RELIEF FOR BUSINESSES UNDER THE CARES ACT

By Naomi Smith &
K. Dwayne Vande Krol

The Coronavirus Aid, Relief, and Economic Security Act of 2020 ("CARES Act") is the largest economic relief bill in U.S. history, intended to mitigate the impact of the economic crisis caused by the COVID-19 pandemic by providing financial assistance to individuals and businesses. Since its enactment on March 27, much of the focus for Iowa businesses has been the Paycheck Protection Program, a program to provide small businesses with cash flow assistance through federally guaranteed loans which may be ultimately forgiven.

However, the CARES Act also provides other sources of economic aid for businesses through new tax programs and modifications to current tax provisions. While the CARES Act includes a number of income tax provisions, this article will focus on two employment tax provisions which provide immediate relief to businesses.

EMPLOYEE RETENTION TAX CREDIT

Section 2302 of the CARES Act provides for an employee retention tax credit ("Employee Retention Credit"). An "eligible employer" will be allowed a refundable credit against the employer portion of employment taxes for each calendar quarter in an amount equal to 50 percent of the "qualified wages" paid to each employee from March 13 through and including Dec. 31. The amount of qualified wages which may be taken into account for this credit for all quarters is limited to $10,000 per employee in the aggregate, resulting in a maximum credit of $5,000 per employee.

An employer who receives a loan under the Paycheck Protection Program is not eligible to claim the Employee Retention Credit and will be subject to recapture of the credit if it claimed the credit before or after receiving the loan. Other details regarding eligibility for this credit, calculation of qualified wages and limitations are summarized below.

ELIGIBLE EMPLOYERS

An eligible employer is any employer carrying on a trade or business during 2020 which meets either the "governmental order" test or the "reduced gross receipts" test. Eligibility is determined on a quarterly basis. An organization described in 501(c) of the Internal Revenue Code may qualify as an eligible employer under either test, and the requirements relating to a "trade or business" will apply to all operations of the organization.

Under the "governmental order" test, an employer is eligible if operation of its trade or business is partially or fully suspended during the quarter due to orders from a governmental authority limiting commerce, travel or group meetings due to COVID-19. For example, an employer operating a restaurant subject to a governmental order prohibiting in-person dining but permitting take-out would meet this test. However, an employer operating a grocery store exempted from a governmental order restricting food service, gathering size or travel outside the home would not meet this test, even if its business was impacted by such governmental order (though the employer may be eligible under the reduced gross receipts test).

Under the "reduced gross receipts" test, an employer is eligible in the first quarter of 2020 in which its gross receipts are less than 50 percent of the gross receipts for the same quarter in the prior year, and continues to be eligible each quarter thereafter until the quarter after the quarter in which the employer's gross receipts are more than 80 percent of gross receipts for the same quarter the prior year. For example, if the employer's gross receipts for each quarter in 2020 as a percentage of gross receipts for each of the same quarters in 2019 are 50 percent, 37 percent, 81 percent and 70 percent, the employer would become eligible beginning in the second quarter (i.e, the first quarter its gross receipts fell below 50 percent of the prior year) and would no longer be eligible in the fourth quarter (i.e., the quarter after its receipts increased to above 80 percent of the prior year).

Governmental employers are not eligible employers. Also, self-employed individuals are not eligible for this credit for their self-employment services or earnings.

QUALIFIED WAGES

"Qualified wages" include wages and compensation paid by an eligible employer to employees from March 13 through and including Dec. 31 and the employer's "qualified health plan expenses."

For eligible employers that had an average of more than 100 full-time and full-time equivalent ("FTE") employees during 2019, qualified wages include only wages paid to retained employees for time such employees are not providing services. The wages are not to exceed the amount an employee would have been paid for working an equivalent duration during the 30 days immediately prior to the period in which the employer met either the governmental order test or the reduced gross receipts test. For example, an employer who pays an employee for working 40 hours per week but only requires the employee to work 15 hours per week may include wages paid to the employee for 25 hours per week as "qualified wages."

For eligible employers with an average of 100 or fewer full-time employees during 2019, qualified wages include all wages paid to employees either during the period of time in which the eligible employer meets the governmental order test or during the calendar quarter in which the eligible employer meets the reduced gross receipts test. For employers meeting the governmental order test but not the reduced gross receipts test, only wages paid during the period of time to which the governmental order applies are considered qualified wages.

Qualified wages also include the amount of the eligible employer's "qualified health plan expenses." Qualified health plan expenses include the amounts paid or incurred by the employer to provide and maintain a group health plan, but only to the extent that such amounts are excluded from the gross income of employees (which generally includes all employer-provided coverage under a group health plan). The portion of such expenses included in computing the Employee Retention Credit is the amount properly allocable to qualified wages. The IRS has not published much guidance on how qualified health plan expenses are properly allocated for purposes of the Employee Retention Credit, though it has published helpful guidance in its FAQs with respect to the allocation of qualified health plan expenses for purposes of the sick and family leave credit under the Families First Coronavirus Response Act ("FFCRA").

The Joint Committee on Taxation stated that the authority granted by the CARES Act to the Secretary of the Treasury permits the secretary to treat qualified health plan expenses as qualified wages in a situation in which there are no other qualified wages paid by the eligible employer. This

situation may arise for employers that are continuing health care coverage for furloughed employees. The IRS has not published guidance on this issue.

Other rules and limitations apply in determining qualified wages:

- The maximum amount of qualified wages per employee is $10,000.
- For purposes of determining whether an eligible employer had more than 100 full-time/FTE employees during 2019, certain aggregation rules will apply which may result in persons being treated as a single employer.
- Special rules apply to exclude the wages of related parties.
- No "double dipping" with other tax credits taken by the employer, such as the work opportunity tax credit.
- Qualified wages do not include the amount of qualified sick and family leave wages for which the employer received tax credits under the FFCRA.

CREDIT; PROCEDURES

An eligible employer will report the amount of total qualified wages and related credits for each calendar quarter on its federal employment tax return (Form 941 or equivalent form). The IRS will update the federal employment tax return forms and related instructions prior to the due date for the second quarter 2020 to permit the required reporting. The current Form 941 includes a note to taxpayers that, for purposes of the Employee Retention Credit, qualified wages paid between March 13 and March 31 will be reported on the second quarter 2020 Form 941.

The Employee Retention Credit is applied against the employer's portion of social security taxes under Section 3111(a) of the Code, and the portion of taxes imposed on railroad employers under section 3221(a) of the Railroad Retirement Tax Act (collectively, the "employer's share of social security taxes"). If the amount of the credit for the quarter exceeds the employer's share of social security taxes on all wages paid to all of the employer's employees for that quarter, the excess will then be applied to offset any remaining tax liability on the federal employment tax return and the amount of any remaining excess will be reflected as an overpayment on the return and refundable to the employer.

The Employee Retention Credit provides immediate financial relief for eligible employers by permitting employers to utilize the credit in advance by accessing federal employment taxes required to be deposited with the IRS and, if necessary, by requesting an advance of the credit. An eligible employer that pays qualified wages to its employees in a quarter before it is required to deposit federal employment taxes with the IRS for that quarter should first reduce its federal employment tax deposits for wages paid in the same quarter by the maximum allowable credit. If the anticipated credit exceeds the deposits for that quarter, eligible employers may file Form 7200, Advance Payment of Employer Credits Due to COVID-19, to claim an advance refund for the amount of the credit in excess of federal employment tax deposits. Eligible employers must account for the reduction in deposits and any advance credits taken by filing Form 7200 when filing federal employment tax returns. Employers will not be subject to penalty for failing to deposit federal employment taxes relating to qualified wages in a calendar quarter if certain conditions are satisfied.

DEFERRAL OF EMPLOYMENT TAX DEPOSITS AND PAYMENTS

Section 2302 of the CARES Act provides another source of immediate relief for employers and self-employed individuals. This provision of the CARES Act permits employers to defer the deposit and payment of the employer's share of social security taxes and permits self-employed individuals to defer payment of the equivalent of the employer's social security portion of SECA taxes, in each case that would otherwise be due during the period beginning on March 27 and ending on Dec. 31. Half of the amount of deferred taxes will be due on or before Dec. 31, 2021, and the remaining amount of deferred taxes will be due on or before Dec. 31, 2022.

Any employer and self-employed individual is eligible for the deferral described above; however, any employers or self-employed individuals who received a loan under the Paycheck Protection Program become ineligible to continue deferring the deposit and/or payment of such taxes the day after receiving a decision from the lender that the loan has been forgiven. Any taxes deferred through such date will continue to be deferred and will be due on the applicable dates as described above.

Employers and self-employed individuals will not need to make a special election to take advantage of the tax deferral under Section 2302 of the CARES Act. The IRS will revise the federal employment tax return forms (Form 941 or equivalent forms) and related instructions for second quarter 2020 to permit employers to reflect the deferred deposits and payments on such return.

For more detailed information on this tax deferral and the Employee Retention Credit, see the CARES Act; IRS FAQs and other IRS guidance at https://www.irs.gov/coronavirus/coronavirus-and-economic-impact-payments-resources-and-guidance; and the Joint Committee on Taxation, *Description of the Tax Provisions of Public Law 116-136, the Coronavirus Aid, Relief, and Economic Security Act (JCX-12-20),* April 22, 2020.

OTHER BUSINESS TAX PROVISIONS

The CARES Act contains a number of other business tax provisions, most of which are modifications to tax provisions implemented by the Tax Cuts and Jobs Act of 2017, including modification of limitations on charitable deductions (Section 2205), modifications to limitations and carrybacks for net operating losses (Section 2303), elimination of loss limitations for pass-thru businesses (Section 2304), acceleration of alternative minimum tax credit (Section 2305), increased business interest expense deduction (Section 2306), establishment of 15-year depreciable life for qualified improvement property (Section 2307) and temporary exception from excise tax for alcohol used to produce hand sanitizer (Section 2308). Taxpayers will need to carefully consider the impact of business tax provisions in the CARES Act and evaluate opportunities to utilize these benefits during the time periods available.

Naomi D. Smith's practice areas include business transactions, wealth transfer and tax planning. She is located at Nyemaster Goode's Cedar Rapids office.

K. Dwayne Vande Krol's practice includes assisting clients with tax planning and compliance related to major business transactions, as well as representing clients before the Internal Revenue Service and other tax authorities. He is located in Nyemaster's Des Moines office.