Valuation of Promissory Notes for Transfer Tax Purposes

Timothy C. Ladd

To estimate the fair market value of a promissory note, the valuation analyst typically considers the professional guidance provided by the Internal Revenue Service, particularly in Revenue Ruling 67-276. Revenue Ruling 67-276 states "the existence of an over-the-counter market for such securities and the quotations and opinions of value provided by brokers and real estate appraisers will not be accepted as conclusive evidence of the fair market value of such securities." This Revenue Ruling also indicates that the analyst who estimates the fair market value of a promissory note should consider (1) all available financial data and (2) all relevant factors affecting the fair market value.[1] *However, this professional guidance may be too general for the individual analyst developing a particular promissory note valuation. First, this discussion summarizes relevant regulations and judicial decisions with regard to transfer-tax-related promissory note valuation. Second, this discussion summarizes the generally accepted promissory note valuation methodologies considered both in relevant judicial decisions and in the professional valuation literature.*

Introduction

Estates often seek to structure promissory notes to secure needed liquidity for the grantor's relatives. When a family member—or a related entity, such as a trust—has poor credit or requires capital and cannot get a loan from a bank or similar institution, intrafamily loans and promissory notes can provide the needed liquidity.

Loans and promissory notes differ slightly. These differences are summarized below.

Loan agreements are evidenced by the signing of a loan agreement. A loan agreement is effectively a contract between a lender and a borrower. The loan agreement stipulates the terms and conditions of the loan—along with the rights and obligations of both the lender and the borrower.

A promissory note is a written promise from the borrower to pay a stated amount of principal and interest until a maturity date.

A promissory note can also be characterized as a negotiable instrument. A promissory note, as opposed to a loan agreement, benefits the lender with some degree of liquidity. A promissory note can be transferred without the consent of the borrower unless the promissory note restricts a transfer.

This discussion focuses on estimating the fair market value of promissory notes. The valuation methodology discussed can also be applied in estimating the fair market value of loan agreements.

This discussion also addresses numerous issues concerning the fair market value valuation of promissory notes for transfer tax purposes.

First, this discussion examines relevant gift and estate tax regulations regarding the fair market value valuation of promissory notes.

Second, this discussion analyzes relevant judicial decisions and summarizes note valuation methodologies considered in the relevant court cases and in the valuation professional literature.

Finally, this discussion recommends financial data and relevant factors that valuation analysts may consider in estimating the fair market value of intrafamily notes within the meaning of Internal Revenue Service Technical Advice Memorandum ("TAM") 8229001.

Bona Fide Loans

The Internal Revenue Service (the "Service") may treat a transfer of property or assets between family members as a gift—even though a promissory note was given in return for the transfer. If it appears to the Service that the loan would likely never be repaid, then the Service may regard the transfer as a gift.

Transfers between family members are treated as gifts unless the transferor can prove the receipt of "an adequate and full consideration in money or money's worth."[2]

However, taxpayers may rebut the Service's position regarding a gift by demonstrating that, at the time of the transfer, the transferor had:

1. a real expectation of repayment and
2. an intention to enforce the loan.

In the *Estate of Lockett v. Commissioner*, when the transferor made a demand for payment, the promissory notes transferred between family members were treated as loans.[3,4]

The U.S. Tax Court considered the following factors to determine:

1. a real expectation of repayment and
2. an intention to enforce the loan.

The following nine factors were originally listed in the Tax Court memorandum decision *Miller v. Commissioner:*[5]

1. Whether there was a promissory note or other evidence of indebtedness
2. Whether interest was charged
3. Whether there was any security or collateral
4. Whether there was a fixed maturity date
5. Whether a demand for repayment was made
6. Whether any actual repayment was made
7. Whether the transferee had the ability to repay
8. Whether any records maintained by the transferor and/or the transferee reflected the transaction as a loan
9. Whether the manner in which the transaction was reported for federal tax purposes is consistent with a loan

Miller v. Commissioner involved a non-interest-bearing unsecured demand note for which a taxpayer made transfers to her son in return.[6]

In the *Miller* decision, the Tax Court concluded that the transfer was a gift and not a bona fide loan, based on the fact that "the mere promise to pay a sum of money in the future accompanied by an implied understanding that such promise will not be enforced is not afforded significance for federal tax purposes, is not deemed to have value, and does not represent adequate and full consideration in money or money's worth."[7]

Relevant Judicial Decisions Related to Note Valuation

Once a promissory note is determined to be a gift or included in an estate, a valuation analyst may need to estimate the fair market value of the note for transfer tax compliance purposes.

Treasury Regulation Section 1.148-5(d) defines the fair market value of an investment as "the price at which a willing buyer would purchase the investment from a willing seller in a bona fide, arm's length transaction."

Regulations Sections 20.2031-(b) and 25.2501-1 define fair market value as "the price at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts."

For gift or estate tax purposes, the fair market value of a promissory note is "the sum of the unpaid amount of principal and accrued interest to the date of gift or death, unless the evidence shows that the note is worth less than the unpaid amount or is uncollectible either in whole or in part."[8]

A taxpayer assumes the burden of proof to submit compelling evidence that the promissory note is worth less than the face value plus accrued interest.[9]

Judicial precedent may provide relevant professional guidance to valuation analysts engaged in developing the fair market value valuation of promissory notes.

There is limited professional guidance provided by the Service concerning appropriate market rates, discounts, or methodologies—except for Revenue Ruling 67-276. Revenue Ruling 67-276 indicates

that market surveys, quotations, and opinions of brokers and real estate appraisers will not be accepted as conclusive evidence of fair market value.[10]

Bernat v. Commissioner

In the Tax Court memorandum decision *Bernat v. Commissioner*, Barbara Given and Julian Bernat were the executors of the estate of Meyer B. Berkman ("Berkman").

Berkman made several transfers to his daughter and son-in-law between 1968 and 1970 in exchange for five promissory notes with a total face amount of $275,000.[11]

Each of the five promissory notes was a 20-year unsecured note, bearing 6 percent annual interest, payable monthly, with no payment of the principal until the maturity of the note. Upon maturity, the full balance of the principal was due.

At the time of his death in 1974, Berkman owned these five promissory notes and had not reported the transfers as taxable gifts.

In defining the term "taxable gift," the Tax Court acknowledged that, with respect to Section 2512(b), "where property is transferred for less than an adequate and full consideration in money or money's worth, then the amount by which the value of the property exceeded the value of the consideration shall be deemed as a gift."

However, the Tax Court also considered that an exception to Section 2512 includes all bona fide transfers at arm's length in which no donative intent presents.

Finally, the Tax Court concluded that the decedent's transfers were not at arm's length within the meaning of Regulations Section 25.2512-8.[12]

The following factors were considered by the Tax Court:

1. Berkman was over 75 years old at the time of the initial transfers in exchange for promissory notes due in 20 years.
2. Berkman took no security on these notes.
3. The promissory notes did not require any principal payments until maturity.
4. In his will, Berkman directed that all his property be divided equally between his daughters.

After careful consideration, the Tax Court concluded that the estate had not provided compelling evidence that the transfers were at arm's length and free of donative intent. Accordingly, the court determined the amount of gift as the difference between:

1. the amount of the loans and
2. the fair market value of the promissory notes under Section 2512(a) and (b).[13]

To calculate the fair market value of the promissory notes, the Tax Court considered the following factors:

1. The rate of interest available in the market (i.e., the U.S. prime rate) compared to the interest rate of the notes
2. The date of maturity
3. The lack of security
4. The solvency of the debtors

Exhibit 1 presents (1) the fair market value of the first four promissory notes and (2) the amounts of the gifts. Issued in 1972 within three years of the date of death, the fifth note was included in the decedent's estate—and excluded from Exhibit 1.

The Tax Court also concluded that the promissory notes were to be included in the decedent's gross estate at fair market value as of the date of his death. This was because the decedent died owning the five promissory notes.[14]

The Tax Court considered the valuation of notes under Regulations Section 20.2031-4 as follows: "[T]he fair market value of notes, secured or unsecured, is presumed to be the amount of unpaid principal, plus interest accrued to the date of death unless the executor establishes that the value is lower or that the notes are worthless."

Exhibit 2 presents the fair market value of the five promissory notes on the date of the decedent's death, including accrued interest.

Certain of the transfer of $55,000 to the daughter and son-in-law within three years of the decedent's death, the court concluded that this amount was to be included in the decedent's gross estate under Section 2035.[15]

However, the transfer was applied to an exception of Section 2035, where a bona fide transaction for adequate and full consideration exists.[16]

From the promissory note, the decedent received 6.00 percent interest at a time when the U.S. prime rate was only 4.75 percent. Considering the higher interest rate of the note than the market provided, the court concluded that the loan resulted in a bona fide transfer for adequate and full consideration, and the transfer was not includable in the decedent's gross estate.

Smith v. United States

The matter of *Smith v. United States* involved the valuation of a promissory note with an original principal balance of $10.3 million, which was payable over a period of 20 years.

The annual principal payments were $515,600 along with 6 percent simple interest computed beginning at inception to the date of payment.[17]

The accrued interest resulted in progressively larger payments due to the passage of time. There was a dispute regarding the promissory notes valued by the decedent on the date of death. The dispute was litigated in *Smith v. United States.*[18] Evelyn Smith was the executrix of the estate of Verna Mae Taylor Crosby.

St. Regis Paper Company ("St. Regis") issued the original promissory note on May 17, 1977, and the payments due under terms of the promissory note were paid to L.O. Crosby Jr. until his death in 1978. The decedent's will bequeathed a two-thirds interest in the promissory note to Mr. Crosby's wife, Verna Mae Crosby.

On May 17, 1981, two separate promissory notes were executed by St. Regis to the decedent's wife along with Ochsner Medical Foundation ("OMF"), which was the one-third beneficiary, in exchange for their respective interests in the original promissory note of $10.3 million.

One of the promissory notes had a face amount of approximately $5.5 million, with yearly principal payments of approximately $343,733 payable to the decedent's wife. The yearly payments were scheduled to begin on May 17, 1982, and were scheduled to continue on the same day each year before concluding in 1997.

The remaining one-third interest (approximately $2.7 million) was given to OMF.

On January 31, 1985, St. Regis merged into Champion International Corporation ("Champion"). Champion was expected to pay the unpaid note balance of approximately $5.5 million to the decedent's wife.

Verna Mae Crosby passed away on April 28, 1988. At the time of Ms. Crosby's death, (1) the unpaid principal due under the note totaled $3.4 million and (2) the interest required to be paid over the remaining term of the note totaled $4.1 million.

In estimating the value of her promissory note, the taxpayer's valuation analyst applied a 10.09 percent effective interest rate of a publicly traded bond that Champion issued as a starting point.

The valuation analyst then added a series of adjustments to the starting point in order to compensate for the differences between the publicly traded debt of the issuer and the promissory note of the estate.

Exhibit 3 presents a series of adjustments that the valuation expert applied in the estimation of the value of the promissory note.

The adjustments were made based on the following characteristics of the Champion publicly traded debt instruments:

1. Well documented (i.e., prospectus supplement, financial statements, and legal opinions)
2. Tradeable in denominations as low as $1,000
3. Having significant legal protections in the event of default
4. Having restrictions on the business operations of Champion to provide further security

Exhibit 1
The Estate of Meyer B. Berkman
Fair Market Value and Amount of Gift of the Promissory Notes

Promissory Note Issue Date	Note Face Amount	Fair Market Value	Amount of the Gift
November 15, 1968	$100,000	$ 85,000	$ 15,000
April 24, 1969	$ 50,000	$ 37,500	$ 12,500
November 19, 1970	$ 30,000	$ 24,000	$ 6,000
November 19, 1970	$ 40,000	$ 32,000	$ 8,000

Source: Bernat v. Commissioner, T.C. Memo. 1979-46.

Exhibit 2
The Estate of Meyer B. Berkman
Fair Market Value of the Promissory Notes for Estate Taxes

Promissory Note Issue Date	Note Face Amount	Fair Market Value
November 15, 1968	$100,000	$ 50,080
April 24, 1969	$ 50,000	$ 24,040
November 19, 1970	$ 30,000	$ 13,524
November 19, 1970	$ 40,000	$ 18,032
March 2, 1972	$ 55,000	$ 22,044

Source: Bernat v. Commissioner, T.C. Memo. 1979-46.

Exhibit 3
Smith v. United States
Adjustments to Required Yields

Base Yield	10.09%
Adjustments:	
Lack of Marketability	0.5%
Lack of Indenture or Covenant	1.0%
Lack of Formal Acknowledgement by the Borrower	1.0%
Subordination to All Better Documented Debt of the Borrower	1.0%
Uncertainty regarding the Legal Entity Bearing Liability	1.0%
Unusual Payment Schedule	0.5%
Lack of Divisibility	0.5%
Semiannual Payout Rate	15.6%
Convert to Annual Convention (note payments on annual basis)	16.2%
Required Yield Used	16.0%

Source: Smith v. United States, 923 F.Supp. 896 (S.D. Miss. 1996).

The taxpayer's valuation analyst testified in the U.S. District Court trial that the absence of these factors were important in determining potential buyers for the estate's promissory note.

The valuation analyst made an adjustment based on a lack of response from the issuer, Champion. When the taxpayer's valuation analyst tried to obtain adequate information for the valuation from Champion, he only received a one-page letter with incorrect information about the promissory note.

The valuation analyst surmised that a hypothetical purchaser would have similar issues securing information about the promissory note.

Finally, the U.S. District Court for the Southern District of Mississippi found the taxpayer expert's valuation of the promissory note to be reasonable.

The District Court concluded that the taxpayer analyst's valuation was consistent with the facts known and knowable at the time that the interest in the promissory note was determined and would have been available to a good faith purchaser at that time.

Estate of Hoffman v. Commissioner

The U.S. Tax Court decision in the *Estate of Hoffman v. Commissioner* concerned the valuation of two unsecured promissory notes issued from a family partnership held by Marcia P. Hoffman (the decedent) with a 20-year term.[19]

At the date of death, the decedent owned a 27.5 percent ownership interest in Clubside, a family partnership owned by the decedent and her family.

The Service and the estate disagreed on the fair market value of the promissory notes issued by Clubside.

One promissory note was payable to the decedent and the other note was payable to Hoffman Associates, Inc. At the time of Marcia Hoffman's death, the decedent owned all 7,500 shares of stock in Hoffman Associates.

The estate's valuation analyst estimated the fair market value of the Clubside promissory notes based on a required rate of return on similar market investments. The estate's valuation analyst relied on Moody's, Standard & Poor's, and Fitch ratings agencies to find comparable debt securities.

The estate's valuation analyst considered the lack of marketability discount because the Clubside notes lacked a public market for sale. Taking into account this lack of marketability, the estate's valuation analyst concluded an investor would require a rate of return of at least 25 percent higher than the 18 percent return offered by his comparable publicly traded bonds.

Therefore, the estate's valuation analyst determined the appropriate rate of return for the Clubside notes was 22.5 percent.

The Service's valuation analyst contended that the value of the promissory note was based on the payments and the rate of return that a holder of the notes would require.

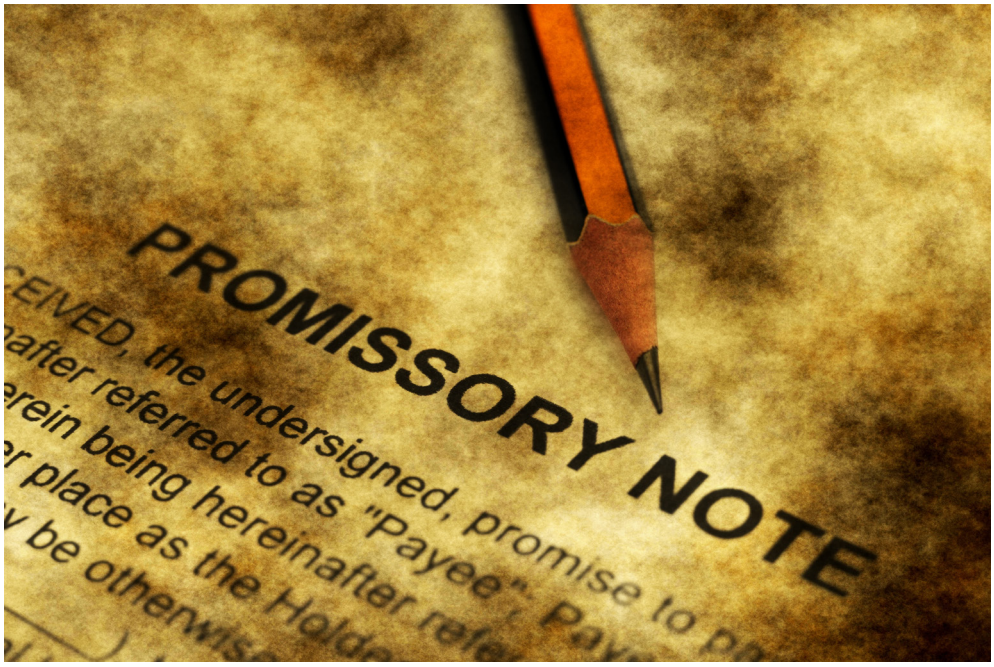
To determine an appropriate rate of return, the Service's valuation analyst considered the following factors:

1. Interest rates of various debt securities
2. Corporate bonds of various ratings
3. Interest rates for 30-year conventional mortgages
4. Yields on U.S. Treasury securities
5. U.S. prime rate
6. Venture capital returns

The Service's valuation analyst concluded that the promissory notes did not have characteristics similar to highly speculative and default bonds. The Service's valuation analyst concluded 12.5 percent as the appropriate rate of return required for the promissory note inclusive of the lack of marketability of the promissory note.

The Tax Court ultimately concluded that:

1. a 12.5 percent rate was appropriate and
2. the Service's valuation analyst had correctly valued the promissory notes.



Promissory Note Valuation Methodology

In the above three judicial decisions, the courts considered the fair market value of a promissory note under Sections 20.2031-4 and 25.2512-8 of the Internal Revenue Code. The valuation analysts offered evidence to prove that the fair market value of a promissory note was lower than the sum of unpaid principal and accrued interest.

In *Bernat v. Commissioner,* the Tax Court determined the fair market value of the promissory notes, considering the following factors:

1. Interest rates available in the market as compared to the interest rate of the notes
2. The date of maturity
3. The lack of security
4. The solvency of the debtors

In *Estate of Hoffman v. Commissioner*, the Service's valuation analyst determined the fair market value of the notes based on a required rate of return and the timing of payments.

In estimating the value of promissory notes, both cases applied a required rate of return that a note holder would demand of an issuer, considering rates of return on similar investments available in the market as of the valuation date.

The required rate of return applicable to the notes is determined based on the risk inherent in the investment. In other words, an investor (or lender) would accept a rate of return no lower than that available from other investments with equivalent risk.[20]

When the rate of return on the note appropriately reflects the risk of the borrower, the fair market value of the note equals its principal amount (or its "face value").[21]

The value of a financial instrument generating future payments at a specific time is determined by its present value at the transaction date. To the lender, the fair market value of a promissory note equals the present value of future principal and interest payments discounted at a risk-adjusted rate of return to the valuation date.[22]

When the risk associated with the future payments of the note increases, the rate of return the lender requires will increases. And, accordingly, the present value of the note will decrease. The opposite result occurs when the risk and the required rate decrease.[23]

Accordingly, the required rate of return of a note reflects the risk associated with the future payments and determines the fair market value of the note.

For example, if a note secures collaterals, the required rate of return will be lower than that of an unsecured note.

In *Estate of Hoffman v. Commissioner*, to determine an appropriate required rate of return, the Service's valuation analyst considered rates of return available in the market, such as interest rates of debt securities, corporate bonds ratings, interest rates for conventional mortgages, U.S. Treasury

"[T]he proper way to value notes and mortgages is to consider all available financial data and all relevant factors affecting the fair market value."

securities yields, the U.S. prime rate, and venture capital returns.

Once an appropriate required rate of return is determined based on inherent risk in the note, a valuation analyst should carefully consider how to estimate the fair market value of the note discounted at such required rate of return to the valuation date.

One example is a promissory note required to pay periodic interest payments with the principal balance due at maturity (similar to an ordinary annuity).

The present (i.e., fair market) value of the periodic coupon payments and maturity value (or par value) is calculated using the Figure 1 formula according to the *Handbook of Fixed Income Securities.*[24]

Internal Revenue Service Technical Advice Memorandum 8229001

In *Smith v. United States,* in the calculation of an appropriate required yield, the taxpayer's valuation analyst applied adjustments to the publicly traded debt of the promissory note issuer, thereby increasing the required yield from approximately 10.1 percent to 16.0 percent. The increase in the required yield accounted for the specific risk of the promissory note compared to that of publicly traded debt in the market.

In addition, in *Bernat v. Commissioner*, the Tax Court considered the rate of interest available in the market (effectively the U.S. prime rate at the time), as well as the following factors:

1. The maturity date
2. The lack of security
3. The solvency of the debtors

The rationale for these adjustments is within the scope of TAM 8229001.[25]

TAM 8229001 defines the meaning of Revenue Ruling 67-276 in determining the value of a mortgage owned by a decedent at the day of death.[26]

According to TAM 8229001, although a sentence of the Revenue Ruling indicates a secured mortgage must be valued at face value,[27] the meaning of the Revenue Ruling is that "the proper way to value notes and mortgages is to consider all available financial data and all relevant factors affecting the fair market value."[28]

To describe what kind of financial data and relevant factors an analyst should consider in estimating the fair market value of a promissory note, the following list of factors provides a summary of TAM 8229001. These factors are also illustrated in the previously mentioned judicial decisions.

Figure 1
Illustrative Promissory Note Valuation Formula

$$PV = \frac{c}{(1+i)^1} + \frac{c}{(1+i)^2} + \frac{c}{(1+i)^3} + \ldots \frac{c}{(1+i)^n} + \frac{M}{(1+i)^n}$$

$$PV = c \left[\frac{1 - \left[\frac{1}{(1+i)^n} \right]}{i} \right] + \frac{M}{(1+i)^n}$$

Where:
PV = Present Value of a Promissory Note
c = Periodic Interest Payment ($)
n = Number of Periods
i = Required Yield
M = Maturity Value (or face value)

Presence or Lack of Promissory Note Covenants

Covenants are set forth within an indenture, or a formal debt agreement. Covenants confirm whether certain activities will (affirmative covenants) or will not (negative covenants) be carried out.

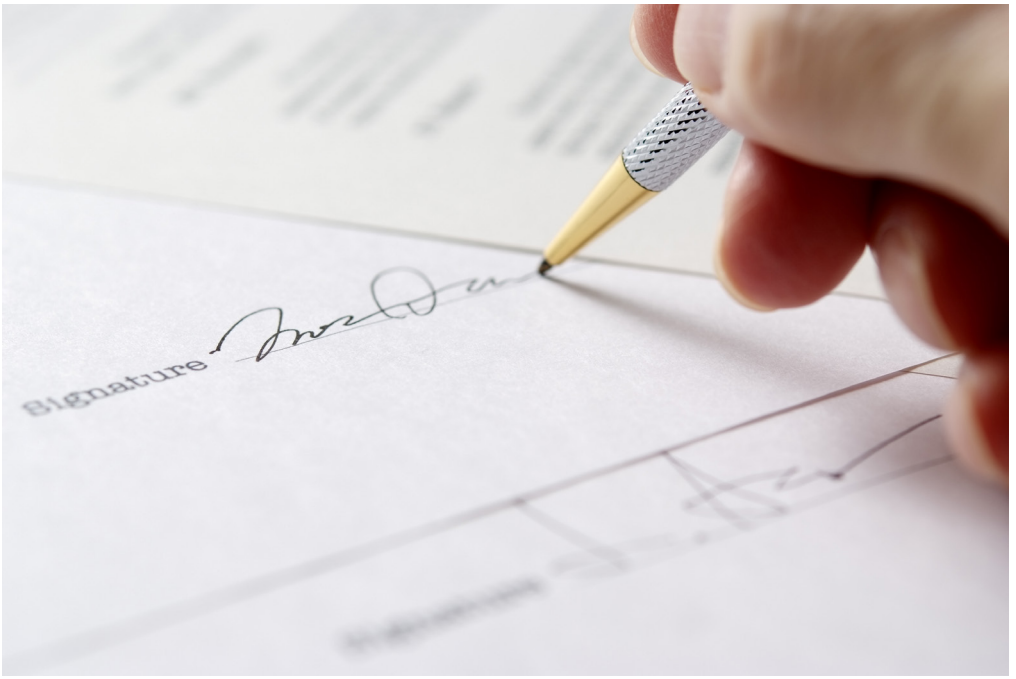
Covenants include, but are not limited to, working capital requirements, interest coverage ratios, prepayment penalties, debt/equity ratios, and dividend payments. Such covenants are intended to protect the interests of the lender.

Therefore, covenants tend to reduce lender risk and often result in a lower required yield.

The Solvency of the Borrower

With regard to the *Bernat v. Commissioner* decision, the Tax Court considered the borrowers' solvency as one of relevant factors in estimating the fair market value of the promissory notes.

Strong debt solvency and repayment ability of the borrower will result in lower risk for the lender and a lower required rate of return.



Value of the Security

Both Revenue Ruling 67-276 and TAM 8229001 indicate the value of the security as an important factor in estimating the value of the promissory note. "Security" here specifies collateral or the pledged security of the borrower. The higher the security value, the lower the risk of the lender, and the lower the required rate of return.

Term of the Note

All debt holders confront interest rate risk, which is the risk that a note's investment value would change given a fluctuation in interest rates. Such investors also confront reinvestment risk if they are unable to reinvest proceeds from the existing note at the same interest rate as the current rate of return.

The longer the duration of the note, the higher the interest rate risk and reinvestment risk, and the higher the required rate of return.

Comparable Market Yield

In *Estate of Hoffman v. Commissioner*, in his determination of an appropriate required rate of return, the Service's valuation analyst considered market yields such as interest rates of debt securities, corporate bond rates, mortgage rates, U.S. Treasury securities rates, the U.S. prime rate, and venture capital returns.

A comprehensive valuation analysis typically considers a wide range of financial instruments with different risk and return characteristics.

Payment History of the Borrower

Payment history of the borrower is important to measure the risk of the borrower. If payments are current and have been made in a timely manner, the risk associated with the promissory note decreases and, therefore, the required rate of return decreases.

Size of the Note

To calculate the required yield to discount the promissory note, the plaintiff's valuation analyst in the *Smith v. United States* decision compared the promissory note to the publicly traded debt of the issuer (or lender).

One of the differences between the promissory note and the publicly traded debt is that the publicly traded debt was tradeable in denominations as low as $1,000.

Potential buyers of the note will be limited because buying the note requires sizable money to invest. Accordingly, the larger the size of the note, the higher the required rate of return.[29]

In addition, TAM 8229001 states that the effect of Section 20.2031-4 is to recognize "(1) that any principal amount payable in the future normally carries an interest accrual with it and (2) that when the stated interest rate on the obligation is fair (equal to the current market rate of interest for such type of obligation), the total present value of all payments of principal and interest will equal the principal amount of the obligation."

The TAM also indicates that the present value of such payments is less if the stated rate of interest on the note is less than the current market rate of interest.

In summary, under TAM 8229001, the Service indicated that "all available data and all relevant factors affecting the fair market value must be considered,"[30] in determining the value of a promissory note.

Face value plus accrued interest[31] is not necessarily the value to be included in the gross estate or taxable gift. A promissory note can be valued at less than face value plus accrued interest if the donor or estate demonstrates by satisfactory evidence that the value is lower.[32]

Summary and Conclusion

Valuation analysts are often engaged to estimate the fair market value of a promissory note for transfer tax compliance purposes.

The fair market value of a promissory note is the sum of the unpaid principal and accrued interest to the date of gift or death under Regulations Sections 25.2512-4 and 20.2031-4.

However, these regulations also indicate that the taxpayer may rebuke this value by presenting compelling evidence that the promissory note is worth less than the sum of the unpaid principal and accrued interest.

This discussion presented note valuation methodologies and various factors that the analyst may consider in estimating the fair market value of a promissory note. It also summarized several relevant judicial decisions and valuation professional literature.

This discussion especially clarifies the meaning of TAM 8229001 and its application in estimating the fair market value of promissory notes.

In conclusion, in estimating the fair market value of a promissory note, the analyst may carefully consider the following factors:

1. Whether the note represents a bona fide transaction for adequate and full consideration
2. Whether the required yield reflects the inherent risk of the note and its issuer (borrower), considering various factors that this discussion suggests

Accordingly, the valuation analyst may estimate the fair market value of the promissory note future cash flow by discounting the note based on an appropriate required yield rate.

Notes:

1. Internal Revenue Service Technical Advice Memorandum 8229001 (February 1, 1982)
2. Treasury Regulations §25.2512-8; 25.2511-1(g)(1).
3. Estate of Lockett v. Commissioner, T.C. Memo 2012-123 (Apr. 25, 2012) at 21 (citing Van Anda v. Commissioner, 12 T.C. 1158, 1162 (1949)).
4. Estate of Lockett v. Commissioner at 22-23, 25-27.
5. Miller v. Commissioner, T.C. Memo. 1996-3 (Jan. 11, 1996).
6. Ibid.
7. Ibid.
8. Treasury Regulations § 25.2512-4, §20.2031-4.
9. Estate of Hoffman v. Commissioner, T.C. Memo. 2001-109 (May 9, 2001).
10. Revenue Ruling 67-276, 1967-2 C.B. 321.
11. Bernat v. Commissioner, T.C. Memo. 1979-46 (Jan. 31, 1979).
12. Treasury Regulation. § 25.2512-8.
13. Internal Revenue Code § 2512 (a), (b).
14. Internal Revenue Code § 2031.
15. Internal Revenue Code § 2035.
16. Internal Revenue Code § 2035(d).
17. Smith v. United States, 923 F.Supp. 896 (S.D. Miss. 1996).
18. Id.
19. Estate of Hoffman v. Commissioner, T.C. Memo. 2001-109.
20. Aaron M. Stumpf and Jesse A. Ultz, "Intra-Family Loan Valuation Issues," Stout Risius Ross newsletter (Spring 2010).
21. Robert Schweihs, "AFR and the Value of Debt," Willamette Management Associates *Insights* (Summer 2012).
22. Ibid.
23. Frank J. Fabozzi and T. Dessa Fabozzi, *Handbook of Fixed Income Securities*, 4th ed. (Chicago: Richard D. Irwin, 1995), 55.
24. Ibid.
25. Internal Revenue Service Technical Advice Memorandum 8229001.
26. Revenue Ruling 67-276, 1967-2 C.B. 321
27. Ibid.
28. Ibid.
29. Treasury Regulation §20.2031-4.
30. Ibid.
31. Ibid., Treasury Regulation § 25.2512-4, §20.2031-4.
32. Internal Revenue Service Technical Advice Memorandum 8229001.

Tim Ladd is a manager in our Chicago practice office. Tim can be reached at (773) 399-4301 or at tcladd@willamette.com.