

FLP AUDIT SURVEY

Business Planning Group Meeting
American Bar Association
Section of Real Property, Trust & Estate Law
Spring Symposium
Washington, D.C.
May 2, 2008

James D. Spratt, Jr.
King & Spalding LLP
Atlanta, Georgia

The Business Planning Group of the American College of Trust & Estate Counsel conducted a survey of its members to obtain information on recent estate and gift tax audits involving family limited partnerships. The ACTEC survey was conducted by Peter Brown of Overland Park, Kansas, and David Pratt of Boca Raton, Florida.

The Business Planning Group of the Section of Real Property, Trust & Estate Law was also polled for similar experience.

The attached pages contain responses relating to ten estate or gift tax audits that seem representative of the experience reported by both groups.

Audit 1

Estate or gift tax audit	Estate
Settlement date	Feb-07
Aggregate of discounts	31%
<i>Lack of control discount</i>	13%
<i>Lack of marketability discount</i>	20%
Percentage of marketable securities	23%
Percentage of real property	0%
Percentage of LP interests held by decedent	72%
Was decedent the GP?	Yes
Did decedent make gifts of LP interests?	Yes
Did decedent sell LP interests?	No
Were there non family member partners?	No
Were there distributions to partners? Prorata?	Yes/Yes
Were partnership assets used to pay estate taxes?	Yes, but minimal distribution to estate
Bad facts?	Most of p'ship's assets were decedent's
Other issues	Terms of Graegin loan Partnership created 20 years before DOD

Audit 2

Estate or gift tax audit	Estate
Settlement date	2007
Aggregate of discounts <i>Lack of control discount</i> <i>Lack of marketability discount</i>	30%
Percentage of marketable securities	100%
Percentage of real property	0%
Percentage of LP interests held by decedent	99.9%
Was decedent the GP?	No
Did decedent make gifts of LP interests?	No
Did decedent sell LP interests?	No
Were there non family member partners?	No
Were there distributions to partners? Prorata?	Yes/Yes
Were partnership assets used to pay estate taxes?	
Bad facts?	Partnership assets not actively managed
Other issues	Partnership created 7 years prior to DOD

Audit 3

Estate or gift tax audit	Estate
Settlement date	May-07
Aggregate of discounts	43%
<i>Lack of control discount</i>	15%
<i>Lack of marketability discount</i>	35%
Percentage of marketable securities	100%
Percentage of real property	0%
Percentage of LP interests held by decedent	97%
Was decedent the GP?	Owned 1/3 of corporate GP
Did decedent make gifts of LP interests?	No
Did decedent sell LP interests?	No
Were there non family member partners?	No
Were there distributions to partners? Prorata?	No distributions from partnership
Were partnership assets used to pay estate taxes?	No, Graegin loan obtained from bank
Bad facts?	Almost all assets came from decedent
Other issues	Audit initiated 26 months into SOL IRS ran out of time and issued no change closing letter 2 weeks before statute ran Partnership created 7 years prior to death

Audit 4

Estate or gift tax audit	Both
Settlement date	Oct-07
Aggregate of discounts	40%
<i>Lack of control discount</i>	20%
<i>Lack of marketability discount</i>	25%
Percentage of marketable securities	27%
Percentage of real property	73%
Percentage of LP interests held by decedent	95%
Was decedent the GP?	No
Did decedent make gifts of LP interests?	No
Did decedent sell LP interests?	No
Were there non family member partners?	Yes
Were there distributions to partners? Prorata?	No
Were partnership assets used to pay estate taxes?	No
Bad facts?	Established 21 days before DOD Decedent terminally ill on formation Decedent did not participate in formation Partnership held residence
Other issues	Adjusted fractional interest discount on residence from 30% to 20% Adjusted underlying value of residence

Audit 5

Estate or gift tax audit	Estate
Settlement date	Dec-07
Aggregate of discounts	35%
<i>Lack of control discount</i>	
<i>Lack of marketability discount</i>	
Percentage of marketable securities	20%
Percentage active business	40%
Percentage of real property	20%
Percentage of LP interests held by decedent	95%
Was decedent the GP?	No
Did decedent make gifts of LP interests?	Yes
Did decedent sell LP interests?	Yes
Were there non family member partners?	Yes
Were there distributions to partners? Prorata?	Yes/Yes
Were partnership assets used to pay estate taxes?	Yes, loan to estate
Bad facts?	Created 3 years prior to death Contained personal use assets
Other issues	

Audit 6

Estate or gift tax audit	Estate
Settlement date	Dec-07
Aggregate of discounts <i>Lack of control discount</i> <i>Lack of marketability discount</i>	34%
Percentage of marketable securities	40%
Percentage active business	55%
Percentage of real property	5%
Percentage of LP interests held by decedent	4%
Was decedent the GP?	Yes, 100% of voting interest
Did decedent make gifts of LP interests?	No
Did decedent sell LP interests?	Yes
Were there non family member partners?	No
Were there distributions to partners? Prorata?	No
Were partnership assets used to pay estate taxes?	No
Bad facts?	
Other issues	IRS allowed discounts on an asset class basis on the authority of McCord: 39% for real estate partnerships owned by master FLP, 52% for real estate and 24% for marketable securities In effect the value of the installment note was revalued. Decedent had 1% GP interest, 4% LP interest and sold in 2000 95% LP interests to a grantor trust

Audit 7

Estate or gift tax audit	Estate
Settlement date	Dec-07
Aggregate of discounts <i>Lack of control discount</i> <i>Lack of marketability discount</i>	15%
Percentage of marketable securities	
Percentage active business	
Percentage of real property	
Percentage of LP interests held by decedent	
Was decedent the GP?	
Did decedent make gifts of LP interests?	
Did decedent sell LP interests?	
Were there non family member partners?	
Were there distributions to partners? Prorata?	
Were partnership assets used to pay estate taxes?	No
Bad facts?	Letter to family that purpose was to save estate tax
Other issues	

Audit 8

Estate or gift tax audit	Estate
Settlement date	Nov-06
Aggregate of discounts <i>Lack of control discount</i> <i>Lack of marketability discount</i>	18%
Percentage of marketable securities	100%
Percentage active business	
Percentage of real property	
Percentage of LP interests held by decedent	95% in QTIP Trust
Was decedent the GP?	No
Did decedent make gifts of LP interests?	No
Did decedent sell LP interests?	No
Were there non family member partners?	No
Were there distributions to partners? Prorata?	Yes/Yes
Were partnership assets used to pay estate taxes?	No
Bad facts?	
Other issues	IRS claimed trustees of QTIP breached fiduciary duty by transferring assets to partnership, so transaction could be set aside by beneficiary. Thus, no discounts. Appeals officer refused to deviate from IRS settlement "guidelines" Settled valuation issues and filed Tax Court petition on other issues

Audit 9

Estate or gift tax audit	Gift
Settlement date	Nov-05
Aggregate of discounts <i>Lack of control discount</i> <i>Lack of marketability discount</i>	31%
Percentage of marketable securities	100%
Percentage active business	
Percentage of real property	
Percentage of LP interests held by decedent	
Was decedent the GP?	
Did decedent make gifts of LP interests?	Yes
Did decedent sell LP interests?	
Were there non family member partners?	No
Were there distributions to partners? Prorata?	Yes/Yes
Were partnership assets used to pay estate taxes?	
Bad facts?	Send issues on funding
Other issues	Gifts were made with defined value clause Discounts on 709 in excess of 40% IRS honored defined value clause and resolved audit by adjusting partnership interests rather than assessing gift tax

Audit 10

Estate or gift tax audit	Estate
Settlement date	
Aggregate of discounts	22%
<i>Lack of control discount</i>	
<i>Lack of marketability discount</i>	
Percentage of marketable securities	100%
Percentage active business	
Percentage of real property	
Percentage of LP interests held by decedent	99.9%
Was decedent the GP?	No
Did decedent make gifts of LP interests?	No
Did decedent sell LP interests?	No
Were there non family member partners?	No
Were there distributions to partners? Prorata?	Yes/Yes
Were partnership assets used to pay estate taxes?	Yes, Graegin loan
Bad facts?	2 years before DOD; large block of low basis stock; partners never met; partnership made Graegin loan to estate for estate taxes
Other issues	50% of interest deduction on Graegin loan disallowed