March 27, 2020

CARES Act: Federal Income Tax Relief for Individuals and Businesses in Response to the Coronavirus Pandemic

On March 27, 2020, the President signed into law the "Coronavirus Aid, Relief, and Economic Security Act," or the "CARES Act" (the "Act").[1] The stated purpose of the Act is to provide emergency assistance and health care response for individuals, families and businesses affected by the 2020 coronavirus pandemic. The Act signifies the third phase of Congress's legislative moves to provide relief in response to the pandemic.[2] The Act makes a number of significant changes to the U.S. federal income taxation of both individual taxpayers and businesses, including with respect to elements of the broad tax reform enacted at the end of 2017 known as the "Tax Cuts and Jobs Act" (the "TCJA"), as well as certain technical corrections to existing law. Such changes generally include:

Provisions Generally Affecting Individuals

- *Immediate Cash Payment*. Providing a $1,200 ($2,400 in the case of a joint return) tax credit to eligible U.S. individuals, with an additional $500 tax credit per qualifying child, subject to phase-out such that taxpayers with adjusted gross income in excess of $99,000 ($198,000 in the case of a joint return) would not receive such credit. These amounts are to be paid directly to individuals as rapidly as possible by the government.
- *Expanded Charitable Contribution Deductions*.
  - *Extra Deduction for Charitable Contributions by Non-Itemizers*. For eligible individuals who do not itemize tax deductions, permitting up to $300 of certain charitable contributions made in cash in 2020 to be treated as "above-the-line" deductions.
  - *Increased Deductibility for Charitable Contributions*. Increasing the deductibility of certain charitable contributions made in cash by electing individuals during 2020, by suspending the 60% of adjusted gross income limitation.
- *Increased Availability of Losses for Non-Corporate Taxpayers*. Delaying applicability of the TCJA's loss limitation rules applicable to pass-through businesses and sole proprietors, by making the

[1] Please see our separate client alert discussing other elements of the Act.

[2] The first two phases were signified by the "Coronavirus Preparedness and Response Supplemental Appropriations Act, 2020" and the "Families First Coronavirus Response Act" (discussed in our prior client alert).

limitations on the utilization of "excess business losses" (generally defined as deductions attributable to a trade or business that exceed the income from such business by a threshold amount ($500,000 for joint taxpayers)) applicable starting with the 2021, rather than 2018, tax year.

- *Retirement Accounts.*
  - *Flexibility Regarding Withdrawals from Retirement Accounts.* In the case of distributions to certain individuals directly affected by coronavirus, waiving the 10% withdrawal penalty tax on early distributions from eligible retirement plans (up to $100,000), permitting coronavirus-related distributions to be recontributed to such retirement plans over a three-year period (not subject to the annual cap that would otherwise apply), and allowing any taxable income attributable to such distributions to be recognized over a three-year period.
  - *Suspension of Minimum Distribution Requirements.* Allowing certain defined contribution plans and IRAs to suspend required minimum distributions in 2020, with respect to certain eligible participants, so that such participants are not forced to receive distributions based on 2019 year-end account valuations given the significant decline in market conditions since the end of 2019.
- *Income Exclusion for Certain Employer Payments of Student Loans.* Excluding from an employee's income payments made by an employer (whether to the employee or the applicable lender) before 2021 of principal or interest due with respect to a qualified education loan incurred by the employee for education of the employee (subject to the existing $5,250 annual cap on the amount of all educational assistance that an employee may receive from its employer on a tax-free basis).

Provisions Generally Affecting Businesses

- *Extended Due Date for Employer Portion of Social Security and Self-Employment Taxes.*[3] Delaying the payment of certain employer payroll taxes and 50% of self-employment taxes for the period between the enactment of the Act and December 31, 2020, until December 31, 2021 and December 31, 2022, with 50% of such taxes payable by each such date.
- *Increased Availability of NOL Carryforwards and Carrybacks.* With respect to net operating losses ("NOLs"), (1) for tax years prior to 2021, suspending the TCJA rule limiting the use of NOL carryforwards in a given year to 80% of taxable income and (2) for losses generated in the 2018, 2019

3 On Friday March 20th, the government announced that the due date for filing 2019 income tax returns, making payments of 2019 income taxes, and making estimated tax payments (including in respect of self-employment tax) for the first quarter of 2020 will be delayed to July 15th, 2020 (discussed in our prior client alert).

or 2020 tax year, permitting NOL carrybacks to the prior five tax years, with special rules for real estate investment trusts and insurance companies.

- *Increased Section 163(j) Limitation on Deductibility of Interest*. Increasing the Section 163(j) business interest deductibility limitation, enacted pursuant to the TCJA, from 30% of an amount generally equivalent to earnings before interest, taxes, depreciation and amortization ("EBITDA") to 50% of EBITDA for the 2019 and 2020 tax years (subject to the ability to elect out of such increased limitation), with taxpayers able to use 2019 EBITDA for purposes of calculating their Section 163(j) limitation for the 2020 tax year. Different technical rules apply for partnerships.

- *Employee Retention Credit for Employers Subject to Closure or Significant Decline in Business Due to Pandemic*. Allowing employers subject to a full or partial suspension of business due to orders from a governmental authority, or suffering a more than 50% decline in gross revenue (as compared to the same quarter from the prior year), a refundable credit against applicable employment taxes for each calendar quarter, in an amount equal to 50% of the "qualified wages" (including allocable qualified health plan expenses) paid to each employee of such employer for such calendar quarter during the period from March 13, 2020 through the end of 2020 (with "qualified wages" for each employee capped at $10,000 for all calendar quarters). For eligible employers whose average number of full-time employees during 2019 was greater than 100, "qualified wages" are wages paid to employees when they are not providing services due to business operations being fully or partially suspended as a result of a government shut-down order; for eligible employers whose average number of full-time employees during 2019 was 100 or fewer, "qualified wages" include all employee wages, whether the employer is subject to a shut-down order or open for business. In addition, certain controlled-group rules apply to treat multiple persons as a single employer for purposes of these rules. To avoid a double benefit, any wages taken into account in determining the credit allowed under these rules will not be taken into account in determining the employer credit for paid and family leave. Moreover, the eligible employer is not allowed a tax deduction with respect to wages for which the employee retention credit is claimed.

- *Accelerated Recovery of AMT Credit Carryforward Refunds*. Accelerating the ability for corporations to recover alternative minimum tax ("AMT") credit carryforwards, which the TCJA made refundable over a period running through 2021 in connection with its repeal of the corporate AMT, by permitting such credits to be recovered immediately.

- *Immediate Deduction for Certain Capital Expenditures*. Enabling certain businesses (including those in the hospitality industry) to take an immediate tax deduction (rather than depreciation deductions over a 39-year period) for costs associated with improving building facilities.

- *Increased Deductibility for Charitable Contributions*. Increasing the deductibility of certain charitable contributions made in cash by electing corporations during 2020, by increasing the 10% of taxable income limitation to 25%.

The legislative process for passing the Act was expedited given growing adverse economic impacts resulting from the coronavirus pandemic. It is likely that the Act may raise certain technical questions, and the Internal Revenue Service and Treasury Department are likely to undertake regulatory projects to provide guidance with respect to many aspects of the Act. The Act may have unexpected consequences on transactions, including transactions that have closed in prior years (for example, the NOL carryback provisions may have unexpected effects on closed M&A deals that did not anticipate these rules would return after they were repealed by the TCJA). We urge everyone to consider the impacts of the Act on themselves, on their businesses and on pending or closed transactions.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

Brian S. Grieve +1-212-373-3768 bgrieve@paulweiss.com	Robert Holo +1-212-373-3637 rholo@paulweiss.com	Patrick N. Karsnitz +1-212-373-3084 pkarsnitz@paulweiss.com
David W. Mayo +1-212-373-3324 dmayo@paulweiss.com	Brad R. Okun +1-212-373-3727 bokun@paulweiss.com	Lindsay B. Parks +1-212-373-3792 lparks@paulweiss.com
Jeffrey B. Samuels +1-212-373-3112 jsamuels@paulweiss.com	David R. Sicular +1-212-373-3082 dsicular@paulweiss.com	Scott M. Sontag +1-212-373-3015 ssontag@paulweiss.com

Associate Sohail Itani contributed to this Client Memorandum.