September 22, 2016

The Honorable Warren Davidson
1011 Longworth House Office Building
Washington, D.C. 20515

Dear Representative Davidson:

On behalf of the International Franchise Association and its members, thank you for introducing H.R. 6100, the Protect Family Farms and Businesses Act, which would restrict the future implementation of the U.S. Department of Treasury's proposed changes to Section 2704 on estate and gift tax valuation discounts. If adopted, the proposed rules will make it harder for families to pass their businesses down to their children and grandchildren. Franchisees are especially vulnerable to these changes due to the special circumstances surrounding the franchise agreement.

The proposed regulations seek to eliminate the discounts commonly used by small businesses to determine the amount of tax owed when a family business is transferred from one generation to the next, such as discounts due to a lack of marketability, minority ownership status, and lack of control. Family businesses often have these restrictions on shares in the business that they gift to their children. Shares of a family business are not like publically traded shares of a big company that can be routinely and easily sold for a publically known value on the open market. There simply are too few non-family buyers interested in purchasing a share in a family business, regardless of how successful it is. For this reason, the discount in valuation down from a "fair market value" makes sense. The proposed changes to the regulations would allow the Internal Revenue Service to value those gifts as if they were shares of a large, publically traded company, which will substantially increase the amount of estate taxes owed by the family. Franchisees will be particularly hard hit if these regulations are enacted due to factors particular to franchising that naturally depress a franchise business' price.

First, ownership of a franchise is only for a set period of time and there is no guarantee of renewal for an additional term. Hence, the valuation of the business may decline as the contract term runs. Second, in a franchise agreement, franchisors typically have the power to apply fees on transfers of a franchise and may deny the transfer altogether if they do not believe the transferee is capable of running the business and maintaining the brand standards. Third, most of the time, only an approved franchisee of the system is even eligible to buy the business, which may further decrease the market value.

There are legitimate reasons franchisors impose these restrictions – they protect the brand and ensure all of the franchisees in the system have the ability to prosper. Responsible franchisors seek to prevent consolidation of franchisees in a geographic market and try to ensure that buyers are able to operate the additional units well enough to protect the brand value of the whole system. However, the proposed rules do not recognize these discounting factors at all.

The IFA is the world's oldest and largest organization representing franchising worldwide, including 733,000 franchise establishments that support nearly 7.6 million direct jobs and $674 billion of economic output for the U.S. economy. IFA members include large and small franchise companies in over 300 different business format categories and over 15,000 individual franchisees, many of whom hope to pass along their small business to their children. We appreciate your recognition of the harms these proposed regulations would impose on all small business owners and, especially, franchise small business owners.

Sincerely,

Elizabeth Taylor

Elizabeth Hays Taylor
Vice President, Federal Government Relations & General Counsel