

CARES Act: Tax-Related Provisions

March 27, 2020

The Coronavirus Aid, Relief, and Economic Security Act (CARES Act) includes provisions to provide employment tax credits and relief to businesses and to reduce or eliminate the restrictions on the use of losses or deductions. There are also significant benefits for charitable contributions and the widely reported possibility of a direct payment to taxpayers.

Paycheck Protection Program Loans

A significant feature of the CARES Act is the loan program known as the Paycheck Protection Program. Applicants can receive loan proceeds to be used for the payment of compensation, commissions, health care costs, interest on debt obligations, rent and utilities as well as other traditionally allowable uses. Loan proceeds expended for those purposes during the 8 week period following the origination of the loan may be forgiven upon application by the borrower.

Ordinarily, loan forgiveness is treated as income for federal income tax purposes. But, the forgiveness of a Paycheck Protection Program loan will be excluded from gross income for tax purposes.

Participation in the Paycheck Protection Program may affect the availability of the employment tax benefits discussed below.

Employment Tax Benefits

Postpone Payment of Employer's Share of Social Security Tax. Employers will be able to delay the payment of the employer portion of the Social Security payroll tax until year-end. Payment of the hospital insurance ("Medicare") tax is not postponed. The postponed amount would be paid equally over the two succeeding years. Half of self-employment tax would be similarly postponed and paid.

If the employer has loan forgiveness under the Paycheck Protection Program, the provision permitting the employer to postpone the payment does not apply.

Credit for Employment Taxes. For employers other than those who participate in the Paycheck Protection Program, a credit against Social Security taxes is available for employers whose operations are fully or partially suspended due to a governmental order limiting commerce, travel or group meetings or for employers whose gross receipts are less than half of the gross receipts for the comparable calendar quarter of 2019 (and continuing until the calendar quarter after gross receipts reach 80% of 2019 gross receipts for the same calendar quarter).

For employers with more than 100 full-time employees, wages paid to an employee who is not providing services qualify for the credit (although the amount of such wages is limited to \$10,000 per calendar quarter). For employers with 100 or fewer full-time employees, all wages paid during the suspension qualify and as do wages paid during the calendar quarters qualifying due to the reduction in gross receipts.

The credit amount is limited to 50% of the qualifying wages. The employment taxes against which the credit may be taken are first reduced by the credits against those taxes allowed under the Families First Coronavirus Response Act (by reason of paid sick leave or paid family leave).

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Some clarification on the refundability of a credit amount in excess of the employment tax liability may be needed. The credit applies only to wages paid after March 12, 2020 and before January 1, 2021.

Employers participating in the Paycheck Protection Program are not eligible for the credit.

Changes to Restrictions on the Use of Losses and Deductions

NOL Carryback. The 2017 Tax Cuts and Jobs Act (TJCA) eliminated the ability of firms to “carry-back” losses. Under the CARES Act, businesses will be able to carryback a net operating loss from 2018, 2019, or 2020 for five years.

NOL Limitation. The TJCA limited the use of a net operating loss carryover to 80% of income for a business. That limitation will not apply to losses for taxable years beginning before January 1, 2021 so that NOL carryovers and carrybacks can eliminate taxable income without limitation.

Business Loss Limitations applicable to Individuals, Trusts and Estates. The TJCA provision limiting the business losses in excess of business income to \$250,000 (\$500,000 in the case of a joint return) will not apply until years beginning after December 31, 2020. Taxpayers affected by this provision for 2018 or 2019 could submit an amended return.

Minimum Tax Credit Limitation. The TCJA eliminated the corporate alternative minimum tax (AMT). Payment of the corporate AMT generated credit against future payments. When the corporate AMT was repealed, these credits were made refundable over the next several years. The CARES Act allows firms to accelerate recovery of these credits.

Business Interest Deduction Limitation. The TJCA limited the deductibility of interest to 30 percent of a firm’s adjusted taxable income. The CARES Act would relax that limitation to 50 percent for tax years beginning in 2019 and 2020 and allow the taxpayer to use the 2019 adjusted taxable income.

Benefit Plan Provisions

Waiver of 10% Early Withdrawal Penalty. The CARES Act waives the 10 percent early withdrawal penalty for qualifying individuals, who may withdraw up to \$100,000 from retirement accounts without facing penalty. A qualifying individual is one who has been diagnosed as having SARS or COVID-19, whose spouse or dependent is so diagnosed or who has experienced adverse financial consequences as a result of being quarantined, furloughed, laid off or otherwise affected by those diseases. The CARES Act provides for flexible tax treatment of that withdrawal and allows taxpayers to restore any withdrawn funds without tax to the extent of restoration within three years of the withdrawal.

Loans From Retirement Plans. The permitted amount of loans to qualifying individuals was increased to \$100,000 and the due date for existing loans was extended.

Required Minimum Distributions for 2020. A waiver of the required minimum distribution rules for distributions otherwise required to be made during 2020 is available.

Student Loan Payments. An employer’s payment of an employee’s student loan during 2020 will be considered to be “educational assistance” that may be excluded from income under Code Section 127.

Charitable Contribution Provisions

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“Above-the-Line” Charitable Contribution Deduction. Individuals who do not itemize deductions can claim a \$300 deduction for cash contributions made to public charities (other than supporting organizations or donor advised funds).

Percentage Limitation Eliminated For Cash Gifts Made in 2020. The percentage limitation on deductibility of gifts by individuals to public charities is eliminated in 2020 for cash gifts. But, this benefit does not apply to gifts to donor advised funds or supporting organizations.

Increase in Limitation for Contributions by Corporations. The percentage limitation on deductibility of gifts by corporations to public charities is increased to 25% in 2020 for cash gifts.

Increase in Limitation for Gift of Food Inventory. The limitation on the deduction for charitable contributions of food was increased from 15% of income to 25% of income.

Payments To Individuals

Direct Payments to Individuals. Based on 2019 income tax filings (if available), the CARES Act provides direct payments to individuals and families. For individuals with incomes up to \$75,000, the Act provides a payment of \$1,200 (\$2,400 for a joint return) plus an additional \$500 per child under age 17. The payment is phased out at a rate of 5% of income in excess of \$150,000 for a couple filing a joint return, \$112,500 for a head of household and \$75,000 for others. People who can be claimed as a dependent are not eligible for the benefit. 2018 income tax information can be used where the 2019 returns have not yet been filed.

Additional Information

This is part of a series of our **COVID-19 alerts** providing clients with practical advice on measures they can take to navigate through these troubled times. Please contact your Miller Canfield attorney to discuss your questions about the CARES Act.

This information is based on the facts and guidance available at the time of publication, and may be subject to change.