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Subject: FW: The FMV Valuation Alert - Sumner Redstone v. Commissioner
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From: Lance S. Hall, ASA [REDACTED]
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Subject: The FMV Valuation Alert - Sumner Redstone v. Commissioner

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A Tale of Two Brothers: (A Deceased Brother's Revenge)

(*Sumner Redstone v. Commissioner* ^[1])

By Lance S. Hall, ASA*

A few weeks ago, the Tax Court released its decision in the case of *Edward Redstone v. Commissioner* ^[2]. While the Tax Court agreed with Edward, it disagreed in a later decision involving Edward's brother, Sumner - arguments about similar facts, but with a haunting twist of beyond the grave revenge.

Background³

In the mid 1960s, Edward owned a one-third interest in National Amusement, Inc. ("NAI") along with his brother, Sumner, and his dad, Mickey. Later, Mickey exchanged his interest for preferred stock and gave a 20% voting interest to the Grandchildren's Trust. This left Edward and Sumner with a 40% voting interest. ^[4] Edward was given the responsibility of running the back office operations and property development, while Sumner had the more glamorous responsibility of dealing with the movie studios for NAI's theater operations. As often happens, Edward felt marginalized by his more well-known, and capable, brother. When Sumner "hired Jerry Swedrow to take over Edward's responsibilities" in the family business, Edward became "incensed" and quit NAI. Upon leaving, Edward demanded that he be bought out, or he would sell his shares to an unrelated party.

Mickey, desiring to keep the family business within the family, thwarted any possible sale to an outsider by refusing to give Edward his stock certificates. As the reason for not providing Edward with his stock certificates, Mickey argued that there was an oral

agreement that some of the stock was for the benefit of Edward's children, and not for Edward. To bolster this argument, Mickey pointed out that he had contributed 48 percent of NAI's capital and had only received 33 percent of its stock. The differential, according to Mickey, was what he contributed to Edward's and Sumner's children by oral agreement (the "oral trust").

While contentious negotiations proceeded, Mickey refused to allow the shares to be sold to an outsider. He also refused to repurchase Edward's shares, without Edward's explicit acknowledgement of the "oral trust." Soon, full-blown litigation ensued. This greatly embarrassed the family, especially Edward's mother, Belle, who urged Edward to settle. The litigation finally settled, with Edward able to sell two-thirds of his stock to NAI and agreeing that his other third "had always been held by Edward, 'for the benefit of his children ... in trust and not as beneficial owner.'" NAI purchased two-thirds of Edward's interest for \$5 million. In addition, Edward executed an "irrevocable declaration of trust ... for the benefit of his children" and all parties signed the customary releases. The agreement was filed with the Massachusetts Superior Court and the Court "issued a Final Decree incorporating the terms of the Settlement Agreement."

Three weeks after the Final Decree was issued, Sumner, in support of his father's wishes, "executed irrevocable declarations of trust for the benefit of his two children" and transferred a similar amount of shares to this trust in a manner similar to what Edward had done under the Final Decree. Sumner, like Edward, never filed a gift tax return.

O'Connor Litigation

At Edward's death, the IRS received his 706 filing and Googled his name. The result of the Google was the discovery of the O'Connor litigation.^[5]

In 2006, almost four decades after the Final Decree settlement, further litigation arose in which various family trusts argued that more shares should have been transferred to the children's trusts as a result of the oral agreement. In other words, the math didn't work. The differential between the 48 percent of assets contributed by Mickey and the one-third of the stock he received was supposed to go the grandchildren under the "oral trust" argument espoused by Mickey. If there was an "oral trust," more shares should have gone to the grandchildren than what was provided for in the Final Decree. In the O'Connor trial, Sumner was adamant that this may be true for Edward, but his gifts were voluntary and not part of the oral agreement. Sumner testified,

I voluntarily set up an arrangement - call it what you will - where my own children would get a third of the stock. ... I wanted to do the same thing that my brother did, only he did it as a result of litigation. I did it voluntarily.

The Tax Court's Decision

In Edward's trial, the Court declared,

All the elements of arm's-length bargaining existed here. There was a genuine controversy among Edward, Mickey, and Sumner; they were represented by and acted upon the advice of counsel; they engaged in adversarial negotiations for a protracted period; the compromise they reached was motivated by their desire to avoid the uncertainty and embarrassment of public litigation; and their settlement was incorporated in a judicial decree that terminated the lawsuits.

As a result, the Court concluded that there was no gift made by Edward.

However, at Sumner's trial, the Tax Court stated,

There is no evidence that any dispute existed in 1971-1972 concerning ownership of Sumner's stock or that Mickey was determined to withhold any of Sumner's shares from him. To the contrary: the evidence showed that Mickey and Sumner were working in concert to drive Edward out of the company and that the "oral trust" theory was a weapon they deployed against Edward in an effort to achieve that goal. Because no demand was ever placed on Sumner's shares, no negotiations ever occurred concerning his ownership of those shares. Sumner never filed a lawsuit, and he received no release of claims from Mickey upon transferring his stock. ... [Moreover, the Final Decree] had been finally executed three weeks *before* Sumner made his transfer. ... By its terms, the [Final Decree] imposed no obligations on Sumner except that he execute releases in exchange for reciprocal releases from each of the other parties. [emphasis added]

Once the Court determined that a gift had been made, the issue of valuation was easily settled as the Court relied on the price of the shares determined in the Final Decree.

In regards to any penalties for not declaring a gift, participants from the firm that provided accounting services for Sumner and NAI some 40 plus years ago, testified about uncertain memories and vague discussions with now deceased partners. A key memory, however, was the fact that one of the accountants recalled that a now deceased senior partner had told Sumner that there was no need to file a gift tax return because of the Final Decree. Since Sumner was relying on the advice of competent professionals, no penalties were added.

Somewhere, Edward is smiling.

[1](#) T.C. Memo. 2015-237 (December 9, 2015)

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[2](#) 145 T.C. No. 11 (October 26, 2015)

[3](#) This section comes from my prior article regarding the *Edward Redstone v. Commissioner* case

[4](#) Today, NAI is the owner of many companies, including Viacom, and is run by Edward's brother, Sumner

[5](#) *O'Connor V. Redstone* - 896 N.E.2d 595 (Mass. 2008)

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