

## White Paper - Fractional Interest Discounts in Real Estate

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A fractional (or partial) interest discount on the value of a real estate property is allowable by the IRS when there is less than a 100% interest in the business entity that owns the real estate. The discount relates to the fact that the ownership interest has a "Lack of Control" over the operation and disposition of the real estate and a "Lack of Marketability" due to the difficulty in selling an interest that is not publically traded and is not easily financeable.

Examples of ownership entities that own a fractional interest include: general partnerships (GP), limited partnerships (LP), limited liability companies (LLC), tenants in common (TIC), and undivided interests. The two instances where this discount generally applies are for the gifting of a fractional interest or upon the death of a person that owns a fractional interest in real estate. Courts have held that discounts for lack of control and marketability exist in the market and should therefore be considered when valuing a fractional ownership interest. Discounts can vary depending upon the particular ownership entity to be valued, the percentage of ownership, the rate of return on the investment, the amount of debt and the market time and conditions in which it is to be considered. Based on our experience in the market we have seen discounts as low as 15% and as high as 67%. The majority of these transactions ranged from a discount of 25% to 35%. In each instance, the ownership interest needs to be valued based on its own specific merits. Finally, the IRS requires support in the form of an appraisal for the determination of a discount pertaining to a fractional interest.

Per IRS guidelines, the appraisal must consist of a "qualified appraisal" and be completed by a "qualified appraiser". Valbridge Property Advisors is the largest independent commercial real estate valuation firm in the United States and includes a proprietary national database of fractional interest sales. With over 70 offices nationwide, we can quickly manage large estates of various property types and locations. Our appraisals are the most comprehensive in the industry and will help your client sleep better at night knowing their estate filings will pass IRS scrutiny.



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