Estate of William T. Piper, Sr. , Deceased, William T. Piper, Jr. , Thomas F. Piper, and Howard Piper, Executors, Petitioner v. Commissioner of Internal Revenue, Respondent, 72 T. C. 1062 (1979); 1979 U. S. Tax Ct. LEXIS 59

When valuing restricted stock held by investment companies for gift tax purposes, consider the potential for registration and apply discounts for portfolio composition and lack of marketability.

Summary

William T. Piper, Sr. gifted all outstanding shares of two investment companies, Piper Investment Co. and Castanea Realty Co. , to his son and trusts for his grandchildren. The companies held unregistered Piper Aircraft Corp. (PAC) stock. The Tax Court determined the value of these shares for gift tax purposes, considering the PAC stock as restricted but capable of registration. The court applied a discount for registration costs, rejected discounts for prepaid expenses and potential capital gains tax, and allowed additional discounts for the companies' undiversified portfolios and lack of marketability of the gifted shares.

Facts

William T. Piper, Sr. created Piper Investment Co. and Castanea Realty Co. to hold PAC stock and real estate, aiming to minimize taxes while retaining control of PAC. On January 8, 1969, he gifted all shares of these companies to his son and trusts for his grandchildren. The companies' primary asset was unregistered PAC stock, which was actively traded on the New York Stock Exchange. Piper and his family owned about 28% of PAC stock, with Piper serving as chairman and his sons in key positions at PAC.

Procedural History

The Commissioner of Internal Revenue determined a gift tax deficiency for Piper's 1969 tax return. The estate contested this valuation in the U. S. Tax Court, which held hearings to assess the fair market value of the gifted shares based on the net asset value of the companies, considering discounts for various factors.

Issue(s)

1. Whether the unregistered PAC stock held by Piper Investment and Castanea was restricted stock for gift tax valuation purposes?
2. If so, what discount should be applied to the PAC stock's market price to account for resale restrictions?
3. Should prepaid or deferred expenses of Piper Investment and Castanea be included in their net asset value?
4. Is a discount for potential capital gains tax at the corporate level warranted?
5. Is a further discount for the companies' nondiversified portfolios justified?
6. Is an additional discount for lack of marketability of the gifted shares

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appropriate?

Holding

1. Yes, because Piper was a "control person" of PAC and could have compelled registration, the PAC stock was treated as restricted but valued at the NYSE price less registration costs.
2. Yes, a 12% discount was applied to reflect the cost of registration and sale.
3. No, because these expenses were already accounted for in the value of other assets, and their tax benefit was negligible.
4. No, as there was no evidence of planned liquidation that would trigger such a tax.
5. Yes, a 17% discount was allowed due to the companies' undiversified portfolios.
6. Yes, a 35% discount was applied for lack of marketability due to the absence of a public market for the shares.

Court's Reasoning

The court applied the fair market value standard under Section 2512(a), considering the hypothetical transaction between a willing buyer and seller. The court found Piper to be a "control person" of PAC due to his family's ownership and positions, meaning the PAC stock was restricted under securities laws. However, Piper could compel PAC to register the stock, thus the court valued the stock at the NYSE price minus a 12% discount for registration costs, as supported by expert testimony. The court rejected including prepaid or deferred expenses in the net asset value, as these were already reflected in other asset values and their tax benefit was too small to consider. The court also rejected a discount for potential capital gains tax due to the lack of evidence of planned liquidation. Discounts for the companies' undiversified portfolios and lack of marketability were deemed appropriate based on market data and the nature of the assets held.

Practical Implications

This decision guides the valuation of restricted stock held by investment companies, emphasizing the need to assess the potential for registration and the impact of resale restrictions. It clarifies that discounts should be applied for portfolio composition and lack of marketability but not for potential capital gains tax unless liquidation is imminent. Legal practitioners should carefully analyze the control status of stock holders and consider registration feasibility when valuing similar assets. Businesses structuring investment vehicles need to be aware of how securities laws can affect asset valuation for tax purposes. Subsequent cases, such as *Bolles v. Commissioner*, have built on this reasoning when dealing with restricted stock valuation.

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