

The COVID-19-related Estate Planning Opportunity You Won't See Anywhere in the CARES Act

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On March 17, 2020, President Trump signed the Coronavirus Aid, Relief and Economic Security (CARES) Act into law. The CARES Act provides for billions of dollars in relief for American workers and businesses. However, mentioned nowhere in the bill is a major tax cut that in the long-term could be worth far more to owners of businesses and substantial estates than any of the short-term benefits in the

CARES Act.

There is no mention because the tax cut was not provided by Congress, but by the stock market. **The 18% drop in the S&P 500 index from 3393.52 in February to 2789.82 as of April 9th (over 30% at one point) has significant implications for the valuation of private businesses in the coming months. This drop may offer a unique opportunity to reduce your estate by transferring assets at lower values.**

Now to be clear, for most business owners, their priorities are (1) the health of loved ones and employees, and (2) making payroll, paying rent and staying in business. But to paraphrase Kipling, "If you can keep your head when all about you are losing theirs...a substantial tax break could await you."

The current period of confinement offers a perfect opportunity to consider how the bear market benefits estate and gift planning. Interests in privately-held businesses gifted during this bear market for stocks will benefit from the lower valuations produced under the market approach to value. Under the comparable public companies method of the market approach, multiples of business enterprise value to sales, EBITDA (earnings before interest, taxes depreciation and amortization) and EBIT are commonly used to value businesses. For most public companies, these metrics are lower now, and private company valuations should also reflect this.

The income approach to valuing private companies should also generate reduced value in most cases. Inputs to the income approach, such as revenue growth forecasts, should be revised to reflect the reality of the near-term future prospects of a company. In many cases, reductions in sales volume combine with fixed costs to dramatically lower projected profitability in the near term. Lower earnings will produce lower valuations in discounted cash flow models.

Even if a net asset approach to value is used, the potential for tax savings exists, as intangible assets and goodwill have likely decreased in value.

In some cases, companies may be able to file lost profit claims with insurers. A lost profit analysis provides a snapshot of value lost over a certain period. An independent valuation expert may use the lost profit claim to adjust the business

value in certain cases, providing an added benefit.

Finally, in valuing partial interests in businesses, a discount for lack of marketability (“DLOM”) is usually applied. While hard data has yet to emerge, the investor preference for liquidity in uncertain times potentially could produce an increase in the DLOM. Valuation experts can capture this uncertainty using option models, which could result in larger DLOMs and further estate and gift tax savings.

As an added note, if a person died in the 6-month period before the COVID-19 outbreak drove the market down, the estate should consider using the alternative valuation date to value the estate.

So the current confinement period provides an opportunity for Kiplingesque clear-headed thinking about estate and gift planning (or marital and divorce planning for that matter, as the lower values will affect pre-nups and equitable distribution settlements). Those who can keep their heads when those about them are losing theirs have a chance to reap significant tax savings.

Please contact your Anchin Relationship Partner or Raymond Dragon, a member of Anchin’s Litigation, Forensic, and Valuation Services Group, at 212.840.3456 or Raymond.Dragon@anchin.com for additional information about your situation.

Disclaimer: Please note this is based on the information that is currently available and is subject to change.