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NOTES

INCOME TAX—CAPITAL GAINS TAX—Meaning of "More Than 80 Percent in Value of the Outstanding Stock" Under Section 1239

The sale of property by a taxpayer to a corporation which he controls has been a frequently attempted method of tax reduction for more than thirty years.[1] Such a transaction has the advantage of maintaining ownership of the property in virtually the same hands, while at the same time resulting in a substantial mitigation of tax liability. For instance, in the post-World War II period, when property values were generally increasing, a taxpayer could sell to his controlled corporation at a gain depreciable property with a basis lowered by adjustments for prior depreciation allowances.[2] The gain was immediately taxable at the capital gains rate,[3] but the sale price established a new basis for depreciation for the controlled corporation, which, in subsequent years, permitted substantial annual depreciation deductions from income taxable at ordinary income rates.[4] The resulting savings in income taxes often outweighed the initial payment of the capital gains tax on the sale.[5] To preclude this method of tax avoidance,[6] section 1239 of the Internal Revenue

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1. H.R. REP. No. 704, 73d Cong., 1st Sess. 23 (1934); 78 CONG. REC. 2511 (remarks of Representative Dougton), 5847-48 (remarks of Senator Harrison) (1934).

2. INT. REV. CODE OF 1954, §§ 167, 1016.

3. INT. REV. CODE OF 1954, § 1231(a). The kind of property to which this section is applicable is partly set out in subsection (b), and includes the depreciable property to which section 1239 is applicable.

4. INT. REV. CODE OF 1954, § 167(a).

5. H.R. REP. No. 586, 82d Cong., 1st Sess. 26 (1951):

> Thus, in effect, the immediate payment of a capital gains tax has been substituted for the elimination, over a period of years, of the corporate income taxes on an equivalent amount. The substantial differential between the capital-gains rate and the ordinary rates makes such a substitution highly advantageous when the sale may be carried out without loss of control over the asset . . . .
>
> The opportunity for tax mitigation may be shown by a hypothetical example: The transferor holds property the basis of which has been reduced by depreciation deductions to $2,000. He sells the property for $6,000 to his controlled corporation, paying the maximum capital gains tax of 25% on the $4,000 gain ($1,000). After a few years the basis of the property is again reduced by the corporation's depreciation deductions to $2,000, during which time the corporation has been allowed to deduct $4,000 from ordinary income. If the corporation is in the 50% bracket, the $4,000 in depreciation deductions has saved the corporation $2,000 in income taxes. Thus, the transferor paid $1,000 in capital gains tax but saved $2,000 in income taxes, a net saving of approximately $1,000. *See* United States v. Parker, 376 F.2d 402, 407 n.5 (1967).

6. S. REP. No. 781, 82d Cong., 1st Sess. 69-70 (1951); H.R. REP. No. 586, 82d Cong., 1st Sess. 26 (1951); 97 CONG. REC. 6918 (remarks of Representative Mills), 11739-40 (remarks of Senator Humphrey) (1951).

Code of 1954[7]—first enacted as section 328 of the Revenue Act of 1951[8]—provides for taxation of the initial gain at ordinary income rates, rather than the lower capital gains rates, when the transferor owns "more than 80 percent in value" of the transferee corporation's outstanding stock. Thus, the problem becomes one of determining whether a taxpayer owns "more than 80 percent in value of the outstanding stock" of the transferee, that measure being the congressional definition of a controlled corporation for purposes of section 1239.[9]

The United States Court of Appeals for the Fifth Circuit was squarely confronted with this problem in *United States v. Parker.*[10] The lower court had found,[11] and the Fifth Circuit agreed, that Parker owned exactly 80 percent, by numerical count, of the outstanding shares of a corporation to which he had made a sale of depreciable property, the remaining 20 percent being owned by one other stockholder. However, the Fifth Circuit also agreed with the Tenth Circuit's recent statement in *Harry Trotz v. Commissioner*[12] that section 1239 does not contemplate a simple numerical count test; both courts felt that such a test would read the words "in value" out of the statute.[13] The Fifth Circuit then enunciated a "block

7. INT. REV. CODE OF 1954, § 1239:
GAIN FROM SALE OF CERTAIN PROPERTY BETWEEN SPOUSES OR BETWEEN AN INDIVIDUAL AND A CONTROLLED CORPORATION.
(a) Treatment of Gain as Ordinary Income.—In the case of a sale or exchange, directly or indirectly, of property described in subsection (b)—
(1) between a husband and wife; or
(2) between an individual and a corporation more than 80 percent in value of the outstanding stock of which is owned by such individual, his spouse, and his minor children and minor grandchildren;
any gain recognized to the transferor from the sale or exchange of such property shall be considered as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231.
(b) Section Applicable Only to Sales or Exchanges of Depreciable Property.—This section shall apply only in the case of a sale or exchange by a transferor of property which in the hands of the transferee is property of a character which is subject to the allowance for depreciation provided in section 167.
(c) Section Not Applicable With Respect to Sales or Exchanges Made on or Before May 3, 1951.—This section shall apply only in the case of a sale or exchange made after May 3, 1951.

8. 65 Stat. 504 (1951).

9. In some cases § 1239 may be avoided completely by the use of either § 1245 or § 1250, both of which, subject to certain limitations, tax the gain realized upon the sale of a depreciable asset as ordinary income. Under §§ 1245 and 1250, however, complete recovery of the realized gain as ordinary income cannot be accomplished if the sale price of the asset exceeds its original cost, if the asset is a building which has been held for more than one year, or if the asset is "section 1245" property acquired before 1962 or "section 1250" property acquired before 1964. Recent Development, *Retention of Control Over Stock Constitutes "Ownership" Under Section 1239 of the Internal Revenue Code—Harry Trotz*, 63 MICH. L. REV. 1504, 1505-06 (1965).

10. 376 F.2d 402 (5th Cir. 1967).

11. 242 F. Supp. 117, 121 (W.D. La. 1965).

12. 361 F.2d 927, 930 (10th Cir. 1966).

13. The court noted that the dissimilar wording of the test for control of a corporation in § 368(c) (" '[C]ontrol' means the ownership of stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote and at least 80 percent of the total number of shares of all other classes of stock of the cor-

value" test, which was based upon a fair market evaluation of Parker's *block* of shares. Finding that an 80 percent shareholder's control of corporate activities added some unquantified value to his block of shares, and that restrictions on the alienability of the 20 percent shareholder's stock devalued those shares by an undetermined amount, the court concluded that Parker, by owning 80 percent of the shares, owned something more than 80 percent *in value* of the shares.[14] The very difficult question of how much value was added to Parker's shares by these factors was happily avoided, that determination being unnecessary to the disposition of this particular case.

Following the Fifth Circuit's decision in *Parker*, the Tax Court, in a memorandum opinion,[15] decided the *Trotz* case on remand, applying, without so acknowledging,[16] the block value test propounded by the Fifth Circuit in *Parker*. However, primarily because the transferee corporation was not a "going concern," the Tax Court held that 79 percent of the shares, by numerical count, was 79 percent in value of the shares.[17]

Although the test produced different results in the two cases, it is important to note that both courts applied essentially the same block value test. This test assumes initially that all shares in a given class of stock are of equal value.[18] It then inquires whether any incremental value need be attached to a taxpayer's block of shares in a hypothetical sale by reason of the number of shares that he owns or the relatively limited restrictions on the alienability of those shares.[19] Thus, the "block value" of a taxpayer's holdings is the sum of the value of the individual shares in the block *plus* the incremental value arising from the above-mentioned factors.

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poration."), and the absence of any reference to that section in § 1239, as compared to § 351(a) which makes specific reference to the control test enunciated in § 368(c), indicated that a different test was to be established in § 1239 than that found in § 368(c). 376 F.2d at 407-08.

14. *Id.* at 409.

15. Harry Trotz, 1967 P-H Tax Ct. Mem. ¶ 67,139 (1967).

16. Although the Tax Court's opinion never mentioned the Fifth Circuit's decision in *Parker*, the Tax Court was likewise concerned with the "block value" of the taxpayer's holdings and in connection therewith considered the same factors: majority control and restricted alienability. Thus, the conclusion seems inescapable that in *Trotz* the Tax Court applied the *Parker* "block value" test.

17. 1967 P-H Tax Ct. Mem. at ¶ 67,139.

18. In a case involving a corporation with multiple classes of stock, the "block value" test would have to determine the value per share of each of the separate classes of stock.

19. Assume, for example, a corporation with 100 shares of stock value at $10 per share. An 80 percent holder ostensibly owns $800 worth of stock. Yet, he may be able to sell his 80 percent block for more than $800, the incremental value being a premium for control, unrestricted alienability, or a volume purchase. Thus, because of this incremental block value, his individual shares are worth more than $10 per share when sold as part of his block. *See* Andrews, *The Stockholder's Right to Equal Opportunity in the Sale of Shares*, 78 HARV. L. REV. 505 (1965); Jennings, *Trading in Corporate Control*, 44 CALIF. L. REV. 1 (1956).

There are persuasive reasons, however, for not using this "block value" test under section 1239. First, such a test provides no reliable or predictable guidelines for the taxpayer who attempts to plan his sale of depreciable property so as to receive the capital gains treatment allowed by section 1239. The 80 percent in value measure was presumably designed, at least in part, to give the taxpayer fair notice of what Congress considered to be a bona fide sale. Moreover, since the 80 percent figure was apparently set as a convenient benchmark for administrative purposes, there is reason to suppose that Congress intended a simple test with a minimum of litigation. It is thus not to be assumed that Congress intended a test so subjective as to place the taxpayer at the mercy of the Internal Revenue Service and the courts. Yet the block value test requires the taxpayer to determine the fair market value of his block in a situation where the means available to him for such a determination are so inadequate and unreliable that the 80 percent measure of section 1239 becomes hopelessly elusive.

Normally, comparable sales of a corporation's own stock are the best indication of the fair market value of other stock in the same corporation.[20] Yet section 1239 will ordinarily be applicable to closely held corporations, with respect to which sales of stock take place only infrequently, if at all.[21] Moreover, the sales which do occur are generally dismissed as unrepresentative.[22] Thus, the taxpayer cannot look to actual sales of the stock of the corporation, or of other closely held corporations similarly situated,[23] as a reliable indication of the fair market value of his holdings. Nor can he obtain a ruling from the Internal Revenue Service as to the value of his holdings, since the Service generally refrains from giving such rulings.[24] Therefore, under the block value test, his only recourse is to an expert's opinion of the fair market value of his block of shares in a sale which is not going to take place in a market which does not exist.[25] Moreover, the expert is necessarily confronted with the problem of measuring the incremental value which would accrue to the taxpayer's block in this hypothetical sale. As there are no guidelines whatever for this quan-

20. 10 J. MERTENS, LAW OF FEDERAL INCOME TAXATION § 59.11 (1943).

21. *Id.* at § 59.25.

22. Section 3.03, Rev. Rul. 59-60, 1959-1 CUM. BULL. 237-38; Furst, *Valuation of Closely Held Corporations*, 47 WYBRAND J. No. 2, at 1 (1966); *see* Schnorbach v. Kavanagh, 102 F. Supp. 828 (W.D. Mich. 1951).

23. There is little likelihood that the few sales of stock of comparable closely held corporations will involve blocks of the same size as the taxpayer's, thereby adding more subjectivity to the incremental value determination.

24. Hartwig, *Valuation Problems Before the Internal Revenue Service and the Tax Courts*, N.Y.U. 13TH INST. ON FED. TAX. 1143, 1159 (1955).

25. *See* Dakin, *Legal Aspects of the Valuation of Corporate Stocks of Closely Held Corporations*, TULANE 6TH TAX INST. 379 (1957); Hartwig, *supra* note 24; Rice, *The Valuation of Close Held Stocks: A Lottery in Federal Taxation*, 98 U. PA. L. REV. 367 (1950); Note, *An Old Formula in New Attire*, 11 TAX L. REV. 190 (1956).

tification of incremental value, the taxpayer is left with a completely subjective determination,[26] with the result that a test based on the fair market value of a particular block of shares in a close corporation is incapable of providing fair notice.[27] This result necessarily follows from the block value test, and unless one is to assume that Congress desired such uncertainty, another test must have been envisioned.

Moreover, courts are in no better position than the taxpayer to measure the incremental value of a block of shares. Thus, a court could assign an arbitrary value to majority control and thereby could justify a conclusion that any taxpayer who owns between 50 and 80 percent of the shares of a corporation owns "more than 80 percent in value" of the outstanding stock for purposes of section 1239. Not only does this judicial maneuverability have an adverse retroactive impact on the taxpayer, but it is inconsistent with the legislative history of section 1239. The Senate Finance Committee objected to the original wording of section 1239, which had established a test of "50 percent in value,"[28] because of its belief that with such a low standard the provision would deny capital gains treatment to some bona fide transactions.[29] In response to the Senate's objections, the conference committee raised the measure from 50 to 80 percent.[30] Yet, as indicated above, one of the effects of the block value test may be to include the 50 to 80 percent holder, which is apparently just what the Senate committee sought to avoid by insisting on a considerably higher standard than "half of the outstanding shares."[31]

26. *See* 10 J. MERTENS, LAW OF FEDERAL INCOME TAXATION § 59.21-.26 (1943), which discusses the valuation of the basic per share value but which fails to suggest how incremental value should be quantified.

27. A hypothetical example will demonstrate what the taxpayer is up against when § 1239 is interpreted to contemplate a "block value" test. Assume a taxpayer owns 60 percent of the shares in a corporation to which the proposed sale of depreciable property is to be made. The taxpayer's expert determines that majority control and unrestricted alienability each add 10 percent in incremental value to the basic value of the shares the taxpayer owns, thus concluding that the taxpayer owns 72 percent in value of the corporation's outstanding stock, apparently well without the "more than 80 percent in value" limit of § 1239. Yet, if the court found that each of these factors added not 10 percent to the value of the taxpayer's block unit but 17 percent, the taxpayer's 60 percent block of shares would equal "more than 80 percent in value." The taxpayer, believing himself to be well without the bounds of the "more than 80 percent in value" measure by holding only 60 percent of the shares, finds himself paying the higher income rates because of a seven percentage point difference between the opinion of his expert and that of the court. As the *Central Trust v. United States* case indicates, a variance of seven percentage points between honest and qualified experts representing different interests is fully to be expected, given the hypothetical sale on the hypothetical market context in which § 1239 will normally be applicable. 305 F.2d 393 (Ct. Cl. 1962).

28. H.R. 4473, 82d Cong., 1st Sess. (1951). J. SEIDMAN, LEGISLATIVE HISTORY OF FEDERAL INCOME AND EXCESS PROFITS TAX LAWS (1953-1939) 1866 (1954).

29. S. REP. No. 781, 82d Cong., 1st Sess., pt. 1, at 70 (1951).

30. J. SEIDMAN, LEGISLATIVE HISTORY OF FEDERAL INCOME AND EXCESS PROFITS TAX LAWS (1953-1939) 1866 (1954).

31. Judging from its understanding that "50 percent in value" meant "half of the outstanding shares" (*see* note 42 *infra* and accompanying text), the Senate Finance

In response to the above objections, it might be argued that while a fair market evaluation of a block of shares in a closely held corporation is admittedly exceedingly difficult and subjective, such appraisals are regularly undertaken in estate and gift tax cases. Revenue Ruling 59-60[32] suggests that a block value test is appropriate for estate and gift tax purposes.[33] Yet section 1239 would seem to require a more predictable standard than is needed in the estate and gift context, since the "80 percent in value" measure was presumably designed, at least in part, as a standard by which businessmen could govern their actions. Moreover, the incremental value of a block of shares is a crucial factor in the estate and gift tax context, where the very object of the tax is the block of shares and the purpose of the appraisal is to measure the total value passing into the hands of the new owner or owners.[34] However, in the section 1239 situation, the ownership of shares is neither being taxed nor is it passing into new hands; it is merely being used as a measure of the substantiality of a particular shareholder's interest in a corporation to which he has sold depreciable property. In this connection, it should be recalled why section 1239 is concerned with the substantiality of a taxpayer's ownership share of a corporation. The section was designed to deny capital gains treatment to those taxpayers whose ownership in a corporation is substantial enough to make it profitable for them to sell appreciated assets to the corporation and suffer the incident capital gains taxes[35] solely for the purpose of permitting the corporation to take subsequent depreciation deductions. Given this design, it would seem that a test for substantiality of ownership should focus on the taxpayer's right to share in the earnings of the corporation, rather than on his control over corporate activities.[36] Thus, the emphasis on control under the block value test appears to be misplaced.

Committee must have believed that the 80 percent measure appearing in the revised bill would establish a standard a full 30 percent higher than half of the outstanding shares.

32. 1959-1 CUM. BULL. 237.

33. There is, however, reason to doubt whether the *Parker* "block value" test is appropriate even in the estate and gift tax context. This writer has found no estate or gift tax case which holds that an incremental value is to be added to a majority stockholder's block in a close corporation by reason of the size of his block. The "size of block" factor mentioned in Rev. Rul. 59-60 has instead been understood to contemplate simply a discount for lack of marketability of a minority block. *See* Central Trust v. United States, 305 F.2d 393 (Ct. Cl. 1962); Worthen v. United States, 192 F. Supp. 127 (D. Mass. 1961); Bader v. United States, 172 F. Supp. 833 (S.D. Ill. 1959). Such a discount would have been inappropriate in *Parker*, however, because the 80 percent holder was contractually obligated to purchase the 20 percent holder's block whenever the minority holder wanted to sell, thereby creating a ready market for the 20 percent holder. United States v. Parker, 376 F.2d 402 (1967).

34. Rice, *supra* note 25.

35. *See* note 3 *supra*.

36. Indeed, if Congress contemplated a control test, it could easily have incorporated the test in § 368. *See* note 13 *supra* and accompanying text.

In view of these patent deficiencies of the block value test, it is surprising that the courts in the two principal cases settled on the same unsatisfactory standard. Both courts agreed that Congress must have intended more than a simple numerical count test by the deliberate use of the phrase "in value" in section 1239, since that language would be rendered surplusage if a mere count of the shares had been contemplated. However, it is a numerical count test for which one finds the most support in the case authority and legislative history.[37] The principal cases were the first in which the "80 percent in value" phrase was directly in controversy, but earlier courts applying section 1239 were necessarily confronted with the meaning of those words. Prior to the lower court decision in *Parker*, every such court had apparently assumed that the language called for a numerical count of the outstanding shares.[38]

This numerical count test finds additional support in the legislative history of section 1239. The provision when first submitted as section 328 of the Revenue Act of 1951 spoke of "more than 50 percent in value of the outstanding stock."[39] In one of three references to the phrase in the House Ways and Means Committee Report the words "in value" are omitted.[40] More significantly, the hypothetical examples included in the Committee Report to clarify the operation of the section apparently speak in terms of percentages based on a numerical count.[41] The Senate Finance Committee, although recommending rejection of the entire section, understood "more than 50 percent in value" to mean more than half of the outstanding stock.[42] The conference committee retained the section with the "in value" language, altering the ownership rules and raising the measure from 50 to 80 percent without ever indicating that the Senate's understanding of the test had been incorrect.[43]

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37. It should be noted that the Fifth Circuit produced no legislative history to support its "block value" test; furthermore, none of the cases cited in support of the test involved § 1239.

38. *E.g.*, United States v. Rothenberg, 350 F.2d 319 (10th Cir. 1965); Mitchell v. Commissioner, 300 F.2d 533 (4th Cir. 1962) (taxpayer owned 79.54% of stock); F. W. Dryborough, 42 T.C. 1029 (1964); Fontaine v. Patterson, 62-2 U.S. Tax Cas. ¶ 9790 (N.D. Ala. 1962); Ainsworth v. United States, 60-2 U.S. Tax Cas. ¶ 9595 (E.D. Wis. 1960); Estate of Walter A. Krafft, 30 P-H Tax Ct. Mem. ¶ 61,305 (1961).

39. H.R. 4473, 82d Cong., 1st Sess. (1951); J. SEIDMAN, LEGISLATIVE HISTORY OF FEDERAL INCOME AND EXCESS PROFITS TAX LAWS (1953-1939) 1866 (1954).

40. H.R. REP. No. 586, 82d Cong., 1st Sess. 26 (1951). *See* STAFF OF JOINT COMM. ON INTERNAL REVENUE TAXATION, SUMMARY OF PROVISIONING OF REVENUE ACT OF 1951, 82d Cong., 1st Sess. 35-36 (1951) (same omission).

41. H.R. REP. No. 586, 82d Cong., 1st Sess. 120-21 (1951).

42. S. REP. No. 781, 82d Cong., 1st Sess., pt. 1, at 69 (1951): "The House Bill attempted to eliminate the tax advantage . . . by denying capital gain treatment to the transferor with respect to sales or exchanges of depreciable property . . . between an individual and a corporation more than half of the outstanding stock of which is owned by or for him . . . ."

43. H.R. REP. No. 1179, 82d Cong., 1st Sess. 77 (1951).

Inquiry into the legislative history of section 267,[44] the "spiritual ancestor"[45] of section 1239, provides little insight into the meaning intended in Congress' first use of a "percentage in value" test. Section 267 disallows the deduction for a loss resulting from the sale of property to a corporation of which the taxpayer owns "more than 50 percent in value of the outstanding stock." The "in value" wording in section 267 replaced language in the original bill which provided for a numerical count of voting stock.[46] While Congress unfortunately did not elaborate on the intended meaning of the substituted phrase "in value,"[47] the courts applying section 267 have consistently resorted to a numerical count test.[48] Thus, with respect to section 267, as perhaps with section 1239, the numerical count test was firmly entrenched in the case authority prior to the district court's decision in *Parker*.

Given this apparent legislative and judicial recognition of the numerical count test, there is reason to question the premise of the courts in the principal cases that section 1239 calls for more than a mere count of the shares in *all* cases. Moreover, the basic assumption underlying this premise—that the employment of a numerical count test reads the phrase "in value" out of the statute—does not bear analysis. It is true that if section 1239 were only concerned with corporations having a single class of stock, the words "in value" would not be necessary; for, assuming that any value added by control or a relative freedom from share transfer restrictions should not be taken into account, a mere percentage count of the shares would reach the same result as a more complicated computation based on a fair market valuation of the corporation and of the taxpayer's shareholdings. However, the phrase "in value" is given content in the situation where the transferee corporation has more than one class of outstanding stock, since in that case a mere count of the shares may not be sufficient.

In a corporation with two or more classes of stock, a taxpayer could own well over 80 percent of the value of all the shares, without holding 80 percent, by numerical count, of the outstanding shares.

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44. INT. REV. CODE OF 1954, § 267.

45. 97 CONG. REC. 11740 (1951) (remarks of Senator Humphrey); Warren, *Sales of Depreciated Properties to Related Entities*, U. SO. CAL. 1959 TAX INST. 797.

46. J. SEIDMAN, LEGISLATIVE HISTORY OF FEDERAL INCOME TAX LAWS (1938-1861) 316 (1938).

47. Three years later, however, the Ways and Means Committee issued hypothetical examples illustrating the ownership provision of § 267 which appear to be based on a numerical count of shares interpretation. H.R. REP. No. 1546, 75th Cong., 1st Sess. 27-29 (1937).

48. *E.g.*, Federal Cement Tile Co. v. Commissioner, 338 F.2d 691 (7th Cir. 1964); McCarty v. Cripe, 201 F.2d 679 (7th Cir. 1953); Gounares Bros. v. United States, 185 F. Supp. 794 (S.D. Ala. 1960); Graves Bros., 17 T.C. 1499 (1952); Arizona Publishing Co., 9 T.C. 85 (1947); Morris Inv. Corp., 5 T.C. 583 (1945); Hosch Bros., 3 T.C. 279 (1944); W. A. Drake Inc., 3 T.C. 33 (1944); Lakeside Irrigation, 41 B.T.A. 892 (1940); Norman Cooledge, 40 B.T.A. 110 (1939).

For example, if a taxpayer owns all 100 shares of a corporation's class A stock valued at ninety dollars per share but none of the 100 shares of class B stock worth ten dollars per share, a mere count of the shares would determine that he owns 50 percent of the shares, and, if this alone were the test, he could qualify for capital gains treatment under section 1239. Assuming that earnings are distributed approximately in proportion to the value of the shares,[49] this obviously would be an unsatisfactory result. Thus, with respect to a transferee corporation with more than one class of stock, a more sophisticated computation is required. First, the total value of each class of shares should be ascertained.[50] Emphasis should be placed on the extent to which each class of stock can share in the earnings of the corporation. Next, the total value of each class should be divided by the number of shares in the class to obtain the value per share. It is then a simple matter to determine the value of a taxpayer's ownership by multiplying the number of his shares in each class by the appropriate per share value. Finally, the taxpayer's percentage ownership "in value of the outstanding stock" is computed by dividing the value of his share holdings, as computed above, by the total value of all the outstanding classes of stock.[51] While the results of this computation are less predictable than those reached under the simpler computation in the single class situation, where actual evaluation is unnecessary, they are significantly more predictable than the results reached under the block value test, where the value added by control must be quantified. Thus, the test outlined herein provides a workable standard for both the taxpayer and the courts, and is entirely consistent with the language of section 1239 and the legislative history.[52]

Courts in the near future are going to be confronted with the

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49. *See* note 35 *supra* and accompanying text.

50. Revenue Ruling 59-60 (1959-1 CUM. BULL. 237) indicates that there are at least eight relevant factors which may be considered in the evaluation of stock in closely held corporations for estate and gift tax purposes. Section 4.01, Rev. Rul. 59-60, 1959-1 CUM. BULL. 237, 238:

(a) The nature of the business and the history of the enterprise from its inception.
(b) The economic outlook in general and the condition and outlook of the specific industry in particular.
(c) The book value of the stock and the financial condition of the business.
(d) The economic capacity of the company.
(e) The dividend-paying capacity.
(f) Whether or not the enterprise has goodwill or other intangible value.
(g) Size of block factor [which is not relevant for our purposes].
(h) The market price of stocks of corporation engaged in the same or a similar line of business having their stocks actively traded in a free and open market, either on an exchange or over-the-counter.

See Baltimore Bank v. United States, 136 F. Supp. 642 (D. Md. 1955) (listing 20 factors); 10 J. MERTENS, LAW OF FEDERAL INCOME TAXATION §§ 59.21-.26 (1943).

51. For example, in the hypothetical above, the taxpayer would be said to own 90 percent in value of the outstanding shares.

52. This test—which results in a numerical count of the shares in the single class of stock situation—is consistent with the Ways and Means Committee's hypothetical examples (*see* note 41 *supra*) explaining the operation of § 1239, examples which cannot really be squared with the "block value" test.

problem of *Parker* and *Trotz* in more difficult contexts. *Parker* was an easy case for the block value test because the subjective quantification of the incremental value, normally necessitated by such a test, was avoided by the fact that any increase at all pushed the taxpayer over the 80 percent level. The court in *Trotz* avoided the quantification problem by determining that value is added only when the transferee is a "going concern." Future courts, regardless of whether they are faced with the quantification problem,[53] should recognize that the test places improper emphasis on the value of control, and thus should ask whether the block value is the proper test for section 1239 after all.

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53. The subjective determination required by the "block value" test has been discussed throughout this Note. *See* text accompanying notes 20-27 *supra*. Furthermore, similar "percentage in value" phrases are referred to in seven other sections of the Internal Revenue Code: §§ 178(b)(2)(B), 179(d)(2)(A), 267(b)(2), 318(2)(c) & (3)(c), 341(e)(8), 503(c) & 1235(d). The "block value" test will certainly be urged for these other sections where until now it appears that a numerical count test was generally used. *See* note 46 *supra*. *See also* Reilly, *An Approach to the Simplification and Standardization of the Concepts "The Family," "Related Parties," "Control," and "Attributation of Ownership,"* 15 TAX. L. REV. 253 (1960).