

**Fall 2003**

## **Family Limited Partnerships Face New Tax Challenge**

The generous tax breaks enjoyed by family limited partnerships face serious new threats, as a result of a recent U.S. Tax Court decision.

Estate planners have long depended on these partnerships to help small-business owners transfer assets to their children while maintaining control over key decisions in managing the partnership.

The primary benefit of these arrangements rests in the fact that the value of the shares given to children can be discounted by as much as 40% on the basis that they cannot be easily liquidated. This offers significant tax advantages in that assets can be shifted without paying gift taxes on their full value.

The latest ruling came in the case of *Estate of Strangi v. Commissioner* (T.C. Memo 2003-145, May 20, 2003). The Strangi Family Limited Partnership (SFLP) had received 98% of Albert Strangi's personal assets shortly before his death in 1994.

Only \$6.6 million of the full \$11 million in assets were claimed by the partnership for tax purposes. Control over those assets was maintained by Albert Strangi's attorney (and son-in-law), as opposed to an independent trustee.

The Tax Court ruled that, under Section 2036 of the tax code, the full amount of the assets transferred to the SFLP must be included in the decedent's estate. In its decision, the court said that "the crucial characteristic is that virtually nothing beyond formal title changed in decedent's relationship to his assets."

The Strangi family is considering an appeal. In the meantime, estate planners are advising donors to reduce or relinquish control over family partnerships and operate them under very strict rules to avoid conflicts of interest and reduce the risk of an IRS challenge.