



# **UNCertainties of Death and Taxes: Defending Estate Tax Returns**

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# **I. Preparation Stage**

## **1. Keep your potential future audience in mind**

- Consider what you write – email, memo to file regarding reasons for partnership formation, time records (for attorneys/accountants), letters, etc.
- The IRS, a judge, or even a jury may eventually be reviewing documents written during the planning stages

# **I. Preparation Stage**

## **2. Keep in mind who your client is**

- Personal Representative vs. Beneficiaries

# **I. Preparation Stage**

## **3. Promptly file for Employer Identification Number (EIN)**

- Difference between SSN and EIN

# I. **Preparation Stage**

## 4. **Create Estate bank/brokerage accounts in a timely manner**

- Consider whether to suggest that PR liquidate securities to minimize market risk

# **I. Preparation Stage**

- 5. Involve an experienced accountant**

# I. Preparation Stage

## 6. Be aware of Personal Liability of PR

- § 2002 - Tax shall be paid by PR
- § 3467 - PR bears personal burden of paying tax *if* he pays debts or makes distributions from estate assets before satisfying debts to U.S. (and Estate is unable to pay)
- § 3713(a) - Debt to U.S. is given priority over all other debts *but not* over estate administration expenses

# I. Preparation Stage

## 7. Be prepared to produce documents in your file to the IRS, if necessary

- In some cases, the evidence to establish motives for various planning options may be privileged



# I. Preparation Stage

## 7. Comply with loan terms, if loans are made

- Any loans made to or by the Estate should be properly documented
- Loan terms should be reasonable
- Payments should be made timely
- *Graegin* notes

*Estate of Graegin v. Comm'r*, 56 T.C.M. (CCH) 387 (1988).

## **II. Estates with Closely Held Interests**

- 1. Refrain from use of Entity assets for Estate's obligations**

*See Estate of Strangi v. Comm'r*, 85 T.C.M. (CCH) 1331 (2003), *aff'd*, 417 F.3d 468 (5th Cir. 2005).

- II. Estates with Closely Held Interests**
  - 2. Consider whether to make a Section 754 election**

## **II. Estates with Closely Held Interests**

### **3. Transfers of entity interests at death**

- Review transfer to determine whether lapse occurs under Chapter 14
- Consider maintaining interest in hands of PR, subject to estate administration, until closing letter is received from the IRS
- Once IRS closing letter is received, document the transfer, to be executed by PR and beneficiary

### **III. Appraisals of Hard-to-Value Assets**

- 1. Obtain independent appraisal from qualified appraiser**
  - Appraiser should be engaged by attorney, not taxpayer

### **III. Appraisals of Hard-to-Value Assets**

#### **2. Encourage communication among appraiser, client, and advisors**

- A good appraisal reflects a high level of communication
  - Bad legal facts + Good appraisal = Bad result
  - Good legal facts + Bad appraisal = Bad result
  - Both scenarios = Unhappy client

## III. Appraisals of Hard-to-Value Assets

### 3. Confirm with the appraiser the interest to be valued

*See, e.g., Estate of Bonner v. United States*, 84 F.3d 196 (5th Cir. 1996);  
*Estate of Bright v. Comm'r*, 658 F.2d 999 (5th Cir. 1981);  
*Estate of Mellinger v. Comm'r*, 112 T.C. 26 (1999).

### **III. Appraisals of Hard-to-Value Assets**

#### **4. Promote defensibility of valuation reports**

- Appraiser should conduct thorough due diligence
- Appraiser should have clear understanding of empirical data
- Appraiser should apply relevant comparative factors
- Appraisal should be well documented
- Appraisal should be readily understood



### **III. Appraisals of Hard-to-Value Assets**

#### **5. Review appraisal closely for facts**

- Distribution policy
- Terms of governing agreement
- Assets
- Cash flow

### **III. Appraisals of Hard-to-Value Assets**

#### **6. Encourage the client to live by factual information provided to appraiser**

- Cash flow, distribution policy, etc.
- Intent (or lack thereof) to transfer or sell

## **IV. Transfer Tax Returns**

- 1. Segregate your planning file from your tax return preparation file**

## **IV. Transfer Tax Returns**

- 2. Beware of rounding on appraisals and tax returns**

## **IV. Transfer Tax Returns**

- 3. Be aware of presentation of tax return**

