Van Der Aa Investments, Inc. v. Commissioner, 125 T. C. 1 (2005)

In a significant ruling, the U. S. Tax Court denied Van Der Aa Investments, Inc. 's motion for partial summary judgment, asserting that the company failed to establish that there were no genuine issues of material fact regarding its built-in gain tax liability. The court ruled that an expert valuation report, crucial to the company's case, was inadmissible hearsay without the availability of the expert for cross-examination. This decision underscores the necessity of live expert testimony in summary judgment motions involving specialized knowledge, impacting how evidence is presented in tax disputes.

Parties

Van Der Aa Investments, Inc. , a dissolved Delaware corporation, represented by Terry L. Van Der Aa as trustee, was the petitioner. The respondent was the Commissioner of Internal Revenue.

Facts

Van Der Aa Investments, Inc. (Investments) was a dissolved Delaware corporation, represented by Terry L. Van Der Aa, trustee. The case centered on the company's 1999 Federal income tax return as an S corporation, where it reported a built-in gain tax liability of $1,520,140. The Commissioner of Internal Revenue issued a notice of deficiency on September 15, 2003, determining a deficiency in Investments' Federal income tax for 1999, amounting to $62,604,069, along with a delinquency addition under section 6651(a)(1) of $12,520,814 and an accuracy-related penalty under section 6662 of $3,124,797. The deficiency resulted from an adjustment that increased Investments' built-in gain tax liability to $64,124,209. Investments sought to support its calculation of the built-in gain tax liability with prior returns, audited financial statements, and a 1995 valuation report prepared by Arthur Andersen for Vancom Holdings, Inc. , which was offered as evidence in the motion for partial summary judgment.

Procedural History

Investments filed a motion for partial summary judgment, seeking adjudication on the issues of its built-in gain tax liability, the delinquency addition, and the accuracy-related penalty. The Commissioner objected, arguing that Investments failed to establish the absence of genuine issues of material fact, particularly challenging the admissibility of the valuation report as hearsay. The U. S. Tax Court, applying the standard of review for summary judgment under Rule 121 of the Tax Court Rules of Practice and Procedure, considered whether there were genuine issues of material fact and whether a decision could be rendered as a matter of law.

Issue(s)

Whether the valuation report, offered by Investments to support its built-in gain tax

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liability calculation, constitutes admissible evidence in a motion for partial summary judgment?

Rule(s) of Law

Rule 121 of the Tax Court Rules of Practice and Procedure governs summary judgment, requiring that there be no genuine issue as to any material fact and that a decision may be rendered as a matter of law. Federal Rule of Evidence 801(c) defines hearsay as a statement, other than one made by the declarant while testifying at the trial or hearing, offered in evidence to prove the truth of the matter asserted. Federal Rule of Evidence 803(6) provides an exception to the hearsay rule for records of regularly conducted activity, but Federal Rule of Evidence 705 requires that experts be available for cross-examination on the facts or data underlying their opinions.

Holding

The U. S. Tax Court held that the valuation report offered by Investments was inadmissible hearsay without the availability of the preparing expert for cross-examination. Consequently, the court denied Investments' motion for partial summary judgment, concluding that there remained genuine issues of material fact regarding Investments' built-in gain tax liability, the delinquency addition, and the accuracy-related penalty.

Reasoning

The court's reasoning focused on the admissibility of the valuation report. It determined that the report constituted hearsay under Federal Rule of Evidence 801(c), as it was offered to prove the truth of the matters asserted therein regarding the fair market value of Vancom, Inc. The court rejected Investments' argument that the report was admissible under the business records exception in Federal Rule of Evidence 803(6), emphasizing that the report expressed an expert opinion, which required the expert's availability for cross-examination under Federal Rule of Evidence 705. The court distinguished this case from others where business records were admitted without live testimony, noting that the valuation report's nature as expert opinion necessitated the expert's presence for cross-examination. The court concluded that without the valuation report, there were genuine issues of material fact that precluded summary judgment on the issues of built-in gain tax liability, the delinquency addition, and the accuracy-related penalty.

Disposition

The U. S. Tax Court denied Investments' motion for partial summary judgment, maintaining that genuine issues of material fact existed that precluded a decision as a matter of law.

Significance/Impact

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The Van Der Aa Investments, Inc. v. Commissioner case is significant for its clarification on the admissibility of expert valuation reports in summary judgment motions within the U. S. Tax Court. It establishes that such reports, when crucial to the case, are inadmissible hearsay unless the preparing expert is available for cross-examination. This ruling has practical implications for legal practice, emphasizing the importance of live expert testimony in tax disputes involving specialized knowledge. Subsequent courts have cited this case when addressing similar issues of evidence admissibility in summary judgment proceedings, highlighting its doctrinal importance in the area of tax law and evidence.

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