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Business Tax Provisions of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act)

Client Advisories

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March 30, 2020 - On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act") was enacted into law. This e-alert summarizes some of the significant business tax provisions contained in the CARES Act.

Employee Retention Credit

Generally, the CARES Act provides for refundable payroll tax credits to an "eligible employer" in an amount equal to 50% of the first $10,000 of "qualified wages" paid to each employee. The credit is applied on a quarterly basis against the employer portion of Social Security taxes. Eligible employers are employers (including tax-exempt organizations) whose operations have been fully or partially suspended as a result of a COVID-19 related government order or that experienced a greater than 50% reduction in quarterly receipts (measured on a year-over-year basis).

For an eligible employer who had on average 100 or fewer full-time employees in 2019, all compensation, including health benefits, paid to employees from March 13 through December 31, 2020 is qualified wages. For a larger eligible employer, any compensation, including health benefits, paid to employees when they were unable to provide services due to COVID-19 related circumstances from March 13 through December 31, 2020 is qualified wages. Aggregation rules treat related parties as a single employer. Employers that receive small business loans pursuant to the CARES Act are not eligible for this credit.

Deferral of Payment of Employer Payroll Taxes

The CARES Act allows employers to defer paying the employer portion of Social Security taxes during the period from March 27, 2020 to January 1, 2021; self-employed individuals are allowed to defer payment of 50% of the Social Security-related portion of self-employment taxes. Half of the deferred taxes is due on December 31, 2021 and the remaining half is due on December 31, 2022. The payroll tax deferral does not apply to a taxpayer that receives forgiveness of a small business loan pursuant to the CARES Act.

Net Operating Loss Limitation

The 2017 Tax Cuts and Jobs Act (the "2017 Tax Act") limited the deduction for net operating losses ("NOLs") arising in 2018 and later years to 80% of the taxpayer's taxable income and eliminated the ability to carry back NOLs to prior taxable years. For taxable years beginning after December 31, 2017 and before January 1, 2021 (2018 to 2020 for calendar year taxpayers), the CARES Act eliminates the 80% limitation and allows a taxpayer to carry back NOLs to the prior five taxable years, including to pre-2017 Tax Act years when the corporate tax rate was 35%. Special rules apply for REITs and life insurance companies. NOL carrybacks generally are disregarded for purposes of calculating the Section 965 transition tax. The increased ability to use NOLs may have detrimental effects for some taxpayers, including a reduction in deductions for global intangible low-taxed income ("GILTI") and foreign-derived intangible income ("FDII"); accordingly, some corporations may want to consider electing to forgo NOL carrybacks.

Excess Business Loss Limitation

The 2017 Tax Act disallowed "excess business losses" for taxpayers (other than C corporations) in taxable years beginning after December 31, 2017 and before January 1, 2026 (for calendar year taxpayers, 2018 to 2025) and treats disallowed excess business losses as NOL carryovers. An "excess business loss" generally means the excess of the aggregate deductions attributable to a taxpayer's trades or businesses over the sum of the aggregate gross income or gain of such taxpayer attributable to such trades or businesses, but only to the extent that such net loss exceeds $250,000 (or $500,000 in the case of a joint return), indexed for inflation. The CARES Act suspends the excess business loss limitation for taxable years beginning before January 1, 2021 (2018 to 2020 for calendar year taxpayers). The CARES Act also includes certain technical corrections to the excess business loss provisions.

Corporate AMT Credit

The 2017 Tax Act eliminated the corporate alternative minimum tax ("AMT") and allowed a corporate taxpayer to take certain refundable credits for AMT previously paid. Under the 2017 Tax Act, such credits were taken during a four-year period that included taxable years beginning 2018, 2019, 2020 and 2021. The CARES Act allows corporations to claim such credits in a two-year period including taxable years beginning in 2018 and 2019 (and 100% of any remaining credits in the taxable year beginning in 2019). Alternatively, a corporation can make an election to take 100% of the refundable AMT credit in 2018.

Business Interest Limitation

The 2017 Tax Act generally limited the amount of a taxpayer's deduction for business interest to the sum of its business interest income, its floor plan financing interest (interest related to certain debt incurred in the acquisition of motor vehicles), and 30% of its "adjusted taxable income." Generally, "adjusted taxable income" equals a taxpayer's net income before interest expense, depreciation and amortization (EBITDA) in taxable years beginning before January 1, 2022, and its net income before interest expense (EBIT) thereafter. The CARES Act changes the 30% adjusted taxable income limitation to a 50% limitation for taxable years beginning in 2019 and 2020. In addition, a taxpayer can elect to substitute its 2019 adjusted taxable income for its 2020 adjusted taxable income for purposes of calculating its business interest limitation in the taxable year beginning in 2020.

Special rules apply to partnerships under the 2017 Tax Act and the CARES Act. The business interest limitation under the 2017 Tax Act applies at the partnership level and any business interest not allowed as a deduction to a partnership for any taxable year is treated as excess business interest which is allocated to the partners. Excess business interest allocated to a partner may only be used to offset excess taxable income from the partnership in succeeding taxable years. The CARES Act treats half of the partner's share of excess business interest for the taxable year beginning in 2019 as deductible by the partner in the taxable year beginning in 2020 (without regard to the normal limitations) and the remaining half as subject to the normal limits specified by the 2017 Tax Act with respect to partnership interest expense. The CARES Act also changes the 30% adjusted taxable income limitation to a 50% limitation for the partnership's taxable year beginning in 2020.

Qualified Improvement Property

The 2017 Tax Act provided for a 100% bonus depreciation deduction for property that is acquired and placed in service after September 27, 2017 and before January 1, 2023 if such property has a depreciable recovery period of 20 years or less. The legislative history of the 2017 Tax Act indicated that Congress intended for qualified improvement property, which is certain improvements to the interior of a nonresidential building, to have a 15-year recovery period; however, due to a drafting error, qualified improvement property had a 39-year recovery period. The CARES Act fixes the "retail glitch" by assigning a 15-year recovery period to qualified improvement property, which makes it eligible for bonus depreciation.

Tax Treatment of Emergency Relief Funding

The CARES Act permits the Department of the Treasury to make loans, loan guarantees, and other investments to support eligible businesses, including air carriers. The CARES Act authorizes Treasury to write regulations that provide that the acquisition of warrants, stock options, stock or other equity by the U.S. government pursuant to these investments will not result in an ownership change for purposes of Section 382 of the Internal Revenue Code. Administrative guidance likely will be needed in order to address issues such as the effect of sales by the government of these investments. Similar issues arose in connection with investments by the government under the TARP program created to address the 2008 financial crisis.

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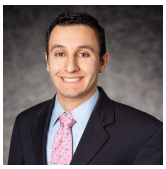

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