

# ***The “Daily Plan-It™”***

*Davis Schilken, PC*

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## ***Petter Estate Is a Big Victory That Highlights a Great Safety Net Plan***

For those of you working with affluent families, you may want to share this article.

### **Anne Petter — Modest Teacher and Favorite Niece**

Anne Petter was a teacher who died in 2008. Her favorite uncle (this distinction may or may not be true) was an early investor in UPS. In 1982, she inherited stock from him. In 2001, she held \$22 million worth of UPS stock. At the time, the top estate and gift tax rates were 55 percent.

### **Step One: The LLC**

Upon a recommendation from her estate planning team, Ms. Petter created a Limited Liability Company (LLC). The operating agreement and the LLC structure were designed to allow the maximum discounting for gifting purposes and to allow Ms. Petter to maintain control while keeping an income stream for life. She conveyed her stock to the LLC. She then gave what she could and sold what she could. She also gave units to her favorite charities.

### **Step Two: The Valuation**

I left one key step out of the process above. Once the LLC was created, and the UPS stock conveyed, the LLC was valued for gift and sale purposes. Now, most of the time clients do not like to pay for the valuation or take the time to have it done, but in a case like Ms. Petter, the valuation is part of the one-two punch of this strategy. Ms. Petter's LLC received a 51 percent discount.

### **Step Three: IRS Disputes the Value and a Brilliant Surprise Move by Ms. Petter**

The IRS disputed the 51 percent discount, and after negotiation the parties agreed to a discount of 36 percent. The key point at issue was this - what was the gift tax that was due to the IRS when the discount value dropped from 51 to 36 percent? The IRS argued that there were additional gift taxes due on the transfer.

What the IRS did not anticipate was that Ms. Petter had specific language in her planning stating that if there were additional taxes due, then the units that were the subject of the taxes would go to charity. The strategy worked like a giant safety net so that any additional gift tax exposure was absorbed by the charity.

The IRS argued that if Ms. Petter got away with this strategy, then it could be adopted by other taxpayers and the IRS would lose its incentive to audit. (Like that would be enough to stop them from an audit!) The tax court disagreed and ruled for Ms. Petter.

### **Warning: This Concept May Not Be Around for Long**

The tax court invited the IRS to change its regulations if it did not like the ruling. Considering the opportunity, this concept may be open for your clients with similar wealth. It would not be surprising if this latest development is addressed and shut down by new IRS regulations. Here's a link to the case (<http://caselaw.findlaw.com/us-9th-circuit/1576509.html>) should you want to read it.

As always, we hope this issue has helped you and your clients. If you need any assistance or would like to discuss this case or any other matter, please contact us.

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**Keith L. Davis, JD, MBA, LLM, CPA**  
**Francis P. Brown, JD, MIM, LLM**  
**Janine A. Guillen, JD, MBA, LLM, RN**  
**Bruce A. Schilken, JD, CPA**  
**Richard W. Kautt, JD, MPA**  
**Gordon E. Schieman, JD**

523 Park Point Drive, Suite 350  
Golden, CO 80401  
Phone: 303-670-9855 Fax: 303-670-5381

925 W. Kenyon Ave., Unit 1  
Englewood, CO 80110  
Telephone: 303-670-9855 Fax: 303-762-0014