DANZIGER & MARKHOFF LLP

Attorneys at Law

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IRS Proposed Regulations to Eliminate Discounts for Gifts

Gifting has always been one of the most common techniques used to minimize estate tax and, since 1993, the IRS has permitted discounting gifts of interests in entities such as corporations and LLCs to family members. The argument has been that if a non-voting interest was transferred, and if that interest was in a private entity, then discounts for minority interest and lack of marketability could be applied.

In other words, gifting a $1,500,000 commercial office building to children or grandchildren (or to trusts for their benefit) would exhaust $1,500,000 of the lifetime $5,450,000 estate and gift tax exemption. However, a gift of $1,500,000 of real estate owned by an LLC or a corporation, assuming a reasonable 33% discount, would only be reported as a $1,000,000 gift, thus using $500,000 less lifetime gift tax exemption.

For years, the IRS has felt that these techniques have been abused and has frequently challenged their use in audits and in court. After much litigation, the IRS reacted on August 2, 2016 issuing proposed regulations to Section 2704 of the IRS Code which would eliminate these discounts for transfers of closely-held family owned entities. A hearing is scheduled for December 1, 2016 about the new regulations and, if adopted, the regulations would be effective 30 days later.

What does this mean for you? First, any discounted gifting made to this point is grandfathered and unaffected. Second, if these regulations do become final, then there is time before the end of 2016 to consider gifting to take advantage of the discounts currently available.

Please call or email Harris Markhoff or Michael Markhoff if you would like to discuss this further.

Contacts:

Harris Markhoff, Esq.

hmarkhoff@dmlawyers.com

914.948.1556 ext. 8001

Michael Markhoff, Esq.

mmarkhoff@dmlawyers.com

914.948.1556 ext. 8017