

Business Valuation, Estate and Gift, and Taxes



Michael Gregory
651-633-5311
mg@mikegreg.com



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Michael Gregory



- ASA and CVA
- 28 years at the IRS
- Headed up business valuation at the IRS for 11 years
- Qualified Mediator with the MN Supreme Court 18 years
- Testified in U.S. Tax Court
- Over 2,500 mediations, negotiations, facilitations
- 12 books and over 45 articles

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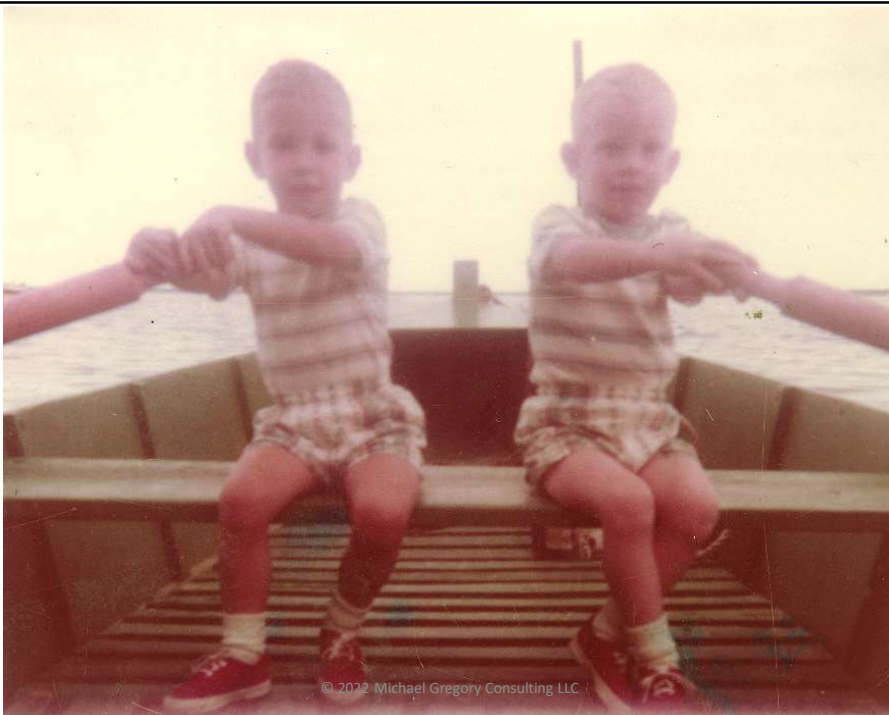


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As a Result of Today's Presentation You Will Be Able to:



- Address pertinent changes at the IRS
- Make recommendations to clients based on risk
- Identify your client's rights and how to bring them up with the IRS
- Apply DLOMs:
 - For holding companies versus operating businesses
 - Based on the size of entities

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As a Result of Today's Presentation You Will Be Able to:

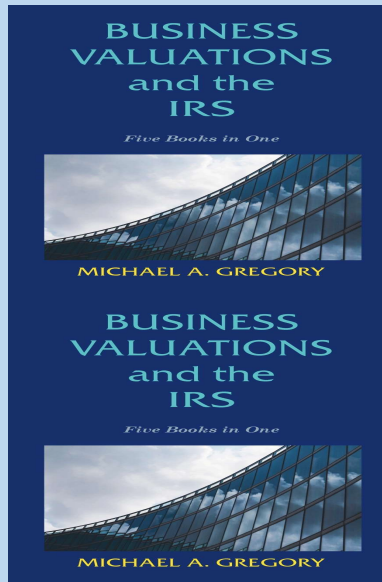


- Reference recent key court cases relevant to business valuation
- Apply techniques to address interests and focus on closure
- Distinguish when unfair treatment may require alternative actions
- Develop a plan to move a case forward positively and professionally

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Business Valuations and the IRS: Five Books in One

852 Pages with 38 Examples and over 180 Practical Pointers

- 1. Part One: IRS Structure and Process**
- 2. Part Two: Resolving Conflict with the IRS**
- 3. Part Three: Valuing Non-Controlling Interests in S-Corps**
- 4. Part Four: Valuing Reasonable Compensation and the IRS**
- 5. Part Five: Discount For Lack of Marketability and the IRS**

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The IRS Big Picture



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Keys to Job Aids

Download Them

Read Them

Key Points

When

What

Why

How It May Be Useful

**Note: Download three IRS Job Aids while searching
“IRS Valuation of Assets”**

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How The Job Aids Can Be Helpful



- Provide insights into how the IRS thought at the time of publication
- Can provide technical commentary to help with issue resolution – “The IRS Job Aid state...”
- Knowing how the IRS approaches an issue can with understanding interests and
- Detailed strengths and weaknesses of most common approaches

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Introduction

1. What the IRS is intending to do in 2023 and beyond
2. What are the implications?
3. What should you do?

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What the IRS Intends to Do



- Quality Audit
- Quantity of Returns
- Taxpayer Bill of Rights
IRS Publication 1

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The IRS Today

- The IRS was behind 21 million pieces of mail
- 2.4 million paper returns from 2019
- 1.7 million returns are in the error resolution unit
- 2.5 million cases are in its account's management unit
- 1.6 million returns are flagged for fraud
- More recent IRS hires of Engineers and Business Valuers

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IRS Engineering and Valuation

- December 2021 about 250 Engineers
- September and October 2021 trained 79 move in BV through NACVA
- Trying to hire about 50 more currently
- By the numbers and implications
 - 130 new employees
 - 115 experienced employees
 - 30 managers and territory managers
 - FY 2022 75% efficiency, FY 2023 90% efficiency

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Where to File Estate and Gift Tax Returns

- **Form 706 and 709**
- ***Effective January 1, 2019***
- Department of the Treasury
Internal Revenue Service Center
Kansas City, MO 64999
- If submitting Form 706 or 709 by private delivery service, mail to:
- Internal Revenue Service
333 W. Pershing Rd
Kansas City, MO 64108

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Classification of Estate and Gift Tax Returns



- **National Classification** Process – Kansas City now versus Cincinnati
- **Local Classification** Process

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How Are Business Valuation Cases Selected for Examination?

- **Discounts including Reconciliation**
- **Assumptions and Limiting Conditions**
- **Income Approach**
- **Market Approach**
- **Cost Approach**
- **Reconciliation**

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IRS Most Significant Issues Adjusted on Business Valuation Cases in 2021



- Discounts
- Reasonable Compensation
- S-Corps
- Common Errors

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Historical Perspective of E&G Filings and Audits

Category	Year	Year	Year	Year
	Totals	% Audited	Totals	% Audited
	2017	2018	2018	2019
< \$ 5 Mil	23,013	2.7%	19,025	2.0%
\$5M<x<\$10M	8,095	12.6%	8,837	9.2%
>\$10 Mil	3,934	31.0%	4,975	21.7%
Estate Totals	35,042	8.6%	32,847	6.9%
Gift Totals	244,974	0.8%	244,770	0.8%

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Historical Perspective of E&G Filings and % Audits

Catetgory	Year	Year	Year	Year	Year	Year	Year	Year	Year
	% Audited	% Audited	% Audited	% Audited	Totals	Total	Totals	Totals	Totals
	2018	2019	2020	2021	2018	2019	2020	2021	
<\$5 Mil	2.7%	2.0%			19,035				
\$5M = x < \$10 M	12.6%	9.2%			8,837				
>=\$ 10 Mil	31.0%	21.7%			4,975				
Estate Totals	8.6%	6.9%	10.0%	5.7%	32,847	25,742	15,023	28,473	
Gift Totals	0.9%	0.8%	0.8%	0.4%	244,770	239,618	158,095	282,054	

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Historical Perspective of Average Tax and Average Refunds

Catetgory	Year	Year	Year	Year
	Avg Add Tax	Avg Refund	Avg Add Tax	Avg Refund
	2020	2020	2021	2021
<\$5 Mil	\$ 130,297	\$ 291,200		
\$5M = x < \$10 M	\$ 90,018	\$ 124,724		
>=\$ 10 Mil	\$ 407,983	\$ 502,295		
Estate Totals	\$ 263,800	\$ 366,505	\$ 819,622	\$ 529,277
Gift Totals	\$ 216,127	\$ 468,262	\$ 410,525	\$ 2,310,946

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Some Other Interesting Facts from IRS Data

- **For Estate Audits 18% are No Changes**
- **For Estate Audits 20% are Refunds**
- **Additional Tax Adjustments for Estates Amount to on Average**
 - \$126,000 for under \$5 million estates
 - \$ 88,000 for \$5 million up to \$10 million estates
 - **\$335,000 for over \$10 million estates**
- **For Gift Audits 43% are No Changes**
- **About 5% of Gift Cases Have Valuations.** If 50% of Change Cases Are Valuations this Amounts to **Approximately 5% Chance of Being Audited**

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Estate and Gift Tax Ramifications

- **Goal to close cases in 6 months**
- **Goal to close out so many cases in FY 2022**
 - October 1, 2021 to September 30, 2022
 - It takes a month to close a case
 - Complete closed cases by no later than August 31 for year end
 - This means an agreed case with the closing letter
 - This means an unagreed case closed out of the group with the 30-day letter response to Appeals
 - If a case has less than 9 months on the statute when it arrives at Appeals, it will not be accepted – docket for court
- **Quantity goal**
- **Quality goal - TCJA**

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Given IRS Budget

Quality will suffer

Taxpayer Bill of Rights IRS Publication Number 1

LB&I IRM 4.46.4.6 (12-13-2018) Information Document Request Process with Exhibit 4.46.4-1

Quantity – will not meet targets, but will try valiantly to meet targets

Outside of Business Valuation Observations

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What Should You Do?

- **Consider what areas IRS business valuers make the most adjustments**
- **Understand how the IRS looks at them and plan accordingly**
- **Consider behavioral elements on audit**
- **Don't be afraid to go to Appeals**

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Three Major Adjustment Areas on Business Valuation Reports

Three IRS Job Aids at <https://www.irs.gov/businesses/valuation-of-assets>

- Reasonable compensation
- Discount for Lack of Marketability (DLOM's)
- 1120 S tax affecting

Other:

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Models to Consider On DLOMs

1. Restricted Stock Studies +
2. Cost of Flotation: about to go public only +
3. Mandelbaum factors, Judge Laro 1995: good first step with 9 – 10 factors +
4. Long-Term Equity Anticipation Securities (LEAPS) Robert Trout 2003, Ronald Seaman 2005 +
5. The Longstaff Study, Journal of Finance, December 1995 +
6. Finnerty model +

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Models to Consider

7. Note VFC DLOM Calculator from Vianello: consider +
8. Ashok B. Abbott: stay abreast
9. QMDM (Christopher Mercer) + possible check
10. NICE (William Frazier) + only income approach
11. NERA (David Tabak) + complex
12. Partnership Profiles (Partnership Spectrum) +FLPs
13. FMV Opinions now Stout + first of three variables
14. Pluris + first of two variables

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Methods to Consider for Various Categories

IRS Feedback on DLOM Methods						
DLOM Method	Consider Recommendation for					
	Holding Company	Operating Entities	Small Entities	Large Entities	Going Public	LLC'S FLPS 1120S
Restricted Stock Studies	X	X	X	X		X
Cost of Flotation	X	X	X	X	X	
Mandelbaum Factors	X	X	X	X		
GPCM - LEAPS		X		X		
GPCM - Longstaff	X	X	X	X	X	X
GPCM - Finnerty		X		X		
QMDM	X	X	X	X	X	X
NICE	X		X	X		X
NERA	X	X		X		
Johnson Park Empirical Method	X	X	X	X		X
Stout formerly FMV Opinions (first of three variables)	X	X	X	X	X	X
Pluris (first of two variables)						
VFC DLOM Calculator	X	X	X	X	X	X
Ashok Abbot	X	X		X	X	
Consider 33 factors: 8 subject interst factors and 25 subject company factors						

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Holding Companies Versus Active Businesses Tendencies



- **Holding Companies**
 - REITS
 - FLPs with Partnership Profiles
 - Explore similar types of entities
- **Operating Companies**
 - Restricted stock studies
 - Mandelbaum factors
 - VFC DLOM Calculator
 - LEAPS
 - Explore similar types of entities
- **No Clear Leaning** – other methods

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Small Entities versus Mid Size and Large Entities Tendencies



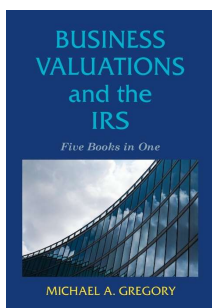
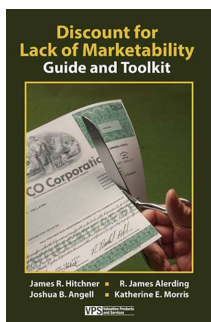
- **Large Entities**
 - Finnerty
 - Longstaff – more for blocks of stock
 - VFC DLOM Calculator – weighted large
 - Stout – weighted large
 - Pluris – weighted large
 - Cost of flotation for IPOs
 - LEAPS weighted large
 - NERA
- **Small Entities**
 - Restricted stock studies – explore the study
 - Mandelbaum factors
- **No Clear Leaning** – other methods

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Sources to Help You



- ***Discount for Lack of Marketability Guide and Toolkit*** by James Hitchner, R. James Alerding, Joshua B. Angell and Katherine E. Morris
- **Business Valuations and the IRS** by Michael A. Gregory
- **Complimentary eBook on DLOMs** at www.mikegreg.com/books

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Summary of DLOM Overview

- **“Discount for Lack of Marketability Job Aid for IRS Valuation Professionals”** at www.irs.gov Prepared 9/2009 for IRS Valuers
- **Comments on the Job Aid**
- **Resolving Issues – Some Thoughts from Neuroscience**
- **Developing your DLOM and working it out with the IRS**

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Recommendations to Determining the DLOM

- **Use Restricted Stock Studies and 33 Factors**
 - If Using a Study – Obtain it, Read it, Use it
 - Follow Approach of Mandelbaum – Judge Laro
 - Use 33 Factors from DLOM Study
- **Stout or Pluris Data Step 1 Private Placements**
 - Step 2 and Step 3 IRS May Have Concerns
 - In Place of Step 2 or 3 Use 33 Factors
- **Use Third Approach From DLOM Study or Newer Models**
 - Choose What Makes Sense
 - Size of Company, Facts
- **Reconcile Approaches**

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Recommendation

- **Select at least three methods of those recommended**
- **Reconcile the methods with a paragraph on each regarding rationale for greater or lesser weight and why**
- **Clearly articulate your conclusion**

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Recall the DLOM Job Aid

- **Executive Summary**
 - Background
 - Objective
 - Approach
 - Conclusion
- **Introduction**
- **Organization**
- **Other Authors' Observations**

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Observations

- IRS Job Aid on DLOMs is **Worth Reading**
- **Look at Why It Was Written and Audience**
- **Nothing Personal – Strictly Analytic**
- **Multiple Approaches Recommended** – Use Judgment and Document Rationale
- **Courts More Analytically Oriented, i.e., Want Data (Stout; Pluris)**
- **See Pro's and Con's of Methods and Choose Accordingly**

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Relevant Historical Court Cases on Tax Affecting S Corps

- **Gross** T.C. Memo 1999-254, aff'd. 272 F.3d 333 (6th Circuit) 2001, cert denied 537 US 827 (2002) (Corp)
- **Wall** TC Memo 2001-75 (Corp)
- **Heck** T.C. Memo 2002-34 (Corp)
- **Adams** T.C. Memo 2002-80 (Corp)
- **Dallas** T.C. Memo 2006-212 (Corp)
- **Guistina** TC Memo 2011-141 (*Limited Partnership*)
- **Gallagher** TC Memo 2011-148 (LLC)

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More Recent Federal Court Cases on Business Valuation



- **Nelson v. Commissioner** June 10, 2020, 5th Circuit Dec 21, 2021
- **Estate of Michael Jackson** May 3, 2021
- **Estate of Warne** February 18, 2021
- **Lucero v. U.S.** October 27, 2020
- **Pierson M. Greive** March 2, 2020
- **Estate of Aaron U. Jones** August 19, 2019
- **Kress v. U.S.** March 26, 2019

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Pertinent Federal Court Cases on Business Valuation



- **Nelson v. Commissioner** June 10, 2020, 5th Circuit Dec 21, 2021 Win for TP
- Estate of **Michael Jackson** May 3, 2021 (Corp) Win for TP
- Estate of **Warne** February 18, 2021 Win for TP
- **Lucero v. U.S.** October 27, 2020 Win for TP
- Pierson M. **Greive v. Comm** March 2, 2020 Win for TP
- Estate of **Aaron U. Jones** August 19, 2019 (Corp) Win for TP (1120S)
- **Kress v. Comm** March 26, 2019 (Corp) Win for TP (1120S)
- Estate of **Gallagher** June 28, 2011
- **Guistina** TC Memo 2011-141 (Limited Partnership)
- **Dallas** T.C. Memo 2006-212 (Corp)
- **Adams** T.C. Memo 2002-80 (Corp)
- **Heck** T.C. Memo 2002-34 (Corp)
- **Wall** TC Memo 2001-75 (Corp)
- **Gross v. Commissioner** T.C. Memo 1999-254, aff'd 272 F. 3d 333 (6th Cir. 2001) cert denied, 537 U.S. 827 (2002) (Corp)

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But First Key Points from the Estate of Gallagher Case TCM 2011-148

- Write a Report for the Court and Judge
- Read Court Cases by Judge on Topic
- What Did Judge Halpern Have to Say?
 - **Report is Testimony Have to Work with What I Have**
 - Should NOT Have Used WACC in This Instance
 - Not Going Public and Do Not Meet Assumptions for WACC
 - Use Equity Approach
 - Do Not Use CAPM or Modified CAPM for the Discount Rate
 - Same Concerns As Above
 - Use Build Up Method

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What Did Judge Halpern Have To Say Continued

- Gross Still Governs – **“We Will NOT Impose** an Unjustified Fictitious Corporate Tax Rate” – IRS is 6 for 6 in Court
- **Don’t Assume Judge Understands Valuation Concepts**
- **Understand Discovery Rules and Process and Work with Attorney**
- **Have a Third Party Review Your Report**
- **Provide Court with Evidence: If It Is Not In Evidence It Does Not Exist -** Valuation Text Book for Example
- Your job is to **EDUCATE THE COURT**

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Nelson v. Commissioner, TC Memo 2020-81, Affirmed 5th Circuit of Appeals Dec 21, 2021

- Mrs. Nelson gifted FLP % appraised at \$2,096,000 on 12/31/2008
- On 1/2/2009 Mrs. Nelson sold \$20,000,000 to her husband and daughters.
- IRS valued the gifts as \$3,522,018
- IRS valued assets sold as \$13,607,038
- IRS claimed Mrs. Nelson transferred FLP interests of 6.14% and 58.65% as specific percentages of the value of the FLP and not specific dollar amounts.

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Nelson v. Commissioner, TC Memo 2020-81, Affirmed 5th Circuit of Appeals Dec 21, 2021

- USTC went with percentages
- 5th Circuit upheld the percentages
 - The agreement is separate from the formula clause
 - The appraiser determined the dollar amount and converted it to a percentage
 - That locked in the percentages even if the value changed
 - Crucial language was missing.
- In terms of dollars a 70% victory for the TP in terms of values of the assets
- Multi-tiered discounts were allowed with DLOCs and DLOMs

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Michael J. Jackson

Asset	Estate	Commissioner	Tax Court	Percentage for the Winner
Jackson's Image and Likeness	\$3,078,000	\$161,307,045	\$4,153,912	99% TP
New Horizon Trust II 50% Interest in Sony/ATV	\$0	\$206,295,934	\$0	100% TP
New Horizon Trust III Mijac Music	\$2,267,316	\$114,263,615	\$107,313,561	94% IRS
Total	\$5,345,316	\$336,866,594	\$111,467,473	68% TP

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Estate of Michael Jackson v. Commissioner,

- Judge Holmes
- And we find, as we have done consistently in the past apart from Estate of Jones, that by a preponderance of the evidence tax affecting is not appropriate here because the Estate has failed to persuade us that a C corporation would be the hypothetical buyer of any of the three contested assets.
- We do not hold that tax affecting is never called for. But our cases show how difficult a factual issue it is to demonstrate even a reasonable approximation [*83] of what that effect would be. In Estate of Jones, there was expert evidence on only one side of the question, and that made a difference.

Estate of Warne v. Commissioner,

T.C. Memo 2021-17 (Feb. 18, 2021)

- LLC operating agreement gave significant power to the majority interest holder; family trust had majority interest in every LLC
- Court values not was contributed, but what charity received
- **Here is a detailed analysis for DLOC for a majority interest**
- Using data and thoroughly supporting in a report will win
- **TP 5% to 8% Mergerstat Control Premium Study – considered factors specific LLC**
- **IRS 2%** closed in funds dissimilar to subject – took bottom of range - court rejected
- **Court 4%**
- **Court stated previously no DLOC for majority interest, in this case slight discount based on DLOC's by both parties**

Lucero v. United States,

U.S. District Court for the District of New Mexico,
October 27, 2020, Civ. No. 17-1065 JCH/JFR

- TP claimed refund from \$2.38/sh to \$0.57/sh
- Prior court settlement – compulsion at play in court case -\$2.38/sh
- Valuation date August 2014 – negative cash flow from beginning 2011 accumulated \$608 million
- Four valuations January to July 2014 \$3.53/sh to \$4.10/sh; Sept 2015 redeemed for \$.48/sh
- TP expert appraisal negative cash flows, used Altman Z-score bankruptcy probability, DLOM 18%, DLOC 25%
- IRS review with opinion of value from exam and court case, agreed with discounts
- Court 100% for TP

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Lucero v. United States,

U.S. District Court for the District of New Mexico,
October 27, 2020, Civ. No. 17-1065 JCH/JFR

- Expert testimony by TP with full appraisal
- IRS supplied a review with an opinion of value – totally discredited by the court
- IRS used a court case determination from litigation where one part was under duress - totally discredited by the court
- Implications at the IRS

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Pierson M. Grieve,

T.C. Memo. 2020-28 (March 2, 2020)

- FMV of gift of 99.8% nonvoting interest in a GRAT Trust and Irrevocable Trust
- FMV by TP Expert
 - Used market and income approaches
 - Used closed end funds for DLOC
 - Used restricted stock studies for DLOM
- FMV by IRS Expert – A willing seller would attempt to take control – concluded a premium to buy out and take control of the controlling interest
- Court – no facts to support IRS theory – facts run contrary to IRS theory – not reasonably probable – no evidence of peer review methodology

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Pierson M. Grieve,

T.C. Memo. 2020-28 (March 2, 2020)

- Cash, cash equivalents, and marketable securities
- Discounts total 35% at issue
- Court firmly rejected Government's assertion that 99.8% would buy 0.2% controlling interests – hypothetical with no basis in facts.
- Valuations very similar - went with original valuation by TP and did not criticize the NICE method; government witness took issue with holding period, but not approach
- No issues raised on the valuations of the entities, so the court did not have to address tax affecting by the TP's expert

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Estate of Aaron U. Jones,

T.C. Memo 2019-101

- Seneca Saw Mill (SSM)
- Seneca Jones Timber Company, LP
- Gifts of stock May 28, 2009
- Mr. Jones died September 14, 2014
- Valuing both entities for gift and estate
- Findings SSM – **Government no appraisal** argued law, **TP won with tax affecting**
- Findings SJTC – Operating vs. Holding Co., TP tax affected and 22% premium; Government did not tax affect – **“Mr. Reilly may not be exact, but it is more complete and more convincing than respondent’s 0% tax rate”.**

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Estate of Aaron U. Jones

T.C. Memo 2019-101 (Aug. 19, 2019)

- **Valuation of SSC lumber mill and STJC timberlands May 28, 2009**
- **IRS SSC no valuation, STJC argued law not facts – tax affecting accepted**
- **TP Experts \$21 M and IRS \$141 M operating vs. holding company**

Category	Columbia (original)	Willamette	IRS	Court
SSC A voting	\$325	\$390	\$1,395	\$390
SSC B nonvoting 1	\$315	\$380	\$1,325	\$380
SSC B nonvoting 2	\$315	\$380	\$1,325	\$380
SJTC limited partnership	\$350	\$380	\$2,511	\$380
Rifle Range			\$4.20 (1%)	\$4.20

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Kress v. United States,

March 26, 2019

- U.S. District Court Case litigated by the Department of Justice Tax Litigation Division
- Both parties' tax affected cash flows minority owned shares
- Government's expert applied an S corp premium to account for perceived tax advantages – court declared itself neutral on this issue
- Note: not a U.S. Tax Court or U.S. Court of Appeals decision
- Note: Court did not address the issue of tax affecting in the opinion
- Note: The government gave recognition to tax affecting

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Kress v. United States

123 AFTR 2d 2019-1224 (ED Wisc. March 26, 2019).

	Emory	Czapinski	Burns	IRS	Court
2007	\$28.00	\$30.37	\$38.04	\$45.97	\$29.20
2008	\$25.90	\$25.92	\$27.61	\$47.63	\$27.01
2009	\$21.60	\$25.06	\$40.05	\$50.85	\$22.50

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Insights on Charitable Contributions From Around the Valuation World 9-2018



- Final Regs non cash contributions and
- §§ 1.170A-15, 16, 17 and 18 from §170
- See the reference, **download it and go over them**
- These relate to charitable donations only
- “flexibility” with other professional standards

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From Around the Valuation World 9-2018



- Cite no credential
- Define qualified appraiser and appraisal
- Effective Dates
- Appraiser declaration
- Provides **three examples of when or when not qualified as an appraiser**

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Specific Regulation Changes



- §§ 1.170A-15(a) and (d)(1);
- 1.170A-16(a), (b), (c), (d), (e), and (f);
- and 1.170A-18(a)(2) and (b).

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Effective Dates



- These final rules apply to contributions made **on or after Jan. 1, 2019**
- Taxpayers **may rely on these rules** for appraisals prepared for **returns or submissions filed after Aug. 17, 2006.** (TD 9836.)

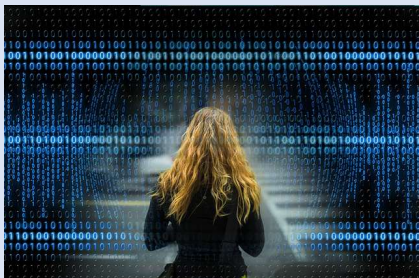
[Lawyers, accountants and appraisers preparing tax **returns should be fully familiar not just a nodding acquaintance**]

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Key Provisions for Business Appraisers



- You need your EIN or SSN on the appraisal report
 - For privacy use your employer EIN
 - If you do not have an EIN apply for EIN at <https://sa.www4.irs.gov/modiein/individual/index.jsp>
 - It is not recommended you use your SSN

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Key Provisions for Business Appraisers



If multiple appraisers each must sign the appraisal, the certification in the appraisal, the appraisal summary if there is one (USPAP), and the accompanying 8283 form

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Key Provisions for Business Appraisers



- Tell clients – different regs for non-cash charitable contributions
- Tell clients – different from E&G
- Tell clients – different requirements for appraisals for each

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Disclosure Requirements

"I understand that my appraisal will be used in connection with a return or claim for refund. I also understand that, if there is a substantial or gross valuation misstatement of the value of the property claimed on the return or claim for refund that is based on my appraisal, I may be subject to a penalty under section 6695A of the Internal Revenue Code, as well as other applicable penalties. I affirm that I have not been at any time in the three-year period ending on the date of the appraisal barred from presenting evidence or testimony before the Department of the Treasury or the Internal Revenue Service pursuant to 31 U.S.C. 330(c)."

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Code Section 6695A

- The lessor of
 - The greater of
 - 10 percent of the amount of the underpayment (defined by IRC section 6664(a)) attributable to the misstatement or
 - \$1,000
 - 125 percent of the gross income received from the preparation of the appraisal
- More Likely Than Not Penalty Exception
 - Would there be a greater than 50% likelihood that appraiser would prevail in court?
 - Based on proper value

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Code Section 6695A Example

- Difference in value with IRS \$200,000
- Tax Rate 40%
- Difference in tax paid = $\$200,000 \times 0.40 = \$80,000$
- \$20,000 appraisal fee
- The lessor of
 - The greater of
 - 10 percent of the amount of the underpayment (defined by IRC section 6664(a)) attributable to the misstatement [\$8,000] or
 - \$1,000
 - 125 percent of the gross income received from the preparation of the appraisal
 $1.25 \times \$20,000 = \text{[\$25,000]}$
- More Likely Than Not Penalty Exception
 - Would there be a greater than 50% likelihood that appraiser would prevail in court?
 - Based on proper value

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Requirements to Attach Appraisal to the Return



- Claimed deduction more than \$500,000
 - For Personal Property greater than \$20,000 – already in the regs for artwork, collectables and antiques
- [Editorial opinion – always attach the appraisal no matter what for classification purposes]**

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What is Mediation and a Mediator

- Mediation
 - Evaluative
 - Facilitative
 - Transformative
- Mediator
 - Qualified Mediator
 - True Neutral

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Thanks, Neuroscience!



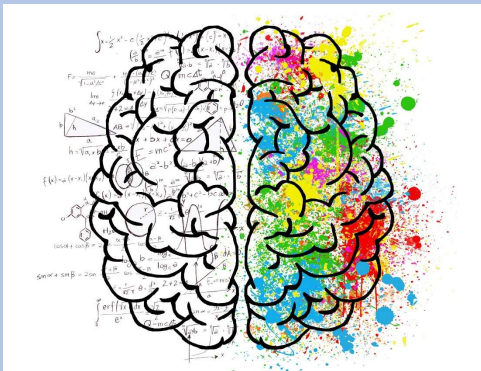
- **Terry Wu**, PhD Vanderbilt Neuroscientist
- **Ericka Garms**, PhD U of MN and Her Team, Neuroscientist
- **John B. Molidor**, PhD Assoc. Dean MSU Medical School
- **Rick Hanson**, PhD Psychologist, Greater Good U of CA Berkeley

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The Brain is Out to Protect Us



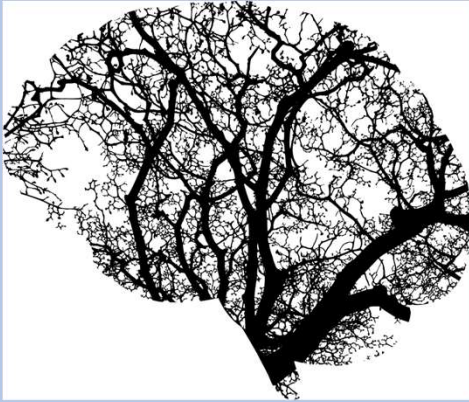
- **The brain is lazy** – chooses least energy approach
- **The brain predicts continuously based on the past**
- **Our brain has two hemispheres that are gated**
- **Right hemisphere is more big picture, left more detail – brain likes big picture first.**

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Connections in the Brain



- Neurons like superhighways
- As we age – tune and prune dendrites
- Tapping into existing memories can drive positive current actions
- Reflexes from habits and goals

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What Can You Do to Help Your Brain?



- **Eat more plant-based foods** – antioxidants (blue berries), dark green, and orange colors best – you are what you eat (100,000 neurons in your gut)
- **Drink more water**
- **Never stop moving** (get appropriate exercise)
- **Have consistent sleep patterns** – consistent wake up time - **MOST IMPORTANT of first four elements**
- **Mindfulness at least 10 minutes a day**

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Working with Others



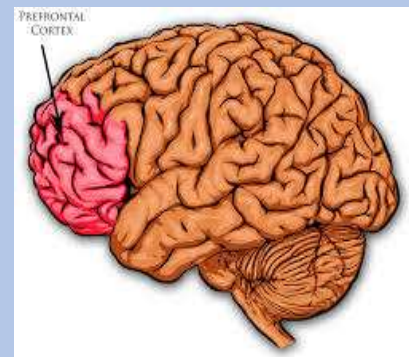
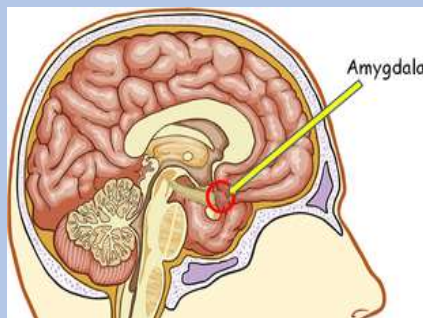
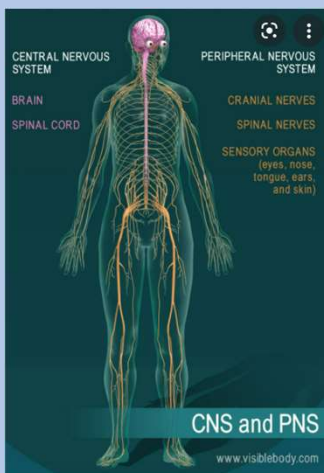
- **Under 25 and Over 25**
- **Neuroplasticity** – only organ to wire and rewire itself
- **Continually exploring**
 - Senses
 - Perceptions
 - Feelings
 - Thoughts
 - Behaviors
- **Biases are received informally and behave externally**

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Nervous System, Amygdala, and Prefrontal Cortex



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Key Points for Discussion



- We are predisposed to **judge negatively** first
- We approach for food, water, sex and shelter
- We defend against everything else

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Reduce the Stress Response



- Maintain a sense of **control**
- Have a sense of **predictability** (routine and rituals)
- Have a sense of **progress** (make big projects into smaller elements and provide affirming feedback)

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A photograph of a golden retriever dog sitting in tall green grass. The dog is looking directly at the camera. In the foreground, two bright green tennis balls are visible. The background shows a brick wall and a window. The image is part of a presentation slide with a blue background.

Choices

- Confrontation
- Collaboration

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Center Ourselves First



- **Calm the fire**
- Realize you need to **be there to help** if you are to overcome conflict with collaboration

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Active Listening



- Paraphrase
- Ask open ended questions
- Suspend judgment
- Summarize
- Empathize
- Do NOT offer advice

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Negotiation

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Two Real World Examination Examples to Set the Tone



- **Discount for Lack of Marketability 10% IRS and 30%)**
 - Relationship, Listening, Education, Negotiation
 - Don't Underestimate Neuroscience
 - Prepare, Prepare, Prepare and Relationships
- **Mediation at the IRS**
 - How to Prepare Administratively
 - How to Prepare Technically

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Official Alternative Dispute Resolution and the IRS

		Stages of IRS Process		
	Pre-Filing	Examination	Collection	Appeals
Type of Taxpayer				
LB&I	Compliance Assurance Program	Fast Track Settlement Early Referral to Appeals		Post Appeals Mediation
SBSE		Same as LB&I	Fast Track Mediation	Post Appeals Mediation
TEGE		Early Referral to Appeals		

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Role of the IRS Examiner

- **Independent**
- **Owns the Case**
- **May or May Now Want Assistance** from Specialist

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Role of the Business Valuer

- **Consultant**, not a decision maker
- **Taxpayer may request** their involvement, but **not guaranteed**
- If involved, can provide **informal consultation, formal consultation, or limited scope examination or full examination**

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Who is the Decision Maker on an Examination

- Estate and Gift Tax Attorney or Agent
- Estate and Gift Tax Attorney Manager or Agent Manager is the ultimate decision maker

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LB&I has an Informal Mediation Process – SBSE Uses This Too

- Business Valuers are Trained in Mediation
- Model – **FIFI** – Facts Issues Feelings and Interests

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Ideas to Assist you in the Appeals Process

- **Prior to the Appeals Conference, Summarize Major Issues on One Page & Follow Up with the Appeals Officer After Your Meeting**
- **Always be Professional**
- **Be There to Help/Educate the Appeals Officer**
- **Offer to do Computations**

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Real World Example at the Appeals Level

- **Taxpayer with Qualified Appraisal and IRS with No Valuation**
- **Taxpayer with a Qualified Appraisal and IRS with An Opinion of Value**
- **Taxpayer with a Qualified Appraisal and IRS with a Qualified Appraisal**
 - Internal Appraisal by IRS Valuer
 - Outside Fee Appraiser

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Litigation Setting

- **U.S. Tax Court**
 - Special rules
 - 90% choose this option
 - Years for a determination
 - IRS attorneys
- **Pay the tax and file a claim**
 - **U.S. District Court or U.S. Court of Federal Claims**
 - 10% choose these options
 - Timely closure
 - U.S. Department of Justice Attorneys

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Litigation Setting

- **Quick Overview U.S. Tax Court Process**
 - Prepare a Report for the Judge
 - Understand Roles of Attorney and Appraiser
 - Write a New Report Consistent with Rule 702
 - Understand Timing with Litigation
- **Quick Process Check with U.S. Tax Court**
 - Overloaded and Overworked
 - A Very High Percentage Settle but You Never Know
 - Let Go to Bite Harder
 - Issue Resolution Still Works

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Important Take Away Information

- **Build A Good Working Relationship**
- **Know Who Your Working with at the IRS and professionally engage**
- **Understand the Role of Participants**
- **Seek to Understand Interests**
- **Do Not Be Afraid to Ask Questions**
- **Consider Options**
 - **Ask** for a Business Valuator or an **Appraiser**
 - **Ask to Elevate in Management** as a Neutral Party Given Ownership of the Issue by the RA or ETA

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The Collaboration Effect

Overcoming Your Conflicts

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Connecting Relationships

Listening Actively

Educating Judiciously

Leads to Building Bridges and Negotiating Closure

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Helpful Questions for Collaboration

Connecting Relationships

- What have you been thinking about?
- What is your story?
- What was the highlight of your week?
- Tell me about yourself/your business
- What are you working on lately?
- What is your passion?

Listening Actively

- What would you like to have happen?
- What worries/concerns do you have?
- What would it take for you to feel satisfied?
- What have we not covered that you would like me to know?
- What can I do to help you?
- Are there any other concerns or problems?

People versus Problems

- Be tough on the problem and gentle on the people
- Acknowledge your emotions and theirs without blame
- Treat others as they would like to be treated

Positions versus Interests

- Positions polarize – interests integrate
- Behind every entrenched position is at least one interest
- Interests hold the seeds to a solution

Resources for Collaboration

- *Peaceful Resolutions: A 60-Step Illustrated Guide to Conflict Resolution*
- *The Servant Manager: 203 Tips from the Best Places to Work in America*

The Collaboration Effect®

Overcoming Your Conflicts

Michael A. Gregory

651.633.5311
mg@mikegreg.com

The Collaboration Effect

Build bridges to a common purpose by:

Connecting Relationships

- Search social media
- Network with others
- Discover common interests

Listening Actively

- Listen with 100% attention
- Ask open-ended questions
- Check for understanding

Educating Judiciously

- Comment honestly and concretely
- Stand ready in spirit of helpfulness
- Demonstrate expertise humbly

Ten Steps to Interest-Based Solutions

1. **Define** the problem or issue and take on only one problem/issue at a time
2. **Listen** to understand the emotion and facts associated with the issue
3. **Identify** and clarify interests
4. **Generate** options
5. **Determine** the impacts of options
6. **Evaluate** the impacts of the options
7. **Select** a solution
8. **Consider** implementing the solution or return to an earlier step
9. **Consider** testing the solution before implementing the solution
10. **Consider** BATNA and WATNA if no solution can be found

Key Terms for Collaboration

- Issues** – Problems to be solved
- Positions** – Demands/statements of what someone says they will or will not do; one party's solution
- Interests** – Underlying needs, concerns, hopes, fears
- Options** – Possible - often creative - pieces of an agreement. Options are not commitments
- Standards** – Customary, objective, and widely-accepted criteria for handling similar situations
- BATNA** – Best Alternative to a Negotiated Agreement: One way to satisfy your interests if the negotiation fails
- WATNA** – Worst Alternative to a Negotiated Agreement: The worst possible outcome if negotiation fails

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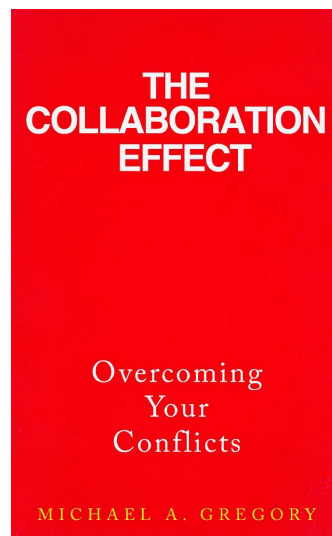
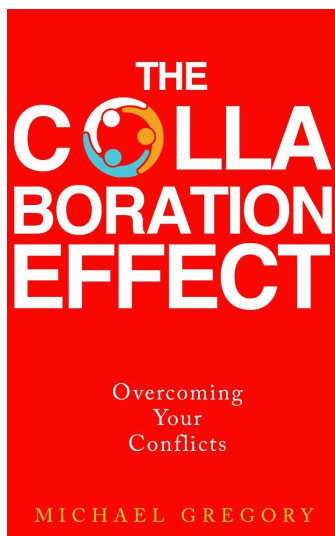
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651.633.5311
mg@mikegreg.com



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As a Result of Today's Presentation You Will Be Able to:



- Address pertinent changes at the IRS
- Make recommendations to clients based on risk
- Identify your client's rights and how to bring them up with the IRS
- Apply DLOMs:
 - For holding companies versus operating businesses
 - Based on the size of entities

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As a Result of Today's Presentation You Will Be Able to:



- Reference key court cases relevant to business valuation
- Apply techniques to address interests and focus on closure
- Distinguish when unfair treatment may require alternative actions
- Develop a plan to move a case forward positively and professionally

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A glowing lightbulb with a human brain inside, symbolizing ideas and innovation.

What Can You Expect with BV at the IRS in 2022 and Beyond?



Presented by Michael Gregory

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My Contact Information



Michael A. Gregory

mg@mikegreg.com

651-633-5311

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