

TAX & ESTATE PLANNING ALERT

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New IRS proposed regulations profoundly affect valuation discounts for family business entities



On Aug. 4, 2016, the Internal Revenue Service (IRS) issued proposed regulations that substantially limit estate planning options for taxpayers with family-owned business entities. For some time, business valuation discounts have been used to ease federal estate and gift tax consequences resulting from intra-family transfer of business interests. Currently, taxpayers implementing proper discount planning are able to reduce the federal transfer tax value of their family business interests by 25 to 45 percent (with the appropriate discount being determined by an appraiser in light of all relevant facts), resulting in substantial tax savings. If appropriately structured, a couple holding \$1 million of stock in a family business could give that same stock to a trust for the benefit of their child at a potential gift tax value of only \$550,000 (assuming a 45 percent discount), effectively transferring \$450,000 of value free of federal gift taxes. However, if the IRS finalizes these new proposed regulations as presently written, they will severely restrict the availability of these favorable discounts and increase transfer tax consequences for those with significant family business interests. The same couple holding \$1 million in family business stock would likely lose the ability to transfer any value to their family members free of federal transfer taxes.

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The loss of valuation discounts might be further exacerbated after the upcoming elections. Estate tax reforms are among the agenda items for current presidential and congressional candidates. Proposed reforms include decoupling and reduction of the federal estate and gift tax exemptions, loss of inflation adjustments for exemption amounts and increases in marginal federal transfer tax rates. Grantor retained annuity trusts and other common estate reduction planning techniques are also likely to come under attack.



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Taxpayers of notable net worth, especially those with family business interests, should act quickly to take advantage of the presently available valuation discounts before the proposed regulations become final. The proposed regulations will be the subject of a public hearing on Dec. 1, 2016. After any post-hearing modifications are made, the regulations will be published and will become final 30 days after publication. Thus, the new regulations could be in place as early as Jan. 1, 2017. Many valuation discount plans require advance planning and extensive documentation, including opinions of value and available discounts rendered by qualified appraisers who have reviewed the facts and circumstances relevant to the subject business interests. Taxpayers who want to take advantage of currently available discounts need to take action well before the end of the year.

For more information about valuation discount planning, contact a member of Porter Wright's [Tax, Estate Planning & Personal Wealth Practice Group](#).