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**NEWS RULINGS VERDICTS**

Friday, April 13, 2012

### Labor/Employment Employer liability for rest breaks clarified by high court

The state Supreme Court issued a ruling Thursday providing long-sought clarity to employers on how they should structure breaks for hourly workers in California.

### Energy Law BrightSource calls off its IPO

In the midst of a struggling market for solar companies, Oakland-based solar project developer BrightSource abruptly reversed course on its long-awaited IPO, announcing it would not go forward as planned.

### Solo and Small Firms The Busch Firm

The Busch Firm's practice includes representing religious organizations, many of which its founder created.

**U.S. Court of Appeals for the 9th Circuit  
9th circuit says ban on political ads for public broadcast is unconstitutional**  
A longstanding federal ban on political ads on public radio and TV stations is an unconstitutional restriction of free speech, a divided 9th U.S. Circuit Court of Appeals panel held Thursday.

**Large Firms  
Another Dewey departure**  
Dewey & LeBoeuf sustained another defection from its Los Angeles office Thursday, this time a corporate mid-level partner jumping to the regional California shop Stradling Yocca Carlson & Rauth, P.C.

**Alternative Dispute Resolution  
Jeffrey M. Mandell**  
ADR neutral brings more than two decades of experience in negotiating thousands of deals for high-flying entertainment and media clients.

**Entertainment & Sports  
MPAA reorganizes legal staff**  
Six months after taking the reins, new entertainment trade group VP Henry Hoberman has restructured his legal team in Los Angeles and Washington, D.C.

**Corporate  
Former Apple IP counsel joins startup**  
The mystery over what Apple Inc.'s longtime intellectual property counsel was up to when he left the company last summer is solved.

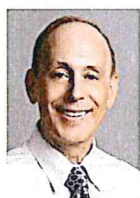
**Tax  
Stars need tax help, too**  
For Hollywood's biggest stars, tax and estate planning is a year-round responsibility - one that many of them simply couldn't handle without the help of specialized lawyers.

**Investments  
Oaktree IPO off to a weak start**  
Oaktree Capital Group LLC, the largest private equity firm in California, drops

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## Estate tax March Madness: taxpayers 3, IRS 0

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Very few taxpayers prevail in the U.S. Tax Court. Why? First, because the Internal Revenue Service usually settles with taxpayers who have attractive facts. Second, because perhaps as many as 90 percent of all taxpayers represent themselves.

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So it is refreshing to report on three taxpayer victories in the estate and gift tax area that occurred in the space of just over a month. These taxpayer victories are helpful because, until the end of 2012, each taxpayer has a \$5,120,000 gift tax exclusion. On Jan. 1, 2013, it will decrease to \$1,000,000. The Obama Administration has proposed a \$3,500,000

exclusion. Some Republican Senators introduced a bill to repeal the estate tax. The uncertainty has motivated many taxpayers to engage in gift tax planning now. These favorable cases will make the use of some important tax planning structures much more comfortable.

One such structure is the family limited partnership, or FLP. The IRS has been consistently able, in the published cases, to convince courts that the FLPs' assets should be included in the parents' estates. However, each IRS victory has involved bad facts, e.g., an FLP established by a nonagenarian or terminally ill octogenarian. In contrast, practitioners know that the IRS does not challenge FLPs established by healthy taxpayers who live to a normal life expectancy.

Now, we have important reminders that, when properly established and operated, an FLP will prevail in spite of IRS opposition in the cases of *Estate of Joanne Harrison Stone*, T.C. Memo 2012-48 (February 22, 2012), and *Estate of Beatrice Kelly*, T.C. Memo 2012-73 (March 19, 2012).

Mr. and Mrs. Stone had a great deal of real estate. They intended to keep one property as a "family asset." On advice of counsel they formed a limited partnership to simplify the gift-giving process and guard against partition suits. After three years of gifts, Mr. and Mrs. Stone only owned a 2 percent interest as general partners; the adult children owned the 98 percent limited partnership interests. Health was not a factor: Mrs. Stone taught Sunday School for 60 years, including the last Sunday before she passed away at age 81, and Mr. Stone was 91 at the time of the trial. The issue before the court was whether the decedent had a legitimate and significant non-tax reason for creating the FLP.

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The IRS argued, and Judge Goeke agreed, that gift giving alone is not an acceptable non-tax motive for forming the FLP. However, creating a "family asset" to be managed by the family is itself a sufficient non-tax motive to avoid estate tax inclusion. Also, even though the Stones had a testamentary purpose, legitimate non-tax purposes are often interwoven with testamentary objectives.

The Stones made mistakes, e.g., they used a "bill of sale" to make the gifts. However, there were strong favorable facts, e.g., Mr. and Mrs. Stone did not depend on



distributions from the FLP; there was no commingling of partners' personal and partnership funds; and there was no discounting of limited partnership interests.

Mrs. Kelly, the focus of the second case, was incompetent, which is a bad way to begin a Tax Court case involving an FLP. However, there was a powerful non-tax motive: the children wanted to avoid litigation among themselves after their mother's death. Therefore, they established, with probate court approval, one limited partnership per child to facilitate an equal post-mortem division. The probate court order confirming the multiple FLP approach mentioned that it would "avoid undesirable tax consequences." However, the Tax Court did not believe that tax savings motivated the structure. Importantly, Mrs. Kelly retained sufficient non-partnership assets for her personal needs and the family observed partnership formalities. This one partnership per child approach had been the key to a taxpayer victory in *Estate of Eugene Stone v. Commissioner*, T.C. Memo 2003-309 (2003).

The third taxpayer victory involved the use of a formula clause to define the amount of the gift. Example: mom and dad give the number of limited partnership units equal in value to \$10,240,000 (their combined 2012 lifetime gift exclusion). At the time of the gift they believe that each unit is worth \$10,240, so the gift is of 1,000 units. The gift document provides that if the IRS later increases the unit value, any excess units will be transferred to charity. On audit the IRS decides that each unit is worth \$11,377.78. Therefore, the number of units needed for the gift to the children is only 900 (900 times \$11,377.78 equals \$10,240,000). As a result, the other 100 units is transferred to charity, giving mom and dad a (100 times \$11,377.78) \$1,137,778 income tax charitable deduction.

The IRS has traditionally fought this approach as being against public policy. One part of the IRS's rationale has been that by having the excess transfer to charity, the defined value gift takes away the IRS's incentive to conduct an income tax audit. In three recent (2006, 2009, and 2011) cases, taxpayers have prevailed. The question left open for practitioners was: will taxpayers prevail if the excess does not go to charity?

*Wandry v. Commissioner*, T.C. Memo 2012-88 (March 26, 2012) is the first case which approves a formula clause without a gift over to charity. The Tax Court indicated that the policy of encouraging charitable gifts, which was a factor in the earlier decisions, was not determinative to the result of the three earlier cases. In *Wandry* the excess units were simply returned to the parents. As a result, many more taxpayers will be using this structure.

*Stone* and *Kelly* confirm that FLPs are important tools to transfer valuable assets at significantly reduced gift (and estate) tax values. *Wandry* confirms the use of an important device to avoid creating a taxable gift. The three are a powerful incentive for taxpayers to use their \$5,120,000 gift exclusion before the end of 2012.

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GIRARDI**

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Finest Legal Minds  
in California  
Talk about the Law

trading after raising \$380.2 million in a downsized initial public offering.

### Tax

#### Amazon.com readies for online sales tax

By cutting a deal, Amazon and lawmakers left the broader tax law question unresolved and made the already convoluted tax system that much more complex.

#### Increased tax burdens on small businesses on the horizon

The IRS is increasing its scrutiny of S Corps while new regulations are looming. By **Alexander Lee** of Paul Hastings

#### Drop it: the remnants of the geographically-based restriction on property tax exemptions for nonprofits

Geographic restrictions on property tax exemptions don't make sense as a policy and create needless administrative burdens. By **Ofer Lion** of Hunton & Williams LLP

### Intellectual Property

#### With passage of America Invents Act, it's a whole new ballgame for inventors. Pt. 2

The act turns our patent system into a "first inventor to file" system instead of a "first to invent" system. By **Hani Z. Sayed** of Rutan & Tucker LLP

### Alternative Dispute Resolution

#### The "Harding Effect" in mediation

Two things happen in mediation: the mediator influences the parties, and the parties influence the mediator. By **Robert S. Mann** of ADR Services

### Perspective

#### Do women 'opt-out' of work, or are they 'forced out'?

A collection of essays exploring the choices that women face when trying to balance the demands of work and family. By **Bernie D. Jones**

### Tax

#### Tax refund claims seen as major risk

A relatively obscure class standing decision out of the state Supreme Court last summer could wreak havoc on local government finances and the services they fund.

#### Estate tax March Madness: taxpayers 3, IRS 0

Recent decisions provide hope for taxpayers' ability to prevail in U.S. Tax Court. By **Bruce Givner** and **Owen Kaye** of Givner & Kaye PC

### Letter to the Editor

#### Unsinking Mr. Kingsley's Titanic

Rebutting the claim that class action lawsuits are the lifeboats of society. By **Jeff Scott** of Greenberg Traurig

### Judicial Profile

#### Cory J. Woodward

Superior Court Judge Kern County (Bakersfield)

### Tax

#### Tax planners say uncertainty abounds in 2012

Tax attorneys in California who advise upper middle-class and wealthy clientele generally are professionals who prize certainty - something they say is in short supply this year with federal tax cuts set to expire in January.

**CHAMPION**

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