

*If you have any questions
about this Advisory,
please contact:*

LEONARD LEADER
203.363.7602
lleader@wiggin.com

ROBERT BENJAMIN
212.551.2602
rbenjamin@wiggin.com

MICHAEL CLEAR
203.363.7675
mclear@wiggin.com

KAREN CLUTE
203.498.4349
kclute@wiggin.com

DANIEL DANIELS
203.363.7665
ddaniels@wiggin.com

HELEN HEINTZ
203.363.7607
hheintz@wiggin.com

DAVID KESNER
203.498.4406
dkesner@wiggin.com

ARSINEH KAZAZIAN
212.551.2632
akazazian@wiggin.com

LISA PAGE
203.363.7635
lpage@wiggin.com

BETH SCHARPF
212.551.2634
bscharpf@wiggin.com

MATTHEW SMITH
203.363.7639
msmith@wiggin.com

New Proposed Regulations Concerning Valuation Discounts: Transfers of Family-Owned Businesses and Other Properties Could Become More Costly

Proposed tax regulations issued on August 2, 2016 could eliminate or radically reduce the availability of valuation discounts in connection with the transfer of interests in closely held entities to family members. These new regulations are sometimes referred to as the “proposed Section 2704 Regulations,” after the section of the Internal Revenue Code to which they relate. The proposed regulations came as some surprise: although new regulations were widely expected, many estate planning professionals predicted that the regulations would impose an upper limit on the size of discounts for federal transfer tax purposes. Instead, the proposed regulations appear to wipe out most valuation discounts in the family context altogether. The proposed regulations may go into effect as early as the end of the year, and accordingly, clients considering transfers of interests in a family-controlled entity (whether an operating business, holding company, vacation home or other asset) should contact us promptly.

The ability to apply valuation discounts to reflect lack of control or ready marketability of a transferred asset has been a bedrock principle of fundamental estate planning for decades. For example, an individual might own a closely held business worth \$100 million. Prior to the proposed regulations taking effect, if the individual transfers, say, a 30 percent interest in the business to her child, an appraiser likely would opine that the value of the gift is not \$30 million (i.e., 30 percent of \$100 million). Instead, the appraiser would apply discounts to reflect the fact that the asset transferred is a minority interest that is not traded on an established exchange. If the appraiser were to conclude that a 33 percent valuation discount should be applied, the value of the gifted property for transfer tax purposes would be only \$20 million. As estate planners often liked to say, \$10 million of value was made to “disappear” from the transfer tax system, saving the family \$4 million of tax (assuming a 40 percent estate tax rate). The proposed Section 2704 Regulations provide that nearly all of the factors historically relied upon to achieve these valuation discounts must be disregarded in the family context, in effect abolishing many of the discounts currently available.

It may be possible to “lock in” discounts by effectuating gifts of interests in closely held entities before the regulations come into effect. If you would like to consider such planning - or if you have questions about the proposed Section 2704 Regulations - don’t hesitate to contact your Wiggin and Dana attorney.

This publication is a summary of legal principles. Nothing in this article constitutes legal advice, which can only be obtained as a result of a personal consultation with an attorney. The information published here is believed accurate at the time of publication, but is subject to change and does not purport to be a complete statement of all relevant issues.