

Selling Equity of a Film

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Selling equity for a loss

Understanding Capital Losses

If you sell a capital asset (like an ownership interest in an LLC) for less than your original cost basis, you realize a capital loss

This loss can be used to offset other capital gains. If your total losses exceed your gains, you can deduct up to \$3,000 (\$1,500 if married filing separately) against your ordinary income each year, carrying any

remaining excess forward to future tax years

For your friends and family, their purchase price becomes their new "cost basis." If they eventually sell the investment, their taxable gain or loss will be calculated based on this new amount

Key Considerations for a Valid Sale

For the IRS to recognize the transaction as a valid sale and allow the loss deduction, it must meet specific criteria:

- **Arm's-Length Transaction:** The sale must resemble a transaction between unrelated parties, with a price based on the fair market value (FMV) of the LLC interest
- . A sale at an artificially low price may be reclassified by the IRS.
- **Documentation is Critical:** Maintain thorough records including a formal bill of sale, promissory note (if payment is installment-based), and communications establishing the business rationale for the sale price.
- **Proving "Worthlessness":** To deduct your entire investment as a loss, you must demonstrate the investment is completely worthless
- . Merely believing it has lost value is insufficient; you need objective evidence such as the LLC ceasing operations, filing for bankruptcy, or other proof it has no potential future value.

The "Disguised Gift" Scenario

If the IRS determines the transaction was not a true arm's-length sale, it may be reclassified as a gift with complex tax consequences:

- **For You (The Seller):** If deemed a gift, you cannot claim a capital loss deduction. Your basis in the investment transfers to the recipient
- **For the Buyer:** Their basis in the investment would be the same as yours (a "carryover basis") rather than the price they paid. If they later sell, their gain will be calculated from your original purchase price, potentially resulting in a larger tax bill for them
- **Gift Tax Rules:** Gifts to individuals are generally not taxable to the recipient. The giver may need to file a gift tax return (Form 709) if the amount to one person exceeds the annual exclusion (\$19,000 per recipient in 2025), though no tax is typically owed until exceeding the lifetime exemption (\$13.99 million in 2025)

How to Proceed

Given the significant tax implications and risk of IRS challenge, taking careful steps is essential:

- **Determine Fair Market Value:** Obtain a formal, independent valuation of your LLC interest to establish a defensible selling price.
- **Formalize the Sale:** Execute a formal purchase agreement documenting all terms of the sale at the determined FMV.
- **Consult a Tax Professional:** This is the most critical step. A qualified tax advisor or CPA can help you structure the transaction properly, ensure compliance, and avoid unintended tax consequences for you and your friends and family.

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