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Post-Death Events Reduced Estate's Charitable Deduction

by Kristen A. Parillo

The IRS properly reduced an $18 million charitable tax deduction for an estate whose executor diverted assets from the intended charity recipient through a series of post-death transactions, the Ninth Circuit held.

Taking post-death events into account when valuing a charitable deduction is consistent with Ninth Circuit precedent that a deduction cannot exceed the amount actually received by the charity, the three-judge panel concluded in a March 12 decision. The decedent, Victoria Dieringer, and some of her family members owned Dieringer Properties Inc. (DPI), a closely held real property management business in Portland, Oregon, of which Victoria was the majority shareholder. Victoria had established a trust and a foundation for which her son, Eugene, was the sole trustee.

Victoria left her entire estate to the trust. Under the trust agreement, after $600,000 was donated to charitable organizations, the remainder — consisting primarily of DPI stock — was to be distributed to the foundation as a charitable deduction.

After Victoria died, Eugene — serving as the estate executor — and his brothers carried out a plan under which DPI redeemed Victoria's voting stock and a large portion of her nonvoting stock from the trust in exchange for unsecured promissory notes. Eugene and his brothers then bought voting and nonvoting shares in exchange for unsecured notes. At the same time, DPI elected S corporation status to avoid a tax on built-in gains.

> ***The value of the charitable contribution should be determined by taking post-death events into account because Eugene's actions reduced the value of the contribution, the IRS argued.***

Those actions reduced the value of the property that was eventually distributed to the foundation. While the estate claimed a charitable contribution deduction of about $18 million, which it based on the date-of-death value of Victoria's DPI shares, the foundation received assets worth only about $6 million.

The IRS issued a deficiency notice to the estate and imposed an accuracy-related penalty of more than $820,000 for error and negligence in using the date-of-death appraisal as the value of the charitable contribution of Victoria's DPI shares. In Tax Court proceedings, the IRS argued that the value of the charitable contribution should be determined by taking post-death events into account because Eugene's actions — particularly his instructions to an appraiser to apply a minority interest discount to the redemption value of Victoria's DPI shares — reduced the value of the contribution.

The Tax Court agreed with the IRS that the deduction should be reduced (*Estate of Dieringer v. Commissioner*, 146 T.C. 117 (2016)).

Decision Upheld

The Ninth Circuit affirmed the Tax Court's decision, finding that it was appropriate to take post-death events into account when valuing the deduction.

The court relied on the reasoning from an earlier decision, *Ahmanson Foundation v. United States*, 764 F.2d 761 (9th Cir. 1981), that because charitable deductions are valued separately from the valuation of the gross estate, the court can consider post-death events in valuing the deduction. "Importantly, we recognized [in *Ahmanson*] that a charitable deduction 'is subject to the principle that the testator may only be allowed a deduction for estate tax purposes for what is actually received by the charity,'" the court said. That principle prevents testators and estate planners from gaming the system and obtaining a charitable deduction that is larger than the amount actually given to charity, the court said.

Applying the rule from *Ahmanson* compels the Ninth Circuit to uphold the Tax Court's decision, the court said, explaining that Victoria "structured her estate so as not to donate her DPI shares directly to a charity, or even directly to the Foundation, but to the Trust." The court said Victoria laid the groundwork for Eugene to commit "almost unchecked abuse of the Estate by setting him up to be executor of the Estate, trustee

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of the Trust, and trustee of the Foundation, in addition to his roles as president, director, and majority shareholder of DPI."

The Tax Court correctly considered the difference between the deduction and the property actually received by the charity "due to Eugene's manipulation of the redemption appraisal value," the Ninth Circuit said. The court upheld the imposition of penalties after concluding that the estate didn't have reasonable cause or good faith when valuing the deduction.

> ***Victoria laid the groundwork for Eugene to commit 'almost unchecked abuse of the Estate by setting him up to be executor of the Estate, trustee of the Trust, and trustee of the Foundation, in addition to his roles as president, director, and majority shareholder of DPI,' the court said.***

The estate in *Dieringer v. Commissioner*, No. 16-72640 (9th Cir. 2019), was represented by W. Michael Gillette, Sara Kobak, and Marc K. Sellers of Schwabe, Williamson & Wyatt PC.

'Incoherent Result'

Russell A. Willis III, a charitable gift planning consultant, told *Tax Notes* he sees flaws in the Ninth Circuit's opinion.

"Obviously the foundation was shorted — in oral argument, the executor's lawyer acknowledged as much — but the question is what should be the remedy," said Willis, who's written about the case for *Tax Notes*. "On the tax side, the IRS should have been seeking to impose excise taxes for self-dealing. The record strongly suggests that the probate court wasn't sufficiently informed of the situation to enter the order it did, approving the redemption after the fact."

Oregon's attorney general should seek to surcharge the executor in his capacity as foundation manager, but so far it appears that isn't happening, Willis said. "We have heard of bad facts making bad law," Willis said. "This is a case in which poor procedural decisions on the part of the tax authority have led to an incoherent result." By opting not to pursue the excise tax remedy and instead seeking to disallow a portion of the claimed charitable deduction, the IRS placed the Tax Court and the Ninth Circuit in a position of having to depart from long-standing precedent to accomplish a sort of rough justice, he said.

Willis said that to extend the decision in *Ahmanson* to a situation in which the executor abused his discretion, the Ninth Circuit had to place blame on the decedent. The court justified that by stating that Victoria knew of and agreed to early discussions of the share redemption plan, but Willis said that's "a very far cry from saying she had any idea her son would intentionally undervalue the stock in implementing the redemption." ■

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