

March 27, 2020

TAX RELIEF IN THE CARES ACT

To Our Clients and Friends:

On Friday, March 27, 2020, Congress passed and President Donald Trump signed into law the third major piece of legislation intended to address the economic impact of the coronavirus (COVID-19) outbreak. The bill, titled the Coronavirus Aid, Relief, and Economic Security Act (the “*CARES Act*”), provides for a number of temporary and permanent changes to the Code.^[1] This alert addresses the provisions of the CARES Act most relevant to the business community.

Modifications of rules applicable to the use of business losses, including net operating losses (“NOLs”). The CARES Act temporarily suspends a number of the business loss limitations that were added to the Code in 2017 as part of the legislation colloquially known as the “Tax Cuts and Jobs Act” (the “*2017 Act*”).^[2] The 2017 Act eliminated the ability of taxpayers to carry back NOLs to previous taxable years, and, although the 2017 Act provided for the indefinite carry forward of NOLs, it in general limited the use of NOLs carried forward to 80 percent of a taxpayer’s current-year taxable income.^[3]

The CARES Act modifies the Code provisions applicable to NOLs in two significant respects. First, under the CARES Act, a taxpayer may carry back NOLs from tax years beginning in 2018, 2019, or 2020 up to five years. NOLs cannot be carried back to offset foreign subsidiary earnings deemed repatriated under section 965. However, taxpayers can elect to exclude any tax years in which the foreign earnings were included in gross income from the calculation of the five-year carryback period, effectively allowing taxpayers to “skip” prior taxable years and reach back to taxable years past the five-year cutoff. Real estate investment trusts (“*REITs*”) will not be able to carry back losses, and losses may not be carried back to any REIT year (regardless of whether the taxpayer incurring the loss is currently a REIT).

Second, for taxable years beginning before January 1, 2021, the CARES Act removes the limitation on NOLs that prevents taxpayers from offsetting in excess of 80 percent of a taxpayer’s current taxable income, temporarily allowing NOLs to offset up to 100 percent of a taxpayer’s current taxable income.^[4]

The CARES Act also modifies the excess business loss limitation applicable to noncorporate taxpayers for 2018, 2019, and 2020, which limited the ability to offset business losses against other income to \$250,000, providing a benefit for these taxpayers by temporarily allowing such business losses to offset up to 100 percent of other taxable income.

Modifications of limitations on deductibility of business interest expense. Generally, the amount of a taxpayer’s business interest expense allowable as a deduction is limited under section 163(j) to 30 percent of the taxpayer’s adjusted taxable income (“*ATI*”), which currently is calculated in a manner

similar to EBITDA, subject to certain modifications. The CARES Act would, for tax years beginning in 2019 and 2020, increase this limit from 30 percent to 50 percent of ATI.[5]

Further, taxpayers may elect to use their 2019 ATI in place of their 2020 ATI for purposes of determining business interest deductibility in 2020.

This 50 percent limit on ATI does not apply to partnerships. Instead, any interest disallowed at the partnership level is passed on to its partners, and is suspended at the partner level under the 2017 Act rules. In 2020, however, 50 percent of this suspended interest “frees up,” and will be fully deductible, while the other 50 percent will remain suspended until the partnership allocates excess taxable income or excess interest income to the partner (or until the partnership is no longer subject to section 163(j)).

Employer payroll tax extension. Certain employer payroll taxes (generally, the 6.2 percent Social Security employer payroll taxes imposed under section 3111(a)) for the period beginning on the date of enactment until the end of the year are deferred.[6] Fifty percent of those taxes are deferred until December 31, 2021, and the remaining 50 percent are deferred until December 31, 2022.[7]

Exclusion of employer-funded student debt relief from employee taxable income. The CARES Act would add employer payments made before January 1, 2021 to an employee or lender for student loan principal and interest to the list of employee education assistance programs that an employee can exclude from his or her taxable income.[8] The total amount of payments from employee education assistance programs that an employee can exclude from income remains capped at \$5,250 per calendar year.[9] These employee education assistance exclusions are unavailable for (i) programs that discriminate in favor of highly compensated employees or (ii) programs under which more than 5 percent of amounts paid are provided to 5 percent or greater owners.

Refundable employee retention credit up to \$5,000 per employee. The CARES Act would add an employment tax credit for each calendar quarter equal to 50 percent of qualified wages paid to each eligible employee for that calendar quarter, up to \$10,000 of wages per employee for all calendar quarters.[10] This credit can be used by businesses (i) the operations of which are fully or partially suspended by a COVID-19 governmental order limiting commerce, travel or group meetings or (ii) that suffer a 50 percent loss in gross receipts in a fiscal quarter in 2020 relative to the same quarter in 2019, until the business recovers to 80 percent of gross receipts relative to the same quarter of 2019.[11]

The qualifications differ for employers of different sizes. For employers with more than 100 full-time employees, qualified wages are only those wages paid to employees during the period that the employees are not providing services due to certain COVID-19-related circumstances. For employers with 100 or fewer full-time employees, all employee wages paid during the applicable period qualify for the credit, whether or not the employee is providing services to the employer.[12]

The credit is effective for wages paid after March 12, 2020 and before January 1, 2021.

Refundable AMT credit modification. The corporate alternative minimum tax (“AMT”) was repealed by the 2017 Act. However, corporate AMT credits were made available as refundable credits over

several years, ending in 2021. The CARES Act accelerates the ability of companies to recover those refundable AMT credits.[13]

Qualified improvement property fixes. The CARES Act makes technical corrections to the 2017 Act to treat qualified improvement property as 15-year property for depreciation purposes, and makes it eligible for bonus depreciation. These corrections are retroactive to the effective date of the 2017 Act (January 1, 2018).

Refundable tax credit for individuals. The CARES Act would provide up to a \$1,200 refundable tax credit for individual returns (\$2,400 for joint returns), with additional amounts of \$500 per child in certain cases.[14] The bill requires the Internal Revenue Service to refund or credit these amounts “as rapidly as possible,” but in no event will any such refund or credit be allowed after December 31, 2020.[15]

These amounts are reduced for taxpayers with \$75,000 or more in adjusted gross income for individual filers (\$150,000 or more for joint filers), and completely phased out above \$99,000 for individual filers (\$198,000 for joint filers).[16]

Retirement fund distributions. Consistent with previously passed disaster-related relief, the CARES Act provides that qualifying individuals can withdraw up to \$100,000 from retirement plans in 2020 without application of the 10 percent early withdrawal penalty.[17] A taxpayer may re-contribute the funds to an eligible retirement plan within three years without regard to that year’s cap on contributions,[18] and income attributable to such distributions would be subject to tax ratably over three years unless the taxpayer elects otherwise.[19]

An individual qualifies for this purpose if the individual or his or her spouse or dependent is diagnosed with COVID-19, the individual experiences adverse financial consequences as a result of being quarantined, furloughed, laid off, having work hours reduced, being unable to work due to lack of child care due to COVID-19, closing or reducing hours of a business owned or operated by the individual, or other factors as determined by the Secretary of the Treasury.[20]

Excise tax holidays. Under the CARES Act, a federal excise tax holiday would apply to: (i) federal taxes applicable to aviation kerosene, including at the refineries, terminals, or importation facilities[21] and (ii) alcohol and distilled spirits in the production of hand sanitizer.[22]

SBA loan forgiveness income exclusion. The CARES Act allows certain small business loan forgiveness necessary to maintain payroll or pay mortgages, rent or utilities, and would exclude income resulting from that forgiveness from taxable income.[23]

Charitable deduction of \$300. The CARES Act allows an “above the line” charitable deduction of up to \$300 for individuals who do not itemize deductions on their tax returns.[24]

[1] Unless indicated otherwise, all “section” references are to the Internal Revenue Code of 1986, as amended (the “*Code*”).

[2] Pub. L. 115-97.

[3] See sections 172(a)(2), (b)(1)(A).

[4] CARES Act, section 2303(a)(1).

[5] CARES Act, section 2306(a).

[6] CARES Act, section 2302.

[7] CARES Act, section 2302(d)(3).

[8] CARES Act, section 2206.

[9] Section 127(a)(2).

[10] CARES Act, section 2301.

[11] CARES Act, section 2301(c)(2). All 501(c)(3) exempt organizations qualify, regardless of COVID-19-related suspension of operations or loss in gross receipts. CARES Act, section 2301(c)(2)(C).

[12] The number of employees used for this purpose is the average number of employees in 2019. CARES Act, section 2301(c)(3)(A)(i).

[13] CARES Act, section 2305.

[14] CARES Act, section 2201(a).

[15] CARES Act, section 2201(a).

[16] CARES Act, section 2201(a). Amounts are based on the taxpayer’s 2019 tax return if filed, or, in the alternative, the taxpayer’s 2018 tax return.

[17] CARES Act, section 2202(a).

[18] CARES Act, section 2202(a)(3)(A).

[19] CARES Act, section 2202(a)(5)(A).

[20] CARES Act, section 2202(a)(4)(A).

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- [21] CARES Act, section 4007.
- [22] CARES Act, section 2308.
- [23] CARES Act, section 1102.
- [24] CARES Act, section 2204.



The availability of the tax relief in the CARES Act to any specific business or individual is subject to a number of qualifications and conditions. Gibson Dunn’s lawyers are available to assist with any questions you may have regarding these developments. For further information, please contact the Gibson Dunn lawyer with whom you usually work, any member of the Tax Practice Group, or the following authors:

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