

CARES Act Provides Significant Payroll Tax Relief and Relief for Business Taxpayers and Individuals

by Katina M. Peterson and Kendall R. Fisher

The federal Coronavirus Aid, Relief, and Economic Security Act (the “CARES Act” or the “Act”), signed into law on March 27, 2020, contains significant (and mostly temporary) changes to federal tax law that provide immediate and short-term economic relief to both individual and business taxpayers. This briefing provides general summaries of these provisions in three categories: (1) payroll tax relief, (2) relief for business taxpayers, and (3) relief for individuals. For more specific information relating to any of these provisions, please reach out to any of the authors.

PAYROLL TAX RELIEF

Employee Retention Credit for Employers Adversely Affected by COVID-19

Section 2301 of the Act provides certain employers adversely affected by the COVID-19 pandemic with payroll tax credits for wages paid to employees in 2020, including related health insurance costs, under specified circumstances. These credits operate similarly to the sick leave and family leave credits provided for under the Families First Coronavirus Response Act (“FFCRA”) enacted on March 18, 2020, although they do not result in credits for the entire amount of wages paid. Under the circumstances that qualify employers for credits, employers may be incentivized by the credits to retain employees for longer than they might otherwise and in any case will be compensated in the form of a payroll tax reduction or refund for up to \$5,000 per employee for all qualified wages paid, mitigating some of the financial strain on employers caused by the emergency.

More specifically, the Act provides “eligible employers” for any calendar quarter in 2020 with credits against FICA tax liability for such quarter in an amount equal to 50 percent of the “qualified wages” paid to employees for the quarter. The aggregate amount of qualified wages that can be taken into account with respect to any employee in 2020 shall not exceed \$10,000, and thus the credit for each employee cannot exceed \$5,000

Related People

- Katina M. Peterson
- Kendall R. Fisher

Related Capabilities

- Tax
- Tax Controversy & Litigation

for the year.

“Eligible employers” are employers carrying on a trade or business during calendar year 2020 (including, for this purpose, tax-exempt organizations) with respect to any calendar quarter in 2020 for which either of the following eligibility thresholds is satisfied:

1. The operation of the employer’s trade or business is fully or partially suspended during the calendar quarter due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to COVID-19 (the “Suspension Circumstances”); or
2. The calendar quarter is within the period beginning with the first calendar quarter in 2020 for which the employer’s gross receipts for the quarter are less than 50 percent of the employer’s gross receipts for the same calendar quarter in the prior year and ending at the end of 2020 (the “Gross Receipts Circumstances”). The Secretary of the Treasury is directed to issue guidance regarding the application of this provision to any employer who was not carrying on a trade or business for all or part of the same calendar quarter in the prior year.

“Qualified wages” is defined differently depending on whether the employer’s average number of full-time employees (as determined under rules set forth in Section 4980H of the Internal Revenue Code of 1986, as amended (the “Code”)) during 2019 was (1) greater than 100, or (2) 100 or fewer, as follows:

1. For employers whose average number of full-time employees during 2019 was greater than 100, “qualified wages” are wages paid *only with respect to which an employee is not providing services* due to the Suspension Circumstances or the Gross Receipts Circumstances. Aggregation rules borrowed from Sections 52 and 414 of the Code apply to treat certain persons as a single employer for purposes of this provision.
2. For employers whose average number of full-time employees during 2019 was 100 or fewer, “qualified wages” are (a) wages paid to *any* employee during any period in which the Suspension Circumstances are present, even if they are providing services; and (b) if not taken into account pursuant the foregoing clause, wages paid to *any* employee during any quarter in 2020 from and after the first quarter in which the Gross Receipts Circumstances are present, even if they are providing services.

The Act further provides that “qualified wages” shall include so much of the eligible employer’s qualified health plan expenses as are properly allocable to the wages described above, but only to the extent that these expenses are excluded from employees’ gross income.

Among other limitations set forth in the Act, “qualified wages” does not include any sick leave or family leave wages for which dollar for dollar tax credits already are provided under the FFCRA or wages paid to specified family members of the employer or controlling owner. Additionally, employers who receive a Paycheck Protection Program loan provided for in Section 1102 of the Act are not eligible for the credits.

Refundable Nature of Credits: The credits are available for the calendar quarter for which the qualified wages are paid, and are refundable to the employer to the extent they exceed the employer’s tax liability for such quarter. The Act provides that the Secretary

shall waive any failure to deposit penalty for applicable payroll taxes if the Secretary of the Treasury determines that such failure was due to the reasonable anticipation of the credits allowed under this section of the Act.

Credits for Amounts Paid to Employees Covered by Railroad Retirement System: The Act provides similar credits and penalty relief for qualified wages paid by eligible employers to employees who are covered under the Railroad Retirement Act system rather than under the FICA tax system.

Effective Date: The credit applies with respect to wages paid after March 12, 2020, and before January 1, 2021.

Delay of Payment of Employer Payroll Taxes

Section 2302 of the CARES Act treats any employer as having timely deposited all “applicable employment taxes” accrued during the period beginning on the date of enactment of the CARES Act and ending on January 1, 2021 (effectively, “applicable employment taxes” due for the remainder of 2020) if 50 percent of such taxes are deposited no later than December 31, 2021 and the remainder is deposited no later than December 31, 2022. For most employers, the “applicable employment taxes” consist of the employer portion of Social Security taxes, which are currently imposed at a rate of 6.2 percent of wages paid to employees (applicable to wages paid up to \$137,700 per employee) (Code Section 3111(a) taxes). A separate definition applies for purposes of the employment taxes with respect to employees who are covered under the Railroad Retirement Act system.

Taxpayers that have indebtedness forgiven under either Section 1106 or Section 1109 of the CARES Act with respect to a Paycheck Protection Program loan are not eligible for the foregoing deferral provisions.

For taxpayers subject to self-employment tax, the CARES Act permits the deferral of 50 percent of self-employment taxes accrued during the period beginning on the date of enactment of the CARES Act and ending on January 1, 2021 (effectively, 50 percent of the self-employment taxes due for the remainder of 2020) if 50 percent of the deferred taxes are deposited no later than December 31, 2021 and the remainder is deposited no later than December 31, 2022. Taxes deferred under the CARES Act will also be excluded for purposes of calculating estimated tax payments under Code Section 6654.

Effective Date: March 27, 2020.

RELIEF FOR BUSINESS TAXPAYERS

Temporary Suspension of Limitations on Corporations’ Cash Charitable Contributions

Section 2205 of the Act modifies the limitations on deductions of qualified charitable contributions. For corporations, the 10-percent of taxable income limitation is increased

to 25 percent of taxable income for qualified contributions, with any excess eligible to be carried forward.

For purposes of this provision, a “qualified contribution” means any charitable contribution if (i) paid in cash during the calendar year 2020 to an organization described in Code Section 170(b)(1)(A) (e.g., churches, education institutions, organizations that receive a substantial portion of support from public contributions, etc.), and (ii) the taxpayer has elected the application of this section with respect to such contribution. Contributions to donor-advised funds and supporting organizations do not qualify.

This provision also increases the limitation on deductions for contributions of certain food inventory to 25 percent of the taxpayer’s aggregate business income from businesses in which such contributions were made (previously, deductions were limited to 15 percent of such income).

Effective Date: This section of the CARES Act applies in taxable years ending after 2019.

Modifications for Net Operating Losses

Section 2303 of the CARES Act delays the effective date through the current taxable year of certain limitations on a corporation’s ability to deduct net operating losses (“NOLs”) that were enacted in the Tax Cuts and Jobs Act of 2017 (the “TCJA”). Under this relief provision, a corporate taxpayer’s NOLs arising in a taxable year beginning after December 31, 2017 and before January 1, 2021 generally can be carried back to the five years preceding the taxable year of such loss (see Code Section 172(b)). In addition, the “80 percent limitation of taxable income” rule regarding use of NOLs will not apply to taxable years after December 31, 2017 and beginning before January 1, 2021 (additional rules are provided for taxable years beginning after December 31, 2020) (see Code Section 172(b)). The increased ability to use NOLs to offset taxable income both in current and previous taxable years should increase an affected corporation’s cash flows to maintain operations and payroll during the COVID-19 emergency.

The TCJA prohibited taxpayers from carrying back NOLs to taxable years ending after December 31, 2017. The CARES Act provides that NOLs that arose in a tax year that “straddled” December 31, 2017 are eligible for the two-year carryback period and twenty-year carryforward provisions that applied prior to the enactment of the TCJA. For the 120 days following the date of enactment of the CARES Act, taxpayers are permitted to file an election under Code Section 6411(a) to carryback eligible NOLs during that arose during a taxable year straddling, but not ending on, December 31, 2017, or to elect to forego the carryback under Code Section 172(b)(3).

The TCJA also introduced what is commonly known as a “transition tax” under Code Section 965, whereby U.S. corporations were deemed to have repatriated certain income from their non-U.S. subsidiaries. For most taxpayers, this deemed repatriation occurred in their 2017 taxable year, unless the taxpayer elected to defer such tax to their 2018 taxable year. For a taxpayer that previously recognized taxable income under Code Section 965, the CARES Act provides that an NOL arising in 2018, 2019 or 2020 cannot

be used to offset such income previously recognized under Code Section 965 (by technically deeming the taxpayer to have made the election provided in Code Section 965(n)). However, the NOL may still be carried back to such Inclusion Year to offset non-Code Section 965 income. Alternatively, the CARES Act permits taxpayers to apply a carryback method which “skips over” Inclusion Years.

Exceptions: NOLs for REITS shall not be an NOL carryback to any taxable year preceding the taxable year of such loss. Any NOL for a taxable year in which a corporation is not a REIT cannot be carried back to a taxable year in which the corporation is a REIT. In addition, if an NOL is carried back for a life insurance company in a taxable year beginning before January 1, 2018, such NOL shall be treated in the same manner as an operations loss carryback. Finally, for any NOLs carried back to any taxable year with respect to a deferred foreign income corporation (see Code Section 965(a)), the taxpayer will be treated as having made the election not to apply NOL deductions with respect to any taxable year so described (see Code Section 965(n)).

Effective Date: The amendments made by this section apply to taxable years beginning after December 31, 2017 (with special rules for NOLs arising in taxable years beginning before January 1, 2018 and ending after December 31, 2017).

Modifications of Limitation on Losses for Taxpayers Other than Corporations

Similar to the relief provided for in Section 2303 of the CARES Act with respect to NOLs, Section 2304 of the CARES Act delays the effective date of the “excess business loss” limitations for non-corporate taxpayers that were enacted in the TCJA.

By way of background, under the TCJA, for any taxable year of a non-corporate taxpayer beginning after December 31, 2017 and before January 1, 2026, the deduction of “excess business losses” was disallowed (see Code Section 461(l)(1)). Any such disallowed excess business losses were treated as an NOL carryover to the following taxable year under Code Section 172 (see Code Section 461(l)(2)). For these purposes, an “excess business loss” means the excess (if any) of:

1. The aggregate deductions of the taxpayer for the taxable year which are attributable to trades or business of such taxpayer (determined without regard to whether or not such deductions are disallowed for such taxable year under Code Section 461), over
2. The sum of (a) the aggregate gross income or gain of such taxpayer for the taxable year which is attributable to such trades or business, plus (b) \$250,000 (200 percent of such amount in the case of a joint venture).

Under Section 2303 of the CARES Act, the effective date of these provisions in the TCJA is delayed from December 31, 2017 to December 31, 2020 (see Code Section 461(l)(1)), so that passthrough entities and sole proprietorships will be able to use excess business losses with respect to 2018, 2019, and 2020. Accordingly, for taxpayers that previously had an NOL carryforward in 2019 resulting from disallowed excess business losses in 2018 will no longer have such NOL resulting from the disallowed excess business losses. For tax years beginning in 2021 through 2026, taxpayers may treat disallowed excess business losses as NOLs for purposes of carrying such disallowed excess

business losses forward to subsequent tax years.

The CARES Act also makes certain technical amendments to the definition of “excess business losses” as provided in the TCJA. These amendments include clarifying that: (i) deductions permitted under Code Sections 172 and 199A will be disregarded in determining excess business losses; (ii) the calculation of excess business losses will include the lesser of (A) capital gain attributable to a trade or business and (B) net capital gain income; and (iii) excess business losses will be determined without regard to any capital losses or any deductions, gross income, or gain attributable to any trade or business or performing services as an employee.

Effective Date: This section of the CARES Act applies to all taxable years beginning after December 31, 2017.

Modification of Credit for Prior Year Minimum Tax Liability for Corporations

The TCJA repealed the corporate alternative minimum tax (the “AMT”) and amended Code Section 53(e) to allow for refunds of outstanding AMT credit carryforwards over a phase-in period ending on December 31, 2021. Section 2305 of the CARES Act would accelerate the ability of corporate taxpayers to claim credits and refunds for their outstanding AMT credit carryforwards.

Under Section 2305 of the Act, a corporate taxpayer’s AMT credit carryforwards are fully refundable in its tax year beginning in 2019. In addition, a corporate taxpayer may elect for the AMT credit carryforward to be fully refundable in its tax year beginning in 2018.

Applications for refunds will be deemed as made under Code Section 6411, which generally means that such applications will be subject to a 90-day review, processing and payment timeline. However, the IRS can disallow an application in whole, or in part, as a result of omissions or errors noted during the 90-day review period. Further, any such refund will be treated as a “tentative refund,” meaning that the refund may be subsequently disallowed upon further examination by the IRS. Special rules may apply to taxpayers filing a consolidated return.

Effective Date: This section of the CARES Act applies to taxable years beginning after December 31, 2017.

Modifications of Limitations on Business Interest

Section 2306 of the CARES Act relaxes the limitations on the deductibility of business interest that were enacted in the TCJA.

By way of background, prior to the enactment of the TCJA, business interest expense was generally fully deductible (subject to potential limitations in cases involving related or foreign parties). Under the TCJA, for tax years beginning after December 31, 2017, Code Section 163(j)(1) limited the deduction for business interest (subject to exceptions for taxpayers in specified businesses or with gross receipts below specified levels and

subject to special rules for passthrough entities) to the sum of:

1. “business interest income” (the term “business interest income” meaning interest includible in gross income and properly allocable to a trade or business);
2. 30 percent of the “adjusted taxable income” of the taxpayer, but, in no event, less than zero (the term “adjusted taxable income” meaning taxable income computed without regard to any item of income, gain, deduction or loss not properly allocable to a trade or business, any interest income or expense, net operating loss, Code Section 199A deduction and, for tax years beginning before January 1, 2022, any deduction for depreciation, amortization or depletion); and
3. “floor plan financing interest” (interest paid on indebtedness used to purchase, and secured by, motor vehicles held for sale or lease).

Any interest expense disallowed due to being in excess of the threshold provided above was considered as paid in the following year and could be carried forward indefinitely.

Section 2306 of the CARES Act relaxes the limitation described above for taxable years of taxpayers other than partnerships beginning in 2019 or 2020 by substituting “50 percent” for “30 percent” in the second part of the limitation. For partnerships, the limitation is relaxed only for taxable years beginning in 2020. In addition, unless a partner elects otherwise, in the case of any excess business interest of the partnership for any taxable year beginning in 2019 which is allocated to the partner, 50 percent of such excess business interest shall be treated as business interest which is paid or accrued by the partner in the partner’s first taxable year beginning in 2020. The limits of Code Section 163(j)(1), as set forth above, do not apply to such excess business interest. Instead, the partner may claim a deduction for such excess business interest to the extent that partner is allocated “excess taxable income” from the partnership as described above. A partner may carry-forward any disallowed excess business interest to future tax years indefinitely.

Any taxpayer may elect out of the foregoing amendments to Code Section 163(j), provided that, in the case of a partnership, the election must be made by the partnership (and applies to all partners with respect to that partnership). Such an election may only be revoked with the consent of the IRS.

The CARES Act also allows a taxpayer to elect to use its adjusted taxable income in its 2019 tax year for purposes of computing the limitation under the second part of Code Section 163(j) above for tax years beginning in 2020. In the case of a short tax year, a proportionate amount of the adjusted taxable income for the taxpayer’s 2019 tax year may be used for computing the limitation for such short tax year. In the case of a partnership, this election must be made by the partnership (and applies to all partners with respect to that partnership). For taxpayers affected by the likely economic downturn in 2020, the ability to use their 2019 adjusted taxable income to determine their business interest deduction for their 2020 tax year will likely significantly increase their ability to claim business interest income expense deductions for their 2020 tax year, reducing their net cost of capital.

Effective Date: Section 2305 of the CARES Act is effective for tax years beginning after

December 31, 2018.

Technical Amendments Regarding Qualified Improvement Property

Section 2307 of the CARES ACT corrects an error in the TCJA regarding the deductibility of “qualified improvement property.” The TCJA erroneously required businesses to depreciate this property using the straight-line method over the 39-year life of a building. The correction enables businesses to write off the cost of this property immediately. “Qualified improvement property” means any improvement to the interior portion of a non-residential building if the improvement is placed in service after the date such non-residential building was placed in service. However, the following types of improvements are not considered “qualified improvement property” for this purpose: (1) enlargements to the building; (2) any elevator or escalator; or (3) any improvement to the internal structural framework of the building.

This correction is anticipated to be particularly beneficial for the hospitality industry.

Effective Date: This provision is effective as if it had been originally included in the TCJA, i.e., for tax years beginning after December 31, 2017. Taxpayers may amend prior year tax returns to claim this deduction.

Temporary Exception from Excise Tax for Alcohol Used to Produce Hand Sanitizer

Section 2308 of the CARES Act provides a temporary exception from the excise tax imposed under Chapter 51 of the Code on distilled spirits used for or contained in hand sanitizer. Under this amendment, any distilled spirits removed from bonded premises after December 31, 2019 and before January 1, 2021 for use in or contained in hand sanitizer products produced and distributed in a manner consistent with guidance issued by the Food and Drug Administration related to the outbreak of SARS or COVID-19 will not be subject to the excise tax imposed under Chapter 51. In addition, any distilled spirits or products described in this section will not be subject to any requirements related to labeling or bulk sales under the Federal Alcohol Administration Act or the Alcoholic Beverage Labeling Act.

Effective Date: This section applies to distilled spirits removed from bonded premises after December 31, 2019 and before January 2, 2021.

RELIEF FOR INDIVIDUALS

Stimulus Payments

Section 2201 of the CARES Act adds new Section 6428 to the Code to provide eligible, individual taxpayers a one-time refundable tax credit. This “recovery rebate” (also referred to frequently in the media as a stimulus payment) is equal to the sum of (i) \$1,200 (\$2,400 for eligible individuals filing a joint return), plus (ii) \$500 for each qualifying child (as defined in Code Section 24(c)) of the taxpayer. An “eligible individual” means any individual who is not any of the following: (1) a nonresident alien

individual, (2) a dependent of another taxpayer, and (3) a trust or an estate.

The amount of the credit allowed under this section will be reduced (but not below zero) by \$5 for each \$100 by which the taxpayer's adjusted gross income exceeds (1) \$150,000 in the case of a joint return, (2) \$112,500 in the case of a head of household, and (3) \$75,000 in the case of an individual taxpayer. For example, the amount is completely phased-out for single filers with incomes exceeding \$99,000, \$146,500 for head of household filers with one child, and \$198,000 for joint filers with no children.

In order to calculate and issue the stimulus payments, the IRS will review information reported on eligible taxpayers' 2019 federal income tax return. If a return has not yet been filed for 2019 (now due on July 15, see earlier Dorsey e-Alert [here](#)), the IRS will review an eligible taxpayer's 2018 federal income tax return. If the IRS doesn't have a 2018 or 2019 tax return, it will review information from a 2019 Form SSA-1099, *Social Security Benefit Statement*, or Form RRB-1099, *Social Security Equivalent Benefit Statement*, to calculate the stimulus check amount.

No action is required by eligible taxpayers to receive a stimulus payment. The IRS will automatically issue the stimulus payment calculated in accordance with new Code Section 6428 based on eligible taxpayers' return information. If a taxpayer is not eligible to receive a stimulus payment now, he or she may still be eligible for a stimulus payment at the time the 2020 federal income tax return is filed. Under new Code Section 6428, payments issued now are treated as advance payments of a refundable credit for the 2020 tax year. So, for taxpayers who do not receive a stimulus payment in 2020, the taxpayer may be able to claim it next year as a refund or reduction of the tax owed on their 2020 federal income tax return.

Above-the-Line Deduction for Certain Charitable Contributions

Section 2204 of the Act adds a new permanent above-the-line deduction by way of adding Section 62(a)(22) to the Code. The new rule provides that, beginning with 2020 federal income tax returns, certain taxpayers who do not elect to itemize will be able to deduct up to \$300 in qualified charitable contributions.

For purposes of this provision, a "qualified charitable contribution" means a charitable contribution: (i) made in cash; (ii) for which a deduction is typically allowed for charitable contributions under the Code (see Code Section 170); (iii) made to a charitable organization, e.g., churches, education institutions, organizations that receive a substantial portion of support from public contributions, etc. (see Code Section 170(b)(1)(A)); (iv) not made to a supporting organization described in Code Section 509(a)(3); and (v) not made for the establishment of a new, or maintenance of an existing, donor advised fund (see Code Section 4966(d)(2)).

Charitable contributions carried over from a prior taxable year will not qualify for the new above-the-line deduction.

Temporary Suspension of Limitations on Individuals' Cash Charitable

Contributions

Section 2205 of the Act modifies the limitations on individuals' itemized deductions of qualified charitable contributions. The 50-percent of adjusted gross income limitation is temporarily suspended for qualified contributions, generally allowing individuals to fully deduct qualified contributions to the extent of their adjusted gross income (reduced by any other charitable contributions otherwise allowed), with any excess to be carried forward.

For purposes of this provision, a "qualified contribution" has the same meaning as set forth above in the discussion of this provision as it affects corporate taxpayers.

This provision also increases the limitation on deductions for contributions of certain food inventory from 15 percent to 25 percent of the taxpayer's taxable income.

Effective Date: This section of the CARES Act applies in taxable years ending after 2019.

Expansion of Tax-Free Employer Educational Assistance to Include Student Loan Repayments

Section 2206 of the Act allows employers to provide a new category of educational assistance benefits to employees on a tax-free basis in 2020, subject to the existing \$5,250 cap on tax-free benefits per employee: student loan repayments made by an employer to an employee or directly to a lender with respect to the principal or interest of an employee's "qualified education loan" as defined in Section 221(d)(1) of the Internal Revenue Code, if made after March 27, 2020, and before January 1, 2021.

Any employee who receives such excluded income from an employer will not be able to also deduct the corresponding amount of interest paid with respect to such employee's student loans (see Code Section 221(e)).

Effective Date: This section of the CARES Act applies to payments made after March 27, 2020.