CARES + FFCR Acts: Tax Benefits and Implications

April 16, 2020
Your Presenters

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• University of Iowa (B.A. in Accountancy)
• Certified Public Accountant
• Children’s Museum of Phoenix, Chairman of the Board of Directors, Past Treasurer
• Firm Audit + Accounting Committee Member

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• University of Illinois (B.S. in Finance)
• Certified Public Accountant
• Jewish Community Foundation Member
• Firm Tax Committee Member

* Information provided is subject to change based on legislative updates.
<table>
<thead>
<tr>
<th>Program</th>
<th>Fund Amount</th>
<th>Purpose</th>
<th>Eligibility</th>
<th>Can apply toward a PPP?</th>
<th>Amount</th>
<th>Duration</th>
<th>LTV</th>
<th>Payroll?</th>
<th>Business Mortgage or Lease</th>
<th>Qualifying Expenses</th>
<th>Other Working Capital?</th>
<th>Other</th>
<th>Timeline</th>
</tr>
</thead>
<tbody>
<tr>
<td>Paycheck Protection Program (PPP)</td>
<td>$349 billion</td>
<td>Capital to cover cost of retaining employees (EE)</td>
<td>Forgivable loan ( forgiven amount considered &quot;grant&quot;) in operations before 2/15/20</td>
<td>no</td>
<td>N/A</td>
<td>2 years</td>
<td>6%</td>
<td>yes</td>
<td>yes</td>
<td>yes</td>
<td>no</td>
<td>no</td>
<td>Small businesses and sole proprietorships can apply 4/30/20; independent contractors and self-employed can apply on 4/1/20; application deadline is 6/30/20</td>
</tr>
<tr>
<td>Economic Injury Disaster Loan (EIDL)</td>
<td>$10 billion</td>
<td>Grace period of smaller amount of cash</td>
<td>Loans up to $10,000 forgivable advance in operations by 1/31/20</td>
<td>yes EIDL received 13-45 can be refinanced into PPP up to $10k advance received</td>
<td>up to $24k; including a $10k advance that does not have to be repaid if loan is declined</td>
<td>10 years; 12-month deferral option</td>
<td>3.75% (business) or 2.75% (nonprofit); interest rate varies during deferment period</td>
<td>yes</td>
<td>yes</td>
<td>yes</td>
<td>Bills that cannot be paid due to a disaster’s impact</td>
<td>Bills that cannot be paid due to a disaster’s impact</td>
<td>Approval: 2-3 weeks; loan disbursement up to 5 days</td>
</tr>
<tr>
<td>Small Business Debt Relief Program</td>
<td>$17 billion</td>
<td>Keep up with payments on current or potential SBA loans</td>
<td>Temporary loan paymen relieff active SBA loan or new loan by 9/30/20</td>
<td>no</td>
<td>Equal 6 months of loan principal and interest</td>
<td>0 months</td>
<td>N/A</td>
<td>no</td>
<td>no</td>
<td>no</td>
<td>Existing qualifying loan payments</td>
<td>Approval: automatic</td>
<td></td>
</tr>
<tr>
<td>Express Bridge Loan (EBL)</td>
<td>N/A</td>
<td>Expedited loan funding while awaiting long-term financing</td>
<td>Short-term financing 3/25/20</td>
<td>no</td>
<td>Up to $25,000</td>
<td>up to 7 years</td>
<td>up to 6.5%</td>
<td>yes</td>
<td>yes</td>
<td>yes</td>
<td>Bills that cannot be paid due to disaster’s impact</td>
<td>Bills that cannot be paid due to disaster’s impact</td>
<td>Approval: 24-36 hours (response time); 90 days (months post-emergency declaration)</td>
</tr>
</tbody>
</table>
## 2020 Federal Government COVID-19 Financial Resources

<table>
<thead>
<tr>
<th>Program</th>
<th>Fund Amount</th>
<th>Purpose</th>
<th>Type</th>
<th>Date</th>
<th>Business Type</th>
<th>Can apply toward a PPP/7</th>
<th>Amount</th>
<th>Duration</th>
<th>IR</th>
<th>Payroll*</th>
<th>Business Mortgage or Lease</th>
<th>Utility</th>
<th>Other Working Capital*</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payroll Tax Deferral</td>
<td>0%</td>
<td>Short-term relief from payroll taxes</td>
<td>Tax deferral</td>
<td>4/1/20</td>
<td>All employers</td>
<td>no (businesses claiming PPP cannot use this program)</td>
<td>equal to employer share of social security tax</td>
<td>through 7/15/20</td>
<td>n/a</td>
<td>social security payroll tax only</td>
<td>no</td>
<td>no</td>
<td>no</td>
<td></td>
</tr>
<tr>
<td>Employee Retention Tax Credit</td>
<td>0%</td>
<td>Credit designed for employer to keep employees (EE) on payroll</td>
<td>Nonrefundable tax credit</td>
<td>4/1/20</td>
<td>All employees that experience a significant decline in gross receipts or suspends operations during 2020 due to COVID-19</td>
<td>no (businesses claiming PPP cannot use this program)</td>
<td>Tax credit is equal to 50% of qualified wages, up to $10,000 per EE</td>
<td>4/1/20 through 1/1/21</td>
<td>n/a</td>
<td>qualifying wages, including qualified healthcare plan expenses up to $10,000</td>
<td>no</td>
<td>no</td>
<td>no</td>
<td></td>
</tr>
<tr>
<td>Emergency Paid Sick Leave and FMLA</td>
<td>0%</td>
<td>Credit designed for employer to pay employees who are not able to work</td>
<td>Nonrefundable tax credit</td>
<td>4/1/20</td>
<td>Any business that is open and has employees working or teleworking</td>
<td>no (businesses claiming forgiveness of a PPP loan will need to exclude wages paid under this act from the forgiveness calculation)</td>
<td>Tax credit is equal to 100% of qualified wages</td>
<td>4/1/20 - 12/31/20</td>
<td>n/a</td>
<td>tax credit is equal to 100% of qualified wages, plus employer healthcare at 1.45%, plus health care costs paid by employer</td>
<td>no</td>
<td>no</td>
<td>no</td>
<td></td>
</tr>
</tbody>
</table>

*Businesses must report paying payroll taxes by 7/15/20; first half of deferred tax liability must be repaid by 12/31/20 and second half must be repaid by 12/31/22.

*Reported on each quarter of federal tax returns up to $5,000 per EE in the calendar year.

*Businesses must report paying payroll taxes by 7/15/20; first half of deferred tax liability must be repaid by 12/31/20 and second half must be repaid by 12/31/22.
Employer Payroll Taxes
Employer Payroll Taxes to Be Discussed

- You retain employees; Government covers 100% of the cost of payroll* at no cost to you:
  - FFCRA mandated sick and leave provisions
  - PPP loans that are fully forgiven
    - *SBA PPP loans that are partially forgiven: you and the Government split the payroll costs

- You retain employees; Government covers part of the cost of payroll to help you conserve cash:
  - Employee Retention Tax Credit
  - Employer Payroll Tax Deferment

* Information provided is subject to change based on legislative updates.
FFCRA

- Signed by the President on March 18, 2020
- Effective April 1, 2020 through December 31, 2020
- 80 hours of emergency paid sick leave for workers who meet certain requirements discussed in following slides
- Provides paid family and medical leave that employees will be able to use to care for family members (not for personal illness) for up to 12 weeks.
  - The first 10 days may be unpaid unless employees use paid time off or EPSL noted above

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**Who is an eligible employer?**

- Less than 500 employees – both full and part time
- If less than 50 employees, can you make the argument that this will jeopardize the viability of your business as a going concern
  - If so, then document the reasons why

**Who is an eligible employee?**

- Any employee that has been employed for at least 30 calendar days before leave is requested (part time and full time count)

* Information provided is subject to change based on legislative updates.*
FFCRA - Paid Sick Leave

Paid sick leave is expanded for an eligible employee and is entitled to up to 80 hours of paid sick leave (over a two week period) for any of the following six reasons:

1. Subject to a Federal, State, or local quarantine or isolation order related to COVID-19.
   - You are not entitled to paid leave because your business closed its doors, voluntarily or involuntarily


4. Caring for an individual who is subject to quarantine or has been advised to self-quarantine.

5. Caring for a son or daughter of such employee if the school or place of care of the son or daughter has been closed, or the child care provider of such son or daughter is unavailable, due to COVID-19 precautions.

6. Experiencing any other substantially similar condition.

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FFCRA – Paid Sick Leave (Continued)

• Employee pay for sick leave und FFCRA
  – If sick leave is for reasons 1, 2 or 3 (employee must be sick), the employee is paid based on the number of hours they would normally work, AND the greater of:
    o The employee’s regular rate of pay,
    o The federal minimum wage, or
    o A state or local minimum wage
    o Total pay is capped at $511/day or $5,110 in the aggregate
  – If sick leave is for reasons 4, 5 or 6 (the employee is caring for someone)
    o The employee is paid based on the number of hours they would normally work, and
    o 2/3 of the employee’s regular rate of pay
    o Total pay is capped at $200 per day and $2,000 in the aggregate

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Emergency FMLA

The Act has provided up to 12 weeks of leave for any period beginning April 1, 2020 and ending December 31, 2020 if you have a “qualifying need” related to a “public health emergency”

• What is a “qualifying need related to a public health emergency”?
  – An emergency with respect to COVID-19 declared by a Federal, state or local authority.
  – An employee is unable to work (or telework) due to a need for leave to care for the son or daughter under 18 years of age of such employee if the school or place of care has been closed, or if the child care provider of such son or daughter is unavailable, due to a public health emergency.
  – As discussed for sick leave, you are not entitled to paid leave because your business closed its doors, voluntarily or involuntarily. You must be caring for a child.

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Emergency FMLA (Continued)

• For the first two weeks of EFMLA is unpaid leave, the employee can elect to use paid vacation, sick leave or EPSL
• For the next ten weeks, the employer must pay employee based on:
  – At least 2/3 of the employee’s regular pay (this must be above the federal minimum wage or the applicable state or local minimum wage), and
  – The number of hours the employee would otherwise be normally scheduled to work. (You must factor in overtime hours into this computation. In addition, a part-time employee is subject to a separate calculation)
• The leave pay is not required to exceed $200/day or $10,000 in the aggregate to any one employee

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FFCRA – Payroll Tax Credits

- Amounts paid for family or sick leave will create a credit that will reduce the employer’s 6.2% share of the Social Security tax
  - 100% of wages paid for up to 10 days of sick leave and ten weeks of family sick leave
  - Plus: employers share of Medicare tax = 1.45%
  - Plus: health care costs paid by employer

* Information provided is subject to change based on legislative updates.
FFCRA – Payroll Tax Credits (Continued)

- The IRS guidance is very friendly as it is giving employers the ability to have cash to pay wages
  - You get an instant reduction of the amount necessary to pay federal income tax withholding and the employer and employee’s share of payroll taxes.
- No need to deposit payroll withholding money with the IRS and then file a Form 941 claiming a credit
  - Reduce your deposits in real time and use the funds to pay the sick and emergency leave wages.
- If credit is greater than the sum of federal income tax withholding and the employer’s and employee’s share of payroll taxes, you can apply for an instant refund
  - Form 7200, Advance of Employer Credits Due

* Information provided is subject to change based on legislative updates.
Examples

• Employer paid $5,000 in EPSL during the quarter. Employer has $8,000 required to deposit, as noted as due on Form 941. Employer required to deposit only $3,000 and the other $5,000 was used to pay employees the EPSL.

• Employer paid $10,000 in EPSL during the quarter. Employer has $8,000 required to deposit, as noted as due on Form 941. Employer can use the entire $8,000 to pay employees the EPSL and then file from 7200 for refund of $2,000.

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Employee Retention Tax Credit

**What is it?**

- A refundable payroll tax credit for employers who are harmed by COVID-19, but retain their employees

**Who qualifies?**

- Employers qualify for the credit if:
  - Their operations were fully or partially suspended due to a COVID-19 related shutdown order
    - OR
  - Their gross receipts for the quarter were less than 50% of the gross receipts for the same quarter in the prior year
- Employers that receive a PPP loan do not qualify for the credit
  - Employers with 500 or less employees per location – most restaurants qualify for the PPP so will not qualify for employee retention tax credits

*Information provided is subject to change based on legislative updates.*
Employee Retention Tax Credit (Continued)

How much is the credit?

• 50% of qualified wages paid to employees between March 12, 2020 and December 31, 2020
• Capped at $10,000 of wages per employee, so the maximum available credit is $5,000 per employee (50% of $10,000)

* Information provided is subject to change based on legislative updates.
Employee Retention Tax Credit (Continued)

What are qualified wages for purposes of the credit?

• Qualified wages include gross wages paid and the cost of providing health care coverage up to the $10,000 maximum
• Emergency sick and FMLA payments mandated by the Families First Coronavirus Response Act by employers with fewer than 500 employees, do not constitute qualified wages (a 100% credit applies)

* Information provided is subject to change based on legislative updates.
Employee Retention Tax Credit (Continued)

How to get the credit

• Identify the amount of qualifying wages perhaps by setting up a new payroll code in your system
  – New codes can track payments that qualify and your system might provide features that cut off at $10,000

• Caution:
  – Most payroll systems do not currently have the allowed health care cost so new procedures must be established to get these amounts added to the payroll disbursement for purposes of credit calculations
  – The total amount from the Employee Retention Payment codes plus the health care cost (up to $10,000 per employee) will be multiplied by 50% to determine the credit amount

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Employee Retention Tax Credit (Continued)

How to get the credit

• Employers collect their own refund via offset to regular payroll deposits
  – Guidance was issued on March 31, 2020 making it clear that the Employee Retention Credit can be offset from the employer’s total federal deposit for each pay period.
  – This guidance also provides the refund procedure to be used when the credit amount exceeds the regular total payroll deposit.
    o Form 7200
    o Should be processed within 2 weeks of filing

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Employer Payroll Tax Deferment

What is it?
• Delay the payment of the employer portion of Social Security tax (6.2%) that would otherwise be due and payable by December 31, 2020

Who Qualifies?
• All employers except an employer who “has had” loan forgiveness under the PPP

* Information provided is subject to change based on legislative updates.
Employer Payroll Tax Deferment (Continued)

What is the deferral period?
• 50% of the deferred amount can be deferred up to December 31, 2021, and any remaining amount can be deferred up to December 31, 2022

What is the impact on my FICA Credit?
• Generally, the FICA Credit equals the amount of employer social security and Medicare taxes paid or incurred by the employer on tips received by the employee
• During the period of deferral, the employer is treated as having made timely deposits of applicable taxes, as long as payments are made when due under the schedule noted above
• Guidance is needed to confirm that this allows restaurants to claim the FICA Credit during the deferral period

* Information provided is subject to change based on legislative updates.
Income
Tax
Benefits
Tax Provisions – Taxpayer Friendly Designed to Get Cash and Cut Taxes

• Four main changes
• Three changes to calculate taxable income
  1. 163(j)
  2. QIP
  3. Excess Business Loans
• Change to NOL rules regarding usage + carrybacks
Section 163(j) – Interest Expense Deduction Limitation

Increased Section 163(j) Limit for 2019 and 2020

• With the exception of partnerships, and solely for taxable years beginning in 2019 and 2020, taxpayers may deduct business interest expense up to 50% of ATI, an increase from 30% of ATI under the TCJA
• Taxpayers may elect out the increased Section 163(j) limit, but the election may be revocable only with the consent of the Secretary

Substitute 2019 ATI for 2020 ATI

• For any taxable year beginning in 2020, the taxpayer may elect to substitute the ATI for the last taxable year beginning in 2019 for the 2020 ATI
• In the case of a partnership, the election shall be made by the partnership
• If 2019 is a short taxable year, the taxpayer is allowed to annualize its 2019 ATI based on the number of months (as opposed to the number of days) of the short taxable year
• Unanswered: How shall the election be made?

Benefits

• Additional business interest deduction equal to 20% of ATI for 2019 and 2020
• If 2019 return was already filed, taxpayers can file a superseding return/amended return to claim refund, if applicable
• Manage financial projections and estimated tax payments for 2020

* Information provided is subject to change based on legislative updates.
Section 163(j) – Rules for Partnerships and Partners

• In the case of partnerships, the increased Section 163(j) limit from 30% to 50% of ATI does not apply to taxable year beginning in 2019, but it does apply to taxable year beginning in 2020.

• In lieu of the increased Section 163(j) limit for taxable years beginning in 2019, the CARES Act provides that:
  – In the case of any excess business interest expense (“EBIE”) allocated from a partnership for any taxable year beginning in 2019, 50% of such EBIE shall be treated as business interest which is paid or accrued by the partner in the partner’s first taxable year beginning in 2020 and which is not subject to the partner’s Section 163(j) limit in 2020.
  – The remaining 50% of EBIE shall be subject to the limitations in the same manner as any other EBIE.

• Each partner has the ability, under regulations to be prescribed by Treasury, to elect to have this special rule not applied.

• No rules are provided for application of this rule in the context of tiered partnership structures.

Benefits

• Substantial tax savings in 2020.
• Manage financial projections and estimated tax payments for 2020.
• Reduces complexities for partnerships by eliminating the need to amend 2019 partnership returns.

* Information provided is subject to change based on legislative updates.
Section 163(j) and Real Estate Entities

• In 2018, real estate businesses that made an election to be excepted from section 163(j) are bound to use longer depreciation lives. Had bonus depreciation been allowed for these companies, they may not have made this election. The section 163(j) election had been irrevocable.

**BREAKING NEWS**

Rev Proc. 2020-22 allows either late election OR revocation of election by amended return.

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Section 163(j) – State Considerations

- “Fixed-date” IRC conformity states that do not update their IRC conformity – no benefit of increased 20% deduction; no elections
- States that follow “old” section 163(j) (California, Georgia, Tennessee in 2020) – no elections
- States that already decoupled (CT, IN, MO, SC, WI) – no direct impact, but must still manage elimination of excess interest carryovers
- Partnerships – CARES Act creates additional layer of complexity, especially for states that tax partnerships at entity level, composite returns
- Section 163(j) was already very complex at the state level; CARES Act makes it even more complex

* Information provided is subject to change based on legislative updates.
Qualified Improvement Property (QIP)

Correction of “Retail Glitch”

- Clarifies that Qualified Improvement Property (QIP) placed in service after 12/31/17 is treated as 15-year property and eligible for bonus depreciation
- Taxpayers that placed QIP in service during 2018 and 2019 may now claim bonus depreciation on such property, rather than depreciating over 39 years as previously required under the 2017 tax reform bill
- Taxpayers with QIP in 2018 that filed their 2018 return treating the assets as bonus-ineligible 39-year property should consider amending that return to claim additional depreciation. C corporations taxpayers that amend their 2018 return can potentially generate NOLs and carry the losses back five years under the new provisions of the CARES Act to tax years when the tax rates were 35% and fully offset income to generate immediate cash savings
  - Alternatively, taxpayers may file an automatic Form 3115 with their 2019 return to claim the missed depreciation as a favorable Section 481(a) adjustment
- Taxpayers with QIP placed in service during 2019 can claim bonus depreciation prospectively on their 2019 return; corporate taxpayers should also consider filing Form 4466 for quick refund of 2019 overpaid estimated taxes

* Information provided is subject to change based on legislative updates.
QIP (Continued)

Correction of “Retail Glitch”

• The QIP fix presents significant opportunities to many taxpayers and cost segregation studies are vital tools that can provide a supportable breakdowns between eligible and ineligible costs

• QIP includes improvements a taxpayer makes to an interior portion of an existing building that is nonresidential real property (residential rental property is excluded); Examples of such qualifying improvements include installation or replacement of drywall, ceilings, interior doors, fire protection, mechanical, electrical and plumbing. Excluded improvements are internal structural framework, enlargements to the building, and elevators or escalators

• Under the Tax Cuts and Jobs Act of 2017, taxpayers who make the real property trade or business election under Section 163(j) must depreciate nonresidential real property, residential rental property, and QIP using the Alternative Depreciation System (ADS), and as such are not permitted to claim bonus depreciation on these assets; However, cost segregation studies can still help to identify personal property still eligible for bonus depreciation

• Increased IRS scrutiny must be assumed

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Excess Business Losses – Applies to Individuals

• Post TCJA could only use $250,000 ($500,000 MFJ) to offset income (salary counted as business income)

• CARES Act changes
  1. 2018, 2019 and 2020 no limitation
  2. Starting in 2021 limitation is back; however, salary does not count as business income
# Net Operating Losses – Pre/Post-TCJA, CARES

<table>
<thead>
<tr>
<th>Pre-TCJA</th>
<th>Post-TCJA</th>
<th>CARES Act</th>
</tr>
</thead>
<tbody>
<tr>
<td>2-year carryback, 20-year carryforward</td>
<td>5-year carryback for NOLs in taxable years beginning after December 31, 2017, and before January 1, 2021.</td>
<td>No limitation on ability to offset current taxable income with NOL deduction, 90% AMT limitation.</td>
</tr>
<tr>
<td>No limitation on ability to offset current taxable income with NOL deduction, 90% AMT limitation.</td>
<td>For years beginning after December 31, 2020, NOL deduction limited to 80% of taxable income following the deduction of any pre-2018 NOLs, before any §199A or §250 deduction.</td>
<td></td>
</tr>
<tr>
<td>Ordering of pre-2018 NOLs ambiguous.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

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Variables in NOL Utilization

Maximizing a carryback involves understanding how the NOL deduction interacts with other provisions and the effective rate:

- Carryback from a 21 percent federal rate NOL back to a 35 percent federal rate year (pre-2018)
- DPAD (repealed for 2018 and later) limited to taxable income, potentially reduced by carryback
- §179 election to expense depreciable assets limited to taxable income, but otherwise carried forward
- Charitable contribution deduction pursuant to §170(b)(2)(A) limited to 10 percent of taxable income, carries forward up to a maximum of five years

* Information provided is subject to change based on legislative updates.
Warning!

- Do not mail anything to the IRS
  – Either USPS or Private Delivery Service
- It likely will not be processed for months
How to Claim NOL Carryback

1. File return which generates loss, e.g. 2019 income tax return
   AND
2. Prepare carryback form
   – 1139 for C Corporation
   – 1045 for Individuals
   OR
3. Prepare amended return for year in which NOL is carried back to, e.g. 2014 income tax return

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Pros + Cons

**Carryback Form**

- **Pro:** IRS must act within 90 days or pay interest on refund claim
- **Pro + Con:** Must be filed by end of year
- **Con:** Cannot be electronically filed

- Special temporary procedure:
  - Fax Form 1139 claims to: 844-249-6236
  - Fax Form 1045 claims to: 844-249-6237

*Information provided is subject to change based on legislative updates.*
Pros + Cons

Amended Return

• **Pro:** Can be electronically filed
• **Con:** No expectation that IRS will process quickly

* Information provided is subject to change based on legislative updates.
Reminders on State NOL Considerations

• Certain states ("fixed-date" IRC conformity states) that adopted the 80% limitation must update their IRC conformity dates to adopt the CARES Act modifications to the limitation.
• Many states do not permit NOL carrybacks.

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Resources:

Henry+Horne
COVID-19 Updates
www.hhcpa.com/covid-19

2020 Federal Government
COVID-19 Financial
Resources Chart

FFCRA Flowchart
Questions?
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