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## CARES ACT HIGHLIGHTS

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On March 27, Congress passed and President Trump signed the Coronavirus Aid, Relief, and Economic Security (“CARES”) Act, a \$2.2 trillion stimulus package to address the economic effects of the ongoing COVID-19 pandemic. This expansive new law enacts a wide range of new programs and changes to existing law that will provide individuals, businesses, and tax-exempt organizations with much-needed economic relief during the current volatile period.

Thompson & Knight has been closely monitoring the legislative activity, and we have summarized the major provisions of key sections in the CARES Act below.

### SMALL BUSINESSES

***The Paycheck Protection Program (“PPP”) –*** The CARES Act amends Section 7(a) of the Small Business Act (“SBA”) to create the PPP to deploy \$349 billion of loans to support small businesses for the period from February 15, 2020 to June 30, 2020 (“the covered period”). The existing SBA structure is largely the same, but there are some changes to extend eligibility requirements and waive certain other requirements. To be eligible for these loans, borrowers must qualify as a small business, which is defined as not more than the greater of 1) 500 employees or 2) if applicable, the existing SBA size standard for the industry in which the borrower operates. Only SBA-approved lenders may issue these loans.

- Proceeds of these loans must be used for payroll costs, leave benefits, interest on mortgage obligations, rent, utilities, and interest payments on debt obligations incurred prior to the covered period.
- The maximum loan amount is determined by a formula, but it is not to exceed \$10 million.
- Lenders must provide complete deferral for a period of between 6 months and 1 year.
- No collateral or personal guarantees will be required. The interest rate will not exceed 4%, and there will be no prepayment penalties.
- Small businesses must certify that the uncertainty of current economic conditions makes necessary the loan request to support their ongoing operations.
- The “affiliations” rule under the SBA will apply to the PPP, with a few exceptions, including: 1) any small business (500 employees or less) in the accommodation and food sectors industry; 2) any small business operating as a franchise that is assigned a franchise identifier code by the SBA; and 3) any business concern that receives financial

assistance from a company licensed under Section 301 of the Small Business Investment Act of 1958.

- Certain amounts of a PPP are forgiven so long as a lender expects a borrower to expend during an 8-week period on the sum of any: 1) payroll costs; 2) payments of interest only on any covered mortgage obligations; 3) payments on any covered rent obligation; and 4) covered utility payments. Any forgiven amounts will be treated as cancelled indebtedness by the lender and forgiven amounts will not be taxable to the borrower. Any borrower seeking loan forgiveness must submit to the lender an application that contains the required information and certifications.

**SBA Section 7(b)(2) Economic Injury Disaster Loans (“EIDL”)** – Borrowers can apply for EIDL’s directly on the SBA website. The CARES Act temporarily waives certain pre-existing Section 7(b)(2) requirements for the covered period. The CARES Act has allocated \$10 billion for emergency advances for those who apply for an EIDL. Each emergency advance can be no more than \$10,000 and must be used for allowable purposes, such as 1) paid sick leave; 2) payroll; 3) meeting increased costs to obtain materials unavailable from the applicant’s original source due to supply chain disruptions; 4) making rent or mortgage payments; and 5) repaying obligations that cannot be met due to revenue losses. Notably, an applicant will not be required to repay any amounts of an advance, even if subsequently denied an EIDL. The emergency grant terminates on December 31, 2020.

[Click here](#) to view the Thompson & Knight Client Alert covering the details of these programs.

## BUSINESS INCOME TAX

**Net Operating Losses (“NOLs”)** – The CARES Act revises existing limits in the Tax Cuts and Jobs Act of 2017 (“TCJA”) for NOLs in tax years beginning before January 1, 2021.

- Allow NOL Carrybacks – NOLs from taxable years beginning after December 31, 2017 and before January 1, 2021; *i.e.*, 2018, 2019, and 2020 taxable years can be carried back five years and carried forward indefinitely.
- Suspend the 80% Cap – For tax years beginning before January 1, 2021, the CARES Act temporarily suspends the 80% limitation on the amount of taxable income that can be offset by NOLs.
- Practical Impact – NOLs from 2018 and 2019 can be quickly carried back to earlier years, generating cash refunds of taxes paid at higher rates in the prior five years than in carryforward years.
- Excess Business Losses – The CARES Act suspends the limitations on excess business losses of non-corporate taxpayers for 2018, 2019, and 2020 taxable years. This change may increase a non-corporate taxpayer’s NOL that can be carried back under the above-discussed NOL provisions.

- **Modify Interest Deduction Limitation** – The CARES Act increases the business interest expense deduction limit from 30% of adjusted taxable income plus business interest income to 50% for taxable years beginning in 2019 and 2020. Another change allows the limitation for taxable years beginning in 2020 to be calculated with respect to adjusted taxable income from 2019.
- **Expanded Bonus Depreciation** – The CARES Act retroactively fixes a drafting error in the TCJA that prohibits certain qualified improvement property from being eligible for 100% bonus depreciation and allows restaurateurs, retailers, and others to claim bonus depreciation.
- **Charitable Contributions** – The percentage limitation on charitable contributions is increased to 25% for corporations for cash and food inventory contributions.

## PAYROLL TAX

***Advance Refunding of Payroll Credit Required for Paid Sick Leave*** – The Families First Coronavirus Response Act (“FFCRA”) allows an employer to claim refundable tax credits for the emergency paid sick leave and emergency paid family leave that an employer is required to provide to employees who are absent from work due to the COVID-19 crisis. The CARES Act expands those provisions by:

- Providing for an advance of the payroll tax credits, subject to the limitations imposed by the FFCRA and calculated through the end of the most recent payroll period in the quarter;
- Requiring the Secretary of the Treasury to prescribe forms and instructions necessary to permit the advancement of the credits; and
- Requiring the Secretary of Treasury to waive penalties associated with the failure to deposit payroll taxes if the failure was due to an employer’s anticipation of the FFCRA credits.

***Payroll Tax Deferral*** – The CARES Act allows employers and self-employed individuals to defer payment of the employer share of the 6.2% social security tax that they are otherwise responsible for paying for the period beginning on the date of enactment of the CARES Act and ending on December 31, 2020. It requires that the deferred taxes be paid over the following two years, with half of the amount required to be paid by December 31, 2021 and the other half to be paid by December 31, 2022.

***Employee Retention Credit*** – The CARES Act provides a refundable payroll tax credit for 50% of qualified wages paid by employers to employees during the COVID-19 crisis.

- The credit is available to employers (including tax exempt organizations) who carried on a trade or business during calendar year 2020 and whose 1) operations were fully or partially suspended due to a COVID-19 related shutdown order, or 2) gross receipts declined by more than 50% when compared to the same quarter in the prior year.
- The credit is based on qualified wages paid to the employee from March 13, 2020 through December 31, 2020. For employers with greater than 100 full-time employees, qualified wages

are wages paid to employees when they are not providing services due to the COVID-19 circumstances described above (suspension of business or drop in gross receipts). For employers with 100 or fewer full-time employees, all employee wages are qualified, regardless of whether the employer is open for business or subject to a shut-down order.

- The total eligible wages per employee are \$10,000, resulting in a maximum credit of \$5,000 per employee.
- Employers receiving emergency small business interruption loans are not eligible for this credit. Further, any wages taken into account for purposes of the retention credit cannot be taken into account for purposes of the credits allowed under the FFCRA, the employer credit for paid family and medical leave under Internal Revenue Code Section 45S, or the work opportunity credit under Internal Revenue Code Section 51.

## INDIVIDUAL INCOME TAX

**Rebates** – Individual taxpayers are allowed a refundable credit against 2020 income tax of \$1,200 (\$2,400 for couples filing jointly), plus \$500 per qualifying child. The credit phases out for taxpayers with adjusted gross income exceeding \$75,000 (\$150,000 for couples filing jointly). The IRS will “refund” the credit amount to taxpayers “as rapidly as possible,” by using the amount that the taxpayers would be allowed based on their 2019 return, if it has been filed, or their 2018 return. If the taxpayers have not filed for 2018 or 2019, the IRS can use information from their Social Security Benefits Statements. The IRS may deposit the rebate directly into a bank account designated by the taxpayers for income tax refunds since January 1, 2018 (followed up by notification by mail to the taxpayers’ last known address indicating the amount of the payment and the method of payment).

**Charitable Contributions** – Individual taxpayers who do not itemize deductions are allowed an “above the line” deduction of up to \$300 of cash contributions.

**Student Loan Repayments** – Gross income of an employee does not include up to \$5,250 of payments made by the employer of principal or interest on qualified education loans after the date of enactment through the end of 2020.

**Retirement Plan Changes** – The CARES Act waives the 10% early withdrawal penalty for distributions up to \$100,000 from qualified retirement accounts for coronavirus-related purposes made on or after January 1, 2020. Income attributable to such distributions would be subject to tax over three years, and the taxpayer may retribute the funds to an eligible retirement plan within three years without regard to that year’s cap on contributions. The CARES Act also provides flexibility for loans from certain retirement plans for coronavirus-related relief.

**Waiver of Required Minimum Distributions for 2020** – The CARES Act waives application of the required minimum distribution rules for certain defined contribution plans and IRAs for calendar year 2020. This waiver provides relief to individuals who otherwise would be required to withdraw funds from such plans and accounts during the economic slowdown due to COVID-19.

**Other Benefit Plan Changes** – The CARES Act includes certain other provisions that impact employee benefit plans, such as funding relief for single-employer defined benefit plans; requirements for group health plans to cover COVID-19 testing, preventive services, and vaccines; and changes permitting over-the-counter drugs to be treated as qualified medical expenses eligible for reimbursement from an HSA, FSA, or HRA.

## EMPLOYMENT AND LABOR

**Employee Paid Leave** – The CARES Act made a few minor clarifications to the Emergency Family and Medical Leave Expansion Act (“EFMLEA”) and the Emergency Paid Sick Leave Act, including that the monetary leave benefit caps are per-employee and not an overall per-day cap. It also clarified that an employee is still eligible for EFMLEA if he or she was laid off after March 1, had worked for the employer not less than 30 days of the last 60 days prior to the layoff, and was later rehired by the employer.

**Pandemic Unemployment Assistance Program** – The CARES Act creates a temporary Pandemic Unemployment Assistance program through December 31, 2020 to expand eligibility for unemployment benefits to individuals not otherwise eligible, such as self-employed workers, independent contractors, those who have exhausted state unemployment benefits, and those with limited work history. Individuals are not eligible for benefits if they have the ability to telework with pay or are receiving paid sick leave or other paid leave benefits. Specifically, the CARES Act provides that a “covered individual” includes anyone who is able and available to work but is unemployed or partially unemployed due to several COVID-19 related-reasons, including any of the following:

- The individual is the primary caregiver for a child or other person in the household who is unable to attend school or another facility as a direct result of COVID-19;
- The individual is unable to reach the place of employment because of a quarantine imposed as a direct result of COVID-19;
- The individual is unable to work because a health care provider has advised the individual to self-quarantine due to COVID-19 concerns;
- The individual has to quit his or her job as a direct result of COVID-19; or
- The individual’s place of employment is closed as a direct result of COVID-19.

The Pandemic Unemployment Assistance program also extends benefits from 26 weeks (in most U.S. states) to 39 weeks and waives the usual one-week waiting period. The amount of benefits includes the amount that would be calculated under state law plus \$600 per week for up to four months. Finally, the CARES Act offers U.S. states the opportunity to receive funding for state-enacted “short-time compensation” programs to subsidize employees who have their hours reduced in lieu of a layoff.

## BANKRUPTCY

**Chapter 11** – The CARES Act makes a significant change to Chapter 11 of the Bankruptcy Code: it increases the debt limit for small business bankruptcy from \$2,725,625 to \$7,500,000. The Small Business Reorganization Act recently created subchapter V, a faster, more flexible, and more cost efficient Chapter 11 reorganization process for small businesses with debts less than \$2,725,625. The CARES Act increases this debt limit to \$7,500,000, allowing many more small businesses to seek the protections of a subchapter V reorganization. This increased debt limit applies only to subchapter V cases filed after the CARES Act is enacted, so current Chapter 11 cases will not be able to convert to a subchapter V. It also contains a sunset clause so that, absent an extension by Congress, the debt will reset to \$2,725,625 after one year.

**Chapter 7 and Chapter 13** – The CARES Act also excludes payments made to people pursuant to the Act from the Chapter 7 means-test calculation and from the disposable income calculation of Chapter 13. It also permits a Chapter 13 debtor who has already confirmed a plan to request modifications for hardships related to the COVID-19 emergency. Both of these changes also contain a one-year sunset clause.

## QUESTIONS?

If you have any questions about these and other complex legal and practical issues raised by the CARES Act, we have the experience and expertise to help. Please contact the Thompson & Knight attorney with whom you regularly work or one of the attorneys listed below.

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*This Client Alert is sent for the information of our clients and friends. It is not intended as legal advice or an opinion on specific circumstances. Furthermore, due to the rapidly evolving nature of the COVID-19 pandemic, you should consult with counsel for the latest developments and updated guidance.*

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