



Duffy Kruspodin, LLP
Certified Public Accountants

San Diego

4225 Executive Square
Suite 900
La Jolla, CA 92037
tel (858) 642-5050
fax (858) 642-5065

4304 Park Blvd.
San Diego, CA 92103
tel (619) 295-2637
fax (619) 299-5549

Los Angeles

21 600 Oxnard St.
Suite 2000
Woodland Hills, CA 91367
tel (818) 385-0585
fax (818) 436-7588

9171 Wilshire Blvd.
Suite 650
Beverly Hills, CA 90210
tel (310) 274-9922
fax (310) 858-1640

www.dklpcpa.com

Member

American Institute of
Certified Public Accountants



California Society of
Certified Public Accountants



www.jhi.com
Associated Worldwide with JHI

March 31, 2020

Dear Clients and Friends,

Having passed the Families First Coronavirus Response Act on March 18th in an effort to limit the spread of the pandemic and support relief efforts, Congress turned to specific measures to stabilizing the economy. President Trump on March 27th signed the \$2 trillion bipartisan Coronavirus Aid, Relief, and Economic Security (CARES) Act (H.R. 748). The CARES Act is considered "phase three" of lawmakers' and the Trump administration's collaborative response to the COVID-19 pandemic. Meanwhile, lawmakers on both sides of the aisle, have said they want to see a fourth economic relief measure.

The CARES Act looks to make a significant impact on the economy by providing loan forgiveness, supporting small businesses, enhancing unemployment insurance, and providing Federal loans to industries severely impacted by the pandemic. In addition, it provides tax relief and tax incentives for individuals and businesses alike. The majority of the tax relief is designed to increase liquidity in the economy, largely through the relaxation of limitations on business deductions and the deferral of taxes, but also the introduction of recovery rebates for individuals. This article will address the Federal tax relief provisions in the Act. It is important to note that each state will determine whether to follow the Federal changes for state income tax purposes.

INDIVIDUAL TAX RELIEF

Individual Recovery Rebate/Credit

New Law: The most well-publicized provision is the recovery rebates for individual taxpayers. Each US individual will receive within weeks up to \$1,200 and an additional \$500 for every child. This amount will be reduced for higher income taxpayers and begin phasing out after \$75,000 in adjusted gross income for a single taxpayer, \$112,500 for a head of household filer, and \$150,000 for married couples who file a joint return. The amount is completely phased-out for single taxpayers with incomes exceeding \$99,000, \$146,500 for head of household filers with one child, and \$198,000 for joint filers. The IRS will base these amounts on the taxpayer's 2019 tax return if filed, or in the alternative, their 2018 return. The rebate amounts are advance refunds of credits against 2020 taxes.

Here is a website to calculate your recovery rebate:

<https://www.kiplinger.com/tool/taxes/T023-S001-stimulus-check-calculator-2020/index.php>

No 10% Additional Tax for Coronavirus-Related Retirement Plan Distributions

Background: An early withdrawal from a qualified retirement plan is subject to a 10% additional tax penalty, unless the distribution meets an exception under Code Section 72(t).

New Law: Consistent with past disaster-related legislation, the Act waives early withdrawal penalties on coronavirus-related distributions from qualified retirement accounts up to \$100,000. A coronavirus-related distribution is any distribution (up to \$100,000), made on or after January 1, 2020, and before December 31, 2020, from an eligible retirement plan.

The Act also allows for such distributions to be repaid at any time over a 3-year period to avoid income tax on the distributions. Any amount of the distribution that is required to be included in the taxpayer's income may be recognized ratably over a 3-year period instead of all at once. The bill also provides flexibility for loans from certain retirement plans.

Required Minimum Distributions Waived for 2020

Background: In general, Code Sec. 401(a)(9) requires a retirement plan or IRA owner to take required minimum distributions (RMDs) annually once the owner reaches age 72.

New law: The Act provides that the RMD requirements do not apply for calendar year 2020.

Charitable Contributions

New Law: The Act enhances tax incentives for making a charitable contribution for the 2020 tax year. It allows an above-the-line deduction of up to \$300 for cash charitable contributions made by individuals (this allows an individual to claim a deduction for a charitable contribution, even if the individual does not itemize deductions). Additionally, the percent-of-adjusted gross income limitations are increased for all taxpayers, as well as, for specific types of contributions.

The new above the line deduction may reverse some of the decline in charitable contributions that were at least in part attributable to the Tax Cuts and Jobs Act of 2017 (TCJA) changes to the itemized and standard deduction. Charitable giving fell by an inflation adjusted 3.4% from the year prior to the passage of the TCJA to the year after, and 2% fewer individuals made charitable contributions after the passage of the TCJA.

Student Loans Paid by Employers

Background: An employee's gross income excludes up to \$5,250 per year of employer payments made under an educational assistance program for the employee's education.

New law: The Act adds to the types of educational payments that are excluded from employee gross income "eligible student loan repayments" made before January 1, 2021. The payments are subject to the overall \$5,250 per employee limit for all educational payments.

BUSINESS TAX RELIEF

Employee Retention Credit for Employers

New law. This provision provides a refundable payroll tax credit for 50% of wages paid by eligible employers to certain employees during the COVID-19 crisis. The credit is available to be claimed on a quarterly basis.

Eligible employers. The credit is available to employers, including non-profits, whose operations have been fully or partially suspended as a result of a government order limiting commerce, travel, or group meetings. The credit is also provided to employers who have experienced a greater than 50% reduction in quarterly receipts, measured on a year-over-year basis. (The credit is not available to employers receiving Small Business Interruption Loans).

Wages paid to which employees? The amount of wages taken into account depends on whether or not the employer averaged more than 100 full-time employees in 2019. For employers who had an average number of full-time employees in 2019 of 100 or fewer, all employee wages are eligible, regardless of whether the employee is furloughed. For employers who had a larger average number of full-time employees in 2019, only the wages of employees who are furloughed or face reduced hours as a result of their employers' closure or reduced gross receipts are eligible for the credit.

Wages. The term "wages" includes health benefits and is capped at the first \$10,000 in wages paid by the employer to an eligible employee. Wages do not include amounts taken into account for purposes of the payroll credits, for required paid sick leave or required paid family leave in the Families First Coronavirus Act.

Other. IRS is granted authority to advance payments to eligible employers and to waive applicable penalties for employers who do not deposit applicable payroll taxes in anticipation of receiving the credit.

Effective date. The credit applies to wages paid after March 12, 2020 and before Jan. 1, 2021.

Delay of Payment of Employer Payroll Taxes

Background: FICA taxes are imposed on both employers and employees on employees' wages at a rate of 6.2 percent for the Social Security Tax and 1.45 percent for the Medicare Tax. Self-employed individuals pay self-employment tax equal to 12.4 percent Social Security Tax and 2.9 percent Medicare Tax.

New law: The Act allows an employer to defer payments of the employer portion of the Social Security Tax and allows a self-employed individual to defer 50 percent of their Social Security tax. The deferred taxes must be paid over the following two years, with 50 percent to be paid by December 31, 2021 and the other 50 percent by December 31, 2022. Employers that are granted loan forgiveness under the Small Business Act loan program created by the CARES Act are not eligible for this deferral.

Net Operating Loss Changes

Temporary repeal of taxable income limitation for net operating losses (NOLs)

Background: The amount of the NOL deduction is equal to the lesser of (1) the aggregate of the NOL carryovers to such year and NOL carrybacks to such year, or (2) 80% of taxable income computed without regard to the NOL deduction. Thus, NOLs are currently subject to a taxable-income limitation and can't fully offset income.

New law: The Act temporarily removes the taxable income limitation to allow an NOL to fully offset income.

Modification of rules relating to net operating loss (NOL) carrybacks

Background: Except for farming losses and losses of property and casualty insurance companies, an NOL for any tax year is carried forward to each tax year following the tax year of the loss but isn't carried back to any tax year preceding the tax year of the loss.

New law: The Act provides that NOLs arising in 2018, 2019 or 2020 can be carried back to each of the five tax years preceding the tax year of such loss. An amended tax return may be filed to claim the benefit back to 2013.

Modification of limitation on losses for noncorporate taxpayers

Background: Under The Tax Cuts and Jobs Act of 2017 (TCJA), for tax years beginning before January 1, 2026, Section 461(l) disallows the “excess business loss” of an individual taxpayer. An excess business loss for a tax year is the excess of aggregate deductions of the individual taxpayer attributable to its trades or businesses, over the sum of aggregate gross income or gain of the taxpayer plus a threshold amount. Losses disallowed by Section 461(l) generally are carried forward and treated as part of the taxpayer’s net operating loss carryforward in subsequent tax years.

New law: The Act turns off this excess loss disallowance for 2018, 2019, and 2020 and modifies these limitations going forward. Individual taxpayers who had losses disallowed in 2018 and 2019 will be able to obtain refunds. The modifications applicable to tax years beginning on or after January 1, 2021 include prohibiting individual taxpayers from counting wages as business income thus further limiting the losses that will currently be deductible.

Corporate minimum tax credit (MTC) is accelerated

Background: The alternative minimum tax for corporations was eliminated by the TCJA for tax years after 2017, and corporations could continue to claim the refundable portion of any unused minimum tax credits through 2021. Under the TCJA, the amount of the refundable credit is limited to 50 percent of any excess minimum tax in 2018 through 2020, and any remaining credit is fully refundable in 2021.

New Law: The Act accelerates the year for which a fully refundable minimum tax credit can be claimed to 2019, and it also allows corporations to elect to claim the fully refundable minimum tax credits in 2018.

Deductibility of interest expense temporarily increased

Background: The TCJA generally limited the amount of business interest allowed as a deduction to 30 percent of adjusted taxable income for tax years beginning after 2017.

New Law: To help businesses increase liquidity if they have debt or must take on more debt during the coronavirus crisis, the Act temporarily and retroactively increases the limitation on the deductibility of interest expense under Code Sect 163(j)(1) from 30% to 50% for tax years beginning in 2019 and 2020.

A taxpayer may also elect for any tax year beginning in 2020 to substitute the adjusted taxable income beginning in 2019 so that it may increase the base to which the 50 percent limit applies. The option to use 2019 adjusted taxable income in calculating the limitation is meant to counteract the likelihood that incomes will not be higher in 2020 because of the economic environment, whereas 2019 was generally a very high revenue year for businesses.

Special rules for partnerships. Under a special rule for partnerships, the increase in the limitation will not apply to partners in partnerships for 2019 (it applies only in 2020). However, a special beneficial rule applies to 50% of a partner's share of a partnership's 2019 section 163(j)-disallowed interest expense.

Bonus depreciation technical correction for qualified improvement property

Background. The TCJA amended Code Section 168 to allow 100% additional first-year depreciation deductions (100% Bonus Depreciation) for certain qualified property. The TCJA eliminated pre-existing definitions for (1) qualified leasehold improvement property, (2) qualified restaurant property, and (3) qualified retail improvement property. It replaced those definitions with one category called qualified improvement property (QI Property). A general 15-year recovery period was intended to have been provided for QI Property. However, that specific recovery period failed to be reflected in the statutory text of the TCJA. Thus, under the TCJA, QI Property falls into the 39-year recovery period for nonresidential rental property. That makes the QI Property category ineligible for 100% Bonus Depreciation.

New law: The Act provides a technical correction to the TCJA, and specifically designates QI Property as 15-year property for depreciation purposes. This makes QI Property a category eligible for 100% Bonus Depreciation. The change is made as if included in the TCJA and, thus, is effective for property acquired and placed in service after September 27, 2017. Thus, taxpayers should consider the ability to amend tax returns to receive this benefit, or consider the ability to file a Form 3115 "Change in Accounting Method".

We are closely monitoring the progress of the CARES Act, as well as IRS and Treasury guidance. Please contact your Duffy Kruspodin advisor if you have any questions on how these changes may affect your specific tax situation.

Sincerely,

DUFFY KRUSPODIN, LLP