BURNS & LEVINSON LLP

TRUSTS & ESTATES UPDATE

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# IRS PROPOSES REGULATIONS THAT WILL ELIMINATE MOST VALUATION DISCOUNTS ON FAMILY-OWNED ENTITIES

**By Clifford Cohen, Co-Chair - Private Client Group**

On August 2, 2016, the IRS issued proposed regulations that would eliminate or limit the use of certain valuation discounts regularly applied when valuing interests in family-owned entities for gift and estate tax purposes.

## CURRENT LAW

Under current law, a business is valued at its fair market value as of the date of transfer for gift and estate tax purposes. In determining the value, the transferor may take advantage of discounts for lack of control and lack of marketability when transferring a non-controlling interest in the business.

## PROPOSED CHANGES

The proposed regulations seek to curtail the use of these discounts by disregarding certain transfer restrictions placed on ownership of the entity when valuing the entity for transfer tax purposes.

By way of example, an individual transfers $5,000,000 of stock in a family business, constituting 30% of the business, to the next generation. Under current law, if the transfer is structured correctly, the value for gift and estate tax purposes of the transferred interest may be reduced by as much as 35% due to the lack of control and lack of marketability. The proposed regulations would restrict the use of these discounts so that the value for transfer tax purposes would be much closer to the $5,000,000 value.

## ACT NOW TO BENEFIT FROM CURRENT REGULATIONS

A public hearing on the proposed regulations is scheduled for December 1, 2016. The regulations will likely become final in the beginning part of 2017. We cannot predict the rules contained in the final regulations, so we recommend that clients who wish to transfer family businesses to younger generations contact us as soon as possible in order to take advantage of the current valuation discounts.

## WHO NEEDS ESTATE PLANNING?

For many people, the value of an estate plan will far exceed its cost due to tax savings. Furthermore, estate planning is not just for individuals who have a net worth in excess of state or federal exemptions (currently set at $1 million for MA, and $5.45 million for the U.S., but subject to change). The following people can greatly benefit from estate planning with experienced legal counsel:

- Individuals or couples who have dependents or beneficiaries with special needs.
- Adoptive parents, who need to make special provisions for inheritance that differ from state law provisions applicable to those without a legally enforceable plan.
- Other non-traditional families, such as those of unmarried couples or domestic partners.
- Married persons who have previous spouses or children from a prior marriage.
- Those who have special charitable goals.
- Those who have ownership shares in a closely held business that could suffer grave disruption from an inheritance battle or significant death taxes on their estates. Such people can benefit from a well-structured agreement providing for life insurance on key owners in amounts adequate to fund the purchase of the decedent's shares, according to valuations set by agreement.

## ABOUT BURNS & LEVINSON

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