

FOREWORD

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When I was hired by the Internal Revenue Service in 1977, there were no such things as desktop computers, cell phones, faxes, Facebook, Instagram, Twitter, and the myriad of other technological advances that have changed our society in so many different ways during the past 40 years.

Similarly, the estate and gift tax system has made significant changes since the first day I began my employment with the IRS. Indeed, over the years I've seen the pendulum swing back and forth due to budget concerns and changes made by the executive and legislative branches of the government. A major change was in 1976 with the unified estate and gift tax system and addition of GST tax. Subsequently, we have witnessed major changes with the unlimited marital deduction, and estate and gift tax rate changes since 1977 (top tax rate was 77% prior to 1977 and remained high at 70% until 1982 when rates began to decrease). With the changes to the exemption amounts, especially with the 2001 changes and the Economic Growth and Tax Relief Reconciliation Act (EGTRRA), fewer estate tax returns have been filed. And more recently, additional changes affecting property passing to the surviving spouse utilizing the portability election and the higher amounts of property that's sheltered by the estate tax exemption of \$5,340,000 will further reduce the number of estate tax returns filed.

With the enactment of these recent legislative changes, fewer estates are affected by the federal estate tax. The tax benefits offered by special-use valuation and deferral provisions under Code §6166 allow estates to defer a portion of estate tax attributable to a decedent's closely held business to enhance the continuity of a business.

As a result of these changes since 1976, the estate tax impact is no longer a concern for most Americans. The current estate tax affects a smaller fraction of estates and raises a smaller amount of revenue. According to the IRS *Statistics of Income*, the number of estate tax returns filed declined from 73,100 in 2003 to about 9,400 in 2012. However, the returns filed in 2012 and thereafter have more complex and larger valuation issues that require a higher degree of competency when preparing a federal estate tax return. And complicating the post-2012 estate tax return is the interplay of the portability election and the marital deduction.

With fewer returns filed, there are fewer IRS estate tax attorneys and appeals officers specializing in estate tax. Since 2008, troubled economic times have put additional challenges on the IRS with further budget cutbacks yet with decreased estate tax receipts, especially beginning in 2012, a higher percentage of estate tax returns are being scrutinized and audited. What this means for practitioners is the need for a greater degree of care in estate planning and preparing an estate tax return.

An important change is the nationwide centralization of the estate tax program by IRS Compliance and Appeals. Estate tax attorneys and the specialized estate tax appeals officers have established nationwide teams to ensure greater consistency in training, legal positions taken, and audit procedures. This move means that returns filed in one state may be audited from a different state or that an appeal may be handled by an appeals officer located in a different geographical part of the country. Similarly, Exam and Appeals each independently have coordinated programs to focus on issues relating to family limited partnership and limited liability companies. Appeals has established appeals settlement guidelines for family limited partnerships and LLCs.

As a result of these changes, the tax practitioner needs to be adept at preparing the estate tax return, which has become more complex. And if engaged to represent an estate at an audit

or appeal, the practitioner must ensure appropriate steps are taken, including specific timeframes for filing appeals and claims. What are the best recommendations to avoid or minimize an IRS audit? When preparing a return, what documents are required? If an estate tax return is audited, what are the best practices to ensure a successful audit without causing unnecessary delays? How do you deal with a difficult examining estate tax attorney or appeals officer? If you disagree with the examining attorney or appeals officer, what steps should you take? What is the impact of previous court decisions on family limited partnerships or valuation of closely held companies? How will various transactions involving family limited partnerships withstand the IRS scrutiny? What if penalties are proposed by the examining estate tax attorney?

This book is designed to help you better understand and prepare the federal estate tax return and handle IRS audits and appeals. The basic aim of Keith Schiller's book is to provide the practitioner with the necessary tools to competently prepare an estate tax return. This allows the practitioner to think critically about each schedule and the overall presentation of the estate tax return that will enhance the likelihood of success in either avoiding an IRS audit or, if audited, successfully reaching a satisfactory resolution. Every chapter explores the substantive attributes of each schedule of the estate tax return and the issues that may arise. Each chapter is full of recent court decisions highlighting potential issues discussed. I've found Keith's First Edition of *Art of the Estate Tax Return* extremely beneficial to me when researching issues or concepts I've encountered during my years with the IRS Appeals Office. Indeed, I often referred to this book after my initial review of a new estate tax case receipt in Appeals.

The book is not just theory but practical application of the estate tax return. What makes this book a pleasure to read is Keith's infusion of substantive statutory law, case law, facts, examples, humor, tax philosophy, and interjecting and correlating these attributes to his passion for movies. At first blush the reader may be puzzled by how movies and preparation of the estate tax return are related. And indeed any textbook on taxes can be viewed by many, especially the layperson, as a very dry subject to read. Yet with each chapter, it becomes readily apparent how the interrelation of movies and the estate tax return comes to life, making this book so satisfying to read. The countless lessons and lifetime experiences dramatized in movies are a mirror to the richness of human experiences we encounter when handling an estate and related tax issues.

As a former IRS estate tax attorney, appeals officer, and Appeals team manager, I'm reminded of thousands of returns I've reviewed, examined, and considered in Appeals. Each return tells a story. Some of these returns could have been characterized as "fiction" or even "science fiction" when evaluating the credibility of appraisals or theories advanced. The story you want to bring to life and communicate on your estate tax return is a non-fiction story that is respected by the IRS rather than an estate tax return that looks like *It's a Mad, Mad, Mad, Mad World* (the 1963 movie produced by Stanley Kramer). The estate tax return you present is a snapshot of a decedent's assets and debts at the time of death. Your objective is the presentation of a tax return that will inspire the confidence of the IRS examiner. Remember that every estate tax return is reviewed by hand by IRS estate and gift tax personnel.

Keith offers sage advice on how best to handle tough issues, including those of valuation with regard to family limited partnerships, real estate, closely held businesses, promissory notes, and personal property. Keith is at the cutting edge of the most recent legislative developments when discussing administration expenses under Code §2053, the portability election under Code §2056, and the huge benefits practitioners can reap when considering the marital and QTIP deduction as a result of the *Mellinger* decision. You will find this authoritative book useful when considering various estate planning transactions. And most important, this book minimizes your exposure to penalties for negligence, failure to timely file a return, substantial undervaluation, and preparer penalties.

The Practical Benefits of Handling an IRS Audit

Throughout the *Art of the Estate Tax Return*, you will find useful guidance to prepare the return and assistance should your return get audited. Keith goes into detail showing common audit issues and awareness of "audit triggers" that may lead to an audit. Among the red flag issues are failure

to attach all the required documents including appraisals, Will and/or trust documents, failure to answer or omission of all the questions on the return, errors in reporting assets or deductions, taking controversial positions on issues (i.e. claiming high valuation discounts), family limited partnerships, questionable marital or charitable deductions, large claims, prior gift tax returns not reflected, gifts of discounted assets including interests in FLPs, and internal inconsistencies between the reported assets or deductions without any or adequate explanation.

AJAC and the Changing IRS Perception

One of the recent and exciting projects I worked on prior to my retirement from IRS Appeals in 2013 was the formation and implementation of a new policy for handling cases. This project, the Appeals Judicial Approach and Culture (“AJAC”), sets forth various recommendations for implementation to promote a quasi-judicial approach in resolving tax controversies with the goal of enhancing internal and external customer perceptions of a fair, impartial and independent Office of Appeals.

As a result of these recommendations, on July 2, 2014, a Memorandum was issued to all IRS Appeals employees with guidance that applies to non-docketed cases. The effective date of this memorandum is December 2, 2014, except for IRM 8.4.1.15.4 (Assistance to Counsel/Appeals), which has an effective date of October 1, 2014. This guidance is in effect for all new Appeals case receipts on or after September 2, 2014, and will be incorporated into the Internal Revenue Manual within two years from the effective date of the memorandum.

One of the issues addressed by our Project team was dealing with new facts, issues, and legal theories presented at the Appeals hearing. Our recommendation was that Appeals will no longer engage in fact finding or raising new issues and made the recommendation to IRM 8.6.1.6.2 to provide for the following:

Appeals will not raise new issues and will focus dispute resolution efforts on resolving the points of disagreement identified by the parties. The Appeals process is not a continuation or extension of the examination process.

Although Appeals may not raise new issues, the new guidance provides that a discussion of new or additional cases or other authorities that support a previously raised theory or argument does not constitute a new issue.

Related to raising new issues, Appeals will not return cases to Exam when the issues have not been fully developed by Exam unless the following circumstances apply:

- Missing protest letter, or fails to satisfy the requirements of a protest letter;
- Some action must be taken or some event must occur before Appeals can adequately consider the case (i.e. valuation of art work when mandatory referral is required)
- Failure to secure timely consents extending the period of limitation for assessment unless the statute is open for other reasons (e.g., fraud, IRC Section 6501(e));
- The taxpayer provides new information or evidence not previously considered by Exam;
- The taxpayer raises a new issue that Exam has not previously considered.

What impact will these changes have on the practitioner? First, it is important to ensure full cooperation during the audit process. During my years managing the Appeals estate and gift tax program, I sometimes received phone calls from practitioners seeking Appeals approval to accept early referral of a case due after reaching a stalemate with the examining estate tax attorney. Under AJAC, Appeals will not take jurisdiction of a case if Exam has not had opportunity to factually develop it. Implicit here is that Appeals must give full, fair, and impartial consideration to the merits of each new issue a taxpayer raises after Exam has had an opportunity to examine the issues. Likewise, if new information or new evidence is raised by the taxpayer that was not previously shared with the examiner, and in the judgment of the Appeals employee merits additional analysis or investigative action, it will warrant returning the case to Exam for their consideration.

An important and big change here is the acknowledgment by Appeals that it will not take investigative actions or perform analysis of new information or new issues. An issue that may arise is where settlement is reached in Appeals except for finalizing final administration expenses in connection with legal fees and litigation costs (if docketed) associated with an appeal. If new evidence is submitted that is not self-evident and requires additional analysis or involves voluminous information, then it's likely the case will be returned to Exam for fact finding to verify the allowance of the additional claimed administration expenses. A good practice to avoid this issue is to resolve any potential issues relating to legal fees at the exam level to minimize your case being returned to Exam at a later time. If new and substantial evidence is submitted at the Appeals level that claims additional administration expenses, it may require additional analysis or further investigative work by Exam.

One of the more significant changes that will affect estate tax disputes is the longer time period required by Appeals to hear an estate tax case. That is, there must be at least 270 days remaining on the statute when the case is received by Appeals before Appeals will accept the case (previously, Appeals would consider any estate tax case received if there was at least 180 days on the statute [IRM Section 8.7.4.2.]. If an estate tax case is received in Appeals with less than 270 days remaining, the case will be returned to Compliance for issuance of a statutory notice of deficiency. This new policy will place greater pressure on the Compliance estate and gift tax program to factually develop an estate tax case at an earlier stage if it wants to avoid issuing a statutory notice of deficiency rather than closing an unagreed case by issuing a 30-day letter. With this new timeframe for Compliance to send unagreed cases to Appeals, most likely Appeals will see more estate tax cases in docketed status after the taxpayer files a petition with the tax court in response to the statutory notice of deficiency.

As Keith makes clear in this book, the practitioner should be aware of these changes and new procedures to ensure the best strategy is utilized when disputing estate tax issues and pursuing available remedies.

Best Practices When Interacting With the IRS

This past June I had the pleasure of visiting Hannibal, Missouri, Mark Twain's home town. This trip was particularly personal to me since I recently discovered that Mark Twain is one of my distant cousins. One of my favorite quotes of his is relevant here:

"It's better to keep your mouth shut and appear stupid than to open it and remove all doubt."

Another quote by Mark Twain sums up best practices:

"Figures often beguile me, particularly when I have the arranging of them myself; in which case the remark attributed to Disraeli would often apply with justice and force;: 'There are three kinds of lies: lies, damned lies, and statistics.'"

As a tax practitioner, you must know the facts in your case, relevant case law, and applicable law. Sounds simple, but I often found practitioners not prepared to discuss their case or know the relevant facts that could be persuasive to either the examining estate tax attorney or the Appeals Officer. This book brings a refreshing insight in the field of the estate tax return to enable you to prepare the best possible estate tax return; and ensure that you have the tools to defend your position on the estate tax return if the return is audited. I'm reminded of another Mark Twain saying:

"To be the first - that is the idea. To do something, say something, see something, before anybody else - these are the things that confer a pleasure compared with which other pleasures are tame and commonplace, other ecstasies cheap and trivial."

When confronted with an audit of an estate tax return, don't be too quick to throw in the towel if you think you've reached a dead-end. On several occasions, I've encountered representatives who wrongly concluded that they missed the time period to timely file a claim for refund or to seek an over-assessment request. That is, the normal time limits under §§6511 and 6532(a) indicate that the Service has no authority to issue a refund or credit within the two-year period. However, this does

not apply to “requests for abatement” (See IRM 25.6.1.10.1). Similarly, under 6511(h), the statute of limitations for filing a claim for refund or credit of an overpayment may be suspended during the time a taxpayer is unable to handle his or her financial affairs for either of mental or physical impairment that is medically determinable. This book highlights recommended techniques to ensure you’ve covered all of your bases.

An alternative approach to consider is whether to request “audit reconsideration.” An audit reconsideration case is the reevaluation of the results of a prior audit when the taxpayer disagrees with the original determination. The taxpayer should provide the information not previously considered during the original examination. I have found this particularly useful for the practitioner who takes over a case previously worked by another practitioner who dropped the ball.

Recently I received a phone call from a practitioner who lamented that a very large penalty assessed for a late filed return was rejected by the Appeals officer. The practitioner concluded that the client did not want to incur additional legal fees to pursue an action in Federal District Court. However, an alternative to litigation is to request Post Appeals Mediation to resolve the penalty dispute. My experiences as an Appeals Officer, Appeals mediator, and Appeals Team Manager have shown that most of these penalty appeal cases can be resolved utilizing post-appeals mediation if the issues are not resolved through the normal appeals processes. And this is the reason why this book is indispensable to any estate tax dispute: to ensure all available options (including fast track settlement and post-appeals mediation) have been considered and nothing has been left undone in your pursuit to resolve your client’s case. As the practitioner, you can make or break a client’s case by offering, or not, solid arguments, relevant facts, case law, and evidence to support your position.

Some Final Thoughts

With any great movie, there’s also a highly esteemed director responsible for its success. It is no coincidence that movies such as the blockbusters *Avatar* or *Titanic* were products of director James Cameron. Or that Stephen Spielberg, as one of the finest contemporary directors, has had a string of wonderful and successful movies including *Saving Private Ryan*, *Schindler’s List*, *Jaws*, *Close Encounters of the Third Kind*, *ET*, *Jurassic Park*, *Aliens*, and *Terminator I and 2*, among many others. And for me, some earlier directors, namely, Alfred Hitchcock, Stanley Kubrick, Orson Wells, and David Lean directed many of my all-time favorite movies. The attribute that all great directors have in common is their uncanny ability to make sure all parts of a film are creatively produced and brought together in a cohesive form that brings clarity and purpose to the movie.

Similarly, Keith Schiller is the “Director” of the *Art of the Estate Tax Return*. He keeps you engaged as you read this book. He brings all of the chapters together as he prepares several estate tax returns by illustrating principles discussed throughout the book. Keith’s work experience and legal background give credibility to this “director” of tax practice. I have known Keith for more than 15 years. I first met him when he was representing an estate on an appeal before the Los Angeles Appeals office. Subsequently, we have had other encounters in Appeals when he represented estates and taxpayers in gift tax cases. Although I may not have always agreed on every particular theory or conclusion he advanced, I’ve always respected his legal analysis, intellectual prowess, ethics, and integrity.

Just as a highly regarded movie director must know his or her craft, Keith thoroughly understands estate and gift tax law, IRS procedures, and hazards of litigation. He believes in submitting a “fat return.” That is, to provide all of the necessary documents with detailed explanations to support the claimed valuations, deductions, and any unusual situations requiring further detailed explanations.

When a case is contested and litigation initiated by Keith Schiller, he appreciates the importance of the Appeals process to resolve tax controversies, without litigation, on a basis that is fair and impartial to both the government and the taxpayer in a manner that will enhance voluntary compliance and public confidence in the integrity and efficiency of the IRS. Through this process, I have found Keith to be a problem solver and wise enough to know when to escalate a case to Appeals or to litigation in tax court or choosing a different path.

As a college adjunct professor and former IRS Appeals team manager, I've encouraged my students and my former employees to exercise good communication skills and apply practical problem solving techniques to resolve disputed conflicts. In this Second Edition of *Art of the Estate Tax Return*, Keith excels in conveying the necessary steps to prepare a quality return and handle related issues in the event the return is audited. By preparing a quality estate tax return and having the necessary tools to handle an audit, the practitioner better able to resolve disputes for the least possible costs to the client.

This book is also the most detailed and easy to understand presentation of the new portability provisions (Code §2056) and the new 2009 regulations pertaining to deductibility of claims. Keith provides an in-depth discussion of the portability election and important considerations of the portability of deceased spousal unused exclusion amount (DSUEA) and whether it's appropriate to opt out of portability. He also explores the possible impact of election of qualified domestic trusts (QDOT). This is by far the best analysis I've read on this subject of DSUEA and portability election!

Equally important is Keith's insightful, passionate, and reasoned analysis on whether the new regulations under Code §2053 pertaining to contingent claims existing at decedent's death will be respected by the circuit courts and Supreme Court; and the importance of understanding the new administration procedures for filing protective claims if the disputed Schedule K claims remained unpaid.

Unlike other texts on this subject, the uniqueness of this book rests not only on scholarly work, but also on practical hands-on-experiences that are relatable to practitioners. Keith's experiences as a tax litigator, negotiator, author, and panel speaker at numerous educational and bar conferences give him credibility as he channels his knowledge and lifetime experiences in this well-written book. He offers clarity to complex tax issues including generation skipping transfer tax, valuation principles pertaining to closely held businesses, conservation easements (the importance of credible appraisal reports), and valuation discounting. To bring further clarity to complex estate tax issues, he demonstrates by showing examples including completed schedules and estate tax returns, sample letters to qualify installment payment of estate tax under §6166 and extension to pay under §6161, and other forms and schedules including the new Schedule PC (Protected Claim for Refund).

This book is invaluable to the practitioner who wants to get the best results for their clients. For example, Keith demonstrates why being responsive to requests by the IRS and dealing with the agency in a respectful and courteous manner is in your client's best interest. Although in the heat of the battle with the IRS, there may be differences of opinions on valuation or legal issues, being angry, disruptive, or argumentative will not necessarily yield the success you want. Refusing to supply relevant information will most likely result in the examining estate tax attorney taking a more aggressive stance or causing the examiner to be more persistent. As Keith explains in this book, the respectful discussion of issues with the IRS, whether by correspondence, telephone conference call, or in-person conference, will make it more likely that you will reach a favorable agreement or settlement at either the audit or appeals level.

And this is the reason I now recommend this book not only to tax practitioners, but also to IRS employees (including estate tax attorneys, Appeals officers, and IRS Chief Counsel attorneys) who specialize in estate and gift tax matters. Likewise, I am recommending this book to post-graduate college students taking advanced tax accounting courses, law school courses on probate and estate tax practice, and probate paralegal programs. This book is clearly the most authoritative book on preparation of estate tax returns and administration procedures related to IRS audits and appeals of estate tax returns I have read and reviewed.

As you read this book, you too will be taken on a journey that will advance your knowledge and practical application of the estate tax return. That knowledge will be the basis of your success in completing an estate tax return and handling an audit or appeal.