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# Multi-Level Discounts for Tiered Entities— Insights from Historical Case Law

by James G. Rabe  
Portland, Oregon\*

## Introduction

How successful have taxpayers been in applying multi-level discounts (e.g., discounts for lack of control and lack of marketability) for tiered entities—holding companies that own an interest in another company? The Tax Court, as well as other courts, have opined on the appropriateness of applying multi-level discounts for tiered entities. This article presents an overview of 11 court cases that have dealt with the valuation of tiered entities. *Astleford*,<sup>1</sup> *Dean*,<sup>2</sup> *Gallun*,<sup>3</sup> *Gow*,<sup>4</sup> *Hjersted*,<sup>5</sup> *Kosman*,<sup>6</sup> *Piper*,<sup>7</sup> and *Whittemore*<sup>8</sup> allowed multi-level discounts; *Martin*<sup>9</sup> largely disallowed multi-level discounts; and *Janda*<sup>10</sup> and *O’Connell*<sup>11</sup> disallowed multi-level discounts.

Although at the audit level the IRS generally challenges as duplicative the application of two layers of discounts for tiered entities, taxpayers have been successful in applying multi-level discounts in a majority of the court cases involving tiered entities. In 9 of the 11 tiered entity court cases reviewed in this article, the courts allowed some degree of multi-level discounts. In addition, in a majority of these court cases, even the IRS’s experts applied multi-level discounts. In the 2 cases that disallowed multi-level discounts, *Janda* and *O’Connell*, there were unique circumstances that contributed to the rejection of multi-level discounts.

The rationale outlined by the courts in these cases provides insights regarding the appropriateness of applying multi-level discounts for tiered entities.

## Court Cases Allowing Multi-Level Discounts

### *Astleford*

#### Facts

In *Astleford*,<sup>12</sup> the Tax Court opined on the fair

market value of a 30 percent limited partnership interest in Astleford Family Limited Partnership (“AFLP”) as of August 1, 1996 and December 1, 1997. AFLP owned (1) a 50 percent general partnership interest in Pine Bend Development Co. (“Pine Bend”), (2) an ownership interest in an elder-care assisted living facility, and (3) 14 other parcels of real estate.

AFLP was formed by Jane Z. Astleford (“Astleford”) on August 1, 1996, as a Minnesota limited partnership. Astleford initially funded AFLP by transferring her ownership interest in an elder-care living facility.

On August 1, 1996, Astleford gave each of her three children a 30 percent limited partnership interest in AFLP, retaining a 10 percent general partnership interest. On December 1, 1997, Astleford transferred the following assets to AFLP: a 50 percent general partnership interest in Pine Bend, and her ownership interest in 14 other real estate properties. This caused her ownership interest in AFLP to increase significantly, and the ownership interests of her 3 children in AFLP to decrease significantly. Simultaneously with this transfer, Astleford gave additional limited partnership interests in AFLP to her three children to increase their limited partnership ownership interest in AFLP to 30 percent each. The fair market value of the gifted limited partnership interests were reported on Astleford’s gift tax returns at \$277,441 in 1996 and \$3,954,506 in 1997. In the notices of deficiency, the IRS determined that the fair market values of the gifted limited partnership interests were \$626,898 in 1996 and \$10,937,268 in 1997.

Six experts presented valuation evidence regarding the fair market value of the AFLP limited partnership interests at the trial, four for the taxpayer and two for the IRS. Throughout the Tax Court decision, these experts are simply referred to as the “petitioner’s expert” and the “respondent’s expert” without

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<sup>1</sup> Estate of Astleford v. Commissioner, T.C. Memo. 2008-128.

<sup>2</sup> Estate of Dean v. Commissioner, T.C. Memo. 1960-54.

<sup>3</sup> Estate of Gallun v. Commissioner, T.C. Memo. 1974-284.

<sup>4</sup> Estate of Gow v. Commissioner, T.C. Memo. 2000-93, *aff’d* 19 Fed.Appx. 90 (4th Cir. 2001).

<sup>5</sup> Estate of Hjersted, 175 P.3d 810 (Kan. 2008).

<sup>6</sup> Estate of Kosman v. Commissioner, T.C. Memo. 1996-112.

<sup>7</sup> Piper v. Commissioner, 72 T.C. 1062 (1979).

<sup>8</sup> Whittemore v. Fitzpatrick, 127 F.Supp. 710 (D. Conn. 1954).

<sup>9</sup> Estate of Martin v. Commissioner, T.C. Memo. 1985-424.

<sup>10</sup> Estate of Janda v. Commissioner, T.C. Memo. 2001-24.

<sup>11</sup> Estate of O’Connell v. Commissioner, T.C. Memo. 1978-191, *aff’d on this point, rev’d on other issues* 640 F.2d 249 (9th Cir. 1981).

<sup>12</sup> Estate of Astleford v. Commissioner, T.C. Memo. 2008-128.