

COVID-19 Business Succession Planning

In just nine months, the COVID-19 pandemic has changed nearly everything – how we work, play, teach, shop, travel. And its full impact is still not known, as the virus continues to claim lives and livelihoods. Amid so much tumult and uncertainty, it's essential for business owners to review and update their business succession plans, especially since today's economic and regulatory climate creates several tax advantages for planning either a sale or transfer of assets.

- 1. Reduced asset values and historically low interest rates.** Because of the continuing financial crisis, business valuations are low. In addition, the Federal Reserve has cut the federal funds rate (the rate that banks charge each other for short-term loans) to near zero. Together, these conditions combine to allow for the ability to participate in cost-effective transfers of business interests.
- 2. Other reduced interest rates.** The reduction in interest rates such as the IRS Section 7520 Rate and the Applicable Federal Rates (AFR) directly affects the taxability of transferring wealth and business interests.

IRS Section 7520 rates are used to determine the gift tax value of certain transfers, including transfers to certain trusts like GRATs (Grantor Retained Annuity Trusts) and CLATs (Charitable Lead Annuity Trusts). The lower Section 7520 rates allow individuals to make larger gifts to their beneficiaries with less gift tax consequences.

The AFRs (Applicable Federal Rates) are used to determine interest charged on loans and promissory notes.

Comparison of rates for December 2019 and December 2020		
Rate	December 2019	December 2020
IRS Section 7520	2.0%	0.6%
Annual AFR short-term	1.61%	0.15%
Annual AFR mid-term	1.69%	0.48%
Annual AFR long-term	2.09%	1.31%

- 3. The federal estate and gift tax exemption and annual exclusion amounts remain at an all-time high.** In 2020, the federal estate and gift tax lifetime exemption is \$11,580,000 per individual, and the annual exclusion for gifts is \$15,000 per recipient per year. However, the federal estate and gift tax lifetime exemption is scheduled to be reduced by almost half in 2026 and could be reduced even sooner during the Biden administration. The likelihood of such reduction in the next couple years may largely depend on the outcome of the upcoming Senate elections.
- 4. Motivated buyers.** For those considering selling their business, today's low interest rates provide incentive for buyers, who might be encouraged to borrow money to make a purchase.
- 5. Transfer to family.** The decreased value of a business allows for transfers to family members while using less of the estate and gift exclusion amounts.

This guidance is designed to provide a brief general overview of business succession strategies. If you have any questions about this Information Memo, please contact any of the [attorneys](#) in our [Trust and Estate practice](#), or the attorney in the firm with whom you are regularly in contact.

