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CARES Act: Tax benefits for individuals and businesses

The Coronavirus, Aid, Relief, and Economic Security Act (CARES Act), enacted on March 27, 2020, in response to the 2019 novel coronavirus (COVID-19) pandemic provides assistance for businesses and individuals. This assistance comes in the form of various tax provisions intended to provide immediate and future tax benefits. The CARES Act also makes certain technical corrections to and rolls back certain provisions of the Tax Cuts and Jobs Act (TCJA).

The following are six rebates and other tax incentive provisions applicable to individuals:

Six tax benefits for individuals

1. Tax rebates

The CARES Act provides immediate rebates of $1,200 per eligible individual, $2,400 for eligible couples filing a joint return and $500 per qualifying child. The statute refers to these as credits against tax imposed for 2020, although the Internal Revenue Service (IRS) is directed to pay out these rebates based on 2019 or 2018 return information.

Eligible individuals are U.S. citizens or residents with a social security number who cannot be claimed as a dependent by someone else. Eligible individuals do not include estates or trusts. The credits are reduced by 5 percent of the amount by which the eligible individual's adjusted gross income (AGI) exceeds $150,000 in the case of a joint return (fully phased out at $198,000), $115,500 in the case of a head of household (fully phased out at $136,500) and $75,000 for individuals (fully phased out at $99,000).

The amount of the credit on the 2020 return is reduced, but not below zero, by any immediate rebate paid to the individual. Thus, if the rebate is less than the allowable credit for 2020, the individual may claim the excess credit on their 2020 return. If the rebate is more than the allowable credit, the individual does not have to repay the excess.

The IRS is directed to issue these advance refunds or credits as soon as possible. An individual who was an eligible individual for 2019, and filed their return, is to be treated as having made a payment against their 2019 tax equal to the amount of the credit the individual would be entitled to if the credit related to 2019, and is entitled to a refund. If the individual has not yet filed a return for 2019, the IRS may base the credit on the individual's 2018 return and issue a refund. If no return has been filed for either year, the IRS may base the credit on certain social security filings and issue a refund.

2. Special rule for use of retirement funds

The normal 10 percent penalty tax on early distributions from qualified retirement plans, including Individual Retirement Accounts (IRAs), does not apply to up to $100,000 of coronavirus-related distributions made during calendar year 2020. Furthermore, an individual who receives such a distribution may, within three years from the date of the distribution, make contributions to an eligible retirement plan, and in such case the individual is treated as having made an eligible rollover.

A coronavirus-related distribution is a distribution to an individual:

- Diagnosed with COVID-19
- Whose spouse or dependent is diagnosed with COVID-19
- Who experiences adverse financial consequences as a result of 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, or closing or reducing the hours of a business owned or operated by them due to COVID-19, or other factors as determined by the IRS.

In the case of a coronavirus-related distribution, unless the taxpayer elects otherwise, the amount required to be included in income shall be included ratably over three years starting with the year of the distribution.

The amount of loans a retirement plan is authorized to make to an authorized individual without such loan being treated as a distribution is increased from $50,000 to $100,000, with the previous cap of 50 percent of accrued vested benefits increasing to 100 percent, in the case of loans made in the first 180 days after the date of enactment of the CARES Act. Furthermore, any payment on an outstanding loan to an authorized individual otherwise due during the remainder of 2020 is to be delayed one year, and any subsequent repayments are to be appropriately adjusted.

Plan sponsors will need to amend their plans in accordance with normal amendment rules and any special additions/exceptions to these rules provided under the CARES Act to allow for coronavirus-related distributions and/or an increase in loan amounts (unless the plan sponsor's retirement plan cross-references the amended Internal Revenue Code limits regarding plan loan amounts).

3. Temporary waiver of RMD rules for 2020

A retirement plan participant or IRA owner generally is required to take required minimum distributions (RMDs) beginning in the calendar year after attaining age 72 (or 70 1/2 for one who attained that age before 2020). The CARES Act temporarily waives the RMD rules for amounts that would otherwise be required to be distributed in 2020 from defined contribution plans, including IRAs and governmental 457(b) plans, but not defined benefit plans and non-governmental 457(b) plans. The waiver also applies to RMDs that need to be taken by April 1, 2020, because an individual attained age 70 1/2 during 2019 and delayed their first minimum distribution to 2020.

Individuals who have taken out amounts in 2020 as minimum distributions might have the opportunity to roll the amount into their IRA if they meet the 60-day rollover requirements.

4. Above-the-line deduction for charitable deductions for years beginning after 2019

The CARES Act allows up to $300 of qualified cash charitable contributions to be taken in computing AGI by an individual who does not itemize deductions. This above-the-line deduction cannot be claimed for contributions to supporting organizations, donor-advised funds and most private foundations. This provision does not apply to amounts treated as being made in the current year by reason of a carryover from a prior year. This deduction is effective for taxable years beginning in 2020.

5. Modification of limitation on charitable contributions during 2020

The CARES Act permits cash contributions by individuals made during 2020 to charitable organizations other than supporting organizations, donor-advised funds and most private foundations to be deducted up to the taxpayer's AGI, notwithstanding the normal percentage limitations. This applies only after all other charitable contributions that are otherwise allowed are taken into account. If the qualified contributions for the year exceeds the contribution base for the year, the excess is carried forward to each of the five succeeding years.

Note: The limitation for corporations for such cash contributions and contributions of food inventory is increased to 25 percent of taxable income. Any excess is treated as a carryover.

6. Exclusion for certain employer payments of student loans

Employer payments to an employee or a lender for principal or interest on a qualified education loan paid under a section 127 educational assistance program are excludable from income of the employee (subject to the limitations set forth in section 127). To the extent excludable under section 127, the interest is not then deductible by the employee under section 221. The payments are subject to the overall limit under section 127 of $5,250 per employee. This section applies to payments made after the date of enactment and before Jan. 1, 2021.

Seven tax benefits for businesses

The CARES Act enacts a number of provisions designed to provide both immediate, and in some cases long-term, increases in cash flow and tax decreases for businesses:

1. Employee retention credit for employers subject to closure due to COVID-19

Certain eligible employers engaged in a trade or business during 2020 are entitled to a credit against the employer's share of the Old-Age, Survivors, and Disability Insurance (OASDI) employment taxes (6.2 percent rate) for each calendar quarter equal to 50 percent of the qualified wages for the quarter. The maximum amount of wages taken into account for any employee may not exceed $10,000. If the amount of the credit exceeds the employer's share of OASDI employment taxes, the excess is treated as an overpayment and is to be refunded.

An eligible employer is one that was carrying on a trade or business during 2020 and during any calendar quarter had either:

- The operation of its trade or business fully or partially suspended during the calendar quarter due to orders from an appropriate governmental authority limiting commerce, travel or group meetings due to COVID-19; or
- Beginning with the first calendar quarter in 2020 in which gross receipts are less than 50 percent of the gross receipts for the same calendar quarter in the prior year and ending with the calendar quarter in which gross receipts are greater than 80 percent of gross receipts for the same calendar quarter in the prior year.

For employers with more than, on average, 100 full-time employees (FTEs) during 2019, the qualified wages are wages paid with respect to an employee that is not providing services due to one of the above circumstances, and for employers with less than, on average, 100 FTEs, qualified wages are wages paid during one of the above periods. Qualified wages may not exceed the amount the employee would have been paid for working an equivalent duration during the 30-day immediately preceding period. Qualified wages also include the employer's qualified health plan expenses.

Employers receiving small business interruption loans under the U.S. Small Business Administration's (SBA's) Paycheck Protection Program (PPP) are not eligible for the credit. The IRS is to waive any penalty for failure to deposit employment taxes if the IRS determines that the failure was due to the reasonable anticipation of this credit. The IRS is given authority to advance payments to employers. This benefit applies only to wages paid after March 12, 2020, and before Jan. 1, 2021.

2. Delay of payment of employer payroll taxes

Deposits of the employer's share of OASDI taxes that are required to be made during the period starting with the enactment of the CARES Act and ending on Dec. 31, 2020 (the payroll tax deferral period) will be treated as timely made if half of such deposits are made by Dec. 31, 2021, and the remainder by Dec. 31, 2022.

Additionally, 50 percent of the 12.4 percent self-employment tax for the payroll tax deferral period is not required to be paid until

Dec. 31, 2021, when the first half is due, with the remainder due by Dec. 31, 2022. Such deferred amount is not required to be taken into account in determining an individual's required estimated tax payments for 2020.

This provision does not apply to businesses that have indebtedness forgiven under the SBA's PPP or under similar programs established by the U.S. Department of the Treasury.

3. Modification of net operating losses

The TCJA imposed a limitation on the use of net operating loss (NOL) carryforwards to offset only 80 percent of current year taxable income. The CARES Act retroactively eliminates the 80 percent limitation for taxable years beginning before Jan. 1, 2021, and in the case of a taxable year beginning after Dec. 31, 2020, the limitation for the year is the sum of NOLs from 2017 and earlier years, plus the lesser of the NOLs from 2018 and later years or 80 percent of the taxable income for the year after offset for NOLs from 2017 and earlier years.

The TCJA also eliminated NOL carrybacks. The CARES Act permits NOLs arising in taxable years beginning after Dec. 31, 2017, and before Jan. 1, 2021, to be carried back up to five years. This change will not apply to real estate investment trusts (REITs).

This provision could result in potential refund opportunities for 2018 returns.

The modifications to permit NOLs to be carried back may free up and give greater certainty to the ability to realize economic benefits from tax assets upon a sale of a company. Buyers and sellers of companies should address the ability to carry back losses to pre-closing years, including losses generated by change of control payments and transaction expenses, and the allocation of any related tax benefit, as well as the effect on working capital or other adjustments to the purchase price.

4. Modification of limitation on losses for taxpayers other than corporations

The TCJA enacted section 461(l), which limited a non-corporate taxpayer from using more than $250,000 of trade or business losses ($500,000 for joint returns) generated in a year from offsetting non-trade or business income in that year. The provision first applied to 2018 and expires at the end of 2025. The CARES Act eliminates the restriction retroactively to its initial effective date and delays the effective date for excess business losses to taxable years beginning after Dec. 31, 2020. The CARES Act also completely removes excess farm losses from the limitation. Technical changes are also made with respect to the effect of capital gains and losses on the computation, the effect of a carryover of a disallowed loss in a future year, and the elimination of consideration of income or deductions attributable to services as an employee.

This provision could result in potential refund opportunities for 2018 returns.

5. Modification of credit for prior year minimum tax liability of corporations.

The TCJA repealed the corporate minimum tax and allowed unused credits to offset tax or be refunded in 2018 through 2021 at a certain rate. The CARES Act allows the remaining credit to be refunded in 2019 (or 2018 at the election of the taxpayer) and to file a tentative refund claim no later than Dec. 31, 2020.

This provision could result in potential refund opportunities for 2018 returns.

6. Modification of limitation on business interest

The TCJA limited the business interest expense deduction to 30 percent of the taxpayer's adjusted taxable income (initially similar to earnings before interest, taxes, depreciation, and amortization (EBITDA), but starting in 2022 similar to earnings before interest and taxes (EBIT)). In the case of taxable years beginning in 2019 or 2020, the CARES Act increases the limitation to 50 percent of adjusted taxable income.

In the case of a partnership, the foregoing does not apply to taxable years beginning in 2019, unless a partner elects otherwise, for any excess business interest of the partnership that is allocated to the partner. Fifty percent of such excess business interest is treated as business interest first paid in 2020 not subject to the interest limitation, with the other 50 percent subject to the interest limitation in the same manner as other excess business interest. Furthermore, a taxpayer may elect to apply this limitation by substituting the adjusted taxable income from 2019 for 2020 in computing the limitation. For partnerships, this election must be made by the partnership. Taxpayers may also elect out of the increased limitation, but the election is irrevocable.

7. Qualified improvement property

The TCJA eliminated definitions for certain property, including qualified leasehold improvement property, qualified restaurant property and qualified retail improvement property, and replaced those definitions with a category defined as qualified improvement property. The property was intended to be 15-year property but was inadvertently categorized as 39-year property—the so-called "retail glitch." The CARES Act classifies qualified improvement property as 15-year property retroactively to 2018, which, in addition to shortening the depreciation period, makes the property eligible for bonus depreciation.

This provision could result in potential refund opportunities for 2018 returns.

Our COVID-19 Resource Center has more practical advice like this on the legal considerations impacting your organization's coronavirus response.

For more information on CARES Act tax provisions, contact a member of Tax and Employee Benefits Practice Groups.