

## U.S. Insight: Summary of the Business Tax and Individual Tax Provisions of the CARES Act, a COVID-19 Relief Measure

On March 27, 2020, President Trump signed the Coronavirus Aid, Relief, and Economic Security Act (the “CARES Act” or the “Act”) into law. A brief summary of the business tax provisions and the individual tax provisions in the Act is provided below.

### Business Tax Provisions

#### 1. *Employee Retention Credit*

The Act creates a refundable credit for “eligible employers” against the employer’s Social Security payroll tax obligations in an amount equal to 50% of the “qualified wages” paid to employees between March 12, 2020 through December 31, 2020.

In general, an “eligible employer” is an employer that was carrying on a trade or business in 2020 and either (1) the employer’s operation of such trade or business was fully or *partially suspended* due to orders from a governmental authority in response to COVID-19 or (2) the employer experienced a significant decline in gross receipts.

For employers with an average of more than 100 full-time employees in 2019, “qualified wages” are generally wages paid to an employee that is not providing services during employer’s COVID-19 effect period. For employers with an average of 100 full-time employees or less in 2019, “qualified wages” generally include all wages paid to employees whether or not the employee is providing services during the employer’s COVID-19 effect period. The amount of qualified wages paid to any employee is limited to \$10,000.

The Employee Retention Credit does not apply to employers that receive a small business loan under the Act.

#### 2. *Payroll Tax Deferral*

The Act allows employers to defer the employer’s portion of the Social Security payroll tax that is due from March 27, 2020 through December 31, 2020. Employers are required to pay half of the deferred payroll taxes by December 31, 2021 and the remainder by December 31, 2022.

The Act creates a corresponding deferral for 50% of the Social Security portion of the self-employment tax.

The payroll tax deferral provision does not apply to an employer that has indebtedness forgiven on a small business loan under the Act.

### *3. Modifications of Net Operating Loss (“NOL”) Carryover and Income Limitation Rules*

Under the Act, the NOL carryover rules are changed to provide that losses that arise between 2018 and 2020 can be carried back 5 years. The entire amount of the NOL for a tax year is carried to the earliest of the tax years to which it may be carried, then carried to the next earliest of those tax years. Accordingly, a NOL generated in 2020 could be carried back to 2015.

Special rules apply with respect to real estate investment trusts and life insurance companies.

Under current law, a taxpayer is generally only allowed a NOL deduction of 80% its taxable income. The Act removes this 80% income limitation for NOLs generated for tax years beginning before January 1, 2021.

### *4. Excess Business Loss Rules*

The Act modifies the effective date for the “excess business loss” provision. Previously, a noncorporate taxpayer was not allowed an “excess business loss” for tax years beginning after December 31, 2017 and before January 1, 2026. Under the Act, the “excess business loss” limitation is not effective until 2021. Taxpayers that were subject to the “excess business loss” limitation in 2018 should consider amending their tax returns.

An “excess business loss” is generally the excess of the taxpayer’s aggregate deductions for the taxable year over the sum of the taxpayer’s aggregate gross income plus \$250,000 (adjusted for inflation). A disallowed “excess business loss” is treated as a NOL.

### *5. Minimum Tax Credit (“MTC”) Refunds*

The Act accelerates the recovery period of the MTC.

Prior to the Act, a corporation’s MTCs were refundable in installments payable between 2018 through 2021. Under the Act, the MTCs are refundable in equal installments in 2018 and 2019.

In addition, a corporation can elect to recover the entirety of the MTC in 2018 by filing IRS Form 1139 (Corporation Application for Tentative Refund) by December 31, 2020.

## *6. Limitation on the Deduction of Business Interest*

The deduction of business interest is generally limited to 30% of a corporation's "adjusted taxable income". The Act increased the 30% limit to 50% for tax years 2019 and 2020. For tax years beginning prior to January 1, 2021, a taxpayer's "adjusted taxable income" is generally equal to its earnings before interest, taxes, deduction, and amortization, generally known as "EBITDA". In addition, for purposes of the computation, a taxpayer can generally elect to use its 2019 adjusted taxable income as opposed to its 2020 adjusted taxable income.

### **Individual Tax Provisions**

#### *1. \$1,200 Tax Credit For Eligible Individuals*

The Act creates a refundable tax credit against an "eligible individual's" 2020 income taxes in the amount of \$1,200 (\$2,400 for individuals filing joint returns) plus an additional \$500 for each qualifying child. An "eligible individual" is generally any individual other than a nonresident alien individual, a dependant, or an estate or trust. Individuals with an adjusted gross income that exceeds \$75,000 are subject to a phase-out of the credit (\$150,000 for individuals filing jointly). The credit is completely phased out for individuals whose income exceeds \$99,000 (\$198,000 for individuals filing jointly).

The Act also creates an advanced refund mechanism for individuals that would have been eligible for the credit based on their 2019 taxable income (or 2018 taxable income if the taxpayer has not filed his or her 2019 tax return).

#### *2. Coronavirus-Related Distributions from Qualified Retirement Plans*

Taxpayers are generally subject to tax on distributions from qualified retirement plans in the year in which he or she receives the distribution.

With respect to a "coronavirus-related distribution," unless the taxpayer elects otherwise, a taxpayer is subject to tax on such distribution over a three-year period. A "coronavirus-related distribution" is generally a distribution made during 2020 to an individual who is diagnosed with COVID-19, whose spouse or dependant is diagnosed with COVID-19, or who experiences adverse financial consequences as a result of COVID-19. Taxpayers can also make repayments of coronavirus-related distributions to the retirement plans over a three-year period.

In addition, taxpayers are generally subject to a 10% additional tax on early distributions from qualified retirement plans. Taxpayers are not subject to this 10% penalty on coronavirus-related distributions, up to an aggregate amount of distributions of \$100,000.

### 3. Charitable Contributions

For taxpayers that itemize their deductions, the Act generally removes many of the restrictions and limitations made in 2020. For taxpayers that do not itemize their deductions, the Act generally provides for a charitable deduction of up to \$300.

For corporations, under current law, charitable deductions are generally limited to 10% of the corporation's taxable income. The Act generally increases this 10% limitation to 25%.

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