

Minority Share Gifts: Court Finds 30% Discount for Lack of Marketability

Mandelbaum v. Commissioner

T.C. Memo 1995-255, 69 T.C.M. (CCH) 2852 (June 12, 1995), *Judge Laro, affirmed*, 91 F.3d 124 (3d Cir. June 10, 1996), *Judge Cowen*.

The parties stipulated to freely traded minority interest values, so the only issue was the lack of marketability. Paul R. Mallarkey, ASA, then of BDO Seidman, now with Houlihan Lokey Howard & Zukin, testified for the IRS. He cited three restricted stock studies and concluded a 30% discount for lack of marketability.

Roger J. Grabowski, ASA, of Price Waterhouse testified for the taxpayer. He cited seven restricted stock studies and three of the pre-IPO studies by Baird & Co. and Willamette Management Associates, as well as a number of company-specific factors (e.g., restrictions on sale). He concluded a 70% discount for lack of marketability on some dates and 75% on others. The opinion does not indicate that either expert cited empirical evidence about factors associated with individual discounts being higher or lower than the studies' averages.

Judge Laro used the studies cited by Grabowski as a starting point (35% average discount for restricted stock studies and 45% average discount for pre-IPO studies). He listed nine factors that might cause the marketability discount for a given instance to be higher or lower than the benchmark averages, concluding that, on balance, the facts and circumstances in the particular case led to a lower discount for lack of marketability than the benchmark averages. The factors cited were: financial statement analysis, dividend policy, nature of the company, management, amount of control in the transferred shares, restrictions on transferability, holding period for the stock, company's redemption policy, and costs associated with public offering. He concluded a 30% discount for lack of marketability.

The Third Circuit affirmed without opinion.