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Memo

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Businesses

CARES Act: Delayed Payment of Employer Payroll Taxes

After days of furious negotiations, Congress has passed the Coronavirus Aid, Relief, and Economic Security (CARES) Act. The $2.2 trillion price tag for tax relief and incentives for individuals and businesses makes it the most expensive piece of legislation ever passed. In order to free up employers' cash flow and retain employees during times of quarantine or shutdown, the CARES Act defers the payment of the employer share of payroll taxes.

In general, under the Federal Insurance Contributions Act (FICA), taxes are imposed on both employers and employees on wages paid to the employee for Social Security (old-age, survivors, and disability insurance (OASDI)), and Medicare hospital insurance (HI). The FICA taxes are imposed on both the employer and the employee at a rate of 6.2 percent for OASDI and 1.45 percent for HI for a total of 7.65 percent for the employee and 7.65 for the employer (15.3 percent total).

Payroll taxes due from the period beginning on the date the CARES Act is signed into law and ending on December 31, 2020, can be deferred. The total payroll taxes incurred by employers, and 50 percent of payroll taxes incurred by self-employed persons qualify for the deferral. Half of the deferred payroll taxes are due on December 31, 2021, with the remainder due on December 31, 2022.

In addition to the payroll tax deferment, the CARES Act also provides for an employee retention credit and advance payment of payroll credits for employee paid sick and family leave.

CARES Act: Excess Business Losses of Noncorporate Taxpayers

Under the CARES Act, the limitation on the deduction of excess business losses for noncorporate taxpayers will not apply for tax years beginning in 2018, 2019, and 2020.

An "excess business loss" is the excess of a taxpayer's aggregate deductions for the tax year from its trades or businesses over the aggregate gross income or gain for the tax year from those trades or businesses plus $250,000 ($500,000 for joint return filers). Under the Tax Cuts and Jobs Act, a noncorporate taxpayer is not allowed to claim a deduction for excess business losses for tax years beginning after December 31, 2017, and before January 1, 2026. However, the CARES Act now modifies the deduction limitation to apply for tax years beginning after December 31, 2020 and before January 1, 2026.

Because the limitation on excess business losses no longer applies to the 2018 tax year, taxpayers who were subject to the limitation for 2018 have an opportunity to file an amended return and claim a potential refund.

The modification to the loss limitation for shareholders and partners of pass-through businesses and sole proprietors, will help noncorporate taxpayers utilize business losses and improve their cashflow.

CARES Act: Depreciation of Qualified Improvement Property

The Coronavirus Aid, Relief, and Economic Security (CARES) Act provides tax relief to individuals and businesses in an effort to support the economy. In addition to numerous other provisions that provide cashflow to businesses, the CARES Act includes a modification to the recovery period for qualified improvement property.

Under the CARES Act, a 15-year recovery period is retroactively assigned to qualified improvement property placed in service after December 31, 2017. Therefore, qualified improvement property may be depreciated over 15 years or, alternatively, qualifies for 100 percent bonus depreciation if all bonus requirements are met.

Qualified improvement property is broadly defined as an internal improvement to nonresidential real property but does not include improvements related to elevators and escalators, the internal structural framework, or an enlargement of the building. The improvement must be placed in service after the date the improved building is first placed in service. The improvement must be made by the taxpayer. Therefore, the 15-year recovery period and bonus depreciation does not apply to a taxpayer that purchases a building that includes qualified improvement property depreciated by the seller over 15 years.

Opportunity to Amend

As a result of the retroactive application of the reduced recovery period, if a taxpayer filed two or more returns using a 39-year recovery period for qualified improvement property placed in service after 2017 an incorrect accounting method was adopted and automatic consent to change to the correct method must be filed on Form 3115. Taxpayers who only filed one return using a 39-year recovery period (e.g., a calendar year taxpayer who has not filed a 2019 return) may file an amended return to correct the recovery period or may file Form 3115 with their current year return.

Generally, a taxpayer must elect out of bonus depreciation by the extended due date of the return for the tax year in which the property eligible for the bonus was placed in service. Some taxpayers may not want to claim 100 percent bonus depreciation on qualified improvement property that retroactively qualifies for the additional allowance. The IRS will presumably issue guidance allowing these taxpayers to make a late election out of bonus depreciation and to file an amended return or Form 3115, as applicable, based on a 15-year recovery period.

The reduced recovery period not only allows businesses to improve their cashflow by filing an amended return, but also encourages investment in further improvements to stimulate the economy.

Plans to Implement Coronavirus Paid Leave and Tax Credits

The U.S. Treasury Department, Internal Revenue Service (IRS), and the U.S. Department of Labor (Labor) announced that small and midsize employers can begin taking advantage of two new refundable payroll tax credits, designed to immediately and fully reimburse them, dollar-for-dollar, for the cost of providing Coronavirus-related leave to their employees. This relief to employees and small and midsize businesses is provided under the Families First Coronavirus Response Act (Coronavirus Response Act), signed by President Trump on March 18, 2020.

The Coronavirus Response Act provides paid sick leave and expands family and medical leave for COVID-19 related reasons and creates the refundable paid sick leave credit and the paid childcare leave credit for eligible employers. Eligible employers are businesses and tax-exempt organizations with fewer than 500 employees that are required to provide emergency paid sick leave and emergency paid family and medical leave under the Act. Eligible employers will be able to claim these credits based on qualifying leave they provide between the effective date and Dec. 31, 2020. Equivalent credits are available to self-employed individuals based on similar circumstances.

The Coronavirus Response Act will help the United States combat and defeat COVID-19 by giving all American businesses with fewer than 500 employees the funds to provide employees with paid leave, either for the employee's own health needs or to care for family members. The new law enables employers to keep their workers on their payrolls, while at the same time ensuring that workers are not forced to choose between their paychecks and the public health measures needed to combat the virus.

Key Takeaways

Paid Sick Leave for Workers

- For COVID-19 related reasons, employees receive up to 80 hours of paid sick leave and expanded paid childcare leave when employees' children's schools are closed, or childcare providers are unavailable.

Complete Coverage

- Health insurance costs are also included in the credit.
- Employers face no payroll tax liability.
- Self-employed individuals receive an equivalent credit.

Employers receive 100% reimbursement for paid leave pursuant to the Act.

- An immediate dollar-for-dollar tax offset against payroll taxes is provided
- Reimbursement will be quick and easy to obtain.

Small Business Protection

- Employers with fewer than 50 employees are eligible for an exemption from the requirements to provide leave to care for a child whose school is closed, or childcare is unavailable in cases where the viability of the business is threatened.

Easing Compliance

- Requirements subject to 30-day non-enforcement period for good faith compliance efforts.

To take immediate advantage of the paid leave credits, businesses can retain and access funds that they would otherwise pay to the IRS in payroll taxes. If those amounts are not sufficient to cover the cost of paid leave, employers can seek an expedited advance from the IRS by submitting a streamlined claim form.

Families First Coronavirus Response Act: Credits for the Self-Employed

On March 18, 2020, the President signed the Families First Coronavirus Response Act (Coronavirus Response Act) which increases funding for various programs and addresses paid sick and family leave, including tax credits for employers and self-employed persons.

The Coronavirus Response Act requires employers with fewer than 500 employees to provide paid sick leave to employees who are forced to stay home due to quarantining or the care for a family member (qualified sick leave) or to care for a child if the school or place of care is closed (qualified family leave).

In the case of sick leave wages paid by an employer to an employee, the employer may receive a refundable credit against its share of either the OASDI or the RRTA portion (as applicable) of the payroll tax. A separate refundable payroll tax credit applies for family leave wages paid by an employer under the Coronavirus Response Act.

Self-employed persons may also benefit from the sick and family leave credits as if they were an employee of an employer (other than himself or herself). For self-employed persons, the credits are allowed against regular taxes.

Credit for Qualified Sick Leave

The limit on sick leave wages is determined by multiplying the number of days the self-employed person is unable to perform services in their trade or business by the lesser of 67% of the taxpayer’s average daily self-employment income, or $200. The number of days is limited to 10 for the tax year.

The limits are increased to 100% and $511, respectively if the self-employed person is unable to perform services for the following reasons:

- Is subject to a federal, state or local quarantine or isolation order related to COVID-19;
- Has been advised by a health care provider to self-quarantine due to concerns related to COVID-19; or
- Is experiencing symptoms of COVID-19 and seeking a medical diagnosis.

The amount of the sick leave credit is reduced by any sick leave wages the taxpayer might receive as an employee which exceed $2,000 ($5,110 in the case of any day covered for the three reasons described above).

Credit for Qualified Family Leave

The same calculation is made for family leave wages, with days unable to perform services multiplied by the lesser of 67% of the taxpayer's average daily self-employment income, or $200. The number of days is limited to 50 for the tax year.

The amount of the family leave credit is reduced by any family leave wages in excess of $10,000 that the taxpayer might receive as an employee.

Average Daily Self-Employment Income.

The taxpayer's average daily self-employment income is defined as the amount of net earnings from self-employment for the tax year divided by 260.

These credits expire on December 31, 2020. The IRS is expected to provide additional guidance soon.

Families First Coronavirus Response Act: Employer Tax Credits

On March 18, 2020, the President signed the Families First Coronavirus Response Act (Coronavirus Response Act) which increases funding for various programs and addresses paid sick and family leave, including tax credits for employers and self-employed persons.

The Coronavirus Response Act requires employers with fewer than 500 employees to provide paid sick leave to employees who are forced to stay home due to quarantining or the care for a family member (qualified sick leave) or to care for a child if the school or place of care is closed (qualified family leave).

Credit for Qualified Sick Leave

In the case of sick leave wages paid by an employer to an employee, the employer may receive a refundable credit against its share of either the OASDI or the RRTA portion (as applicable) of the payroll tax. The credit can be claimed on a quarterly basis, equal to 100 percent of the amount of sick leave wages paid.

The amount of the credit is limited to $200 per day per employee. However, the credit increases to $511 per day if the employee is on leave for the following reasons:

- Is subject to a federal, state or local quarantine or isolation order related to COVID-19;
- Has been advised by a health care provider to self-quarantine due to concerns related to COVID-19; or
- Is experiencing symptoms of COVID-19 and seeking a medical diagnosis.

The total payroll tax credit is limited to 10 days of wages per employee.

Credit for Qualified Family Leave

A separate refundable payroll tax credit applies for family leave wages paid by an employer under the Coronavirus Response Act. The credit is 100 percent of the amount of qualified family leave wages limited to $200 per day per employee, up to an aggregate of $10,000.

Wages, for purposes of both credits, include a portion of health plan expenses properly allocable to the qualified sick and family leave wages. The paid sick and family leave requirements and the related employer tax credits are temporary. They expire on December 31, 2020.

The IRS is expected to provide additional guidance on these credits soon.

CARES Act: Modifications for Net Operating Losses

The Coronavirus Aid, Relief, and Economic Security (CARES) Act provides tax relief to individuals and businesses in an effort to support the economy. Included in the numerous provisions is a modification to the rules on the tax treatment of net operating losses.

Normally, NOLs arising in tax years beginning after 2017 may only reduce 80 percent of a taxpayer's taxable income in carryback and carryforward years. The two-year carryback period and twenty-year carryforward period, as well as the longer carryback periods for special types of losses, were eliminated under the Tax Cuts and Jobs Act, effective for NOLs arising in tax years ending after 2017. NOLs arising in tax years ending after 2017 are carried forward indefinitely.

However, under the CARES Act, net operating losses (NOLs) arising in tax years beginning in 2018, 2019, and 2020 now have a five-year carryback period and an unlimited carryforward period. The general rule limiting an NOL deduction to 80 percent of taxable income does not apply to NOLs arising in these years.

Extension of time to waive five-year carryback for 2018 and 2019 NOLs. The five-year carryback period may be waived by making an election. For NOLs that arose in tax years beginning in 2018 or 2019, the time for making the waiver election is extended to the due date (including extensions) for filing the taxpayer's return for the first tax year ending after March 27, 2020 (the date of enactment of the new law). Normally, the election is required by the due date (including extensions) of the return for the tax year in which the NOL arose. The regular election deadline continues to apply to NOLs arising in a tax year that begins in 2020.

The extended due date is necessary because the statutory deadline for making the waiver election has expired for some taxpayers. The CARE Act contains no specific relief that allows taxpayers with a 2018 or 2019 NOL to file a late tentative refund application. Since the due date for filing a tentative refund application is statutorily required to be filed within one year after the close of the NOL year the IRS is not able grant administrative relief. Consequently, taxpayers for whom the deadline has passed will need to file amended returns in order to claim refunds.

CARES Act: Increased Deduction Limits for Charitable Contributions

The Coronavirus Aid, Relief, and Economic Security (CARES) Act offers enhanced tax incentives for making charitable contributions for the 2020 tax year.

Individuals

In general, the itemized charitable deduction for individuals is limited to a percentage of the taxpayer's adjusted gross income (AGI). The percentage is determined by the type of organization receiving the donation and the type of property donated. For the 2020 tax year, individuals can claim an unlimited itemized deduction for charitable contributions which are normally limited to 50 percent of AGI.

Also, beginning in tax year 2020, an individual who does not itemize deductions can deduct up to $300 in charitable contributions made to churches, nonprofit schools, nonprofit medical institutions, and other organizations as an above-the-line deduction in calculating adjusted gross income. This allows an individual to claim a deduction for a charitable contribution even if the individual does not itemize deductions.

Corporations

A corporation's deduction is generally limited to 10 percent of the corporation's taxable income, computed with certain adjustments. The percentage limit was temporarily waived for qualified contributions made by a corporation after December 31, 2017, and before February 19, 2020, for relief efforts in qualified disaster areas. Under the CARES Act, the percentage limitation on the charitable contribution deduction for corporations is increased to 25 percent for the 2020 tax year.

Food Inventory

Corporate and noncorporate taxpayers are entitled to an enhanced deduction for charitable donations of food inventory from any trade or business. The food inventory must consist of items fit for human consumption and be contributed to a qualified charity or private operating foundation for use in the care of the ill, the needy, or infants. Normally, a noncorporate taxpayer's total deduction for food inventory donations during the tax year is limited to a maximum of 15 percent of the taxpayer's net income from all trades and businesses from which the donations are made during the tax year. In the case of a C corporation, the deduction is limited to 15 percent of the corporation's taxable income. Under the CARES Act, the deduction for the contribution of food inventory is increased from 15 percent to 25 percent for the 2020 tax year.

CARES Act: Employee Retention Credit

After days of furious negotiations, Congress has passed the Coronavirus Aid, Relief, and Economic Security (CARES) Act. The $2.2 trillion price tag for tax relief and incentives for individuals and businesses makes it the most expensive piece of legislation ever passed. It includes a provision for a refundable payroll tax credit for 50 percent of wages paid by employers to employees during the COVID-19 crisis.

The CARES Act grants eligible employers a credit against employment taxes equal to 50 percent of qualified wages paid to employees who are not working due to the employer's full or partial suspension of business or a significant decline in gross receipts. The credit can be claimed on a quarterly basis, but the amount of wages, including health benefits, for which the credit can be claimed is limited to $10,000 in aggregate per employee for all quarters.

An eligible employer is defined as:

- An employer whose trade or business is fully or partially suspended during the calendar quarter due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to the coronavirus disease (COVID-19); or

- An employer that experiences a 50% decline in gross receipts for the calendar quarter compared to the same quarter in the prior year.

Qualified Wages. The credit applies to qualified wages paid after March 12, 2020 and before January 1, 2021. If the employer has more than 100 full-time employees, qualified wages are wages paid to employees who cannot work during the COVID-19-related circumstances described above. If the employer has 100 or fewer full-time employees, all employee wages qualify for the credit, whether the employer is open for business or subject to a shut-down order.

Comment

This is very similar to the paid leave credits granted to employers under the Families First Coronavirus Response Act signed into law on March 18, 2020, with some changes to the requirements. Most significantly, neither the employee nor the employer has to be directly impacted by the infection.

Please call our office with any questions on the CARES Act. We are here to help you.

The rules are changing minute by minute, we will endeavor to keep you up to date!