



THE CARES ACT

Tax Provisions; A Preliminary Analysis

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INTRODUCTION

On March 27, 2020, President Trump signed into law the Coronavirus Aid, Relief and Economic Security (CARES) Act, which provides relief to taxpayers affected by the novel coronavirus (COVID-19). The CARES Act provides relief for individuals, businesses, governments, the health care system, education, non-profits, and distressed industries.

This document is provided to outline in detail some of the tax provisions.

State and Local Tax (SALT) Implications:

Implications for state purposes of the CARES Act federal tax provisions discussed on the following pages will depend on a specific state's conformity method. "Rolling or Current Conformity" states adopt and conform to all changes in the Internal Revenue Code (IRC) as passed by Congress, unless a specific state passes separate legislation which decouples from such federal provisions. "Fixed-Date or Static Conformity" states adopt and conform to the Internal Revenue Code as of a specific date. Still, other states may take a "selective" approach to federal conformity by adopting only certain provisions or certain provisions as of certain dates. These states must pass legislation to act on and incorporate subsequent federal changes into state statute by either adopting or modifying from such federal changes.

This document addresses only the federal tax provisions of the CARES Act enacted on March 27, 2020. The conformity and non-conformity state questions add another layer of complexity in applying the various tax provisions of the CARES Act. States are constantly updating and changing their current legislation to either adopt to federal changes as a result of COVID-19, or issuing legislation that modifies from it. Careful consideration must be given as to the state impact of these changes, in addition to the federal impact of all years involved.

Please consult your tax professional to review your specific situation and the implications occurring at both the federal and state levels as additional information and guidance is provided by tax authorities.

FEDERAL TAX FILINGS AND PAYMENTS

Due to the COVID-19 Presidential Emergency Declaration, Treasury and the IRS have issued recent guidance related to the 2019 and specific 2020 federal tax filing due dates and payment deadlines.

- Notice 2020-18 superseding Notice 2018-17 defers normal due date of federal income tax returns and federal income tax payments normally due on April 15, 2020, until July 15, 2020.
 - Applies only to federal income tax returns and payments, including Section 965(h) and SE income tax, and
 - Federal estimated income tax and SE income tax estimates due on April 15th in 2020.
- Taxpayers affected by the coronavirus will not have to file an extension to qualify for the automatic 3-month deferral relief.
 - Includes forms and schedules attached to and filed with such federal covered return.
- There is no limitation or dollar threshold on income or taxes due to qualify for relief.
- Does not apply to:
 - Other types of federal taxes such as excise taxes, or
 - Federal informational returns, nor
 - Returns that were due on March 16, 2020, such as Form 1065 and 1120-S.

During deferral period April 15, 2020 – July 15, 2020:

- No interest or penalties will be charged during deferral period for payments due April 15, 2020, and
- Accruals of interest and penalties will begin to accrue on July 16, 2020.

INDIVIDUAL PROVISIONS

RECOVERY REBATES: The bill provides payments to taxpayers — “recovery rebates” — which are being treated as advance refunds of a 2020 tax credit.

Under this provision, individuals will receive a tax credit of:

Taxpayer	Advanced Credit	Phase Out Limitation	Complete Phase Out of Credit
Single	\$1,200	\$75,000	\$99,000
Head of Household	\$1,200	\$112,500	\$136,500
Married Filing Joint	\$2,400	\$150,000	\$198,000
Each Qualifying Child	\$500	Included in above	Included in above

- The credit is reduced (not below zero) by 5% of adjusted gross income that exceeds the applicable phase out limitation (or by \$5 for each \$100 in excess of the phase out limitation).
- The credit is not available to:
 - Nonresident aliens,
 - Individuals who can be claimed as a dependent by another taxpayer,
 - Estates and trusts.
- Qualifying child, as defined by dependency exemption, who hasn’t attained age 17.
- Qualified individuals must have a Social Security Number.

- No actions required for the vast majority of individuals to receive a rebate:
 - IRS will use 2019, or 2018 returns, or 2019 Forms SSA-1099 or RRB-1099.
 - If none of these are available, consider filing a nil 2019 individual income tax return.
- Taxpayers will reduce the amount of the credit available on their 2020 tax return by the amount of the advance refund payment they receive.
- No refund or credit will be made or allowed after December 31, 2020.
- Will be paid electronically to direct deposit accounts utilized on or after Jan 1, 2018, and
- Will send checks through the mail to those who do not utilize direct deposit.

CHARITABLE CONTRIBUTIONS: Allowance of partial above the line deduction for charitable contributions and temporary revised limitations on charitable contributions during 2020. More information will be coming soon from the IRS.

An *above the line deduction* for qualified charitable contributions up to \$300 will be allowed.

- Available only for taxpayers not electing to itemize deductions.
- Eligible taxable years beginning in 2020 (taxable years beginning after December 31, 2019).
- Qualified contributions made in cash.
- Recipients do not include exempt organizations that support other charities (further described in IRC Sec 509(a)(3), or donor-advised funds).
- Does not include carryover contributions eligible for deduction in the current year return.

For taxpayers who itemize deductions, it provides that qualified contributions are disregarded in applying the 60% adjusted gross income limitation on cash contributions, and the carryover of excess contributions.

- Eligible taxable years beginning in 2020 (taxable years beginning after December 31, 2019).
- Qualified contributions are donations made to a 501(c)(3) and certain other charitable organizations (further described in IRC Sec 170(b)(1)(A)).
- Recipients do not include exempt organizations that support other charities (further described in IRC Sec 509(a)(3), or donor-advised funds).
- Does not include carryover contributions eligible for deduction in the current year return.

RETIREMENT PLANS: The CARES Act provides temporary relief and waivers for retirement accounts to help ease the financial burdens caused by COVID-19.

For provisions to apply, there must be a coronavirus-related purpose – a “coronavirus-related distribution” is defined as any distribution from an eligible retirement plan made on or before January 1, 2020, and before December 31, 2020, to an individual:

- Who is diagnosed with COVID-19 with a test approved by the CDC,
- Whose spouse or dependent is diagnosed with COVID-19, or
- Who experiences adverse financial consequences from being quarantined, furloughed, laid-off, reduced work hours, being unable to work due to lack of child care, closing or reducing hours of a business, or other factors identified and due to the COVID-19 pandemic.

Highlights of various relief provisions:

- **2019 Contributions to Eligible Retirement Accounts**
 - Treasury's extension of the 2019 tax return filing deadline has also extended the deadline to make the 2019 IRA Contributions from April 15th to July 15, 2020. A Historical first time ever extension.
 - Applies to individual and employer contributions.
 - Contributions to an H S A or Archer M S A can be made through July 15, 2020.
- **Withdrawals/Distributions from Eligible Retirement Accounts (2020 calendar year)**
 - 10% excise tax on Early Withdrawal Distributions (prior to age 59 ½) is waived for coronavirus-related purposes.
 - Distributions may not exceed \$100,000 in aggregate for any taxable year.
 - Election available to spread income over a 3-year period beginning with 2020.
 - May avoid income recognition by repaying within three years of receipt.
 - Can be contributed back at any time during the 3-year period and exclude from income recognition.
 - Required Minimum Distributions are waived for 2020 for certain defined contribution plans and IRAs.
 - Generally, RMDs required starting at age 72 – Secure Act increased RMD age to 72 for those who turn 70 ½ in 2020 or later.
 - RMD waiver also applies to 2019 RMDs normally due by April 1, 2020. 70 ½ age applies for 2019.
- **Loans from Eligible Retirement Accounts**
 - The Act provides an increase from up to \$50,000 to a \$100,000 limit on loans from qualified plans limited to the present value of the non-forfeitable accrued benefit of the employee under the plan.
 - Loan limit is increased for a 180-day period starting on the date of enactment of the CARES Act.
 - Repayment due dates otherwise due between the enactment of the Act and December 31, 2020, will be delayed for one year. Subsequent repayments adjusted for delay and interest is accrued.

BUSINESS PROVISIONS

EXCESS BUSINESS LOSSES: The CARES Act modifies the Limitations of Excess Business Losses of Non-corporate Taxpayers under Section 461(l).

- Removes the \$250K/\$500K business loss limitations for non-corporate taxpayers using losses from trades or businesses in which they participate.
- Modifications are made retroactively – applies to tax years beginning after December 31, 2017.
- Applies to losses arising in 2018, 2019 and 2020.
New effective date for Section 461(l) excess business loss limitation will apply for tax years beginning after December 31, 2020, and before January 1, 2026.

The Bill also includes technical corrections associated with the 2017 TCJA tax reform.

- Calculation now excludes items attributable to the trade or business of performing services as an employee.
- Section 172 NOL deductions and qualified business income (QBI) deductions under Section 199A are not taken into account in determining excess business losses.
- Deductions for losses from the sale or exchange of capital assets do not increase the limitation. Corrections did not address flowthrough interests related to business capital gains or losses on sale of such interests.

TAX OPPORTUNITY: Amend 2018 and 2019 returns that have been affected by the Section 461(l) limitation.

BUSINESS INTEREST LIMITATION: Temporarily amends the limitation on business interest expense deduction under Section 163(j) for the tax years beginning in 2019 and 2020.

- The deduction for business interest expense is limited to the sum of:
 - Business interest income,
 - 50% of adjusted taxable income (ATI) (increased from 30% of ATI), and
 - Floorplan financing interest expense.
- Special rules apply for short tax years.
- May elect to substitute 2019 ATI for 2020 ATI.
- Partnerships:
 - The 50% limitation applies only to tax years beginning in 2020.
 - Election not to use the increased limitation must be made at the partnership level.
 - A special rule:
 - Partners treat 50% of any excess business interest expense allocated to the partner in a tax year beginning in 2019 as paid or accrued in the partner's first tax year beginning in 2020,
 - With the remaining 50% subject to the default limitation based on allocated excess taxable income (or excess interest income pursuant to Prop. Reg. §1.163(j)-6(g)(2)(i)).
 - A partner may elect out of this special rule.

TAX OPPORTUNITY – Amend 2019 returns filed that were subject to the 30% limitation.

CHARITABLE CONTRIBUTIONS: The Act temporarily modifies the charitable contribution deduction limitation for Corporations. Corporate deduction limit increased from 10% of taxable income to 25% of taxable income for cash contributions.

- Deduction limit for food inventory increased from 15% to 25%.
- None of the increased limits apply to contributions to private foundations nor donor-advised funds.
- In regard to Partnerships and S Corporations, contribution limitation changes are applied on the partner or shareholder individual level.

NET OPERATING LOSSES: The CARES ACT includes several changes to the rules governing net operating losses (NOLs), including a five-year carryback of certain 2018, 2019 and 2020 losses and, temporarily, the ability to fully offset income.

- NOLs are carried back to the earliest tax years to which the loss may be carried, then to the next succeeding tax year.
- Irrevocable election to relinquish carryback period available – must be made by the due date, including extensions.
- Special rules apply to loss carryback treatments for life insurance companies – Section 172(b)(1)(D)(iii).
- REIT NOLs may not be carried back.
- Rules related to Section 965 transition tax years:
 - For NOLs carried back to a 965 inclusion year, the taxpayer is deemed to have made a Section 965(n) election to waive the use of the NOL against the transition tax inclusion. This is automatic with no opt-out option.
 - Affected taxpayers may choose a modified carryback method that skips over the 965 inclusion years.

Federal Net Operating Losses (NOLs) – Three Categories			
Generated NOLs in Tax Years:	Beginning on or before December 31, 2017	Beginning after December 31, 2017, and beginning before January 1, 2021	Beginning on or after January 1, 2021
Carryback Provisions	2-year carryback period	5-year carryback	No carryback, in general
Carryforward Provisions	20-year carryforward period	Indefinite carryforward	Indefinite carryforward
Offset to taxable income	100% offset allowed; AMT considerations	100% offset of taxable income prior to 2021; 80% offset limitation after 2020	80% of taxable income

The Bill also includes technical corrections associated with the 2017 TCJA tax reform.

- Correction provides that taxable income for purposes of applying the 80% NOL limitation is determined after reductions for pre-TCJA tax reform NOLs, and
- Taxable income for purposes of Section 172(a) is determined without regards to Section 199A qualified business income, and Section 250 foreign-derived intangible income (FDII) and global intangible low-taxed income (GILTI) deductions, and
- Fiscal year filers straddling the December 31, 2017 TCJA date may now carryback fiscal year losses generated in tax years ending after December 31, 2017. The 2-year carryback and 20-year carryforward apply.

Observations:

- 2018, 2019 and 2020 losses can be used against pre-2018 ordinary or capital gains that were taxed at rates up to 35% (higher tax rate years) compared to the current 21% corporate rate.

- 80% TCJA NOL limitation is temporarily suspended and the suspension is retroactive. Taxpayers affected should consider the impact of such suspension.
- Taxpayers with significant income capacity in carryback years that are anticipating losses going into 2021 may want to change their accounting year-end.
 - For example, taxpayers may offset a portion of 2021 losses with a year that begins prior to January 1, 2021.
 - A fiscal year tax period beginning December 1, 2020, and ending November 30, 2021.
- No modifications were made to corporate capital loss rules, which continue to qualify for the 3-year carryback and 5-year carryforward provisions.
- Disaster relief provisions under Section 165(i) can allow you to shift 2020 losses into the preceding 2019 tax year.
- Various re-calculations of taxable income limitations in a carryback year will be necessary for items such as Section 163(j) and Section 250(a)(2) limitation on GILTI / FDII deductions, for example, in years 2018 and 2019.

TAX OPPORTUNITY:

- Consider accounting method changes for 2019 and 2020 that defer revenue or accelerate deductions to increase an NOL.
- Consider reverse planning method changes for 2019 that defer deductions or accelerate revenue thereby generating greater losses in 2020 – a greater NOL carryback available.
- Amend returns to carryback NOL.

CORPORATE MINIMUM TAX CREDITS: The Act provides for acceleration of any remaining minimum credit refunds for prior year minimum tax liability of corporations under the pre-TCJA alternative minimum tax regime:

- Effective for taxable years beginning after December 31, 2017.
- Retroactively applies to the first taxable year of such corporation beginning in 2018.
- The bill now allows a 50% credit for 2018, and a 100% accelerated fully refundable credit can be claimed for 2019.
- Alternatively, corporations may elect to claim the fully refundable minimum tax credits in 2018:
 - Taxpayer may 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) of the Internal revenue Code of 1986.
 - Must be filed prior to December 31, 2020.
 - 90 days from the date the application is filed, Treasury will apply, credit or refund such overpayment.
- Special rules apply for consolidated groups.

Observations:

- Minimum tax credits (MTCs) fully utilized to offset regular tax for tax years beginning after 2017 may be due a refund with the temporary reinstatement of a 5-year NOL carryback period. An NOL

carryback may eliminate all or a portion of, for example, a 2018 federal income tax liability that was reduced by the MTCs.

- Interactions with limitation rules may create situations that negatively affect a corporation's ability to use MTCs.
- MTCs not claimed in either 2018 or 2019 appear to be forfeited.

TAX OPPORTUNITY – Amend to capture credits in 2018 or capture the remaining utilized portion of the minimum tax credit in 2019. However, see application for a tentative refund “quickie refund” alternative above.

QUALIFIED IMPROVEMENT PROPERTY (QIP): The CARES Act includes a technical correction to the 2017 TCJA, with respect to qualified improvement property that was an oversight in the original legislature resulting in unintended circumstances.

- Defined as any improvement ***made by the taxpayer***** to an interior portion of a nonresidential building provided that the improvement is placed in service after the date that the building was first placed in service by any person.
 - Includes common areas.
 - Does not include improvements related to the enlargement of a building, an elevator or escalator, or the internal structural framework of the building.
- Changes class life from 39-year property to 15-year property under the general depreciation system, and 40-year property to 20-year property under the alternative depreciation system.
 - 15-year QIP now eligible for bonus depreciation.
- Effective retroactively for assets placed in service after Dec. 31, 2017.
- Partnerships:
 - Federal tax rules relating to tax audits/refunds were substantially revised under the centralized partnership audit regime rules.
 - Effectuating the change can be more complicated if the partners were not able to or did not elect out of these rules.
 - In these instances, refund claims relating to partnership returns are obtained not through amended partnership returns, but instead, through filing an administrative adjustment request.

**** Important Note**: The Bill also adds the phrase “made by the taxpayer” to the definition of QIP as noted above in bold italics. The importance of this is that it appears to remove the benefit when a taxpayer buys a building and has a cost segregation study done to breakout the property that would previously have qualified as QIP, but for the newly added phrase, and then takes bonus on those improvements because these would not have been *made by the taxpayer* but by the previous owner.

TAX OPPORTUNITY – Depending on the filing status of the 2019 returns, there is an opportunity to amend the 2018 tax return, or file a Form 3115 Application for Change in Accounting Methods to capture the benefit of the technical correction.

SINGLE-EMPLOYER PLAN FUNDING: The Act provides single employer pension companies' additional time to meet their funding obligations.

- The Act changes the due date for the calendar year 2020 minimum required contributions.
 - The due date is extended to January 1, 2021.
- Delayed contribution must be increased by interest accrued on the obligation.
 - At the effective rate of interest for the plan, for the plan year that includes the payment date.
 - Between the original due date and the actual payment date.
- Act doesn't appear to extend the timing of the deduction for contributions. May want to consider making contributions earlier to be deductible in the tax year, including extensions.

****Important Note** - Plans under benefit restrictions as outlined in IRC §436 and ERISA §206(g) may elect to treat the plan's adjusted funding target attainment percentage for the last plan year ending before January 1, 2020, as the adjusted funding attainment target for plan years that include the 2020 calendar year.

DEFERRAL OF EMPLOYER PAYROLL TAXES: The delay of payment of employer payroll taxes will begin on the day the CARE Act is signed into law and will include the following:

- Employers receive 100% deferral of payroll taxes beginning on the day the CARES Act is signed into law and ends on December 31, 2020.
- Self-employed individuals will receive a 50% deferral of payroll taxes beginning on the day the CARES Act is signed into law and ends on December 31, 2020.
- Wages paid under the Families First Coronavirus Response Act (PL 115-97) are not eligible.
- Wages paid with Payroll Protection Plan (PPP) loan proceeds are not eligible.
- Deferred payroll taxes will be treated as timely deposited if:
 - 50% of the total deferred payroll tax balance as of December 31, 2020, is deposited by December 31, 2021.
 - 50% of the total deferred payroll tax balance is deposited by December 31, 2022.

EMPLOYEE RETENTION CREDIT: The bill creates an employee retention credit for employers that close due to the coronavirus pandemic.

- **Credit Allowed:**
 - Credit allowed against applicable employment taxes.
 - Equal to 50% of qualified wages and health benefits.
 - Credit can be claimed quarterly and is refundable.
 - Credit per quarter cannot exceed applicable employment tax amounts on wages paid with respect to the employment of all employees of the eligible employer.
 - Employment taxes must first be reduced by:
 - Credit claimed for the employment of qualified veterans,
 - Credit claimed for research expenditures of qualified small business, and
 - Credits claimed under the Families First Coronavirus Response Act (PL 115-97)
 - Claimed for sick pay and paid family medical leave.

- Claimed for FLMA required paid family leave.
 - The credit is not available to employers receiving Small Business Interruption Loans under Sec. 1102 of the Act.
- **Eligible Employers:**
 - Employers who were carrying on a trade or business during 2020, and
 - With respect to the calendar quarter:
 - For which the operation of that trade business is fully or partially suspended due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings due to the COVID-19 outbreak, or
 - Is within a period of significant decline in gross receipts:
 - Employers that have gross receipts that are less than 50% of their gross receipts for the same quarter in the prior year,
 - Until their gross receipts exceed 80% of their gross receipts for the same calendar quarter in the prior year.
 - Tax-Exempt organizations – shall apply to all operations regardless of cessation of trade or business.
- **Qualified Wages**
 - Applies to wages paid after March 12, 2020, and before January 1, 2021.
 - Employers with an average number of full-time employees of more than 100 employees:
 - Wages that the employer pays employees who are not providing services due to the suspension of the business or a drop in gross receipts.
 - Employers with an average number of full-time employees of less than 100 employees:
 - All wages paid qualify for the credit.
 - Wages limited to \$10,000 in aggregate for each employee for all quarters (not per quarter).
 - Wages paid under the Families First Coronavirus Response Act (PL 115-97) are not eligible.
 - Wages paid with Payroll Protection Plan (PPP) loan proceeds are not eligible.
 - May not exceed the amount such employee would have been paid for working an equivalent duration during the 30 days immediately preceding such period.
 - Includes qualified health plan expenses properly allocated to such wages:
 - Amounts paid or incurred by the eligible employer to provide and maintain a group health plan to the extent the amounts are excluded from employee gross income.
 - Allocation shall be treated as properly made if made on the basis of being pro rata among employees and pro rata on the basis of periods of coverage (relative to the periods to which such wages relate).
- **Applicable Employment Taxes**
 - Employers portion of Social Security Tax.
 - Employers portion of Medicare Tax.
- **Excess Credit Refundable**
 - If the amount of credit (50% of Wages) exceeds the applicable employment tax limitation for any calendar quarter,
 - Excess shall be treated as an overpayment that will be refunded.
- **Other:**
 - IRS is granted authority to advance payments to eligible employers, and
 - To waive applicable penalties for employers who do not deposit applicable payroll taxes in anticipation of receiving the credit.

AVIATION EXCISE TAXES: The CARES Act legislates an excise tax holiday for certain aviation excise taxes, which appears to be available to all payers of these taxes, including airlines, charter companies, and private and business aviation.

- The provision is effective after the enactment of the CARES Act and continues through December 31, 2020. It does not apply to payments made on or before the Act.
- No excise tax shall be imposed during the excise tax holiday on the transportation of persons or property by air.
- No excise tax shall be imposed on the use of kerosene used in commercial aviation.
- The excise tax holiday does not pertain to other taxable fuels such as gasoline and diesel fuel.

HAND SANITIZER EXCISE TAX: The Act provides a one-year temporary exception from excise tax for alcohol used to produce hand sanitizer.

Temporary removal of excise tax on distilled spirits removed for use in or contained in hand sanitizer:

- Distributed in a manner consistent with any guidance from the Food and Drug Administration.
- Related to the outbreak of SARS-CoV-2 or coronavirus disease 2019 (COVID-19).
- Affected product not subject to any requirements relating to labeling or bulk sales.

Effective date of removal of distilled spirits:

- Removal after December 31, 2019, and
- Removal before January 1, 2021.

The information contained herein is not intended to be “written advice concerning one or more Federal tax matters” subject to the requirements of Section 10.37(a)(2) of Treasury Department Circular 230.

The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax advisor.