

Estate of Thompson, T.C. Memo 2004-174, July 26, 2004

Note: This case is evidence as to why it is important to utilize an experienced appraiser, not just a CPA with little formal training and experience in valuation.

The Facts: Decedent died in 1998, owing a 20.57% equity interest in Thompson Publishing Co., Inc. (publisher of the Thomas Register). The Estate claimed a fair market value of \$1,750,000, while the IRS claimed the value should be \$35,273,000. The estate's experts were an Alaska attorney and an Alaska CPA, both of whom had little formal training and experience in business valuation. The estate's experts relied solely on the capitalization of income method. They also used a 40% minority interest discount and 45% lack of marketability discount with very little support or credible explanation for the use of either.

The IRS expert used both the guideline public company and discounted cash flow methods in his appraisal. The IRS expert also issued a revised report to make corrections to errors in his original report, and the Court found that significant questionable adjustments were made to his original report in addition to the error corrections. The IRS expert did not apply a minority interest discount because he said he used a minority cash flow and applied a 30% discount for lack of marketability.

The Findings: The Tax Court found both the estate's and IRS' valuations to be "deficient and unpersuasive." The Court specifically cited the lack of experience and training of the Alaska lawyer and accountant and their lack of membership in any professional appraisal organization. The Court also stated that the IRS expert "...did not appear to make an effort to base his valuation of TPC on a real company..." and totally rejected the 11 guideline companies used by the IRS expert as well as his discounted cash flow approach because of significant errors and lack of a minority discount.

The Decision: The Tax Court performed its own valuation calculations, using an 18.5% capitalization rate, a 15% minority interest discount and a 30% lack of marketability discount in arriving at a value of \$13,525,240 for the subject interest.