TAX COURT CASE UPDATE

Citation:

Estate of George H. Wimmer et al. v. Commissioner, T.C. Memo 2012-157, June 4, 2012.

Overview:

In a case involving an estate tax deficiency of over a quarter of a million dollars, the Tax Court has held that gifts of limited partnership interests made by the decedent during life were gifts of present interests that qualified for annual exclusions. While the donees did not receive unrestricted and noncontingent rights to immediate use, possession or enjoyment of the limited partnership interests themselves, the gifts nonetheless qualified as present interests because the donees received such rights in the income from the limited partnership interests.

The Facts:

In 1996 and 1997, George H. Wimmer, and his wife, as trustees of their own trusts, formed the George H. Wimmer Family Partnership, L.P. (The LP), as a limited partnership. The Wimmers, as trustees of their respective trusts, were the initial general partners and limited partners.

The partnership agreement generally restricted transfer of partnership interests and limited the instances in which a transferee could become a substitute limited partner. Notwithstanding these restrictions and limitations, the partnership agreement had an exception for transfers to related parties, as defined in the agreement.

Pursuant to the transfer provisions, the Wimmers made gifts of limited partnership interests to related parties on November. 23, 1996, January 9, 1997, November 21, 1997, March 13, 1998, January 15, 1999, and January 7, 2000. The estate and IRS stipulated that if the gifts qualified for the annual exclusion, the taxable amounts of the gifts would be $1,402, $0, $8,455, $53,376, and $0, respectively.

The LP's primary purpose was to invest in property, including stock, bonds, notes, securities, and other personal property and real estate, on a profitable basis, and to share profits, losses, benefits and risks with the partners. The partnership agreement called for partnership profits and all distributions of net cash flow to be allocated to the partners according to their proportional partnership interests. Distributions had to be made in cash pro rata.

When the partnership was formed, its assets consisted of publicly traded and dividend-paying stock. No additional funding of the partnership occurred, and the partnership never held any assets other than the publicly traded stock and dividends received from these stocks.

In December 1996, the partnership received dividends from the stock and continued to receive dividends quarterly. It made distributions to the limited partners in 1996, 1997, and 1998 for payment of Federal income tax. Beginning in February 1999, the partnership continuously distributed all dividends, net of partnership expenses, to the partners. Dividends were distributed when received and in proportion to partnership interests. Mr. Wimmer died on March

29, 2004. The IRS said the gifts of the limited partnership interests did not qualify for annual exclusions, and therefore, substantially increased Mr. Wimmer's estate tax.

The parties disagreed as to whether the gifts of limited partnership interests were present interests, therefore qualifying for the gift tax exclusion. The Tax Court began its discussion by describing a future interest. What distinguishes a future from a present interest is the postponement of the right to use, possess, or enjoy the property. An interest may vest immediately in the donee, and yet it will be a future interest if the donee cannot enjoy or use it presently.

Discussion:

Under the regulations, a present interest is an unrestricted right to immediate use, possession, or enjoyment of property or the income from property. Therefore, to qualify as a present interest, a gift must confer on the donee a substantial present economic benefit by reason of use, possession, or enjoyment (1) of property or (2) of income from the property.

The Tax Court observed that with respect to the limited partnership interests themselves, the donees' rights were limited. While they could transfer their interests to other partners and related parties, all other transfers were restricted unless various requirements were met. Therefore, the donees did not receive unrestricted and noncontingent rights to immediate use, possession, or enjoyment of the limited partnership interests themselves. However, the gifts could still qualify for annual exclusions if the donees received such rights in the income. To show that they did, the Tax Court said that the estate had to prove that:

> ... the partnership would generate income,
> ... some portion of the income would flow steadily to the donees, and
> ... that portion of income could be readily ascertained.

The Tax Court observed that, in September 1996, before the gifts were made, the partnership held publicly traded and dividend-paying stock. It received its first quarterly dividend in December 1996 and continued to receive dividends for each quarter thereafter. Therefore, with respect to the first prong, the estate proved on each date a gift was made, the partnership expected to generate income.

Various evidence showed that on the date of each gift, some portion of partnership income was expected to flow steadily to the limited partners. Thus, the second prong of the test was met.

The Tax Court also found that the portion of income flowing to the limited partners could be readily ascertained. The LP held publicly traded, dividend-paying stock and was thus expected to earn dividend income each year at issue. Because the stock was publicly traded, the limited partners could estimate their allocation of quarterly dividends on the basis of the stock's dividend history and their percentage ownership in the partnership. As a result, the third prong of the test was met.

Conclusion:

On the basis of the specific facts and circumstances presented in the case, the Tax Court found that the limited partners received a substantial present economic benefit sufficient to render the gifts of limited partnership interests as present interest gifts on the date of each gift. Therefore, the gifts qualified for the gift tax annual exclusion under Code Sec. 2503(b). This is the fourth annual exclusion case, the first being *Hackl* (118 T.C. 279 (2002)), followed by *Price* (T.C. Memo 2012-2) and *Fisher* (105 AFTR 2d 2010-1347).