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CITATION:
Astleford v. Commissioner, T.C. Memo. 2008-128, May 5, 2008

SUMMARY:
The Tax Court calculated the discounts for lack of control and marketability for a family limited partnership and a 50% interest in a related general partnership owned by the FLP.

DETAILS:
The IRS challenged the valuations of gifts of Astleford Family Limited Partnership (AFLP) limited partnership interests made by Jane Z. Astleford in 1996 and 1997. In particular, the IRS challenged the value of Minnesota farmland owned by AFLP, whether the 50% interest in the Pine Bend general partnership should be valued as a partnership interest or assignee interest, the proper discounts for lack of control and marketability to apply to the Pine Bend interest, and the proper discounts to apply to the gifted AFLP interests.

Value of Minnesota Farmland
Both the underlying value of the farmland and the “absorption discount” were disputed. The absorption discount was based on selling the property piecemeal over 4 years. The Court accepted the underlying land value of the IRS appraiser and applied a 10% present value adjustment over the four year sale period, a level approximately midway between the discounts calculated by the taxpayer and IRS experts.

Valuation of 50% General Partnership Interest as Assignee Interest

Pine Bend was a general partnership formed by MG and Jane Astleford and each owned 50%. MG died in 1995, leaving his interest to a marital trust. Jane transferred her 50% interest to AFLP in 1997. The taxpayer argued that AFLP's 50% interest was merely an assignee interest, but the Tax Court adopted the "substance over form" doctrine and rejected the taxpayer's argument.

Pine Bend General Partnership Discounts for Lack of Control and Marketability
For purposes of calculating the discounts for lack of control and marketability, the IRS expert relied on publicly traded REIT data and the taxpayer expert relied on publicly registered real estate limited partnerships (RELP) data. The Court said, *"We decline to declare either RELP or REIT data generally superior to the other … We believe that when considering the size, marketability, management, distribution requirements, and taxation of RELPs and REITs, RELPs more closely resemble AFLP and Pine Bend, and we believe that the low trading volume on the RELP secondary market is not so low as to render available RELP data unreliable. We also believe, however, that the large number of REIT sales transactions tends to produce more reliable data compared to the limited number of RELP sales transactions. We believe further that differences between REITS, on the one hand, and Pine Bend and AFLP, on the other, may be minimized given the large number of REITs from which to choose comparables."*

The taxpayer expert applied a 40% discount that the Tax Court did not believe was well explained, while the IRS expert applied no discount, believing any discounting should be done only at the AFLP level. The Court noted that tiered discounts have been both accepted and rejected depending on the portion of total assets represented by the lower level entity. The Court concluded, *"The 50-percent Pine Bend interest constituted less than 16 percent of AFLP's NAV and was only 1 of 15 real estate investments that on Dec. 1, 1997, were held by AFLP, and lack of control and lack of marketability discounts at both the Pine Bend level and the AFLP parent level are appropriate."*

The Court did its own analysis of the RELP data and concluded that a 30% combined discount for lack of control and marketability was appropriate at the Pine Bend level.

Astleford Family Limited Partnership Discounts for Lack of Control and Marketability
The Tax Court concluded that the RELP comparables used by the taxpayer expert were too dissimilar from AFLP and that the 45% lack of control discount for the two gifts was excessive. Rather than "sift through RELP data for more appropriate RELPs" the Court decided to use the IRS expert's REIT data. The REIT data showed that in 1996 in the public marketplace REITs traded at a median .1% premium to per share Net Asset Value (NAV) and in 1997 at a median 1.2% discount to per share NAV. The Court noted, *"this does not mean that a lack of control discount is nonexistent but suggests that an [sic] REIT's share price is in part affected by two factors, one positive (the liquidity premium) and one negative (lack of control). Thus, in analyzing REIT comparables and their trading prices, it is appropriate to identify and to quantify, and then to reverse out of the trading prices, any liquidity premiums that are associated with REIT comparability data, which calculation results in an REIT discount for lack of control*

that can be applied to the subject property."

Based on a regression analysis, the IRS expert calculated a 7.79% liquidity premium for REITs over illiquid investments, but the Court found this "unreasonably low" when compared to other studies. The Court determined a 17.47% discount for lack of control was appropriate.

The taxpayer expert used a 15% lack of marketability discount while the IRS expert used 21.23%. The Court simply accepted the 21.23% discount without further discussion.

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