CARES Act Summary

This memorandum is designed to provide our clients and friends a summary of the key business and tax related provisions contained in the CARES Act signed by President Trump on March 27, 2020. The CARES Act is estimated to cost $2.2 trillion and contains numerous tax provisions aimed to benefit both businesses and individuals. Accordingly, we have divided this summary into these two sections.

A. Businesses

Expansion of Eligibility for Small Business Administration ("SBA") Loans: Under the paycheck protection program ("PPP"), eligible employers, self-employed individuals, charitable organizations and Tribal businesses are eligible to borrow SBA-backed loans to fund payroll expenses, healthcare benefits, rent, utilities and other designated operating costs. Loans obtained under this program can have up to a 10-year term and must have an interest rate of up to 4%. Unlike other types of SBA loans, loans made under the paycheck protection program will be non-recourse; that is, no personal guarantees will be required.

The amount of the loan is subject to a limitation that is based on the lesser of $10,000,000, or the product of average monthly payroll costs of the borrower for the one-year period prior to the making of the loan multiplied by 2.5. Certain payroll costs are excluded from this calculation, such as payments of salaries in excess of $100,000 and payments covered under the Families First Coronavirus Relief Act.

A borrower of a PPP loan is eligible for loan forgiveness for amounts spent during the 8-week period after the origination date, subject to proper documentation, on (1) rent, (2) defined payroll costs, (3) mortgage interest, and (4) utilities, not to exceed the principal of the loan. The amount of the PPP loan forgiveness may be reduced if the borrower reduces the number of employees or salaries and wages (for employees with annual salaries less than $100,000) during the 8-week period following the origination of the loan. However, this reduction penalty doesn't apply to the extent the borrower restores their workforce count and salaries/wages by June 30, 2020.

The period to apply for a payroll protection loan ends on June 30. Among the conditions for obtaining a payroll protection loan, the borrower must be unable to obtain credit from another source and that the borrower covenant to the lender that the borrower will use the borrowed funds solely to maintain payroll, make rent or mortgage payments or pay other designated expenses.

Employee Retention Credit: A tax credit against employment taxes is available for certain businesses. An employer is eligible for this credit if the operation of the trade or business is fully or partially suspended during the calendar quarter due to orders of a governmental authority that limited commerce, travel or group meetings. An employer is also eligible for this credit in the first calendar quarter in which the employer has a reduction of gross receipts of more than 50% in a calendar quarter as compared to the same calendar quarter in the prior year. Eligibility for the

credit ends with the calendar quarter following the calendar quarter in which the gross receipts exceed 80 percent of the corresponding calendar quarter of the prior year. For purposes of computing the credit, qualified wages paid to an employee during the relevant period may not exceed an amount that would have been paid to such an employee within the preceding 30 days.

The amount of the tax credit is 50% of the qualifying wages of the employer. In general terms, qualifying wages for each employee are limited to $10,000 for all quarters, and wages paid to certain employees are subject to additional limitations or exclusions. In addition, because of loan forgiveness provisions under the Payroll Protection Loan ("PPL") Program, the credit is not available if the employer is such a borrower under the PPL Program. Further, the amount of the credit is reduced by any credits allowed under Section 7001 or 7003 of the Families First Coronavirus Relief Act (i.e., the sick leave and family leave credits).

If paid by employers with *greater than 100* full-time employees, eligible wages are then paid to employees when they are not providing services for the period that the employer qualifies as an eligible employer, as defined above. For employers with *100 or fewer* full-time employees, eligible wages are paid to all employees, whether the employee is providing services or not, for the period that the employer qualifies as an eligible employer, as defined above.

This credit is available through December 31, 2020. This credit is not available to employers with Small Business Interruption Loans. These are loans issued under the Coronavirus Preparedness and Response Supplemental Appropriations Act, passed earlier in March.

Deferral of Payroll Taxes: Employers are responsible for paying a 6.2% Social Security tax on employee wages or salary, up to a maximum level of wages that is adjusted each year (employees pay the remaining portion of the 12.4% tax through payroll deductions). From the time the CARES Act is signed into law through December 31, 2020, many employers will be allowed to defer paying their share of this Social Security tax. Half of this deferred amount would be due on December 31, 2021 and the other half by December 31, 2022. Similar provisions apply to self-employed individuals, however, 50% of the self-employment tax still needs to be remitted on the existing deadlines.

Net Operating Losses ("NOLs"): The Tax Cuts and Jobs Act (the "TCJA"), which was enacted in 2017, eliminated net operating loss carrybacks for "C" Corporations after 2017. NOLs arising after 2017 could be carried forward indefinitely, but were limited to 80% of taxable income in the relevant period. These rules are changed by the CARES Act to allow NOLs arising in tax years 2018, 2019 and 2020 to be carried back five years. In addition, the 80% limitation created by the TCJA has been eliminated for tax years beginning before January 1, 2021.

Taxpayers will be able to amend tax returns for the applicable years to claim refunds arising from the use of these NOLs. Amended returns seeking refunds for earlier years must be filed by the due date, including extensions, of the taxpayer's return for the first taxable year ending after the enactment of the CARES Act. Thus, calendar year corporate taxpayers have until March 15, 2021 (or September 15, 2021 if the return due date is extended) to file refund claims. Note that there are special provisions for REITs (denying carrybacks for any year the REIT was a REIT) and for companies that recognize foreign income under the "Subpart F" rules of the Code.

Taxpayers seeking to carry back 2020 losses to earlier years will have to wait until their 2020 returns are filed, which may not be until 2021, to apply for a refund for prior years related to a 2020 NOL. Nonetheless, these NOL carryback rules provide opportunities for businesses to retool and prepare for the recovery. For example, businesses can purchase needed equipment and machinery in 2020 and claim a deduction for the cost of these items under the existing "bonus depreciation" rules. Similarly, in connection with an acquisition of developed real estate, the real estate owner can increase deductions available under the bonus depreciation rules by doing a cost segregation study to identify the property eligible for this bonus depreciation treatment. In either case, if the increased deductions arising from bonus depreciation creates an NOL in 2020, it can be applied to a prior year so that a refund can be claimed.

Limitation on Losses for Non-Corporate Taxpayers: The TCJA added Section 461(I) to the Code, which limited non-corporate taxpayers' (individuals, trusts, estates) ability to deduct excess business losses. Excess business losses are defined basically as the excess of aggregate business gross deductions over aggregate business gross income. Deduction of these excess business losses by non-corporate taxpayers was limited to $250,000 per year ($500,000 married filing jointly). Unused excess business losses are carried forward as NOLs. These limitations continue through the 2026 tax years. The new provision delays the application of the excess business loss limitation until 2021. Non-corporate taxpayers may be able to deduct all excess business losses created through the end of the 2020 tax year. Taxpayers with losses in 2018 and 2019 that were disallowed by the limitation may file for refunds.

This is potentially a very significant benefit to many businesses. For example, individuals in the real estate business may be able to deduct large losses arising from the 100% bonus depreciation provision in the TCJA (as well as other losses) that would otherwise be limited. This may be especially valuable to individuals who qualify as "real estate professionals," generally by spending at least half their time (and at least 750 hours) materially participating in real estate businesses. However, based on what we know so far, the new provision does not override the passive loss and at-risk limitations, so the provision may be less favorable for passive investors.

Employer Student Loan Payments: Employers are allowed to provide a limited student loan repayment benefit to its employees on a tax-free basis. Specifically, employers may contribute up to $5,250 annually to each employee on a tax-free basis. The annual limitation applies to both the new student loan repayment benefit as well as other educational assistance provided by the employer under current law (ex. tuition, fees, books, etc.). The provision applies to student loan payments made after the enactment date and before January 1, 2021.

B. Individuals

Recovery Rebate Checks: Recovery rebate checks of $1,200 ($2,400 for taxpayers married filing jointly) will be made available to individuals with gross income up to $75,000 ($150,000 for married persons), with an additional $500 for each child. These recovery rebate checks are reduced by $5 for each $100 a taxpayer's income exceeds $75,000 ($150,000 for taxpayers married filing jointly and $112,500 for head of household). This means that taxpayers making below $99,000 ($198,000 for taxpayers married filing jointly) will generally receive at least some amount of a recovery rebate check, and those over that level of income will not.

These new rules provide that qualifying income levels can be tentatively based on the taxpayer's most recently filed tax return (either 2019 or 2018). Certain taxpayers that are not required to file a tax return, such as when receiving Social Security benefits, are still eligible for the recovery rebate checks. Instead of using a tax return the government can use information from the Social Security Information.

The rebate checks are generally not taxable income and are instead treated as an advance of the refund a taxpayer would normally receive when filing their 2020 tax return.

Retirement Accounts: The CARES Act provides some retirement account relief for coronavirus related distributions. First, the 10% early withdrawal penalty from qualified retirement accounts is waived for distributions of up to $100,000 if a withdrawal from a retirement account is for a coronavirus-related distribution. A "coronavirus-related distribution" is defined as a distribution made to an individual: (1) who is diagnosed with COVID-19, (2) whose spouse or dependent is diagnosed with COVID-19, or (3) who 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 due to COVID-19, or other factors as determined by the Treasury Secretary. Reason (3) is likely to predominate. In addition, the time period in which to pay the income tax attributable to a coronavirus related distribution is extended to allow for payments of this tax over three years. Taxpayers may re-contribute the funds withdrawn for a coronavirus-related distribution within three years without regard to that year's cap on contributions.

The Act also waives the required minimum distribution rules for certain defined contribution plans and IRAs for calendar year 2020. This provision provides relief to individuals who would otherwise be required to withdraw funds from such retirement accounts.

Charitable Deductions: Generally, taxpayers must itemize their deductions to take advantage of charitable deductions. This itemized deduction requirement is eliminated for charitable deductions of up to $300 per donee for most contributions for the 2020 tax year. Note that not all charitable deductions are eligible for this treatment. Specifically, charitable contributions made to a private foundation or donor-advised fund, are not eligible for the above-the-line charitable deduction. In addition, the limitation that applies to the amount of a charitable deduction that can be claimed by individual taxpayers is based on a percentage of the individual taxpayer's adjusted gross income is also eliminated for 2020, so individuals can deduct all contributions regardless of their income level.

For more information on small business guidance and loan resources, please go to sba.gov. If you have any questions or concerns, please do not hesitate to contact our office. We will assist you with other resources as needed.

Colin Devlin, Esq. (w) 267-792-3342 | (c) 856-905-7990 | (e) cdevlin@lexnovalaw.com

Buz Eizen, Esq. (w) 267-792-3341 | (c) 215-313-6918 | (e) beizen@lexnovalaw.com