The CARES Act: Tax and Financial Relief for Businesses

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The Coronavirus Aid, Relief, and Economic Security Act (CARES Act), a sweeping third-wave relief package in response to the COVID-19 pandemic, became law March 27. To read the full overview of the bill, click here.

While the CARES Act touches on many areas, the provisions relating to business taxation and finance are of critical importance. Although many of the provisions are focused on providing relief to those businesses negatively impacted by the virus in the short-term, a number of the changes made by this legislation make technical corrections or other tweaks to the reforms of the 2017 Tax Cuts and Jobs Act (TCJA). These legislative efforts have been designed to help jumpstart the economy once the crisis has subsided.

Payroll Tax Relief

Several of the provisions aimed at providing immediate relief to companies involve payroll taxes. First, recent legislation creates an employee retention credit for employers who were subject to closure as a result of the pandemic or whose gross receipts declined by more than 50% when compared to the same quarter in the prior year. The credit is a refundable payroll tax credit equal to 50% of the qualified wages paid by employers to employees during the COVID-19 crisis. The definition of "qualified wages" varies depending on whether an eligible employer has more than 100 full-time employees. The credit is provided for the first $10,000 of compensation paid, including health benefits, to an eligible employee. The employee retention credit is only available for wages paid or incurred from March 13, 2020 through December 31, 2020.

The CARES Act defers the payment of 100% of applicable employer payroll taxes and 50% of self-employment taxes. Under this provision, employers and self-employed individuals may make the deferred FICA/Social Security tax payments over the following two years, interest-free with half of the deferred payments due by December 31, 2021 and the remainder being paid by December 31,

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2022.

The net operating loss (NOL) limitation of the TCJA has also been temporarily modified to allow businesses to utilize NOLs generated. For NOLs generated in 2018, 2019 or 2020 only, NOLs can be carried back five years and the 80% use limitation is removed. For non-corporate businesses, the loss limitation rules have also been modified. Both of these provisions will allow losses to be utilized, returns to be amended, and cash flow to improve.

The TCJA repealed the corporate alternative minimum tax (AMT) and created refundable AMT credits available until 2021. The CARES Act allows companies with outstanding AMT credits to claim a refund now rather than waiting until 2021. Likewise, the TCJA's 30% business interest limitation has been temporarily increased to 50% for tax years 2019 and 2020.

One change related to the TCJA is a technical correction aimed at businesses that will improve property after the crisis is over, as well as those doing so recently. Specifically, the provision enables businesses to immediately write-off costs associated with improving certain facilities, so-called leasehold improvements, rather than depreciating the improvements over the 39-year life of the building. This change is retroactive to the date the TCJA was enacted.

Finally, the CARES Act provides a temporary exemption from the federal excise tax on distilled spirits for any distilled spirits used for on contained in hand sanitizer, so long as the hand sanitizer is produced and distributed in accordance with FDA guidance. The exemption is only valid for 2020

2020 Recovery Rebates and Deductions for Individuals

Big benefits are provided for all individual taxpayers. A new section 6428 of the Internal Revenue Code is added that provides Recovery Rebates in an amount up to $1,200 for individual taxpayers, and up to $2,400 for married couples filing a joint return. Those amounts would increase by $500 for each dependent child.

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Recovery Rebates would be reduced for higher-income taxpayers and begin phasing out for single filers with $75,000 in adjusted gross income (AGI), $112,500 AGI for a head of household, and $150,000 AGI for joint filers. Rebates would completely phase out for single filers with over $99,000 AGI, heads of household with over $136,500 AGI, and joint filers with $198,000 AGI.

The AGI figure would generally be based on each taxpayer's 2019 income tax return. If a taxpayer has not filed its 2019 income tax return, then the rebate will be based on its 2018 income tax return. Rebates paid pursuant to I.R.C. 6428 will not be reduced or offset by a taxpayer's existing debts with the U.S. government, including tax debts.

An increase in above the line deduction for any limitations on charitable contributions is also given. Beginning in tax year 2020, taxpayers are able to deduct up to $300 of their qualified charitable contributions above the line. This means that they would not need to itemize their deductions to realize the benefit of $300 of charitable deductions. For individuals, the charitable contribution limitation is modified to be the taxpayer's entire contribution base (*i.e.*, adjusted gross income).[1] If the aggregate amount of a taxpayer's charitable contribution exceeds their contribution base, such excess can be carried over to the following year. For corporations, the charitable contribution limitation is modified to be 25% of the taxpayer's taxable income.[2] If the aggregate amount of a taxpayer's charitable contribution exceeds their contribution base, such excess can be carried over to the following year.

Special Rules for Use of Pension/Retirement Funds

Relaxed provisions concerning pension plans and 401-K plans have also been provided.

The ten percent additional tax/penalty on early distributions from eligible retirement plans[3] under I.R.C. 72(t) shall not apply to any "coronavirus related-distribution." The term "coronavirus-related distribution" means any distribution from an eligible retirement plan made—

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- (i) on or after the date of the enactment of this Act and before December 31, 2020,
- (ii) to an individual—
  - (I) who is diagnosed with the virus SARS-CoV-2 or with coronavirus disease 2019 (COVID-19) by a test approved by the Centers for Disease Control and Prevention,
  - (II) whose spouse or dependent (as defined in section 152 of the Internal Revenue Code of 1986) is diagnosed with such virus or disease by such a test, or
  - (III) who experiences adverse financial consequences as a result of being quarantined, being furloughed or laid off or having work hours reduced due to such virus or disease, being unable to work due to lack of child care due to such virus or disease, closing or reducing hours of a business owned or operated by the individual due to such virus or disease, or other factors as determined by the Secretary of the Treasury (or the Secretary's delegate).

The aggregate amount of distributions received by an individual which may be treated as coronavirus-related distributions for any taxable year shall not exceed $100,000. There are special repayment provisions associated with coronavirus-related distributions that allow the distributions to be repaid within three years without incurring income tax as if it were a 60-day rollover contribution.[4] If not being repaid, for any coronavirus related-distribution, taxpayers can elect to include the distribution in gross income ratably over a three-year period beginning with the year in which the distribution is made, interest-free.

There is also an increase in the limit on loans not treated as distributions from qualified employer plans under I.R.C. 72(p).[5] The $50,000 limitation is increased to $100,000 for loans made during the "the 180-day period beginning on the date of the enactment of" the CARES Act.

Moreover, the due date with respect to any repayment from a qualified employer plan under I.R.C. 72(p) shall be delayed for 1 year

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(whereas the typical repayment period is five years).

The required minimum distribution (RMD) rules with respect to defined contribution plans under I.R.C. 403(a) and (b), deferred compensation plans under I.R.C. 457(b) and IRAs will not apply in calendar year 2020. This temporary waiver does not apply to any distribution that is required to be made in 2020 by reason of (i) a required beginning date occurring in 2020[6] and (ii) such distribution not having been made before January 1, 2020.

While different versions of the CARES Act have circulated in the last week as lawmakers have struggled with how best to address the COVID-19 pandemic, the following is a summary of the "Economic Stabilization" and "Air Carrier Worker Support" portions of the bill.

Economic Stabilization

This portion of the CARES Act is designed to provide further support for sectors of the economy that have been "severely distressed" as a result of the spread of COVID-19; in particular, it provides for direct lending to the air carrier industry, but it also seeks to provide relief for a broader range of businesses as well.

Notwithstanding other provisions providing liquidity to eligible businesses, this portion of the bill provides for a contribution of $500 billion to the Treasury's Exchange Stabilization Fund. This allows the Secretary of the Treasury to provide loans, loan guarantees, and other investments as follows:

- Direct loans including:
- Up to $25 billion to passenger air carriers meeting certain federal standards.
- Up to $4 billion for cargo air carriers.
- $17 billion for businesses critical to maintaining national security.
- $454 billion including any unused funds from the above references direct lending recipients, to programs or facilities established by the Board of Governors of the Federal Reserve that supports lending to eligible businesses, states, or municipalities.

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While this portion of the CARES Act is mostly directed at aircraft companies, its definition of "eligible businesses" is somewhat broad. In addition to "air carriers," the Secretary is able to grant loans to a "United States business that has not otherwise received adequate economic relief in the form of loans or loan guarantees provided under this Act." While this determination is up to the discretion of the Secretary, it could be a useful tool for industries that have not received other relief.

The Bill also gives broad discretion to the Secretary of the Treasury in overseeing the distribution and application procedures for the loans. Within 10 days of the enactment date, the Secretary will be required to provide more specific guidelines such as the rate amount, procedures for application, and minimum requirements for eligibility.

While the CARES Act grants the Secretary of the Treasury significant discretion it also provides some requirements the Secretary must adhere to when issuing these loans. Requirements for direct lending include:

- The applicant is an eligible business in which alternative financing is not reasonably available.
- The loan or loan guarantee is sufficiently secured or made at a rate that reflects the risk of the loan and is practicable compared to market conditions prior to the COVID-19 outbreak.
- The duration of the loan shall be as short as possible but does not exceed 5 years.
- The eligible business and its affiliates cannot engage in stock buybacks within the first year after the loan is no longer outstanding (can be waived by the Secretary).
- The eligible business cannot pay dividends with respect to common stock of the business within the first year after the loan is no longer outstanding (can be waived by the Secretary).
- Until September 30, 2020, the eligible business will maintain its employment levels as of March 24, 2020 to the extent practicable, but regardless will not reduce employment levels

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by more than 10 percent.

- The eligible business is domiciled and has a majority of its employees based in the U.S.
- The loan cannot be forgiven.
- The eligible business incurred or is expected to incur covered losses such that the continued operations of the business are jeopardized.
- Any lending through a facility established by section 13(3) of the Federal Reserve Act by the Federal Reserve must be broad-based, with verification that each participant is not insolvent and is unable to obtain adequate financing elsewhere. Loan forgiveness is not permissible in such a facility.

Additionally, the CARES Act specifically addresses assistance for mid-sized businesses. It provides that the Secretary must seek to implement a special 13(3) facility through the Federal Reserve that provides financing to non-profit organizations and businesses with between 500 and 10,000 employees. These loans will be subject to additional restrictions such as the fund must be used to retain at least 90 percent of their workforce with full compensation and benefits through September 30, 2020, the recipient will not abrogate existing collective bargaining agreements for the term of the loan plus an additional two years, and the recipient must remain neutral in any union organizing effort for the term of the loan.

Additionally, the Act requires that after the business enters into the agreement with the Secretary, that until the loan is no longer outstanding for 1 year, no employee or officer that received more than $425, 000 in compensation in calendar year 2019 will receive more than what they received in 2019 nor will they receive severance or other termination benefits that exceeds twice the maximum total compensation received in 2019. Also, officers or employees earning more than $3 million in 2019 would also be prohibited from earning more than $3 million plus 50% of the amount their compensation last year exceeded $3 million.

Specific to the aircraft industry, the bill also grants the power to the Secretary to maintain scheduled air transportation services of

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businesses receiving loans. This allows the Secretary to consider air transportation needs of small and remote communities. It also suspends any excise tax on air transportation and tax on aviation fuel.

The remainder of this portion of the Act addresses various issues associated with lending in efforts to make the issuance of relief expedited and efficient. These efforts include:

- Authorizes the FDIC to temporarily establish a debt guarantee program for debt of solvent insured depositories and depository holding companies.
- Authorizes the National Credit Union Administration to increase share insurance coverage for noninterest-bearing transaction accounts.
- Provides more flexibility for Federal Reserve proceedings.
- Grants temporary hiring flexibility to certain government agencies (Department of Housing and Urban Development (HUD), the U.S. Securities and Exchange Commission (SEC), and the Commodity Futures Trading Commission (CFTC)).
- Temporarily lifts some of the OCC's lending limits for nonbank financial companies and transactions the Comptroller of the Currency deems is in the public interest.
- Lowers the Community Bank Leverage Ratio (CBLR) for qualifying community banks from 9 percent to 8 percent, as well as proving a grace period for those with CBLR that fall below the prescribed level.
- Allows financial institutions to elect to suspend GAAP requirements for loan modifications related to the coronavirus pandemic.
- Optional temporary relief from current expected credit losses for an insured depository institution, bank holding company, or any of its affiliates.
- Suspends the limitation on the use of ESF for guarantee programs in the U.S. money market mutual fund industry.
- To meet liquidity needs, enhances access to the Central Liquidity Facility.

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- Waives for a two-year period the requirement for a separate act of Congress to authorize certain projects exceeding $50 million and that leftover funds from the DPAF be swept to the General Fund.
- Creation of an Office of the Special Inspector General for Pandemic Relief within the Department of the Treasury.
- Ineligibility for any company-owned 20 percent or greater by the President, Vice President, executive department head, member of Congress, or spouse, child, son or daughter in law of said person.
- Establishment of a Congressional Oversight Commission consisting of 5 members appointed by the House and Senate majority and minority leaders.
- Provisions to protect credit during the COVID-19 pandemic.
- Prohibits foreclosures on all federally-backed mortgage loans for a 60-day period.
- Up to 90 days of forbearance with no evictions or late fees for multifamily borrowers with a federally-backed multifamily mortgage loan.
- Prohibits landlords from initiating legal eviction proceedings for 120 days.

Each of these provisions are temporary in nature and include additional information and caveats. So, it is important for businesses, state and local governments, and financial institutions to seek additional guidance if any of these provisions pertain specifically to them.

Air Carrier Worker Support

The CARES Act also addresses the needs of air carrier workers. This portion of the bill provides financial assistance for employee wages, salaries, and benefits for passenger air carriers, cargo air carriers, and airline contractors such as persons or entities contractually performing airport ground support or catering services for the air carrier industry. The bill provides some additional guidelines, but instructs the Secretary to publish procedures within 5 days for air carriers and contractors to submit financial assistance requests.

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In sum, the CARES Act offers the opportunity to assist a variety of industries, businesses, and individuals remain financially secure during this time of uncertainty. For more information regarding the remaining portions of the CARES Act or for other general information on how to economically navigate the COVID-19 pandemic, visit the FBT COVID-19 Response Team Webpage.

Tax-Free Small Business Loan Forgiveness Under the CARES Act

Among the stimulus provisions provided in the CARES Act is a significant expansion of small business loans available under Section 636(a) of the Small Business Act (15 USC 636(a)). The CARES Act will forgive certain amounts of Section 636(a) debt incurred to meet certain payroll and operating payments made by borrowers. For federal tax purposes, small business loan forgiveness under the CARES Act will **not** be included as cancellation of indebtedness income under the Internal Revenue Code.

Expansion of Loans Under Section 636(A) of the Small Business Act

Small businesses may now receive loans under Section 636(a) without the pledge of collateral, personal guarantee or the requirement that credit cannot be otherwise obtained. The following is a high-level summary of the loans to be provided by Section 1102 of the CARES Act.

- For the period February 15, 2020 through June 30, 2020, in general, any business concern, nonprofit organization, veteran's organization or tribal business concern which employs not more than 500 employees (or, if applicable, not more than the standard number of employees established by the Small Business Administration for the industry) shall be eligible to receive a loan made under Section 636(a).
- The maximum loan amount is the lesser of: (1) the average monthly payroll costs incurred the one-year period before the date on which the loan is made multiplied by 2.5, or (2)

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$10,000,000.

- Modified average monthly payroll costs calculations are available for seasonal employers and businesses that were not in business during the period February 15, 2019 through June 30, 2019.
- Loan proceeds may be used for the following purposes: (1) payroll costs; (2) cost related to continuation of healthcare benefits for periods of paid sick, medical or family leave and insurance premiums; (2) employee salaries, commissions and similar compensation; (3) mortgage interest payments (payment of principal not included); (4) rent (including rent payments under a lease); (5) utilities; and (6) any other debt obligations incurred before the covered period.

Small Business Loan Forgiveness

Any recipient of a loan described above made during the period February 15, 2020 through June 30, 2020 shall be eligible for forgiveness of the portion of the debt attributable to maintaining payroll continuity during the period February 15, 2020 through June 30, 2020 (the "covered period"). The following provides a high-level summary of the maximum amount of loan forgiveness for each borrower:

- The loan forgiveness cannot exceed the sum of the following payments made during the eight week period beginning on the date of origination of the loan: (1) "payroll costs"; (2) interest on a mortgage entered into prior to the covered period; (3) rent on leases entered into prior to covered period; and (4) utilities (electric, gas, water, transportation, phone, and internet) for services that began prior to the covered period.
- "Payroll costs" include the following payments: (1) salary, wage, commission, or similar compensation; (2) tips; (3) vacation, parental, family, medical or sick leave; (4) severance; (5) required group healthcare and insurance premiums; (6) retirement benefits; (7) state and local payroll tax; and (8) compensation or income of sole proprietors or independent

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contractors that is a wage, commission, income, net earnings from self-employment or similar compensation that is not more than $100,000 in one year.

- "Payroll costs" costs do not include any annual salary and wage compensation to any individual over $100,000 (prorated for the covered period) or qualified sick or family leave wages for which a credit is allowed under Public Law 116-127. The $100,000 limitation on compensation applies only to cash compensation, not to non-cash benefits, including (i) employer contributions to defined-benefit or defined-contribution retirement plans, (ii) payment for the provision of employee benefits consisting of group health care coverage, including insurance premiums, and (iii) payment of state and local taxes assessed on compensation of employees.
- The amount of loan forgiveness is reduced by the percentage equal to the difference of the average number of full-time equivalent employees per month employed by the eligible recipient during the covered period and the average number of full-time equivalent employees during the period February 15, 2019 through June 20, 2019. However, an exemption for employees rehired during the covered period is provided.
- If any full-time equivalent employee who did not receive pay at an annualized rate of $100,000 for any prior pay period has a reduction in salary of more than 25 percent from the most recent full quarter, the forgiveness amount will be reduced by any reduction amount that is in excess of 25 percent for the covered period.

Amounts forgiven shall be treated as canceled indebtedness by lenders authorized under section 7(a). Any cancelation of indebtedness under Section 1106 of the CARES Act shall be **excluded** from the borrower's gross income under the Internal Revenue Code.

To provide guidance and support to clients as this global public-health crisis unfolds, Frost Brown Todd has created a Coronavirus Resource Page. We have also convened a dedicated Coronavirus Response Team, with attorneys on hand to field questions concerning labor and employment matters, commercial contracts, litigation risks, as well as business succession,

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continuity and crisis response planning.

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[1] Previously this limitation was 50% of the entire contribution base.

[2] Previously this limitation was 10% of the taxpayer's taxable income.

[3] The term "eligible retirement plan" has the meaning given to such term by I.R.C. 402(c)(8)(B). These include certain IRA, retirement annuities, deferred compensation plans, and other retirement plans.

[4] This does not apply for I.R.C. 401 qualified pension, profit-sharing, and stock bonus plans, and distributions under I.R.C. 402 and 3405.

[5] Qualified employer plan, etc. For purposes of this subsection— (A) Qualified employer plan (i) In general – The term "qualified employer plan" means— (I) a plan described in section 401(a) which includes a trust exempt from tax under section 501(a), (II) an annuity plan described in section 403(a), and (III) a plan under which amounts are contributed by an individual's employer for an annuity contract described in section 403(b). (ii) Special rule – The term "qualified employer plan" shall include any plan which was (or was determined to be) a qualified employer plan or a government plan. (B) Government plan – the term "government plan" means any plan, whether or not qualified, established and maintained for its employees by the United States, by a State or political subdivision thereof, or by an agency or instrumentality of any of the foregoing.

[6] The beginning date for your first RMD depends on the type of plan. For IRAs, the beginning date is (i) April 1 of the year following the calendar year in which you reach age 70½, if you were born before July 1, 1949 or (ii) April 1 of the year following the calendar year in which you reach age 72, if you were born after Jun 30, 1949. For 401(k), 403(b) and other defined contribution plans, the RMD is generally April 1 following the later of the calendar year in which you: (i) reach age 72 (age 70½ if born before July 1, 1949), or (ii) retire (if your plan allows this).

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