Thomas H. Holman, Jr. and Kim D. L. Holman v. Commissioner of Internal Revenue, 130 T. C. 170 (U. S. Tax Court 2008)

In *Holman v. Comm'r*, the U. S. Tax Court ruled that transfers of Dell stock to a family limited partnership (FLP) followed by gifts of partnership units were not indirect gifts of the stock itself. The court also addressed valuation discounts, rejecting the IRS's argument to disregard certain transfer restrictions in the partnership agreement, and determined specific discounts for minority interest and lack of marketability in valuing the gifts, impacting how FLPs are used for estate planning and tax purposes.

Parties

Thomas H. Holman, Jr. and Kim D. L. Holman (petitioners) were the taxpayers who challenged the IRS's gift tax assessments. They were residents of St. Paul, Minnesota, at the time of filing their petition. The Commissioner of Internal Revenue (respondent) was the opposing party in the case, represented by the IRS.

Facts

Thomas H. Holman, Jr. and Kim D. L. Holman, a married couple, formed a family limited partnership (Holman Limited Partnership) on November 3, 1999. They transferred 70,000 shares of Dell stock to the partnership, while Janelle S. Holman, as trustee of a trust set up for their children, contributed 100 shares. In exchange, the Holmans and the trust received partnership interests proportional to their contributions. On November 8, 1999, the Holmans made a gift of limited partnership units (LP units) to Janelle as custodian for their youngest child, I. , and as trustee for their children. Subsequent gifts of LP units were made in January 2000 and February 2001. The Holmans applied significant valuation discounts to these gifts, which the IRS contested, leading to a dispute over the appropriate valuation and tax treatment of the gifts.

Procedural History

The IRS issued notices of deficiency to the Holmans, determining gift tax deficiencies for the years 1999, 2000, and 2001. The Holmans filed a petition with the U. S. Tax Court challenging these determinations. The IRS amended its answer, increasing the deficiencies. The Tax Court heard the case, considering the IRS's arguments regarding the characterization of the transfers as indirect gifts and the application of valuation discounts. The court's decision addressed the IRS's contentions and determined the fair market value of the gifts, applying appropriate discounts.

Issue(s)

Whether the transfer of Dell stock to the Holman Limited Partnership and the subsequent gifts of limited partnership units constituted indirect gifts of the Dell

© 2025 SCOTUSreports.com. All rights reserved.

stock under Section 2511 of the Internal Revenue Code?

Whether the restrictions on the transfer of limited partnership units in the partnership agreement should be disregarded under Section 2703 of the Internal Revenue Code in valuing the gifts?

What are the appropriate discounts for minority interest and lack of marketability to be applied in determining the fair market value of the gifts of limited partnership units?

Rule(s) of Law

Section 2511 of the Internal Revenue Code imposes a gift tax on the transfer of property by gift, applying to both direct and indirect transfers. 26 C. F. R. sec. 25. 2511-2(a), Gift Tax Regs. , states that the value of a gift is determined by the value of the property passing from the donor, not by the enrichment to the donee. 26 C. F. R. sec. 25. 2703-1(b)(1)(iii), Gift Tax Regs. , provides that restrictions on the right to sell or use property are disregarded in valuation unless they meet certain criteria, including being a bona fide business arrangement, not a device to transfer property to family members for less than full consideration, and having terms comparable to arm's-length transactions.

Holding

The Tax Court held that the transfer of Dell stock to the partnership followed by the gifts of LP units did not constitute indirect gifts of the Dell stock. The court also held that the restrictions on the transfer of LP units in the partnership agreement should be disregarded under Section 2703 of the Internal Revenue Code because they did not meet the criteria of a bona fide business arrangement and were a device to transfer property to family members for less than full consideration. The court determined the fair market values of the gifts after applying discounts for minority interest and lack of marketability.

Reasoning

The court reasoned that the Holman Limited Partnership was formed and funded almost one week before the first gift of LP units, and thus, the transactions could not be viewed as an indirect gift of the Dell shares under Section 2511 or the step transaction doctrine. The court rejected the IRS's argument that the partnership and the gifts should be collapsed into a single transaction, noting the economic risk the Holmans bore due to the potential change in the value of the partnership between the funding and the gifts.

Regarding the transfer restrictions, the court found that they did not constitute a bona fide business arrangement under Section 2703(b)(1) because their primary purpose was to discourage the children from dissipating their wealth, rather than serving a legitimate business purpose. The court also determined that the

© 2025 SCOTUSreports.com. All rights reserved.

restrictions were a device to transfer property to family members for less than full consideration under Section 2703(b)(2), as they allowed for the redistribution of wealth among the children if an impermissible transfer occurred.

In valuing the gifts, the court applied minority interest discounts based on the interquartile mean of discounts observed in samples of closed-end investment funds, rejecting the Holmans' expert's adjustments for lack of portfolio diversity and professional management. The court also applied a marketability discount of 12. 5%, finding that the Holmans' expert's approach was unsupported and that the IRS's expert provided a more reliable estimate, taking into account the potential for a private market among the partners for LP units.

Disposition

The court determined the fair market values of the gifts after applying the appropriate discounts and entered a decision under Rule 155, allowing the parties to compute the final tax liabilities based on the court's findings.

Significance/Impact

Holman v. Comm'r is significant for its analysis of indirect gifts and valuation discounts in the context of family limited partnerships. The case clarifies that the timing and economic risk associated with transfers to an FLP and subsequent gifts of partnership interests can affect whether they are treated as indirect gifts. The court's decision to disregard transfer restrictions under Section 2703 also impacts how FLPs can be structured for estate planning and tax purposes, emphasizing the importance of having bona fide business purposes for such restrictions. The case's valuation methodology, particularly the use of closed-end investment fund data and the consideration of a private market for partnership interests, provides guidance for practitioners in valuing gifts of FLP interests.

© 2025 SCOTUSreports.com. All rights reserved.