

## **Advocacy Comments on IRS Proposed Rules Related to the Valuation of Interests in a Closely Held Business**

On November 1, 2016, the Office of Advocacy (Advocacy) submitted a comment letter to the Internal Revenue Service (IRS) in response to the agency’s proposed rules, issued on August 4, 2016, that relate to the valuation of interests in a closely-held partnership or corporation for estate, gift, and generation-skipping transfer tax purposes. In general, for the transfer of a business interest via estate or gift, the interest is taxed based on the Fair Market Value of the amount of the gift on the transfer date. In the case of an interest in a closely-held corporation or partnership, however, case law has evolved to permit discounts in valuing interests where the interests represent minority positions for which there is no ready market. This tax policy, known as a “valuation discount,” allows the transferor of a closely held business interest to reduce the value of a small percentage of their ownership interest, which reduces the amount of the transfer subject to tax. The IRS proposed regulations would eliminate most of these valuation discounts for operating businesses.

- The IRS certified that the proposed regulations will not have a significant economic impact on a substantial number of small entities. The IRS supports this certification by stating that the proposed regulations will “affect the transfer tax liability of individuals who transfer an interest in certain closely held entities and not the entities themselves.” The IRS adds “any economic impact on entities affected...is derived from the operation of the statute, or its intended application, and not from the proposed regulations in this notice of proposed rulemaking.”
- Small business stakeholders expressed concern to Advocacy that the proposed regulations, if finalized, would be such a large departure from current IRS policy and industry practice that expensive new business valuations would need to be completed for closely held businesses. Moreover, small business owners and representatives indicated that, by eliminating valuation discounts, the proposed regulations would negatively impact succession planning for many small businesses. For these reasons, the IRS’ statement in support of the RFA certification is not valid.
- Advocacy recommends that the IRS subject the proposed rules to a fuller Regulatory Flexibility Act (RFA) analysis, and that the IRS publish for public comment either a supplemental RFA assessment with a valid factual basis in support of a certification or an Initial Regulatory Flexibility Analysis (IRFA).
- By publishing for comment either a supplemental RFA assessment or an IRFA, small businesses will have adequate data to assess the amount of paperwork burden that may be generated by the proposed rules.
- Advocacy also encourages the IRS to extend the comment period for the proposed regulations by 60 days to allow small businesses more time to consider the impact of

the proposed regulations and potentially recommend less burdensome alternatives to the IRS.

For more information, as well as a complete copy of Advocacy's letter to the IRS, please visit Advocacy's website at <http://www.sba.gov/advocacy/816> or contact Assistant Chief Counsel Dillon Taylor by email at [dillon.taylor@sba.gov](mailto:dillon.taylor@sba.gov) or by telephone at 202-401-9787.