



May 2, 2007
Pennsylvania Inheritance Tax
No. INH-07-001
Valuation Discount for Fractionalized
Interest in Estate Asset

ISSUE:

Whether an estate is entitled to discount the value of a parcel of real estate where the Decedent granted various life estates in the parcel to his children, followed by fractional remainder interests?

CONCLUSION:

The estate is not entitled to a valuation discount, as the decedent maintained possession and control of the entirety of the subject parcel until his death. Therefore, the entire parcel would be subject to Pennsylvania Inheritance Tax at full fair market date of death value.

FACTS:

Decedent died in 1989. Paragraph Four of his Last Will and Testament conveyed a parcel of real estate "to my children to be shared in accordance with the percentages as indicated besides their respective names listed below."

Paragraph Seven of the Will also directed the executor of the estate to permit "my [s]ons . . . to reside in my present residence . . . for as long as they desire sharing all pertinent expenses as is required to maintain such premises."

The decedent's sons shared the residence with the decedent until the decedent's death. At issue is whether the property should receive a discounted valuation for the "fractional" ownership interests that resulted from decedent's Will.

DISCUSSION:

Taxpayer does not dispute the taxability of the real estate in question under Section 2107 of the Inheritance and Estate Tax Act of 1982. 72 P.S. § 9107. Instead, Taxpayer's request is limited solely to a determination of whether the estate is entitled to a discounted valuation of the parcel for inheritance tax purposes.

Taxpayer has represented that the decedent's Will effectively established fractional interests in the real estate, held by the decedent's sons and daughters. Further, Taxpayer contends that the real estate cannot be sold unless all four beneficiaries consent to the sale. Taxpayer concludes that these facts justify a reduced valuation in accordance with the principles of valuing many closely held entities such as family limited partnerships.

The Inheritance and Estate Tax Act of 1982 has no provision that allows for the reduced valuation of a parcel of real estate necessitated by fractional shares of ownership by the estate beneficiaries.

Further, the fact that the decedent retained the right to possess the real estate (and actually resided in the real estate until his death) supports the conclusion that the decedent actually owned the entire fee simple interest in the real estate until his death in 1989. Consequently, one hundred percent of the fair market value of the real estate as of the decedent's date of death remains subject to Pennsylvania Inheritance Tax.

This Office notes the distinction between a formalized inter vivos family limited partnership, established with a legitimate business purpose (as well as the subordinate goal of achieving tax savings), and the mere testamentary conveyance of an asset into fractional shares, with no additional restrictions upon the conveyance that would justify a reduced valuation. Estate of Thompson v. Comm'r., 382 F.3d 367 (3rd Cir., 2004).

Taxpayer notes various expenses that may be incurred as a result of the fractional ownership of the real estate. This Office notes that these expenses (insurance, sale and financing costs) are generally deductible as a legitimate estate expense and may be claimed in this case. See generally, 72 P.S. §§ 9126-9129.