Senate passes Phase Three COVID-19 economic stabilization legislation

March 26, 2020

In brief

The Senate late on March 25 voted 96 to 0 to pass a $2 trillion “Phase Three” COVID-19 economic stabilization package, H.R. 748, the ‘Coronavirus Aid, Relief, and Economic Security Act’ (the CARES Act), that features significant tax provisions and other measures to assist individuals and businesses impacted by the economic effects of the COVID-19 pandemic.

Tax relief measures for businesses include a five-year net operating loss (NOL) carryback (including a related technical correction to the 2017 tax reform act), a change in Section 163(j) interest deduction limitations, accelerated AMT refunds, payroll tax relief, a temporary suspension of certain aviation excise taxes, a tax credit for employers who retain employees, and a ‘qualified improvement property’ technical correction to the 2017 tax reform act. Tax relief measures for individuals include ‘recovery rebate checks,’ special rules for the use of retirement accounts, and charitable giving provisions.

The CARES Act provides significant amounts of federal funding for a range of non-tax economic stabilization measures to assist individuals and businesses impacted by the economic effects of COVID-19. The Act provides $500 billion for a Treasury Department Exchange Stabilization Fund to provide loans, loan guarantees, and other investments to eligible businesses and $349 billion for a Small Business Administration ‘paycheck protection program.’ The legislation also includes $340 billion in emergency funding for hospitals, healthcare agencies, and assistance to state and local governments responding to the coronavirus.

The House is expected to vote on the legislation by voice vote on Friday, March 27, in order to avoid having to recall all House members to the Capitol where some members and staff have tested positive for the COVID-19 virus. Congressional leaders hope to send a final bill approved by both chambers to the White House by the end of the week. President Trump is expected to sign the legislation.

Efforts to enact a COVID-19 economic stabilization package follow the March 6 enactment of a ‘Phase One’ package providing $8.3 billion of funding for health agencies and the March 18 enactment of a ‘Phase Two’ relief package. The Phase Two legislation included a new business tax credit, estimated to cost $104.8 billion, for certain employers with fewer than 500 employees to provide paid sick leave and paid family and medical leave through the end of 2020. A “Phase Four” bill may be considered as officials continue to assess the effects of the COVID-19 pandemic on public health and the US economy. In a March 25 interview, House Speaker Nancy Pelosi (D-CA) said the CARES Act “is not going to be the last bill.”

In detail

The CARES Act economic stabilization package approved by the Senate features significant tax provisions and other measures to assist individuals and businesses impacted by the economic effects of the COVID-19 pandemic. The Senate-passed version of the CARES Act is patterned after an earlier Senate Republican version released on March 19 by Majority Leader Mitch McConnell (R-KY).

CARES Act tax provisions

The CARES Act includes the following business tax relief provisions:

- Net operating loss (NOL) changes - Allows an NOL from tax years beginning in 2018, 2019, or 2020 to be carried back for five years. The provision temporarily removes the current-law taxable income limitation to allow an NOL to fully offset income. The provision also makes a retroactive technical correction to the 2017 tax reform act to allow NOLs arising in a tax year beginning in 2017 and ending in 2018 to be carried back two years.

  An NOL limitation applicable to pass-through businesses and sole proprietors is modified to permit utilization of excess business losses for tax years beginning before January 1, 2021.

  The provision includes technical corrections to the 2017 tax reform act clarifying (1) treatment of excess business losses that are carried forward and treated as part of the taxpayer's NOL, (2) that excess business losses are determined without regard to any deduction under Sections 172 or 199A, and (3) that excess business losses are determined without regard to any deductions, gross income, or gains attributable to any trade or business of performing services as an employee (e.g., wages).

Observation: The Senate-passed CARES Act modifies the earlier proposed NOL change so that NOL carrybacks cannot be used against amounts includible in gross income by reason of Section 965(a). However, if the five-year carryback period includes one or more tax years in which an amount is includible in gross income by reason of Section 965(a) (a 'toll charge year'), then the taxpayer may elect to exclude the toll charge years from the five-year carryback period. Some taxpayers may want to elect out of carrying an NOL to a toll charge year to avoid the resulting overpayment being applied to future installment payments required under Section 965(h), but those taxpayers will need to consider the reduced US tax rate applicable for years subsequent to the toll charge year.

- Corporate AMT credit refunds - Accelerates the ability of companies to receive refunds of AMT credits in tax years beginning in 2019. Alternatively, companies could elect to claim the entire refundable AMT credit in tax years beginning in 2018.

- Section 163(j) changes - Increases the 30% adjusted taxable income limitation to 50% for tax years beginning in 2019 and 2020. For 2019, this provision does not apply to partnerships and instead partners may deduct 50% of their distributive share of the partnership's excess business interest in 2020 without regard to Section 163(j). The provision also allows a taxpayer (including partnerships) to elect to use its 2019 adjusted taxable income for its 2020 limitation.

Observation: The Senate-passed bill modifies the earlier proposed Section 163(j) change so that a taxpayer can elect out of the increased Section 163(j) limitation. Some taxpayers may want to elect out of the increased limitation because of interaction of Section 163(j) with other provisions, such as the base erosion and anti-avoidance tax (BEAT).

Note: See below for a discussion of tax accounting considerations related to the proposed NOL and Section 163(j) changes.

- Employee retention credit - The CARES Act provides a new temporary refundable 50% employee retention credit for employers subject to full or partial business suspension due to the COVID-19 emergency, or for employers whose gross receipts have significantly declined due to COVID-19 (defined as a reduction in gross receipts of more than 50% when compared to the same quarter in the prior year). The credit is to be applied against the employer's share of payroll taxes. The amount of qualified compensation (including health benefits) eligible for the credit with respect to any individual employee is limited to $10,000, and the credit is limited to applicable employment taxes on wages paid (reduced by the payroll Work Opportunity Tax Credit, the payroll research credit, and the payroll tax credits under the Families First Coronavirus Response Act). Any excess payments will be refunded.

- Payroll taxes - Delays payment of applicable 2020 employer payroll taxes from date of enactment through December 31, 2020. Half of the deferred tax is to be paid by December 31, 2021, and the remainder by December 31, 2022. Payroll taxes that can be deferred include the employer portion of FICA taxes, the employer and employee representative portion of Railroad Retirement taxes (that are attributable to the employer FICA rate), and half of SECA tax liability.

- Aviation excise taxes - Suspends certain aviation excise taxes, from the date of enactment through December 31, 2020.

- Alcohol excise taxes - Suspends certain alcohol excise taxes for distilled spirits used in the production of hand sanitizer produced in line with guidance issued by the Food and Drug Administration, from January 1, 2020 through December 31, 2020.

- QIP technical correction - Makes a technical correction to the 2017 tax reform act to provide a 15-year recovery period for qualified improvement property (QIP). This technical correction would make QIP eligible for bonus depreciation. This technical correction is effective as if enacted as part of the 2017 tax reform act.

Observation: Finance Committee Chairman Chuck Grassley (R-IA) has stated that “this [retroactive] provision not only increases companies’ access to cash flow by allowing them to amend a prior year return, but also incentivizes them to continue to invest in improvements as the country recovers from the COVID-19 emergency.” It is expected that taxpayers will be permitted to file an automatic Form 3115, *Application for Change in Accounting Method*, in lieu of amending prior year returns.

Provisions that were dropped from the original Senate GOP version include:

- A technical correction to the 2017 Act regarding Section 965 overpayment refunds.

- A provision restoring the limitation on downward attribution of stock ownership in applying constructive ownership rules.

- Changes related to tax filing deadlines, including a provision postponing payments of certain estimated tax payments.

Observation: The Senate-passed CARES Act dropped proposed statutory changes to tax filing deadlines as the focus shifted to calls for Treasury and the IRS to provide more disaster tax relief under their current-law authority. Initial IRS notices delaying certain tax payments and tax filings (Notices 2020-17 and 2020-18) are limited in the scope of relief provided to taxpayers. Business groups and organizations representing taxpayers have sought additional relief and guidance from the IRS. In response, the IRS on March 24 published an online summary of filing and payment deadlines questions and answers. Many state governments also are providing relief from certain state tax payment and filing requirements to individuals and businesses. See below for links to IRS coronavirus guidance and a PwC tracker of state tax relief measures.

In addition, the CARES Act includes:

- "Recovery rebate checks" up to $1,200 for individuals / $2,400 for married couples / $500 per child. The one-time recovery rebate will begin phasing out after $75,000 for a single filer and $150,000 for a joint filer, and is completely phased out after $99,000 for a single filer ($198,000 for a joint filer) with no children. Phase-out ranges are adjusted for each child on a filer’s return. Rebate checks will be issued by the IRS based on a taxpayer’s 2019 tax return if filed, or otherwise on their 2018 return. A Social Security benefit statement will be used for individuals who have not filed tax returns for either 2018 or 2019.

- Special rules for use of retirement funds, including a temporary waiver of the 10% early withdrawal penalty for certain distributions up to $100,000 made on or after January 1, 2020 from qualified retirement accounts for coronavirus-related purposes. A temporary waiver of required minimum distribution rules for certain retirement plans and accounts also is provided, among other changes.

- Partial "above-the-line" deduction up to $300 for charitable contributions and modification of limitations on charitable contributions in 2020 for individuals who do not itemize. Additional charitable giving modifications include increases in the limitations on deductions for charitable contributions in 2020 by individuals who itemize, as well as corporations, among other changes.
- An exclusion is provided for certain employer payments of student loans. An employer may contribute up to $5,250 annually toward an employee's student loans, and such payment would be excluded from the employee's income. The provision applies to any student loan payments made by an employer on behalf of an employee after the date of enactment and through the end of 2020.
- Modifications to certain recently enacted COVID-19-related paid leave and paid sick leave requirements.
- The legislation extends through November 30 certain Medicare healthcare provisions that were set to expire on May 22.

Observation: The Senate-passed CARES Act modifies the earlier proposed recovery rebate provisions to eliminate language that would have reduced the amount of recovery checks for lower-income individuals.

Other CARES Act provisions

The CARES Act provides federal funding for a range of non-tax economic stabilization measures to assist individuals and businesses impacted by the economic effects of COVID-19.

The legislation provides $500 billion for a Treasury Department Exchange Stabilization Fund (the Fund) to provide loans, loan guarantees, and other investments to eligible businesses. The Treasury Department is directed to use the Fund to provide direct lending totaling $50 billion for passenger airlines, $8 billion for cargo carriers, and $17 billion for businesses important to maintaining national security. Companies receiving assistance from the Fund must maintain existing employment levels, to the extent possible. To be eligible, the business entity must be US-based and have significant domestic operations, with a majority of employees based in the United States.

The Senate-passed CARES Act requires public reporting of Fund assistance to eligible businesses and oversight procedures that include an independent inspector general and a Congressional oversight panel. The legislation applies prohibitions on stock buybacks and dividends, and limitations on executive compensation for the term of Fund assistance, plus one year on any company receiving assistance. Certain government officials holding a controlling interest in a business, including the President, the Vice President, Members of Congress, and heads of Executive Departments (and their spouse, child, son-in-law, or daughter-in-law), are prohibited from receiving Fund assistance.

Observation: The CARES Act prohibits recipients of any direct lending from the Fund from increasing the compensation of any officer or employee whose total compensation exceeded $425,000 in 2019; this restriction applies during the two-year period from March 1, 2020 to March 1, 2022. Companies receiving such loans also are prohibited from offering such employees severance pay or other benefits upon termination of employment that exceed twice the maximum total annual compensation received by that employee.

Other non-tax economic stabilization provisions include:

- $349 billion for a Small Business Administration 'paycheck protection program' to provide loans up to a maximum of $10 million to eligible businesses, nonprofits, or veterans organizations with not more than 500 employees. The SBA is authorized to provide covered loans to certain accommodation and food service businesses that employ fewer than 500 employees per physical location. Sole proprietors, contractors, and other self-employed individuals are eligible for the loans; nonprofits that receive Medicaid reimbursement are excluded. The covered loan period begins February 15, 2020 and ends on June 30, 2020.

Covered loans can be used for payroll costs; costs related to certain group health benefits; employee salaries, commissions, or similar compensation; payments on qualifying mortgage or rent obligations; utilities; and interest on any other debt obligations that were incurred before the covered period. Limits include a cap of $100,000 on the amount of an individual employee's compensation that can be funded from a covered loan.

Loan forgiveness is provided for loan amounts spent during an initial eight-week period for certain expenses including payroll costs, with the amount of loan forgiveness dependent on employee retention. Borrowers which rehire workers previously laid off will not be penalized for having a reduced payroll at the beginning of the period. Amounts of cancelled indebtedness under this program will not be included in the borrower's taxable income. 'Express loan' procedures are provided to accelerate the processing of loan applications and cover the cost of certain loan processing fees.

- $260 billion for increased unemployment assistance, including up to four months of full replacement wages up to certain limits for individuals who lose a job or are furloughed due to the coronavirus national emergency. A temporary waiver of waiting period requirements is provided and payments are permitted for individuals not traditionally eligible for unemployment benefits (self-employed, independent contractors, those with limited work history, and others) who are unable to work as a direct result of the coronavirus emergency.

Additional relief provisions include:

- Healthcare provisions addressing Medicare and Medicaid services, medical supply shortages, medical device shortages, support for healthcare providers, and telehealth services.
- Assistance to students, including relief for certain post-secondary student loans.
- A temporary foreclosure prohibition for certain federally backed mortgage loans.
- A temporary moratorium on eviction filings for certain rental properties receiving specified federal assistance.

Emergency supplemental appropriations

The CARES Act provides $340 billion in emergency funding to combat coronavirus outbreaks, including:

- $150 billion for state, local, and tribal governments;
- $117 billion for hospitals;
- $45 billion for the FEMA Disaster Relief Fund;
- $16 billion for the Strategic National Stockpile;
- $4.3 billion for the Centers for Disease Control;
- $11 billion for vaccines, therapeutics, diagnostics, and other preparedness needs;
- $25 billion for food assistance; and
- $25 billion for public transportation emergency relief.

Observation: The inclusion of a $340 billion package of emergency supplemental appropriations in the CARES Act is not expected to end discussion of a potential "Phase Four" COVID-19 response bill. With several members of Congress and their staff having tested positive for the COVID-19 virus, Congress may recess for some period of time after completing action on the CARES Act and not reconvene until the House and Senate are ready to consider additional legislation. The House and Senate could, with adequate cooperation, take action on legislation by unanimous consent to avoid large numbers of members and staff having to return to the Capitol.

Tax accounting considerations

ASC 740 requires that the tax effects of changes in tax laws or rates be recorded discretely as a component of the income tax provision related to continuing operations in the period of enactment. For US federal tax purposes, the enactment date is the date the President signs the bill into law. Among other considerations, the CARES Act allows for federal NOLs generated in certain years to be carried back for five years and temporarily removes the federal 80% of taxable income limitation, allowing an NOL to fully offset taxable income. Further, temporary increases to the Section 163(j) interest expense limitation will be available for 2019 and 2020.

Companies should consider the impacts of these changes on the realizability of deferred tax assets, particularly where carrybacks of NOLs were previously not allowed under federal tax law and therefore carryback was not available as a source of taxable income. Further, when carrying back an NOL to a prior year, companies should consider the impact of utilization at a higher rate (generally 35%, or blended rate for fiscal year taxpayers) than the rate used to record the deferred tax asset currently. The tax rate applied to NOLs generated in the current year should reflect the applicable tax rate for the year in which the NOL is expected to be utilized. Companies should also consider the impact of the technical correction to the treatment of qualified improvement property, including any changes in uncertain tax positions.

The takeaway

The new "Phase Three" COVID-19 economic stabilization legislation features significant new provisions intended to assist individuals and businesses impacted by the pandemic and its economic effects. Stakeholders should carefully review proposals that are intended to help employers retain employees and continue business operations during the current public health emergency. Stakeholders also should continue to engage with policymakers as the legislation is implemented and as additional relief measures affecting their business operations and employees may be considered.

Additional information

For a 35-page Senate staff summary of the overall CARES Act, click here. For a six-page Senate Finance Committee staff summary of the Act's tax and unemployment assistance provisions, click here. For the CARES Act text, click here.

For a Senate staff summary of the emergency supplemental appropriations bill, click here. For appropriations bill text, click here.

For an IRS summary of filing and payment deadlines questions and answers, click here. For IRS guidance updates on coronavirus tax relief, click here.

For PwC's tracker of state and local COVID-19 tax filing relief, click here.

For PwC's March 18 Insight on the "Phase Two" COVID-19 relief legislation, click here.

Let's talk

For a deeper discussion of how this might affect your business, please contact:

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