CC: PA: LPD: PR (REG-163113-02)
Room 5203
Internal Revenue Service
PO Box 7604
Ben Franklin Station
Washington, DC 20044

Re: Comment on the Proposed Rule for Estate, Gift, and Generation-skipping Transfer Taxes: Restrictions on Liquidation of an Interest—Regulatory Information Number (RIN) 1545-BB71.

Dear Secretary Lew:

On behalf of the National Small Business Association, the nation's oldest nonpartisan small-business advocacy organization, representing more than 65,000 small businesses nationwide, I write to express my concerns about the potential impact of the proposed regulations under Internal Revenue Code Section 2704 (the "proposed minority discount rules") released by the Department of Treasury on Aug. 2, 2016. This proposed regulation could significantly change family businesses' succession plans and make it harder for family-owned businesses to transition to the next generation.

The future of the estate and gift transfer tax is a cause for major concern for small, family-owned businesses, many of which are struggling to guarantee that their business survives into the next generation. According to NSBA data, more than 70 percent of all family businesses do not survive through the second generation and 87 percent do not make it to a third generation. NSBA strongly believes family-owned businesses should not be punished because they have been successful or because the owner passes away. NSBA is very concerned about these proposed minority discount rules because, as written, they would impose significant new tax costs on family-owned businesses, diverting capital from business investment, costing jobs and threatening the ability of families to pass businesses on to the next generation of owners.

Family-controlled corporations and partnerships are often utilized as part of a family wealth transfer plan as vehicles for managing and controlling family assets, especially in the context of succession planning for family businesses. Family-controlled entities are attractive, in part, because of the ability to make gifts or bequests of interest in the entity to family members at a reduced tax cost using valuation discounts. The value of the interests transferred to family members is often subject to valuation discounts because of various restrictions imposed on the recipient's ability to participate in management, force a distribution or liquidation and/or sell or transfer the interests.

However, the release of this proposed rule signals the Department of Treasury's intent to curtail the opportunity to use such valuation discounts, and if adopted, would reduce the availability of valuation discounts used in valuing transfers between family members of interests in family-controlled entities where the interests are subject to restrictions on liquidation. Further, the proposed regulations expands the circumstances in which the lapse of certain voting and liquidation rights attached to an interest in a family-controlled entity will be treated as a taxable gift or bequest. Although families have utilized valuation discounts when transferring interests in family-controlled entities for decades, the proposed regulations are anticipated to significantly limit the availability of these discounts. Moreover, the broad proposal would largely eliminate the consideration of control and marketability for a wide swath of family businesses when valuing them for estate and gift tax purposes.

Other areas of concern for NSBA is the proposed regulations will essentially create a new definition of value that does not mirror the reality of many situations. A controlling shareholder of a family-controlled entity can make two identical gifts of minority interests; one to a family member and one to a charity. Under these proposed regulations, the gift to the charity will be eligible for valuation discounts while the gift to the family member will not. Additionally, the proposed rule of ignoring valuation discounts on gifts made within three years of a transferor's death will apply to gifts made prior to the implementation of the regulations. This means that if the proposed regulations become final as of the end of 2016, gifts made by a donor as far back as Jan. 1, 2014 could be impacted.

As a result, NSBA firmly believes that these changes proposed to section 2704(b) would drastically remove legitimate valuation discounts for estate, gift, and generation skipping taxes which businesses have used for the past two decades in order to prevent the Internal Revenue Service (IRS) from overvaluing their businesses at death. Any changes in the law affecting the valuation and tax treatment of family businesses may require extensive alterations to estate plans, increased legal fees for additional consultations with attorneys and accountants, resulting in drawing valuable resources away from the ability of small, family-owned businesses to grow, invest and create jobs. Thus, these regulations will essentially add more burdensome challenges to family-owned businesses who are already dealing with complicated and costly estate and gift tax rules.

Instead, the Department of Treasury should pursue policies that encourage the creation and growth of family-owned businesses, not those that will increase the tax burden on families and make it more difficult to transfer ownership to the next generation. NSBA has long supported permanent repeal and reform of the estate tax, and will continue to work to protect American small businesses from onerous tax policies and regulations. It is crucial that we allow these small businesses to focus on growing their business, hiring employees, and greater expansion, rather than working to ensure their families are able to pass on their businesses to future generations.

Before issuing a final rule, NSBA recommends you consider the impact and consequences these proposed minority discount rules will truly have on small, family-owned businesses overall, and consider alternative approaches.

Sincerely,

Todd McCracken
President & CEO