

## Business Tax Update: Benefits and Credits Available Under COVID-19 Federal Legislation

On March 27, 2020 Congress passed, and President Trump signed, the Coronavirus Aid, Relief, and Economic Security Act (the CARES Act). The CARES Act is the largest stimulus package in U.S. history, costing \$2.2 trillion, building on prior COVID-19 legislation, including the Families First Coronavirus Response Act (the FFCRA).

This recent legislation eases tax compliance burdens and expands certain tax benefits, providing some relief for the economic pain caused by the COVID-19 pandemic. This alert focuses on the business tax changes, including tax credit programs included in the FFCRA and the CARES Act, as well as certain changes to the Internal Revenue Code (the Code) impacting businesses. First, this information memo discusses advance payroll tax credits under the FFCRA and the employee retention credit under the CARES Act. Then, the memo outlines some of the changes to the Code that benefit businesses and may create much needed cash flow, including a discussion of recent IRS guidance and procedures.

### Advance Tax Credits

Generally, when employers pay their employees, they are required to withhold federal income taxes and the employees' share of Social Security and Medicare taxes from their compensation. Employers are required to deposit these taxes, along with the employer's share of Social Security and Medicare taxes, with the IRS and file quarterly payroll tax returns (Form 941). In order to provide employers with additional liquidity during the COVID-19 crisis, employers who are eligible for the COVID-19 payroll tax credits will be able to retain these payroll taxes, in anticipation of receiving the tax credits described below, rather than remitting them to the IRS.

The payroll taxes available for retention include withheld federal income taxes, the employee's share of Social Security and Medicare taxes, and the employer share of Social Security and Medicare taxes with respect to all employees. To provide for this benefit, the IRS will waive failure to deposit penalties for employers who retain payroll taxes in advance of the credits, as long as the amounts not timely deposited do not exceed the amount of anticipated payroll tax credits.

If the anticipated tax credits exceed an employer's required deposits otherwise due for the calendar quarter, an employer may file IRS Form 7200, Advance Payment of Employer Credits Due to COVID-19, to claim an advance refund in the amount of the excess. Click here for a copy of [Form 7200](#) and the [instructions](#). The IRS has indicated that it will try to issue these refunds on an expedited basis.

### Paid Sick and Family Leave Refundable Credit

The FFCRA provides paid sick leave for employees and amends the Family and Medical Leave Act to include a new qualifying reason for leave related to COVID-19. Businesses with fewer than 500 employees are required to provide these expanded benefits.

To offset the economic burden to employers, the FFCRA includes tax credits for providing employees with this federally mandated paid sick, family and medical leave, as well as for certain expenses incurred with respect to employer-maintained health plans. The credits are applied against payroll taxes and are refundable credits, meaning that any excess credit (that is not applied against taxes due) will be paid in cash to the employer like a typical income tax refund. These credits are outlined below and apply to taxes incurred as of April 1, 2020.

**Sick Leave Credit:** Subject to the limitations described below, employers are generally entitled to a credit against the employer's share of applicable Social Security and Medicare payroll taxes for each quarter equal to 100 percent of the qualified sick leave wages paid to employees during each respective quarter. The amount of this credit is capped per employee, and the cap depends on the circumstances. If sick time is being paid due to: (i) a quarantine or isolation order; (ii) advice by a health care provider to self-quarantine; or (iii) exhibiting coronavirus symptoms and seeking medical diagnosis, the cap equals \$511 per employee, per day or \$5,110 in the aggregate. Otherwise, the cap equals \$200 per individual, per day or \$2,000 in the aggregate.

**Family Leave Credit:** Employers are also entitled to a credit against the same employment taxes noted above for paid qualified family leave wages. Qualified family leave wages are wages payable to an employee who is unable to work because of a need to care for an individual subject to quarantine, or a child due to school closure or a child-care provider being unavailable for reasons related to COVID-19. This credit is equal to two-thirds of the employee's regular pay, capped at \$200 per day or \$10,000 in the aggregate. Up to 10 weeks of qualifying leave can be counted towards the credit.

Eligible employers claiming the credits outlined above must retain records and documentation related to, and supporting, each employee's leave to substantiate the claim for the credits, as well as retain the applicable Forms 941 and 7200, and any other applicable filings made to the IRS requesting the credit. See IRS FAQ for additional information [here](#).

### Employee Retention Credit

Lastly, under the CARES Act, employers (i) whose operations were fully or partially suspended due to a COVID-19-related shut-down order; or (ii) who have had a decline in gross receipts of more than 50 percent when compared to the same quarter last year are eligible for the employee retention credit (the ERC). Employers qualifying for the ERC under prong (ii) are only eligible to claim the credit until gross receipts for a calendar quarter are greater than 80 percent of the gross receipts for the same calendar quarter in the prior year.

The ERC applies against the employer's share of Social Security payroll taxes for each quarter and equals 50 percent of the qualified wages paid to employees after March 12, 2020 and before January 1, 2021. Qualified wages are capped at the first \$10,000 in wages, so the maximum credit is \$5,000 per employee, and do not include the qualified sick and qualified family wages noted above.

If an employer has more than 100 full-time employees on average during 2019, certain limitations apply. Such employers can only claim the ERC for wages paid to employees who are retained but unable to work due to suspension of the employer's business or a decline in gross receipts, i.e., the employer's basis for claiming the credit. Employers may not claim the ERC to the extent they borrow under the Paycheck Protection Program (PPP) provided in the CARES Act. Click [here](#) for a description of that program.

Employers that paid qualified wages between March 13, 2020, and March 31, 2020, inclusive, will include 50 percent of those wages together with 50 percent of any qualified wages paid during the second quarter of 2020 on their second quarter Form 941, 941-SS, or 941-PR to claim the ERC. Employers should not include the ERC on their first quarter Form 941, 941-SS, or 941-PR. See updated cover sheet with Form 941 available [here](#).

### Credit for Health Plan Expenses

For each of the credits outlined above, the wages used to compute the credits may include allocable qualified health plan expenses. These expenses include amounts paid or incurred by the employer to provide and maintain a group health plan (i.e., a plan to provide health care to employees, former employees and their families). Employers must reasonably allocate expenses to wages, as applicable. Qualified health plan expenses include the amount paid or incurred by the

employer to provide and maintain a group health plan, but only to the extent such amounts are excluded from the gross income of employees by reason of Section 106(a) of the Code, which excludes employer provided coverage under an accident or health plan. This means the credits may only apply to premium costs.

### Other Tax Benefits

In addition to the tax credits described above, the CARES Act expanded the availability of tax deductions and other tax benefits. Therefore, although it might seem odd, this might be the time to file amended federal income tax returns in order to take advantage of the expanded deductions and benefits available under the CARES Act. Although these refunds will not result in an immediate cash infusion into a business (sources predict these refunds will be available in early 2021), significant refunds may be available.

**Deferral of Payroll Taxes:** Employers will be able to defer depositing and remitting the employer portion of Social Security taxes incurred from March 27, 2020 through the end of 2020. The deferred amounts will be due in two equal installments on December 31, 2021 and December 31, 2022. The deferral is not available to employers who have obtained forgiveness of a loan issued under the PPP, however, deferral is available through the date the lender issues a decision to forgive the PPP loan. Taxes deferred prior to the forgiveness of the PPP loan will continue to be deferred and will be due on December 31, 2021 and December 31, 2022.

**Business Interest Deduction:** The CARES Act increases the amount of business interest that can be deducted by a taxpayer from the amounts permitted pursuant to the Tax Cuts and Jobs Act (the TCJA). The deduction for business interest expense is generally increased to 50 percent of adjusted taxable income (ATI) from 30 percent of ATI for tax year 2020 for partnerships, and tax years 2019 and 2020 for other taxpayers. To account for the fact that many taxpayers may have significantly reduced income in 2020, the CARES Act allows taxpayers to elect to substitute 2019 ATI for 2020 ATI for purposes of applying the limitation. Taxpayers can elect out of this increased threshold, any election not to use the increased limitation by a partnership must be made at the partnership level.

**Business Losses (NOLs):** The CARES Act rolls back restrictions implemented as part of the TCJA, which eliminated the carryback of NOLs arising after 2017 and restricted NOLs to offset no more than 80 percent of taxable income. Now, with respect to NOLs arising in taxable years ending after December 31, 2017 and before January 1, 2021, taxpayers are permitted to carryback 100 percent of NOLs for the five-year period preceding such loss. The 80 percent taxable income limitation has also been removed for carryforward of NOLs. There are special rules for real estate investment trusts (REITs), life insurance companies and the Section 965 transition tax.

The IRS has recently issued several pieces of guidance with respect to NOLs, which are described below.

The IRS granted an extension of time to file applications for refunds with respect to the carryback of NOLs. In [Notice 2020-26](#), the IRS grants corporations a six-month extension of time to file Form 1045 with respect to the carryback of an NOL that arose in the period beginning calendar year 2018 and ending on or before June 30, 2019. Temporary procedures to fax Form 1045 due to COVID-19 can be found [here](#). It is worth noting that all claims (including those received before the IRS processing centers were closed) will be processed in the order of receipt.

Eligible partnerships can also file amended partnership returns to take advantage of the retroactive NOL relief. [Revenue Procedure 2020-23](#) allows eligible partnerships to file amended partnership returns using a Form 1065 (U.S. Return of Partnership Income) by checking the "Amended Return" box and issuing amended Schedules K-1, Partner's Share of Income, Deductions and Credits, to each of its partners. Partnerships filing these amended returns should write "FILED PURSUANT TO REV PROC 2020-23" at the top of the amended return.

The IRS has also issued guidance to taxpayers with NOLs that are carried back under the CARES Act. [Revenue Procedure 2020-24](#) outlines procedures for waiving the carryback period for NOLs arising in taxable years beginning after December 31, 2017 and before January 1, 2021; excluding Section 965 years from the carryback period; and waiving a carryback period, reducing a carryback period or revoking an election to waive a carryback period for a taxable year that began before January 1, 2018 and ended after December 31, 2017.

**Qualified Improvement Property:** Section 2307 of the CARES Act provides a technical correction to the TCJA with respect to “qualified improvement property.” Now such property is assigned a 15-year recovery period (rather than a 39-year recovery period without the correction) and eligible for bonus depreciation. The technical amendment takes effect as if included originally in the TCJA.

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For more CARES Act information please see these additional information alerts:

- [Paycheck Protection Program Will be First-Come, First-Served](#)
- [Unemployment Insurance Benefits Under the CARES Act](#)
- [Update: Small Businesses May Apply for the Paycheck Protection Program Starting Friday, April 3, 2020](#)
- [Summary of Federal Relief Loans Available to Small Businesses Amid the COVID-19 Pandemic](#)
- [The Importance of Documentation During Extraordinary Times](#)
- [EIDL Loan Advance Update](#)
- [Update: Financial Assistance for Health Care Providers](#)

We will continue to analyze and provide guidance with regard to the updated tax payment and filing rules as they are issued. If you have any questions or concerns regarding your tax obligations, please contact any of the [attorneys](#) in our [Tax Law Practice](#), or the attorney in the firm with whom you are regularly in contact. We are closely following these ever-evolving regulations and would be happy to help.



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