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Tax planning strategies to consider before the end of the year

Taxpayers should consider a variety of tax planning steps before the end of the year, including evaluating whether to make any $14,000 annual exclusion gifts. The exclusion applies to both gift tax and generation-skipping transfer tax, making it particularly valuable for gifts to grandchildren. This annual exclusion amount does not carry forward to the next year if unused, so taxpayers must make these gifts each year in order to take maximum advantage of the exclusion. Remember that a taxpayer can make exclusion gifts to an unlimited number of individuals and that a taxpayer and his spouse each have their own $14,000 exclusion amount. Gifts can be made directly to college savings accounts and to trusts (but trusts involve some technical rules, so be sure to contact us for assistance).

Taxpayers who have realized capital gain income, particularly short-term capital gain income, should examine their portfolios to determine whether they have any unrealized losses they would like to harvest before the end of the year. Note, however, that a taxpayer who sells a stock at a loss and buys the same stock within 30 days before or after the sale will have that loss disallowed under what is referred to as the "wash sale" rule.

It is also advisable to consider whether tax-deductible items, such as charitable contributions and state income taxes, should be paid before the end of the year. The alternative minimum tax makes this planning complex. Many itemized deductions, including the deduction for state income taxes, are not allowed for purposes of computing the alternative minimum tax. Therefore, a taxpayer who pays the alternative minimum tax should defer these deductions when possible. Other deductions, including the charitable contribution deduction, are allowed against alternative minimum taxable income as well as against regular taxable income and do not need to be deferred.

A taxpayer who makes a charitable contribution during a year in which he pays alternative minimum tax will realize less value than if the contribution had been made during a year in which the alternative minimum tax was avoided. Unfortunately, many taxpayers pay the alternative minimum tax virtually every year and have no choice. This is often the case for taxpayers who reside in states with high income tax rates, such as California and New York. Fortunately, a taxpayer can increase the benefit of the charitable contribution deduction by making a charitable gift of highly appreciated capital assets held long term, such as stocks. These contributions allow the taxpayer to deduct the capital asset's fair market value without recognizing the unrealized tax gain, and thus receive a form of double benefit. Taxpayers who have stock and want to continue to own it can contribute the stock, then use cash to buy equivalent shares and obtain the higher cost basis. The wash sale rule noted above does not apply in this situation.

Taxpayers with unusually high income this year should evaluate whether it would be beneficial to pay related state income taxes during 2014 rather than waiting until early 2015. Taxpayers sometimes have the opportunity to pay more state income tax before reaching the alternative minimum tax in a high-income year. Additionally, taxpayers may derive a greater benefit from charitable contributions made during high-income years. Of course, careful planning is required because higher income will cause more itemized deductions to be phased out. It is a good idea to review all of these matters with an accounting advisor.

The IRS announces inflation-adjusted amounts for 2015

In October, the IRS announced the 2015 amounts in the Internal Revenue Code (the IRC or the Code) that are subject to annual inflation adjustments. The most significant changes for high-income taxpayers include:

- Tax rates. A married couple filing a joint return will not reach the highest marginal rate of 39.6 percent until their taxable income reaches $464,850 (compared to $457,600 in 2014). For unmarried individuals, the maximum rate is reached at $413,200 (compared to $406,750 in 2014). Trusts and estates will reach the maximum rate at $12,300 (compared to $12,150 in 2014).
- Personal exemption and itemized deduction phaseout. Married taxpayers will begin to lose their personal exemption deductions and have their itemized deductions scaled back when their adjusted gross income reaches $309,900 (compared to $305,080 in 2014). For unmarried individuals the phaseouts begin at an adjusted gross income of $258,250 (compared to $254,200 in 2014). As in the past, a taxpayer cannot lose more than 80 percent of his itemized deductions.
- Estate, gift and generation-skipping transfer tax exemption. The lifetime exemption against these transfer taxes will increase by $90,000, from $5,340,000 to $5,430,000. Taxpayers who have previously used their maximum exemption amounts can now give additional gifts of up to $90,000 without incurring transfer taxes.
- Annual exclusion amount for gifts. The annual exclusion for present interest gifts to an unlimited number of donors will remain at its current level of $14,000.

Case update: Taxpayer's deduction for interest capitalized in loan restructuring is disallowed

In *Copeland (TC Memo 2014-226)*, an October 2014 U.S. Tax Court case, the taxpayer fell behind on his residential mortgage loan and negotiated a loan restructuring with his mortgage lender. In connection with the restructuring, the lender increased the loan's principal balance in an amount equal to the interest that had accrued on the loan. When filing his taxes for the year in which the restructuring occurred, the taxpayer claimed an income tax deduction equal to the amount of the capitalized interest.

After auditing the taxpayer's return for the year in question, the IRS disallowed the interest deduction on the basis that it was inconsistent with the taxpayer's use of the cash receipts and disbursements accounting method for income tax purposes. Under the cash method, which is used by most individual taxpayers, expenses may be deducted for tax purposes only if they are actually paid. If interest is capitalized and added to the loan balance, the taxpayer has not made any actual interest payments and may not deduct interest expenses under the cash accounting method. The Tax Court agreed with the IRS and upheld the denial of the taxpayer's interest deduction.

The taxpayer in *Copeland* might have been able to obtain a deduction if the lender had agreed to make an additional loan to the taxpayer so that the taxpayer could use the loan proceeds to pay the accrued interest on his original loan. The case law on this strategy is mixed, and it is not clear whether an interest expense deduction would be allowed under this arrangement. To have any realistic expectation of getting an interest expense deduction under this arrangement, however, the taxpayer must ensure that the lender deposits the proceeds of the new loan into an account that is controlled solely by the taxpayer. If the taxpayer then writes a check on that account to pay the interest on the original loan, there is some case law to suggest that he would get a deduction. Most lenders, however, will resist depositing additional funds into the hands of a distressed debtor without receiving adequate controls over the debtor's use of those funds.

Case update: The sale of stock triggers both capital gain and ordinary income

In *Brinkley (TC Memo 2014-227)*, an October 2014 U.S. Tax Court case, the taxpayer was the founder of a company called Zave Networks (Zave). He originally held 9.8 percent of the company's stock but this was diluted over time by various rounds of venture capital funding. On multiple occasions, the taxpayer expressed a desire that he never be diluted below 3 percent of the total outstanding stock, but subsequent financings in fact reduced his ownership to 0.8 percent.

Google became interested in buying Zave. The taxpayer thereupon demanded that he receive 3 percent of the total amount paid by Google, notwithstanding his 0.8 percent interest in Zave's outstanding shares. The company gave in to his demand, largely because Google insisted that Mr. Brinkley sign a Google employment agreement and assign certain intellectual property to Zave.

On his income tax return, the taxpayer took the position that the full 3 percent of the proceeds he received all gave rise to capital gain income from the sale of his stock. The taxpayer argued that he had effectively negotiated a higher price per share for his stock than the price obtained by the other Zave shareholders. The IRS refuted this position, and the Tax Court found that Mr. Brinkley's proceeds over the 0.8 percent attributable to his stock holdings constituted compensation for services and gave rise to ordinary income.

The court had little trouble concluding that only 0.8 percent of the total proceeds was paid for the taxpayer's stock, the same price as received by the other Zave shareholders. The court further ruled that the additional 2.2 percent of proceeds were paid to the taxpayer in return for his signing the Google employment agreement and assigning intellectual property to Zave, both of which were requirements imposed by Google to complete the transaction.

Private letter ruling update: IRA is permitted to purchase shares in a gold trust without the purchase being treated as a deemed distribution

Items of personal property that are treated as a "collectible" under the Code are subject to certain tax-related ownership restrictions. Additionally, a 28 percent tax rate applies to any gain resulting from the disposition of collectibles, rather than the 20 percent rate that applies to most other capital gain income. Collectibles include art, rugs, antiques, metals, gems, stamps, coins and alcoholic beverages. Ownership restrictions applied by the Code prohibit taxpayers from holding collectibles in an Individual Retirement Account (IRA) or in an individually directed account in a qualified retirement plan. If an account does acquire a collectible, the cost of the collectible purchase is treated as having been distributed to the participant with respect to the account.

The Code provides an exemption from collectibles ownership restrictions for certain types of bullion. In order to qualify for the exemption, the bullion must meet certain fineness criteria and must be in the physical possession of a trustee that meets IRA trustee qualifications imposed by the Code. These trustee qualifications essentially require the trustee holding exempt bullion to be a bank. In a December 2013 private letter ruling (*PLR 201446030*), the IRS ruled that a gold trust with exchange-traded shares qualified to be held in an IRA. The trust was set up as a grantor trust for income tax purposes and allowed each shareholder to exchange his shares for gold bullion of equivalent value. The trustee of the gold trust was a bank, as required by the IRA exception. The IRS ruled that the acquisition of shares of this trust by an IRA trustee would qualify for an exemption from ownership restrictions and would not be treated as a distribution. The IRS clarified, however, that a distribution would be found if the IRA trustee were to exchange any shares to take possession of actual bullion.

It is important to bear in mind that the above exception for the ownership of gold trust shares by an IRA account does not apply to protect a taxable investor from paying the 28 percent collectibles tax rate if it owns shares of this type of trust and sells them at a gain. The exception is limited such that only IRAs may hold these trust shares.

IRS Chief Counsel advice: S corporation's "accumulated adjustments account" does not survive termination and subsequent re-election of Subchapter S status

The shareholders of a corporation that has elected to be treated as an S corporation are taxed each year on the corporation's taxable income. In general, the corporation itself does not pay income taxes. A shareholder who pays tax on an amount of income but does not receive a distribution equal to the full amount of this income may withdraw the taxed amount in a later year, free of additional taxes. These previously taxed amounts are tracked through an account called the "Accumulated Adjustments Account" or "AAA." These amounts used to be referred to as "previously taxed income," which actually seems like a more logical description.

In November 2014, the IRS' Office of Chief Counsel issued written advice (*CCA 201446021*) relating to an S corporation that had a positive AAA account balance when its majority shareholder revoked the corporation's Subchapter S election. The corporation became a C corporation following the revocation but subsequently made a new election to be treated as an S corporation. After the re-election, the corporation's shareholders sought to withdraw the AAA amounts that had built up during the first period in which the corporation was an S corporation.

The IRS concluded that the AAA amount from the prior years did not carry over to the period when the corporation's status as an S corporation was reinstated. It pointed to language in the Code that describes the AAA amount as being attributable to a "continuous period" during which a corporation is treated as an S corporation. The IRS reasoned that shareholders' income tax basis in their shares reflects the amount in the AAA account so that they can ultimately withdraw that amount tax-free, even without the amount still being in the AAA account. In this case, however, the corporation had accumulated earnings and profits (essentially retained earnings) from the years it was a C corporation (*i.e.*, the years in between its two periods of S corporation treatment). Any withdrawals by the shareholders in excess of the current year's earnings are deemed to come from earnings and profits to the extent thereof, and are subject to tax as a dividend. When all of the C corporation earnings and profits have been distributed, future distributions would be tax-free as a recovery of tax basis, to the extent of the shareholders' tax basis in their shares.

The shareholders of the corporation could have avoided this negative result had they availed themselves of special rules that control the transition period after a corporation's status as an S corporation ends. If a corporation distributes cash to its shareholders within one year after the end of its S corporation status, that distribution will be treated as coming from the AAA account to the extent of the balance in that account. The distribution will therefore be tax-free to the shareholders even if it has earnings and profits from earlier C corporation years. Because distributions of property other than money do not qualify for this special treatment, this tax-free distribution can be made only if the corporation has access to sufficient cash to distribute the AAA amount.

Case update: Court finds that taxpayer who sold a contract right to purchase land realized capital gain income

Only a taxpayer selling a "capital asset" may realize capital gain income on the sale of property and benefit from the lower tax rate that applies to this income. Also, the taxpayer must have held the capital asset for more than one year. Only property or a property right can be treated as a capital asset. The right to a stream of income is not considered to be property for this purpose. Certain things that are not obviously property may sometimes be considered property for tax purposes, as seen in the recent case of *Long v. Commissioner (CA 11, November 20, 2014)*. In *Long*, the United States Court of Appeals for the Eleventh Circuit reversed a prior decision of the Tax Court and allowed capital treatment for a taxpayer who had essentially sold a contract right.

In 2002, the taxpayer entered into a contract to purchase real property in order to construct a condominium building and then sell the condominium units. In 2004, before the sale had been completed, the seller defaulted on the contract. The taxpayer sued the seller and obtained a judgment, which the seller appealed. While the appeal was pending, the taxpayer sold his position in the contract, including the judgment, to a third party for $5.75 million, representing a substantial gain.

The IRS determined, and the Tax Court held, that this was ordinary income. The court's rationale was that the taxpayer would have developed and sold condominium units if he had been able to purchase the real property. Property held by a taxpayer for sale in the ordinary course of his business is not a capital asset. In effect, the court characterized the taxpayer's rights under the contract based on his intent to develop and sell interests in the land that he had attempted to purchase.

The Eleventh Circuit reversed the Tax Court and held that the taxpayer was entitled to long-term capital gain treatment. The Court of Appeals determined that the asset sold was the contract itself, including the judgment the taxpayer had obtained on that contract. The character of this asset could not be determined with reference to what the taxpayer would have done with the land itself. The court determined that the taxpayer did not acquire the contract or the judgment with the prior intent of selling either. Therefore, his contractual right to purchase the land was itself a capital asset and his gain arising on the sale of the contract was subject to tax at the lower capital gain rate.

This case may also be beneficial for other taxpayers who sell their interests in court judgments, a practice which has become fairly common. Where litigation is based on rights arising under a contract for the purchase or sale of property, the *Long* case may serve as authority for capital gain treatment, at least in the Eleventh Circuit. However, the IRS is not likely to concede this issue and the Tax Court does not have to follow the precedent of the Eleventh Circuit in any future case that would be appealable to a different circuit.

House of Representatives and Senate pass a one-year tax "extenders" bill

A variety of beneficial tax provisions expired at the end of 2013. There has been hope that this Congress would retroactively reinstate some or all of those provisions for 2014 and later years. Among the most significant of these expired provisions are:

- the ability to deduct state and local sales taxes instead of income taxes;
- the "research and experimentation" tax credit;
- the ability to expense the first $500,000 spent on depreciable equipment for business;
- the 50 percent additional first-year bonus depreciation available with respect to certain property;
- the ability to treat as an expense the cost of producing a motion picture or television program;
- the ability to exclude 100 percent of the gain realized on the sale of "qualified small business stock";
- the ability to receive a tax-free distribution from an IRA that is used to make a charitable contribution;
- a variety of energy-based tax credits; and
- the reduction of the Subchapter S "built-in" gain recognition period from 10 years to five years.

On December 3, 2014, the United States House of Representatives passed by a wide margin the "Tax Increase Prevention Act of 2014," which would extend most of these provisions through 2014. The Senate also passed the Act by a wide margin on December 16, and President Obama is expected to sign it.

Non-managing member of LLC liable for New York sales tax

A recent Administrative Law Judge decision evaluated a provision of New York tax law that treats all members of a limited liability company (LLC) as responsible officers liable to collect and remit New York sales taxes based on the LLC's transactions. The ALJ decision found that the New York tax provision overrides the general purpose of the limited liability company law – to provide limited liability to the members from acts of the company. In *Boissier*, two members of an LLC with less than 15 percent membership interests were assessed sales tax, interest and penalties owed by the LLC. Neither member had managerial responsibility, the ability to hire or fire employees, knowledge of or control over the LLC's financial affairs, or authority to sign the LLC's tax returns. The provisions of New York's tax laws are clear: having chosen to act as members of an LLC, the members must accept the consequences of their choice of business organization.

Pursuant to applicable provisions, the administrative law judge reduced the LLC members' tax liabilities according to their proportionate interest in the LLC. As we previously reported, the policy recognizes that the law can result in a harsh result for a member of an LLC or a limited partner who has no involvement in or control over the LLC/LP's business affairs. Under the policy, limited partners and minority members in an LLC are eligible for relief if they demonstrate that they were not under a duty to act in complying with New York tax laws on behalf of the business and cooperate with New York authorities to identify other potentially responsible persons (particularly those involved in the day-to-day affairs of the business). Courts may also consider the pending expiration of any statute of limitations on assessment of the New York sales tax when granting relief. Relief would limit an LLC member's tax liability to his pro rata share of the business's liability for the New York sales tax and related interest, based on his ownership interest in the business or his share of the profits and losses of the business, whichever is higher. No penalty will be due from the eligible person.

New York tax law changes for 2015

The 2014-2015 New York budget made various changes in New York's tax laws that generally become effective on January 1, 2015.

Corporate income tax

Corporate income tax exposure. Whether a corporation is subject to income tax in New York is based on economic nexus, which has been expanded to include deriving receipts from business activities in New York, subject to a $1,000,000 de minimis threshold.

Corporate tax rates. New York corporate income tax liability is calculated with reference to the highest of a corporation's entire net income (ENI), capital (which is being phased out) or the fixed dollar minimum. The tax rates are as follows:

ENI	2014	2015	2016	2017	Thereafter
Qualified NY Manufacturer (QNYM) & Eligible QNYM	0.0%	0.0%	0.0%	0.0%	0.0%
Qualified Emerging Technology Co. (QETC)	5.9	5.7	5.5	5.5	4.875
Small Business[1]	6.5	6.5	6.5	6.5	6.5
Other	7.1	7.1	6.5	6.5	6.5

[1] For 2014 and 2015, graduated rates apply for income between $290,000 and $390,000.

Capital	2014	2015	2016	2017	2018	2019	2020	Thereafter
QNYM & Eligible QNYM & QETC	.136%	.15%	.106%	.085%	.056%	.038%	019%	0
Co-ops	.04	.04	.04	.04	.04	.04	.025	0
Other	.15	.15	.125	.1	.075	.05	.025	0

Fixed Dollar Minimum (tax liability expressed in dollar amounts)

QNYM & QETC NY Receipts	2014	2015	2016	2017	Thereafter
Up to $100,000	$23	$22	$21	$21	$19
$100,001-$250,000	68	66	63	63	56
$250,001-$500,000	159	153	148	148	131
$500,001-$1,000,000	454	439	423	423	375
$1,000,001-$5,000,000	1,362	1,316	1,269	1,269	1,125
$5,000,001-$25,000,000	3,178	3,070	2,961	2,961	2,625
Over $25,000,000	4,500	4,385	4,230	4,230	3,750

Other C Corporations NY Receipts	2014	Thereafter
Up to $100,000	$25	$25
$100,001-$250,000	75	75
$250,001-$500,000	175	175
$500,001-$1,000,000	500	500
$1,000,001-$5,000,000	1,500	1,500
$5,000,001-$25,000,000	3,500	3,500
$25,000,001-$50,000,000	5,000	5,000
$50,000,001-$100,000,000	5,000	10,000
$100,000,001-$250,000,000	5,000	20,000
$250,000,001-$500,000,000	5,000	50,000
$500,000,001-$1,000,000,000	5,000	100,000
Over $1 billion	5,000	200,000

The Metropolitan Transportation Authority (MTA) surtax is based on the New York State (NYS) tax before credits and is apportioned to the MTA based on an equally weighted three-factor formula, based on payroll, property and receipts.

The alternative minimum tax is eliminated for tax years beginning after 2014. So is the separate treatment of subsidiary capital and income.

<u>New definition of income.</u> The definitions of investment capital and investment income have been narrowed, and these incomes are not subject to tax. Other categories of tax-exempt income have been created.

<u>Prior net operating loss conversion.</u> Prior net operating loss (NOL) carryovers are converted into a prior net operating loss conversion (PNOLC) subtraction to stabilize their value for financial accounting purposes. The amount is apportioned and tax effected based on 2014 (so QNYMs get no benefit because their 2014 tax rate on ENI is 0 percent) and divided by 6.5. The balance can then be subtracted from apportioned business income at the rate of one tenth in each year (with the balance carried over through year 20), or deducted one half in each of 2015 and 2016 (with any unused amount being lost after 2016). Qualified small-business taxpayers are not subject to the limits.

<u>Net operating loss deduction.</u> NOLs incurred after 2014 can be carried back three years (but not to a tax year before 2015) and can be carried forward 20 years. NOLs are apportioned in the year incurred, and are subtracted from apportioned business income in the carryover period. As a result, no NOL is created for a year in which the corporation was not subject to tax in New York. The NOL deduction is no longer limited by the federal NOL source year or amount.

<u>Apportionment.</u> Business income is apportioned based on a single receipts factor using customer sourcing rules. Specific sourcing rules for particular revenues are added. For example, receipts from digital products are generally sourced to the customer's primary use location of the product. Where the sourcing rules for financial transactions rely on commercial domicile, the following hierarchy is imposed: location of the treasury function; seat of management and control; and billing address of the customer.

<u>Combined reporting.</u> New York adopted a full unitary water's-edge method for combined reporting, with a 50 percent stock ownership test based on voting power. A combined group is generally treated as a single entity. The prior requirement for substantial intercompany transactions is eliminated. Taxpayers can also make a commonly owned group election to include all non-unitary corporations that are subject to New York tax and meet the ownership test in the combined group. The election is effective for seven years and is automatically renewed for an additional seven years unless the group affirmatively declines. If the election is declined, a new election cannot be made for three years.

<u>Nuisance taxes.</u> The organization tax, the tax on changes in capital of domestic corporations, and the license and maintenance fees applied to foreign corporations have been repealed.

<u>Tax credits.</u> The commercial production credit has been extended through 2016 and the threshold minimum activity required for production outside the Metropolitan Commuter Transportation District ("MCTD") has been reduced to $100,000. The low-income housing credit has been increased. Beginning in 2014, QNYMs are allowed a new credit equal to 20 percent of real property taxes paid during the tax year for real property owned (or leased from an unrelated landlord if the lease expressly requires the tenant to pay these taxes directly to the tax authority) by the manufacturer in New York and principally used for manufacturing. This credit was provided in lieu of the previous deduction for real estate taxes paid (provided these real estate taxes are not the basis for any other tax credit). Approved businesses participating in the STARTUP NY program may receive a refundable credit equal to the 25 percent

excise tax paid on purchased telecommunications services. The youth work tax credit has been increased and extended. A new refundable credit equal to 25 percent of certain costs (capped at $4,000,000 a year) between 2015 and 2018 was enacted to encourage touring musical and theatrical productions in theaters in upstate New York. The film production credit has been expanded to include wages earned in Albany and Schenectady counties. A new credit is available in an amount equal to 15 percent of wages paid to full-time and 10 percent of wages paid to qualified part-time employees with developmental disabilities.

Personal income tax

Real property tax circuit breaker credit. For 2014 and 2015, the credit is equal to a percentage (1.5 to 4.5 percent) of the real estate taxes in excess of a certain percentage of income (4 to 6 percent) for homeowners and renters with household gross income of less than $200,000. For the purposes of this tax credit, a renter is deemed to have paid real estate taxes equal to 15.75 percent of his adjusted rent for the tax year.

Resident trusts. New York beneficiaries of exempt resident trusts are now subject to New York income tax on accumulated income that is distributed to them. In addition, the New York grantor of an incomplete gift, non-grantor trust is taxed on the income of the trust.

Minimum tax. The add-on minimum tax has been repealed.

MCTD tax. The due dates for a self-employed individual to file and make estimated tax payments of the Metropolitan Commuter Transportation Mobility Tax are the same as for the individual's personal income tax.

Sales tax. Sales tax incentives have been extended for businesses that locate or relocate their offices in the area below Murray Street or in the World Trade site, World Financial Center or Battery Park City area.

Fifth Circuit reverses Tax Court on amount of discount allowed in determining estate tax value of works of art

We previously reported on the Tax Court case *Elkins v. Commissioner (March 11, 2013)* (Vol. 8, No. 2, May 2013). At issue was the value, for estate tax purposes, of 64 pieces of art owned by the decedent taxpayer. At his death, the decedent held fractional interests in the art, with the balance held by his children. The estate claimed a 44.75 percent discount due to the fractional ownership. The Tax Court allowed only a 10 percent discount, largely based on evidence in the record that the decedent's children very much wanted to keep the art in the family. In the court's analysis, if an unrelated party did acquire the decedent's interest, the children likely would have to pay nearly full value to get it back.

The United States Court of Appeals for the Fifth Circuit reversed the decision of the Tax Court and handed the estate an even better result than it claimed on the decedent's estate tax return. The Fifth Circuit found that there was no evidence in the record to support the 10 percent discount selected by the Tax Court. The IRS did not present any expert witnesses on valuation at the Tax Court trial, arguing instead that no discount should be allowed because the IRS does not impose any discount on the value of fractional gifts given to charities.

The Fifth Circuit deemed the presentation made by the taxpayer's experts in the Tax Court trial to be credible and awarded discounts consistent with their analysis ranging from 65.57 percent to 79.74 percent: a major taxpayer victory.

Another Tax Court reversal before the Ninth Circuit

The Tax Court did not have a good quarter in the United States Court of Appeals. *Estate of Natale B. Giustina v. Commissioner (9th Cir., December 1, 2014)* represents another reversal of the Tax Court, this time by the Ninth Circuit Court of Appeals. As in the *Elkins* case, the Ninth Circuit reversed the Tax Court for utilizing assumptions that were not supported by the trial record.

The decedent held a limited partnership ownership interest as a limited partner. The decedent's estate valued that interest based on going concern value, rather than using liquidation value. The estate presented evidence that the general partners believe strongly that the business should continue and no limited partner had ever sought to dissolve the partnership or seek the redemption of his interest.

Despite this evidence, the Tax Court assigned a 25 percent probability that a limited partner might band together with other limited partners and vote for a dissolution of the partnership. The court then computed the value of decedent's interest by using a blend of going concern value (75 percent) and liquidation value (25 percent). This increased the value of the interest from $12 million to $27 million, resulting in a significant estate tax increase. The Ninth Circuit rejected the Tax Court's analysis because there was no evidence in the record supporting the assumption that there was a 25 percent likelihood that the partnership would be liquidated. The case was sent back to the Tax Court to reconsider the value using only going concern valuation concepts..

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