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Coronavirus Aid, Relief, and Economic Security (CARES) Act Tax update

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Four new liquidity programs are created

Paycheck Protection Program	Federal Reserve Liquidity Facilities	Treasury Loans and Loan Guarantees	Treasury Direct Payments
Small Businesses and Nonprofits	*Other Businesses*	*Airlines and Critical Businesses*	*Airlines*
• Generally available to businesses and nonprofits with 500 or fewer employees • Federally-guaranteed loans; a portion may be forgiven if used for payroll and other specified costs • May preclude business from claiming certain tax benefits under the Act	• Businesses that do not otherwise receive adequate relief from loans and loan guarantees under the Act • Loans, loan guarantees, advances, or direct purchase of borrower's debt • Restrictions on stock buybacks, dividend payments, executive compensation, and severance payments generally apply	• Airlines and businesses critical to national security • Direct loans or loan guarantees from Treasury • Restrictions on stock buybacks, dividend payments, executive compensation, severance payments, and employment levels • Treasury to take equity stake in the company	• Airlines and airline contractors • Must be used for wages, salaries, and benefits • Restriction on stock buybacks, dividend payments, executive compensation, severance packages, involuntary furloughs, and pay/benefit reductions • Treasury to take equity stake in the company

Key Tax Provisions for Businesses

Net Operating Loss Carryback

- Since 2017, Congress generally has not allowed businesses with losses to carry back those losses to prior years to reclaim previously paid taxes.
- The CARES Act temporarily allows losses from 2018 – 2020 to be carried back 5 years and makes other changes to help cash-strapped corporations and flow-through business owners.

AMT Credit Acceleration

- In 2017, Congress repealed the Corporate Alternative Minimum Tax, which operated in parallel with the regular tax system.
- The CARES Act accelerates the refund of AMT credits into 2019 (or even faster into 2018), a potential way to increase liquidity of affected companies.

More favorable rules on interest expense

- In 2017, Congress limited the amount of net business interest expense that a company could deduct.
- The CARES Act relaxes these rules in two ways that may help companies that are or may soon become highly leveraged.

Charitable contributions

- For corporations able to make substantial charitable deductions in 2020, the CARES Act increases the limits on deductions from 10% of a corporation's taxable income to 25% and from 15% to 25% for certain food donations.

Expensing of qualified improvement property

- In 2017, due to a drafting error, Congress excluded certain retail, restaurant and leasehold improvement costs (e.g., remodeling of hotels, retail establishments, and restaurants) from full expensing which was allowed for most other capital expenditures.
- The CARES Act fixes this error, the effect of which may be to allow companies that incurred these costs in 2018 and 2019 to amend their tax returns for those years to apply for refunds of overpaid taxes.

AMT Refundable Credit

- The TCJA repealed the corporate alternative minimum tax (AMT) but, through new section 53(e), enabled corporations to recover previously generated AMT credits against regular tax (or, if in excess of regular tax, as refundable credits) after 2017 and before 2022.
  - The CARES Act generally would enable corporations to accelerate any remaining AMT credits they have not yet utilized into 2019.
  - Provides a mechanism by which a taxpayer can elect to take the entire remaining refundable credit amount in 2018.
- Section 2304(d) of the CARES Act provides special rules allowing a taxpayer to file an application for a tentative refund of any amount for which a refund is due by reason of an election under section 53(e)(5).
  - The application (Form 1139) must be filed prior to December 31, 2020 in the form and manner prescribed by the Secretary.
  - Within 90 days of filing, the IRS is to review the application, determine the amount of overpayment, and apply, credit, or refund the overpayment.

Net Operating Loss (NOL) Rules

- Carryback – NOLs generated in tax years beginning after December 31, 2017 and before January 1, 2021 (i.e., 2018, 2019, and 2020 losses) can be carried back to the preceding 5 taxable years.
  - TI Limitation – Suspends the TCJA 80% taxable income limitation for NOLs generated in tax years beginning after December 31, 2017 and before January 1, 2021.
    - The 80% taxable income limitation remains in place for taxable years beginning after December 31, 2020.
- Special rule in the case of an NOL arising in taxable year beginning before January 1, 2018, and ending after December 31, 2017. Pursuant to section 2302(d)(4) of the CARES Act, an application under section 6411(a) for a “tentative refund” with respect to the carryback of such an NOL can be made within 120 days after the date of the enactment of the CARES Act.

Employment Tax Provisions Overview

- HR 6201 – payroll credit for qualified paid family leave and sick leave
- CARES Act:
  - Advance Refunding of Credits (Sec.3606)
  - Employee Retention Credit for Employers Subject to Closure Due to COVID-19 (Sec. 2301)
  - Delay of Payment of Employer Payroll Taxes (Sec. 2302)

H.R. 6201 – Payroll Tax Credit

- Payroll tax credits provided for under H.R. 6201 apply ***only*** to employers that are subject to the paid family leave and paid sick leave requirements of H.R. 6201 and the CARES Act. Employers who are not subject to these requirements are not entitled to payroll tax credits.
- **Employers should consult with legal counsel** on whether the employer is subject to the required paid family leave and paid sick leave requirements of H.R. 6201, including any limitations imposed under the CARES Act.
- The paid leave and family and sick provisions under H.R. 6201 may not apply to all employers based on applicable labor laws:
  - The paid family leave provided under Division C of H.R. 6201 applies to employers with fewer than 500 employees, with possible exemptions for certain health care providers and first responders and businesses with ***fewer*** than 50 employees.
  - The paid sick leave provided under Division E of H.R. 6201 applies to 1) a private entity employer with ***fewer*** than 500 employees and 2) a public agency (e.g., government) and any entity that is not a private entity or individual with more than one employee.
- **CARES Act (Section 3606) allows for advance refunding of credits of qualified paid family and sick leave wages**

The CARES Act: Advance Refunding of Credits (Sec. 3606)

Overview

- Payroll credits related to the payment of qualified paid family and sick leave ("qualified wages") are available under H.R. 6201 can be **advanced to employers** based on the anticipated amount of the credit
  - Calculated through the end of the quarter
- Any **penalties** for failure to make deposits for the employer portion of Social Security tax (6.2%) **will be waived** if the failure was due to anticipation of the credits
  - No mention of penalties for employer portion of Medicare tax (1.45%)
- Employers should monitor the release of forms and instructions that may be used to implement the tax credit advance

The CARES Act: Employee Retention Credit for Employers Subject to Closure Due to COVID-19 (Sec. 2301)

Overview

1. Determine if company is an eligible employer → **2. Determine if company paid qualified wages** → **3. Calculate the amount of the credit** → **4. Claim the credit**

The CARES Act: Employee Retention Credit for Employers Subject to Closure Due to COVID-19 (Sec. 2301)

1. Determine if company is an eligible employer

- Eligible employer includes employer who either
  a) Fully or partially **suspended operations** due to governmental orders related to the coronavirus, or
  b) Experienced a **significant decline in business**
     – Gross receipts of the business in a given quarter are < 50% of receipts from the same quarter in the prior year
     – Business will remain eligible until reaching 80%+ of receipts from prior calendar year
- Employers are no longer entitled to the employee retention credit once the employer receives a Paycheck Protection Program SBA loan. (Note: the employer would remain eligible for the payroll credit for sick or family leave under the Family First Coronavirus Response Act.).

1. Determine if company is an eligible employer → 2. Determine if company paid qualified wages → 3. Calculate the amount of the credit → 4. Claim the credit

The CARES Act: Employee Retention Credit for Employers Subject to Closure Due to COVID-19 (Sec. 2301)

2. Determine if company paid qualified wages

- Determine if the employer averaged more than 100 full-time employees during 2019. Aggregate employees and treat the company as a "single employer" based on rules in IRC 52(a)/(b) and 414(m)/(o).
  - If > 100 employees: wages limited to wages paid to employees who are **not providing services**
  - If 100 or fewer employees: **all wages** are included
- Includes wages paid March 13, 2020 to December 31, 2020
- Add qualified health plan expenses
- Exclude wages which have been taken into account for purposes of paid sick or family leave under H.R. 6201
- Qualified wages limited to **$10,000 per employee**

1. Determine if company is an eligible employer → **2. Determine if company paid qualified wages** → **3. Calculate the amount of the credit** → **4. Claim the credit**

The CARES Act: Employee Retention Credit for Employers Subject to Closure Due to COVID-19 (Sec. 2301)

3. Calculate the amount of the credit

- Credit is equal to **50% of qualified wages** paid
- Thus, maximum amount of the credit per employee is **$5,000** ($10,000 maximum qualified wages times 50%)

1. Determine if company is an eligible employer → **2. Determine if company paid qualified wages** → **3. Calculate the amount of the credit** → **4. Claim the credit**

The CARES Act: Employee Retention Credit for Employers Subject to Closure Due to COVID-19 (Sec. 2301)

4. Claim the credit

- Credit is claimed on a quarterly basis against the **employer portion of social security tax** (6.2%) on Form 941
- Any credit in excess of the social security liability for the quarter is **refundable**
- Deductible salaries or wages paid for the taxable year must be reduced by the amount of the retention credit claimed
- IRS FAQs and Form 7200, *Advance Payment of Employer Credits due to COVID-19* – key takeaways
  - Applies for employee retention credits and H.R. 6201 credits for paid sick and family leave
  - Credits can be used against employer deposits required for:
    - Federal income tax withheld from employees
    - Employee and employer share of Social Security and Medicare taxes
- Employers should continue to monitor the release of forms and instructions that may be used to implement the tax credit advance

1. Determine if company is an eligible employer → **2. Determine if company paid qualified wages** → **3. Calculate the amount of the credit** → **4. Claim the credit**

The CARES Act: Delay of Payment of Employer Payroll Taxes (Sec. 2302)

Overview

- Employers may defer the **employer portion of social security tax** (6.2%) due from the effective date of the Act through December 31, 2020
- Employers may consider applicable payroll tax credits, including retention credits in the deferral calculation
- Any payments deferred will be due as follows:
  - 50% due by December 31, **2021**, and
  - the remaining 50% due by December 31, **2022**
- Employers are no longer eligible to delay payment of employer payroll taxes if indebtedness is forgiven with respect to a Paycheck Protection Program SBA Loan.

Emerging ASC 740 Issues

- Valuation Allowance
- AETR
- Section 163(j) Business Interest Limitations
- NOLs
- Impairments
- Indefinite Reinvestment (APB 23)

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