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Tax
Employee Benefits & Executive Compensation

March 27, 2020

Key Tax and Employee Benefits Provisions of the CARES Act

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On March 27, the United States House of Representatives passed the Coronavirus Aid, Relief, and Economic Security (CARES) Act (the "Act"). The Act was previously passed by the Senate and is expected to be signed into law by the President. This alert summarizes key tax and employee benefits provisions of the Act.

Payments to Individuals

The Act calls for the Department of the Treasury to make cash payments to eligible individuals as rapidly as possible. The payment amounts generally will be $1,200 per adult individual ($2,400 for joint filers) plus $500 for each child. The payments are phased out for individuals reporting adjusted gross income over $75,000 ($150,000 for joint filers) for 2019 (or 2018, for those who have not yet filed a 2019 return). Payments will be treated as advances against a tax credit allowable on 2020 tax returns.

Delayed Payment of Payroll Taxes

The Act defers the payment of employer Social Security payroll tax (currently 6.2% of covered wages), and 50% of self-employment taxes, through Dec. 31, 2020. The deferred taxes are payable over two years, in 2021 and 2022. Employers with small-business loan debt forgiven under the Act are ineligible for the payroll tax deferral.

Retirement Plan Provisions

Penalty-Free Distributions

The Act allows an eligible individual to receive a "coronavirus-related distribution" of up to $100,000 from an eligible retirement plan (such as a tax-qualified pension or 401(k) plan, 403(b) plan, IRA, or 457(b) plan) before Dec. 31, 2020. Individuals are eligible for a "coronavirus-related distribution" if they (i) are diagnosed with COVID-19, (ii) have a spouse or dependent who is diagnosed with COVID-19, or (iii) experience adverse financial consequences as a result of any of the following:

- Being quarantined
- Being furloughed or laid off or having work hours reduced due to COVID-19
- Being unable to work due to lack of child care due to COVID-19
- The closing or reduced hours of a business owned or operated by the individual due to COVID-19
- Other factors as determined by the Department of the Treasury

Funds distributed are treated as a tax-exempt rollover contribution if repaid during the three-year period beginning on the day after the date on which the distribution was received. If funds are not repaid, they are taxed as income over three years (beginning with the year of distribution).

Plan Loan Limit Increased

During the 180 days after the Act's enactment, the limit on plan loans for eligible individuals is doubled—from the lesser of $50,000 or half the plan's vested benefit to $100,000 or the full value of the plan's vested benefit. Also, the Act affords individuals affected by COVID-19 an extra year to repay an outstanding retirement plan loan that is otherwise due by Dec. 31, 2020.

Minimum Required Distributions

The Act waives the requirement that individuals receive required minimum distributions under individual account plans (e.g., IRAs and defined contribution plans) for 2020.

Pension Funding

The Act extends the time to make any pension fund contributions that would otherwise be due during 2020 to Jan. 1, 2021. The contributions deferred must be increased for interest.

For purposes of determining whether underfunded benefit restrictions apply, a plan sponsor may elect to treat the plan's adjusted funding target attainment percentage (AFTAP) for the last plan year ending before Jan. 1, 2020, as the AFTAP for plan years that include calendar year 2020.

Health Plan Provisions

For plan years beginning on or before Dec. 31, 2021, a high-deductible health plan may provide telehealth and other remote care services without a deductible. The Act also will allow health savings accounts (HSAs) and other spending accounts, such as flexible spending arrangements (FSAs), to cover menstrual products without a prescription.

Unemployment Benefits

The Act extends unemployment benefits for up to 39 weeks to individuals who are unemployed, or unable or unavailable to work because, among other things, (i) the individual has been diagnosed with COVID-19 or is experiencing symptoms of COVID-19 and is seeking a medical diagnosis, (ii) a member of the individual's household has been diagnosed with COVID-19, (iii) the individual is providing care for a family or household member who has been diagnosed with COVID-19, (iv) the individual must provide care for a child who is unable to attend school because of COVID-19, or (v) the individual's place of employment is closed due to COVID-19. Self-employed individuals who meet these criteria can also qualify for unemployment benefits. Individuals are not eligible for this benefit if they can telework for pay or are receiving paid sick leave or other paid leave benefits. This unemployment benefit applies to cases of unemployment beginning on or after Jan. 27, 2020, and before Jan. 1, 2021.

In addition, employees who qualify for unemployment benefits are eligible for an additional $600/week for weeks of unemployment ending on or before July 31, 2020. Called "Federal Pandemic Unemployment Compensation," an individual need not be unemployed due to COVID-19 to receive this additional unemployment benefit.

The Act also provides full funding of state "short-term compensation" programs through Dec. 31, 2020. Such programs provide prorated unemployment benefits when an employer reduces workers' hours rather than laying off workers.

Employee Retention Tax Credits

To induce employers to keep their workers on payroll during the COVID-19 crisis, the Act provides employers with a temporary refundable credit against the employer portion of Social Security taxes in an amount equal to 50% of the qualified wages of each employee per calendar quarter, up to an aggregate of $10,000 of the qualified wages paid per employee.

Qualified wages are limited to wages paid after March 12, 2020, and before Jan. 1, 2021. For employers that averaged more than 100 full-time employees in 2019, qualified wages for any period cannot exceed the wages the employee would have been paid for working an equivalent duration during the 30 days immediately preceding such period. Qualified wages include amounts paid or incurred by an employer to provide an employee with group health coverage.

An employer is generally eligible for the credit during a time in which it either (i) fully or partially suspends operations for any calendar quarter in 2020 (including the quarter ending March 31, 2020) due to governmental COVID-19 orders, or (ii) suffers a significant decline in gross receipts. A significant decline in gross receipts is generally defined as a calendar quarter in 2020 in which an employer's gross receipts are less than 50% of the gross receipts for the same quarter during 2019. Governmental employers and employers that receive stimulus small-business payroll loans are not eligible for this tax credit. Tax-exempt 501(c) organizations are eligible for the credit if they fully or partially suspend operations due to governmental COVID-19 orders.

For employers that averaged more than 100 full-time employees in 2019, the credit applies with respect to the qualified wages of furloughed employees during the time that the employer qualifies for the credit. Employers that averaged 100 or fewer full-time employees in 2019 can qualify for the credit with respect to the qualified wages of both employees who continue working and those who are furloughed. Certain affiliated persons and entities are treated as a single employer for purposes of the employee retention credit.

Expanded Allowance of Charitable Contribution Deductions

The Act allows non-itemizing individuals to deduct up to $300 for contributions of cash to certain charities during taxable years beginning in 2020. For individuals who itemize deductions on their 2020 returns, the existing income-based deduction limitations on qualified cash contributions to certain charities are temporarily suspended. Contributions to donor-advised funds, supporting organizations, and most private foundations will not qualify for purposes of these rules. The limitation on deductions for cash contributions by corporations to charities other than donor-advised funds, supporting organizations, and most private foundations is increased from 10% to 25% of taxable income for donations during the 2020 calendar year. The limitation on deductions for donations of food inventory is increased from 15% to 25% of taxable income (up from 15%) for donations during the 2020 calendar year.

Exclusion for Certain Employer Payments of Student Loans

The Act allows employees who receive employer contributions toward student loan repayments to exclude those contributions from their taxable income. To qualify for the exclusion, the employer must make such student loan payments (either to the employee or directly to a lender) after the date of enactment and before Jan. 1, 2021. An employee may not exclude more than $5,250 of all employer-provided educational assistance (including tuition assistance and other expense payments, as well as loan repayments) per year. To the extent an employee receives repayment assistance that qualifies for this exclusion, the employee's ability to deduct student loan interest will be reduced.

Expanded Ability to Use Net Operating Losses

The Act temporarily lifts restrictions on corporations' use of net operating losses (NOLs) for tax years beginning in 2018, 2019, and 2020. Corporations may now generally carry back NOLs from any of those years for up to five years (which may allow offsets to income taxable at the pre-2018 35% rate). The 80% cap on NOL deductions is eliminated for the effective period, so that corporate taxpayers may fully deduct NOLs against income from tax years beginning before 2021. These changes may allow taxpayers to amend returns and claim refunds for prior years.

Modification of the Limitations on Deducting Excess Business Losses

Beginning with the 2018 tax year, noncorporate taxpayers were prohibited from deducting "excess business losses" against nonbusiness income. Generally, excess business losses are business losses that exceed the taxpayer's gross income by more than $250,000 ($500,000 for joint filers; both figures adjusted for inflation). Under the Act, the limitations on deducting excess business losses are deferred until tax years beginning after Dec. 31, 2020, which may allow taxpayers to file amended returns and claim refunds for 2018 and 2019.

Changes to Timing of the Alternative Minimum Tax (AMT) Credit

The Act accelerates a corporation's ability to claim the AMT refundable credit, which was previously scheduled to be fully recoverable through 2021.

Modifications of Limitation on Business Interest

The Act modifies Section 163(j) of the Internal Revenue Code to allow business interest expense deductions up to 50% (increased from 30%) of "adjusted taxable income" for 2019 and 2020, although partnerships remain subject to the 30% limitation for 2019. In case of a partnership, if any "excess business interest" is disallowed for 2019, allocated to its partners, and carried forward, 50% of the carryforward amount will be fully deductible in 2020. The deductibility of the other 50% will remain subject to the restrictions under the normal rules. For 2020, a business may elect to use its 2019 income in determining its business interest deduction limitation.

Technical Amendments Regarding Qualified Improvement Property

The Act includes a technical correction to fix the so-called "retail glitch," a drafting error in the Tax Cuts and Jobs Act (enacted in 2017) that resulted in an unintended lengthening of the depreciation period for certain nonresidential building improvements. As a result, such qualified improvement property now has a 15-year recovery period (or a 20-year recovery period under an alternative depreciation system) and is eligible for "bonus depreciation," allowing an immediate deduction for the full cost of such property. This technical correction is intended to be retroactive, so that businesses may amend previously filed returns to claim increased deductions for qualified improvement property.

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

For the calendar year 2020, the Act waives the federal excise tax imposed on distilled spirits used for or contained in hand sanitizer that is produced and distributed in a manner consistent with guidance issued by the Food and Drug Administration related to the outbreak of COVID-19.

Suspension of Certain Aviation Excise Taxes

The Act suspends certain aviation-related federal excise taxes for the period beginning after the date of enactment through the end of 2020. No tax will be imposed on amounts paid after the date of enactment for the taxable transportation by air of people or of property during this excise tax holiday. Although several excise taxes imposed on aviation-grade kerosene used in commercial aviation will be suspended under the Act, such fuel will continue to be subject to the 0.1-cent-per-gallon tax collected to fund the Leaking Underground Storage Tank Trust Fund during the excise tax holiday period.

Tax Treatment of Small-Business Loan Forgiveness

The Act establishes a loan forgiveness program for certain loans guaranteed under the Small Business Act. For more detail on this and other loan programs under the Act, please see our alert "Emergency Relief Legislation for Businesses and Individuals: CARES Act-Loan Programs." The amount of such loan forgiveness will be excluded from taxable income for federal income tax purposes.

Postponed Income Tax Filing and Payment Deadlines

The Act does not provide for additional time to file federal income tax returns or make federal income tax payments. However, the Internal Revenue Service ("IRS") has announced that any taxpayer with a federal income tax payment or federal income tax return due on April 15 will now have until July 15 to file and make such income tax payments. This applies both to the 2019 tax year and to estimated payments for 2020. The IRS confirmed that second-quarter estimated payments will be due (June 15) before first-quarter estimated payments (July 15) this year. Notably, this relief does not apply to any other federal taxes (including gift or estate taxes).

It is expected that state and local governments will follow the lead of the federal government, and some have, but there is still uncertainty in some jurisdictions. For example, California has expressly moved back the deadline to July 15 for filing and paying income taxes. In New York, Governor Cuomo announced that the state intends to move the deadlines to July 15, but there appears to be no written notice or policy at this time.

To see our prior alerts and other material related to the pandemic, please visit the Coronavirus/ COVID-19: Facts, Insights & Resources page of our website by clicking here.

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