CARES Act Analysis

By: Brandon Pratt, CPA, Tax Officer

On March 27, Congress passed the Coronavirus Aid, Relief, and Economic Security (CARES) Act. This legislation provides financial aid for individuals and businesses in response to the COVID-19 pandemic. The following document provides key points and analysis of the CARES Act and how it will assist individuals and businesses.

Individuals

Personal Tax

Recovery Rebates for Individuals

Key Points:

- The rebate is the advance of a refundable credit that will be claimed on the 2020 tax return
- The credit amount is $1,200 per individual, $2,400 for married filing joint taxpayers, plus $500 for each qualifying child
- Qualified children include children who qualify for the existing child tax credit (generally, dependent children under age 17)
- Individual taxpayers with Adjusted Gross Income of $75,000 or less receive the full credit. Married Filing Joint taxpayers with Adjusted Gross Income of $150,000 or less receive the full credit. The credit is phased out for higher income earners.
- Taxpayers who are NOT eligible for the credit include:
  - Nonresident aliens
  - Qualified dependents of another taxpayer
  - Estates and trusts
- No credit will be given after December 31, 2020
- Income eligibility will be determined based on the taxpayer's Adjusted Gross Income on their 2019 tax return. If the taxpayer has not yet filed their 2019 tax return, Adjusted Gross Income from their 2018 return will be substituted.
- No credit will be allowed for taxpayers who do not include valid identification numbers for each taxpayer and qualified child on their tax return. (Special rules apply for adopted children and military members filing married filing joint.)

Example 1:

Single Taxpayer, no qualified children, with Adjusted Gross Income of $60,000 will receive a $1,200 advanced refund.

Example 2:

Married Filing Joint Taxpayers, three qualified children, with Adjusted Gross Income of $140,000 will receive a $3,900 advanced refund.

Example 3:

Married Filing Joint Taxpayers, three qualified children, with Adjusted Gross Income of $190,000 will receive a $1,900 advanced refund. ($3,900 – ($190,000 - $150,000 = $40,000 x 5% = $2,000) = $1,900)

Example 4:

Married Filing Joint Taxpayers, three qualified children, with Adjusted Gross Income of $228,001 will receive no advanced refund because they are fully phased out based on their Adjusted Gross Income. ($3,900 – ($228,001 - $150,000 = $78,001 x 5% = $3,900.05) = $0)

Qualified Charitable Contributions

Key Points:

- An above the line deduction of up to $300 for qualified charitable contributions made by taxpayers not electing to itemize deductions on their taxable year starting in 2020
- Qualified charitable contributions are:
  - Made in cash
  - Deductible under section 170 to an organization other than “supporting organizations” or Donor Advised Fund contributions
- Individuals making qualified contributions shall be allowed a deduction limited to the excess of their 2020 Adjusted Gross Income over other non-qualified charitable contribution deductions
- Corporations making qualified contributions shall be allowed a deduction limited to 25% of the taxpayer’s taxable income over other non-qualified charitable contribution deductions
- Important: Excess contributions will not carryforward at the increased limit. Individual excess amounts will be subject to the 60% of Adjusted Gross Income limitation. Corporate excess amounts will be subject to the 10% of Taxable Income limitation.

IRA Provisions

Special Rules for Coronavirus-related Retirement Distributions

Key Points:

- Individuals impacted in one of the following ways (based on their own certification) are eligible for special relief relating to distributions from qualified retirement plans and IRAs:
  - The individual (or their spouse or dependent) is diagnosed with SARS-CoV-2 or COVID-19 by a CDC approved test; OR
  - The individual experiences adverse financial consequences as a result of being quarantined, furloughed, laid off, having work hours reduced, or is unable to work due to a lack of childcare. Note: individuals who continue to work full-time on a reduced salary are not eligible.
- Relief includes:
  - The 10% early withdrawal penalty is waived for up to $100,000 (total from all retirement accounts combined) in distributions taken during calendar year 2020, and all such distributions are exempt from tax withholding.
  - Any distribution amount required to be included in taxable income from coronavirus-related distributions shall be included ratably over three taxable years beginning with the year of distribution.
  - Distributions may be repaid at any time up to three years after the date of distribution by making one or more repayment contribution(s) to any eligible retirement account to which the individual may make a rollover contribution. All such repayment contributions will be permissible rollover contributions.
  - The usual 60-day rollover period and one-IRA-rollover-per-year rules do not apply to such repayment contributions. All repayment contributions would reduce income otherwise required to be recognized.

    - Loan limits from qualified plans are increased to $100,000 (up to 100% of the present value of the participant's benefit under the plan) during the first 180 days after enactment of the CARES Act. For outstanding loans to plan participants, any loan repayment due between now and December 31, 2020 is delayed for one year. Additionally, any subsequent repayment shall be appropriately adjusted to reflect the delay in due date.
- Eligible retirement plans include IRAs, individual retirement annuities, qualified trusts, annuity plans described in §403(a), eligible deferred compensation plans described in §457(b), and annuity contracts described in §403(b).
- Retirement plan administrators and IRA trustees/custodians may rely on an individual's certification to document eligibility for coronavirus-related relief.

Waiver of Required Minimum Distribution Rules for calendar year 2020

Key Points:

- Required Minimum Distribution rules for the 2020 calendar year are waived for the following:
    - Defined contribution plans described in §403(a) or §403(b)
    - Eligible deferred compensation plans described in §457(b), restricted to plans maintained by employers described in §457(e)(1)(A)
    - Individual Retirement Plans, including IRAs
- Distributions required due to age attainment in 2019, are waived for 2020.
- Calendar year 2020 does not count toward distributions subject to the so-called "5-year rule."

Unemployment Benefits

Emergency Increase in Unemployment Compensation Benefits

Key Points:

- Eligible individuals will receive the regular unemployment compensation plus an additional $600 per each eligible week.
- To receive the emergency increase, individuals must be otherwise entitled under State law to receive regular compensation.
- Additional $600/week payments will begin after the date of agreement between State and Federal governments and will end on or before July 31, 2020.
- Fine print: Each State must enter into agreement with the Federal Government for its eligible residents to qualify for the Emergency Increase.

Pandemic Emergency Unemployment Compensation

Key Points:

- Provides unemployment compensation to individuals who have exhausted all rights to regular unemployment compensation with respect to a benefit year within a State and are able, available and actively seeking work.
- A qualified individuals weekly benefit amount is the amount otherwise payable as regular unemployment compensation plus the $600 emergency increase.
- Qualified individuals must register with the State agency and satisfy the "actively seeking work" standards prescribed by the State.
- Fine print: State must enter into agreement with Federal Government for its eligible individuals to qualify for Emergency Increase. There is no cost to the state so presumably they will all participate.

Businesses

Employer

Exclusion for Certain Employer Payment of Student Loans

Key Points:

- Employer payments of employee student loan principal and interest balances made between enactment and January 1, 2021 qualify as “education assistance” and is excludable from the employee’s income up to the $5,250 maximum exclusion.
- Any interest paid by the employer is not deductible as student loan interest by the employee.

Employee Retention Credit for Employers Subject to Closure Due to COVID-19

Key Points:

- Eligible employers shall be allowed a credit against applicable employment taxes for each calendar quarter an amount equal to 50% of qualified wages.
- Each employee’s qualified wages are capped at $10,000 per quarter.
- Any credit in excess of applicable payroll taxes for a quarter shall be treated as an overpayment that shall be refunded.
- Applicable employment taxes include the 6.2% employer portion of FICA.
- Eligible employer means:
    - Any employer carrying on a trade or business in 2020 whose operations are fully or partially suspended during the calendar quarter due to governmental orders limiting commerce, travel, or group meetings due to COVID-19, or;
    - Employers experiencing a greater than 50% reduction in gross receipts compared to the same calendar quarter 2019. Such businesses are no longer eligible employers the first calendar quarter in which gross receipts are greater than 80% of the gross receipts of the same calendar quarter in the prior year.
- Tax-exempt organizations qualify as an eligible employer if they meet the suspension of operations or reduction in gross receipts test provided for trade or businesses.
- Qualified wage determination depends on the employer’s number of full-time equivalents:
    - Employers with more than 100 full-time equivalents include wages paid to an employee not providing services due to full or partial shutdown or “significant decline” in gross receipts. Employee wages cannot exceed what the employee would have been paid for working an equivalent duration during the 30 days immediately preceding such period.
    - Employers with less than 100 full-time equivalents affected by full or partial shutdown include all wages paid with respect to an employee during any qualifying calendar quarter.
    - Employers with less than 100 full-time equivalents affected by “significant decline” in gross receipts include wages paid to an employee during the calendar quarter of significant decline.
- Qualified wages include amounts paid for qualified health plan expenses related to employees who have qualified wages, if the health plan expenses are excluded from gross income of employees.
- Applies to wages paid after March 12, 2020 and before January 1, 2021.

Delay of Payment of Employer Payroll Taxes- FICA, not MEDICARE

Key Points:

- Employer FICA tax (6.2%) due between enactment and before January 1, 2021 is allowed deferred until the applicable date.

- The two applicable dates are December 31, 2021 and December 31, 2022. 50% of the deferred amount is due by December 31, 2021. The remaining deferred amount is due by the second applicable date of December 31, 2022.
- An employer shall be treated as having timely made all deposits of applicable employment taxes if all such deposits are made no later than the applicable date.

Business/Corporate

Modification of Net Operating Losses

Key Points:

- Losses arising in 2018, 2019 and 2020 shall be a net operating loss carryback to each of the 5 taxable years preceding the taxable year of such loss.
    - i.e. a net operating loss generated in 2018 is carried back to the 2013 – 2017 tax years.
    - There was no federal election to forgo carryback in 2018 or 2019, therefore, any taxpayer with a net operating loss in these years should be allowed applicable carryback.
- Tax years 2018, 2019, and 2020 are no longer subject to the 80% of taxable income limitation for net operating loss deductions. Net operating loss deduction can now offset the full amount of taxable income before the section 199A and 250 deductions.
- The 80% taxable income limitation still applies to taxable years beginning after December 31, 2020.

Modification of Excess Business Loss Limitation applicable to Non-Corporate Taxpayers

Key Points:

- The Excess Business Loss Limitation no longer applies to non-corporate taxpayers for tax years beginning before January 1, 2021.
- Importantly, the effective date of this change applies to tax years beginning after December 31, 2017. This means taxpayers that were previously subject to Excess Business Loss Rules that have not utilized the net operating loss carryforward amount should consider amending their return(s) to allow full business loss, which can offset other ordinary income during the current year or be carried back 5 years to available taxable income.
- Amends language defining the calculation of Excess Business Loss to exclude any deductions, gross income, or gains attributable to any trade or business of performing services as employee. i.e. W-2 wages are not included in the calculation of trade or business income for the purpose of the Excess Business Loss Limitation calculation.
- Technical correction regarding inclusion of capital gains and losses provides that capital losses from sales/exchanges of capital assets shall not be included in the calculation of total losses under the calculation. Capital gains are limited to the lesser of net capital gains attributable to a trade or business or the taxpayer’s capital gain net income for the year.

Modification of Corporate AMT Credit Refundability

Key Points:

- Accelerates timeline for 100% refundability of prior year AMT Credit Carryforward to 2019.
- There is a special election to claim entire refundable credit in 2018, rather than 2019.
- Corporations can utilize form 1139 to claim the refund associated with AMT Credit Refundability, if filed prior to December 31, 2020 and the claim will be verified under the same accelerated review period (90 days from submission) as other Corporate Application for Tentative Refund submissions.

Modification of Limitation of Business Interest under IRC §163(j)
Key Points:

- Provides an increase in applicable percentage to 50% from 30% for tax years beginning in 2019 and 2020.
- This increase in applicable percentage does not apply to partnerships for taxable years beginning in 2019, unless a partner elects out of the favorable splitting of any 2019 interest limitation described next.
- Excess business interest allocated to a partner for any taxable year beginning in 2019 will be split as follows:
    - 50% of such business interest shall be treated as business interest paid or accrued by the taxpayer in the partner's first taxable year beginning in 2020 and is not subject to the limitation provided by paragraph (1) of IRC §163(j). i.e. this interest will be deductible in 2020 regardless of excess business income.
    - 50% of such business interest shall be subject to the limitation of IRC §163(j) in the same manner as any other excess business interest so allocated.
- Taxpayers may elect to use 2019 adjusted taxable income for the purpose of their IRC §163(j) calculation for any taxable year beginning in 2020. This election will be made at the partnership level, rather than the partner level. Special rules apply to short tax years.

Depreciation

Qualified Improvement Property Technical Corrections
Key Points:

- Added Qualified Improvement Property to the MACRS 15-year class and 20-year ADS class.
- Allows Qualified Improvement Property to be bonus eligible under section 168(k).
- Retroactively effective as if included in Tax Cuts and Jobs Act of 2017.
- Taxpayers can amend 2017, 2018 and (2019 if already filed) returns to claim 100% bonus depreciation on Qualified Improvement Property.
- Amending prior years would allow any loss generated in that prior year to then be carried back 5 years from the loss year.
- Alternatively, if a net operating loss is not created in prior years or many K-1s are issued, taxpayers could file a change in method of accounting (form 3115) to claim the bonus deprecation deduction for all prior years in the current tax year. This would forgo any interest on prior year refunds but would be administratively more feasible in certain situations. Also, any carryforwards utilized after the 2020 tax year will be subject to the 80% taxable income limitation.

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