

Possible Changes Coming for Valuations of Family Limited Partnerships and Limited Liability Companies

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On Tuesday, the Treasury Department and Internal Revenue Service issued proposed regulations which will make it more difficult to pass wealth to future generations while minimizing estate and gift taxes. For decades families have used family limited partnerships ("FLPs") and limited liability companies ("LLCs") as a core component of their estate plans. An attractive feature of FLPs and LLCs has been the sizable discounts afforded for "lack of control" and "lack of marketability" when valuing gifts of non-controlling interests in these entities. These discounts reduce the value of a gift and its transfer tax impact. Not surprisingly, the IRS has employed a variety of methods to reduce the availability and size of valuation discounts. One of its common means of doing so is through the application of Internal Revenue Code Section 2704.

Section 2704 requires that certain types of restrictions in operating agreements and partnership agreements be disregarded when determining the fair market value of interests transferred between family members. When it applies, Section 2704 essentially eliminates the "lack of control" and "lack of marketability" discounts that would otherwise be available.

On Tuesday, the IRS proposed new 2704 regulations. The proposed regulations effectively expand the applicability of Section 2704 in an effort to further restrict the use of the discounts. The proposed 2704 regulations are expected to go through a 90-day public comment period and will become effective 30-days after the government issues the final regulations.

Barley Snyder is closely monitoring the release of the final 2704 regulations and advising clients of the possible implications on their estate plans. If clients are considering making gifts or transfers of their closely held business interests to minimize their gift and estate tax liability, now is the time to strongly consider and evaluate those transfers.

If you have questions, or if we can provide any assistance, please do not hesitate to contact us.

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