section 2036 as the arguments were not raised in the notice of deficiency. (As is typical in the Tax Court, this shifting of the burden of proof was meaningless.)

2. **<u>Economic Substance</u>**. The entities were validly formed under state law, and potential purchasers would not disregard the partnerships. Thus, the partnerships had sufficient substance to be recognized for Federal estate tax purposes. (Citing *Knight v. Commissioner*, 115 T.C. 506, 513-515 (2000); *Estate of Strangi v. Commissioner*, 115 T.C. 478, 485 (2000), *aff'd on this issue, rev'd., and remanded* 293 F.3d 279, 282 (5th Cir. 2002) (This is a dead issue, even in the Tax Court.)

3. **<u>Section 2036</u>**. Based on the facts and circumstances surrounding both the transfer of the property to the partnership and the subsequent use of the property, the court found an implied agreement or understanding that the Decedent retained the enjoyment and economic benefit of the property transferred to the partnership. Therefore, the court held that the value of the property transferred to the

partnerships was includable in the Decedent's estate under Section 2036(a)(1). The court also found there was no bona fide sale for adequate and full consideration in regard to the formation of the partnerships for purposes of Section 2036(a). In effect, this case was a "recycling" of *Estate of Harper v. Commissioner*, T.C.M. (CCH) 2002-121; *Estate of Reichardt v. Commissioner*, 114 T.C. 144 (2000); and *Estate of Schauerhamer v. Commissioner*, T.C.M. (CCH) 1997-242.

C. The Bad Section 2036 Facts As Interpreted by the Tax Court. Almost everything that was done or not done in regard to the partnerships was viewed by the Tax Court as supporting the implied agreement. Those matters included:

1. Before the formation of the partnerships, the Decedent's daughter had sought assurances from his financial advisors that the Decedent would be able to withdraw assets from the partnerships to make annual cash gifts.

2. The partnerships had made distributions to the Decedent in both years to allow him to make substantial gifts at Christmas to family members.

3. The Decedent had transferred almost all of his wealth to the partnerships, and a distribution from one of the partnerships was required prior to his death for "an infusion" of funds to cover his personal expenses.

4. The composition of the portfolio transferred by the Decedent to the partnerships changed little prior to the Decedent's death, and there was a mere "recycling of value."

5. The partnerships were not involved in active businesses.

6. Based on the Tax Court's interpretation of various arrangements regarding the assets contributed by the younger generation, the court concluded that they had retained the income from the assets contributed by them, i.e., another "recycling."

7. The partnerships made loans exclusively to family members, which "lacked any semblance of legitimate business transactions."

D. Comments.

1. **The Tax Court and Section 2036**. The Tax Court is enamored with its new "recycling" characterization of FLPs and views Section 2036 as applicable to "return the assets of an elderly and wealthy individual who [places] the bulk of his or her assets into a partnership controlled by that individual and his family, while the individual [possesses] continued use of the assets," based on any bad facts the Tax Court can find or imply. As a result, the Tax Court should be avoided if there are any bad facts, and the Tax Court will find most facts to be bad. If at all possible, any proposed deficiency should be paid and a refund pursued in Federal district court.

2. ***Church v. United States*, 85 A.F.T.R. 2d 2000-804 (W.D. Tex. 2000), *aff'd without published opinion*, 268 F.3d 1063 (5th Cir. 2001) (*per curiam*), *unpublished opinion available at* 88 A.F.T.R. 2d 2001-5252 (5th Cir. 2001)**. This case has been totally ignored by the Tax Court. Contrary to the Tax Court's reasoning, the district court held that a contribution of assets to a pro rata family limited partnership constituted a bona fide sale for an adequate and full consideration. As a result, it held that Section 2036 does not apply to a pro rata partnership. Of course, the Decedent in *Church* died two days after the formation of the partnership, leaving little time for the generation of bad facts to support an implied agreement argument by the IRS. Deathbed cases do have their advantages.

IV. ANOTHER FLP "RECYCLED" UNDER SECTION 2036. *Estate of Strangi v. Commissioner*, TC Memo 2003-145 (2003).

A. Facts. In August 1994, the Decedent formed an FLP, receiving a 47% stock interest in the corporate general partner and a 99% limited partner interest. The Decedent transferred approximately $10,000,000 of assets to the limited partnership. The actual formation and transfers were handled by the Decedent's son-in-law under a power of attorney (the "POA"). The FLP named the general partner as managing general partner with the sole discretion to determine distributions and conduct the business affairs of the FLP. The shareholders of the general partner then granted such authority to the POA under the management agreement. The POA therefore acted on behalf of the Decedent and the general partner of the FLP, with full authority to make distribution decisions. Approximately 2 months after formation, the

Decedent died from cancer at the age of 81, when the value of the transferred assets had increased to over $11,000,000.

B. **History**. This case is another example of the Tax Court's recycling of FLP's under Section 2036. The case originated as a reviewed decision in the Tax Court, where the Tax Court rejected the IRS' arguments that the FLP should be ignored under the no business purpose and no economic substance theory of the IRS, and rejected the IRS' strained interpretation that Section 2703 is broad enough to ignore a partnership as a restriction on the right to sell or use the transferred assets. The Tax Court also found there was no gift on formation of the partnership and accepted the IRS expert's combined discount of 31% for the lack of control and the lack of marketability of the limited partnership interest.

Significantly, the Tax Court initially denied as untimely the IRS' Section 2036 argument set forth in a motion filed 52 days before trial. On appeal, however, the Fifth Circuit disagreed, holding that the denial was an abuse of discretion. The Fifth Circuit remanded the case to the Tax Court for consideration of the Section 2036 issue, instructing the Tax Court to either (1) set forth its reasons for adhering to its denial, or (2) reverse its denial and consider the Section 2036 claim. The Fifth Circuit affirmed all other decisions made by the Tax Court. *Estate of Strangi v. Commissioner*, 115 T.C. 478 (2000), *aff'd in part, rev'd in part and remanded sub nom., Gulig v. Commissioner*, 293 F.3d 279 (5th Cir. 2002), *reh'g and reh'g en banc denied*, 2002 U.S. App. Lexis 18782 (5th Cir. Aug. 22, 2002). The Tax Court considered the Section 2036 claim on remand.

C. **Holding on Remand - Transfers Includible under Section 2036**.

1. **No Bona Fide Sales Exception - Assets "Recycled" through Family Entities**. The Tax Court determined that there was no bona fide arm's length sale in connection with the transfer of assets to the FLP by Decedent's attorney-in-fact/son-in-law. The Tax Court found that there was no negotiation with any anticipated interest holders and no full and adequate consideration was given in return for the assets.

2. **Decedent Retained Right to Income**. The Tax Court found that the documents gave the Decedent an unfettered right to distribute income to himself, and that there was an implied agreement that Decedent would retain possession or enjoyment of transferred assets, particularly where the

transfers consisted of 98% of his wealth. In so holding, the Tax Court noted that the FLP made numerous payments for Decedent's personal and estate expenses; Decedent held a 99% interest in the FLP and a 47% stake in the corporate general partner; and Decedent's relationship to the assets did not change after the transfers.

3. **Decedent Retained Right to Designate**. The Tax Court also upheld the alternative argument set forth by the IRS, which was that the Decedent held legally enforceable rights to designate persons who shall possess or enjoy transferred assets and their income. The Tax Court agreed, finding that the governing documents gave Decedent the right to revoke and liquidate the FLP and to declare corporate dividends, which rights were subject to no significant limitation by interposition of any independent trustee, by minimally meaningful intrafamily fiduciary duties or by any oversight of charity which held mere gratuitous 1% interest.

D. IRS Limited to Amount Determined in Deficiency Notice. The IRS failed to assert the increased deficiency in its deficiency notice. The Tax Court held that IRS could not assert a higher value than that determined in the deficiency notice. Moreover, the Taxpayer would be credited on Rule 155 computations with any allowable deductions for costs and expenses incurred subsequent to the initial trial.