Economic Stimulus Legislation:

Federal Response to the Coronavirus Pandemic

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Contents

Course Introduction

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), legislation designed to provide economic relief for those impacted by COVID19, became law. This course provides a general review of the principal provisions of the CARES Act and of other federal tax-related stimulus legislation passed during 2020, including the Tax Relief Act of 2020 signed into law on December 27, 2020.

Course Learning Objectives

After completing this course, students should be able to:

- Apply the recovery rebate rules;
- Describe the provisions of the Paycheck Protection Program;
- Recognize the rules related to unemployment benefits under the Pandemic Unemployment Assistance program;
- Apply the provisions regarding expanded tax-favored use of retirement funds;
- Identify the changes to net operating loss (NOL) carryback rules;
- Apply the changes in charitable contribution rules;
- Describe the changes in health savings account (HSA) rules related to first-dollar payment for telehealth and COVID-19 testing and treatment;
- Apply the rule changes to qualified improvement property depreciation; and
- Recognize the rules related to miscellaneous provisions, including –
    - Changes to the rules related to the business deduction of food and beverages,
    - Changes to the CTC and EITC rules,
    - Changes to the foreign income exclusion,
    - Section 1031 exchange timing,
    - Correction of the deductible period applicable to qualified improvement property,
    - Modification of limitation on losses for non-corporate taxpayers,
    - Changes to the limitation on business interest expense deductions,
    - Exclusion of certain employer payments of student loans, and
    - Expansion of economic injury disaster loans (EIDLs).

Chapter 1 – Rebates, Payroll, and Unemployment Assistance

Introduction

The CARES Act was passed to meet multiple objectives related to the United States' health and economic needs following the onset of the COVID-19 pandemic roiling the world. Of particular importance to tax planners and preparers among its provisions are those designed to provide emergency appropriations for keeping employees paid, businesses functioning and workers employed. This chapter will examine three important provisions of the CARES Act: recovery rebates, the Paycheck Protection Program (PPP) and federal Pandemic Unemployment Assistance.

It will consider the CARES Act recovery rebates specifically with respect to filing status, the associated amount of the rebate, and the effect of a taxpayer's adjusted gross income on the tax treatment of the rebate and the taxpayer's eligibility for it. The PPP's provisions for SBA forgivable loans and taxability of loan proceeds will be discussed. The federal Pandemic Unemployment Assistance (PUA) provisions of the CARES Act will also be considered, including the extension of unemployment benefits, the enhancement and augmentation of normal unemployment benefits provided, and the ways PUA benefits differ from other types of unemployment benefits.

In addition, this chapter will briefly consider the principal changes made to the federal response to the economic fallout resulting from the pandemic by the COVID-Related Tax Relief of 2020 (TRA 2020), included as part of the Consolidated Appropriations Act of 2021.

Learning Objectives

When you have completed this chapter, you should be able to:

- Recognize the nature and amount of recovery rebate authorized under the CARES Act;
- Apply the recovery rebate eligibility limitations;
- Calculate the amount of rebate based on a taxpayer's adjusted gross income and filing status;
- Describe the rules applicable to the Paycheck Protection Program, including those related to –
    - Eligibility,
    - Maximum loan amounts, and
    - Forgiveness criteria;
- Identify the rules governing the Pandemic Unemployment Assistance program, including –
    - The additional unemployment benefits available,
    - The eligibility requirements,
    - The tax treatment of benefits, and
    - The credit for employee retention.

Recovery Rebates (Economic Impact Payments)

Direct payments to taxpayers are authorized under Section 2201 of the CARES Act. These rebates are referred to in the CARES Act as "2020 recovery rebates" and in IRS materials and elsewhere as "stimulus payments" or "economic impact payments." Subject to adjusted gross income (AGI) limitations, these refundable tax credit payments are authorized not exceeding:

- $1,200 for single filers and heads of household;

- $2,400 for joint filers; and
- $500 for each qualifying dependent child age 16 or under by the end of the tax year.

The rebate-related provisions of the CARES Act were modified by TRA 2020 to provide an additional refundable tax credit. Those additional tax credits provide a second round of direct payments and are authorized not exceeding:

- $600 per individual taxpayer;
- $1,200 for married taxpayers filing jointly; and
- $600 per qualifying child under age 17.

No amount is determined under this subsection with respect to any qualifying child of the taxpayer if:

- The taxpayer was deceased before January 1, 2020, or
- In the case of a joint return, both taxpayers were deceased before January 1, 2020.

As a tax credit, the recovery rebate is nontaxable and is not counted as income with respect to determining a taxpayer's eligibility for income-based programs such as Medicaid or health insurance Marketplace subsidies.

Income eligibility requirements for both Medicaid and premium tax credits under the Affordable Care Act are based on taxpayers' Modified Adjusted Gross Income (MAGI), and both programs are designed to facilitate access to healthcare. Although Medicaid eligibility may vary from one state to another, depending on whether it chose to expand Medicaid under the Affordable Care Act, a taxpayer with a MAGI of less than 133% of the federal poverty level (FPL), is normally eligible for Medicaid.

In contrast to the less-than-133% of FPL eligibility for Medicaid, taxpayers are eligible to receive refundable tax credits for purchase of one or more qualified health plans provided they their household income is not less than 133% and not more than 400% of the federal poverty level and they meet certain other criteria. However, eligibility for neither program is affected by a taxpayer's receipt of a stimulus payment.

As noted, the recovery rebate is a "refundable credit." A refundable credit is one that might reduce a taxpayer's liability to less than $0, resulting in a refund. That is, an eligible taxpayer who does not even owe tax can receive a payment from the Treasury in the case of a refundable credit.

Example

> If Tom Taxpayer owes $400 in taxes and qualifies for a $1,200 refundable credit, he would receive a refund of $800 in taxes. That is, instead of paying $400 in taxes, he would take the tax liability of $400 and subtract the refundable credit of $1,200, giving him a balance of ($800). The negative amount represents the amount of the "refund" he would actually receive from the federal government.

During 2020, each eligible taxpayer is treated as though the credit rules had been in place in 2019. The recovery rebate is considered an advance rebate. When the 2020 tax year rebate is calculated based on actual 2020 financial information, a taxpayer who has been underpaid by the advance can request a payment for the balance. If the taxpayer ends up being overpaid based on this calculation, the excess does not have to be returned.

Rebate Eligibility

A taxpayer eligible for the recovery rebate is an individual OTHER THAN:

- A non-resident alien,
- A person who can be claimed as a dependent on another person's tax return, or
- An estate or trust.

AGI Limitations

No reduction of the recovery rebate applies if the taxpayer's AGI does not exceed specified threshold amounts based on the taxpayer's filing status. That is, the rebate amount is phased out for higher income taxpayers. The threshold amount, at which point the rebate begins to be reduced, is between $75,000 and $150,000 depending on the taxpayer's filing status. The rebate phases out completely at $99,000 to $198,000 depending also on the taxpayer's filing status.

For individuals and families with qualifying children, each of these threshold amounts increases by $10,000 for each qualifying child. There is no limit on the number of qualifying children.

The recovery rebate is reduced by $5 for each $100 of AGI over the indicated threshold, and the rebate is phased out entirely for taxpayers whose AGI exceeds the amounts shown in the chart below:

Filing Status	Threshold Amount	CARES Act Rebate Phased Out	TRA 2020 Rebate Phased Out
Joint filers	$150,000	$198,000	$174,000
Head of household filers	$112,500	$146,500	$124,500
All other filing statuses	$75,000	$99,000	$87,000

Calculating the rebate is fairly straightforward, and a demonstration of how the rebate phases out can be helpful. Examples of the rebate calculation are as follows.

Example: Joint Filer

For a joint filer, the maximum rebate is $2,400 and the threshold is $150,000. The table below demonstrates the rebate calculation under two scenarios: the first in which the taxpayer's AGI is between the threshold and rebate phase-out amounts, the second in which the taxpayer's AGI exceeds the rebate phase-out amount.

(1)	(2)	(3)	(4)	(5)	(6)	(7)
Maximum CARES Act Rebate (Joint Filer)	AGI	Threshold Amount	Excess (2 – 3)	Divide (4) by $100	Multiply (5) by $5	Subtract (6) from (1)
$2,400	$170,000	$150,000	$20,000	200	$1,000	$1,400
$2,400	$202,000	$146,500	$55,500	555	$2,775	$0

The joint filer with AGI of $170,000 is eligible for a rebate of $1,400. The $170,000 in AGI is above the threshold amount but below the phase-out of $198,000. A partial rebate is therefore available.

Example: Head of Household (or Single) Filer

The head-of-household (or single) filer with AGI of $130,000 is eligible for a rebate of $325. The $130,000 in AGI is above the threshold amount but below the phase-out of $146,500. This taxpayer is eligible for a partial rebate.

(1)	(2)	(3)	(4)	(5)	(6)	(7)
Maximum CARES Act Rebate (HH Filer)	**AGI**	**Threshold Amount**	**Excess (2 – 3)**	**Divide (4) by $100**	**Multiply (5) by $5**	**Subtract (6) from (1)**
$1,200	$130,000	$112,500	$17,500	175	$875	$325
$1,200	$150,000	$112,500	$37,500	375	$2,775	$0

Additional Per-Child Credit

The CARES Act provides for an additional payment of $500 per eligible dependent child, and TRA 2020 provides for an additional payment of $600 per eligible dependent child. These refundable tax credits are available without the AGI limitations that affect the taxpayer. That is, there is no threshold or phase-out level. There is no limit on the number of eligible dependent children.

Taxpayers who filed a 2019 federal income tax return will generally have their rebates automatically issued and either deposited directly into the account on file with the IRS from that 2019 return or sent by mail if there is no such account. Even if not required to file a tax return, Social Security beneficiaries and railroad retirees will also receive recovery rebates automatically and directly. Supplemental Security Income (SSI) recipients and eligible veterans and beneficiaries also automatically receive direct payments. For taxpayers not within any of the above categories, there is an IRS portal through which benefits can be requested.

If an eligible taxpayer had not filed a 2019 return at the time the recovery rebates were being distributed, the IRS used information from the 2018 return. The IRS used information from Social Security benefits statements if necessary. Details on program administration and steps for non-filers to take to receive their rebates can be found on the IRS website.[1]

If an eligible taxpayer fails to receive an automatic CARES Act stimulus payment, he or she may simply claim the refundable credit when filing his or her 2020 tax return. Similarly, an eligible taxpayer failing to receive an automatic TRA 2020 stimulus payment may claim the credit when filing his or her 2021 tax return.

Additional Recovery Rebate (Economic Impact Payment) Issues

Recovery rebate payments will not be reduced to pay past-due taxes under a payment agreement with the IRS or to pay other state or federal debts. In general, creditors cannot get access to the money for reduction or offset and direct payment to themselves. The CARES Act only allows offsets to cover past-due child support payments.

However, once the proceeds are deposited into a bank account, they become accessible by creditors. The rules governing creditor access to such funds (after they are deposited) are generally part of state law.

[1] At https://www.irs.gov/coronavirus/economic-impact-payment-information-center

Paycheck Protection Program

Section 1102 of the CARES Act addresses the Paycheck Protection Program, a program managed by the U.S. Small Business Administration (SBA) designed to provide a direct incentive for small businesses to keep workers on the payroll. Under the program, a federally-guaranteed loan not exceeding specified limits may be made to a small business, and the SBA will forgive the loan if certain requirements are met. Let's examine the program more closely and consider:

- Eligibility,
- Maximum available loan,
- Loan forgiveness requirements, and
- Tax treatment of the forgiven loan.

Paycheck Protection Program Eligibility

Participation in the paycheck protection program during the covered period is available to any business concern, nonprofit organization, veterans organization or Tribal business concern[2] whose principal place of residence is in the United States if it employs no more than the greater of:

- 500 employees, or
- The size standard in number of employees established by the SBA for the industry in which the concern operates.

A size standard, which is usually stated in number of employees or average annual receipts, represents the largest size that a business (including its subsidiaries and affiliates) may be to remain classified as a small business for SBA and federal contracting programs. The definition of "small" varies by industry. Eligibility includes sole proprietors, independent contractors and eligible self-employed individuals. The "covered period" means the period beginning on February 15, 2020 and ending on June 30, 2020.

Maximum Loan Amount

The maximum amount with respect to a covered loan under the program, as published April 15, 2020 in the Federal Register, is the lesser of A or B in which:

A. Is equal to –

$$\frac{\text{(Annual payroll costs – compensation over \$100,000)}}{12} \times 2.5 + \text{(Outstanding amount of EIDL made between 1/31/20 and 4/3/20 minus any EIDL advance)}$$

B. Is equal to $10 million

Note that this formula refers to an "EIDL" or an "economic injury disaster loan." As you will see later in this course, the availability of such loans is not the result of creation of a new program. Instead, it is an existing Small Business Administration (SBA) program and is the principal means of federal assistance for repairing and rebuilding non-farm, private sector disaster losses. It is assumed that an EIDL will be refinanced by the PPP loan.

[2] As described in Section 31(b)(2)(C) .

As you can see from the formula above, the loan amount is based on an approximation of 2.5 months of payroll costs. The annual payroll cost is divided by 12 to determine the average monthly cost, and this average monthly cost is then multiplied by 2.5.

Example

Assume, for example, that total annual payroll costs are $554,000 (i.e., the total of compensation paid to all employees, independent contractors and sole proprietors) as shown in the inset below.

Name	Position	Annual Compensation	Compensation Exceeding $100,000
Helen Carlson	CEO	$250,000	$150,000
Robert Wilson	General Manager	$113,000	$13,000
Toby Wenzel	Sales	$106,000	$6,000
Shirley Edmunds	Sales	$85,000	$0
	Total	$554,000	$169,000

The compensation exceeding $100,000 is $169,000. To calculate the monthly payroll amount for purposes of the PPP, subtract the compensation exceeding $100,000 from the total payroll to obtain $385,000. Then divide the result by 12 to get $32,083. This $32,083 is the average monthly payroll cost.

In order to replace 2.5 months of payroll costs, the $32,083 monthly cost is multiplied by 2.5, giving us $80,207. If there has also been an Economic Injury Disaster Loan (EIDL) of $10,000, the total under scenario A is $90,207.

$$\frac{(\$554{,}000 - \$169{,}000)}{12} \times 2.5 + \$10{,}000 = \$90{,}207$$

Because A, i.e. $90,207, is less than B, i.e. $10 million, the maximum loan amount would be $90,207.

Small Business Association Covered Loan Forgiveness

The loan forgiveness amount may be up to the full principal amount of the loan and any accrued interest, provided the borrower uses all the loan proceeds for forgivable purposes. In order for the entire loan proceeds and accrued interest to be forgiven, the following requirements must be met:

- All employees must be kept on the payroll for eight weeks, and
- The money must be used for –
    - payroll (at least 60% of loan[3]),
    - rent,
    - mortgage interest, or
    - utilities.

For example, if the employer borrows $100,000 and uses at least $60,000 for the purposes listed above, the entire $100,000 plus any accrued interest will be forgiven. In a June 8, 2020 joint statement issued by the Treasury and the SBA, rules related to **partial** loan forgiveness were set forth. If the borrower in

[3] The original threshold was 75%. It was lowered to 60% on June 5, 2020.

the $100,000 example uses only $50,000 for payroll costs, only the $50,000 will be forgiven. Prior to this rule clarification, the understanding was that there would be **no** loan forgiveness if the indicated threshold was not met.[4]

On October 8, 2020, the SBA and Treasury issued new interim final rules concerning PPP forgiveness for small loans. Under the interim final rules, a borrower* of a PPP loan of $50,000 or less may use SBA Form 3508S to apply for loan forgiveness. A borrower that uses Form 3508S (or the lender's equivalent form) is exempt from any reduction in the forgiveness amount based on:

- Reductions in full-time equivalent (FTE) employees; or
- Reductions in employee salary or wages.

Important Note on Applicability of Exemption of Reduction

*Note: The exemption from reduction in forgiveness applicable to a PPP loan of $50,000 or less does not apply to a borrower that, together with its affiliates, received loans totaling $2 million or greater.

Tax Treatment of Loan Forgiveness

If a taxpayer borrows money that he or she is legally obligated to repay, that taxpayer has incurred debt. When debt is forgiven or discharged for less than the full amount owed, the canceled portion is generally considered income for federal tax purposes. There are some exceptions to the taxation of cancelation of debt income (CODI). CODI would be reported in income for the year in which the associated debt was canceled.

Exceptions to taxability of canceled debt are as follows:

- Debt canceled in a Title 11 bankruptcy case;
- Debt canceled to the extent insolvent;
- Cancellation of qualified farm indebtedness;
- Cancellation of qualified real property business indebtedness; and
- Cancellation of qualified principal residence indebtedness that is discharged subject to an arrangement that is entered into and evidenced in writing before January 1, 2021.

When debt is canceled based on one of these exceptions, certain tax attributes (credits, losses, carryovers, and others) are lost. These attributes must be reduced by the amount of debt canceled.

The canceled indebtedness resulting from a forgiven covered loan under the Paycheck Protection Program is excluded from the borrower's gross income. Absent this provision for exclusion, PPP loan forgiveness would be includible in income.

In Notice 2020-32, intending to provide tax-preparation guidance related to the Paycheck Protection Program (PPP), the IRS stated "… section 265(a)(1) of the Code disallows any otherwise allowable deduction under any provision of the Code, including sections 162 and 163, for the amount of any payment of an eligible section 1106 expense to the extent of the resulting covered loan forgiveness (up to the aggregate amount forgiven) because such payment is allocable to tax-exempt income. Consistent with the purpose of section 265, this treatment prevents a double tax benefit." In short, the expenses

[4] See https://home.treasury.gov/news/press-releases/sm1026

used to obtain forgiveness under the PPP—expenses that would otherwise be deductible—are not tax-deductible.

That IRS position, i.e., the non-deductibility of expenses to the extent of forgiven debt, has been reversed by TRA 2020. Under the provisions contained in § 278 of TRA 2020 providing for clarification of tax treatment, the law states:

For purposes of the Internal Revenue Code of 1986—

- *(1) no amount shall be included in the gross income of a borrower by reason of forgiveness of indebtedness described in section 1109(d)(2)(D) of the CARES Act,*
- *(2) no deduction shall be denied, no tax attribute shall be reduced, and no basis increase shall be denied, by reason of the exclusion from gross income provided by paragraph (1), and (3) in the case of a borrower that is a partnership or S corporation—*
  - *(A) any amount excluded from income by reason of paragraph (1) shall be treated as tax exempt income for purposes of sections 705 and 1366 of the Internal Revenue Code of 1986, and*
  - (B) *except as provided by the Secretary of the Treasury (or the Secretary's delegate), any increase in the adjusted basis of a partner's interest in a partnership under section 705 of the Internal Revenue Code of 1986 with respect to any amount described in subparagraph (A) shall equal the partner's distributive share of deductions resulting from costs giving rise to forgiveness described in section 1109(d)(2)(D) of the CARES Act.*

Accordingly, normally-deductible business expenses used as the basis for PPP loan forgiveness continue to be tax-deductible.

Payroll Tax Deferral – Employer Share

The employer's share of Social Security tax may be deferred, with half of the required amount due by December 31, 2021, and the other half by December 31, 2022. If the deferred amount is not repaid, the employer is solely liable for taxes and penalties. Prior to a rule change enacted on June 5, 2020, an employer was not eligible for this deferral if it has had indebtedness forgiven under a PPP loan. The June 5 amendment does away with this rule so that even if an employer's PPP loan is forgiven (in part or in whole), the employer may defer payment and deposit of its share of payroll tax.[5]

In order to defer the employer's share of payroll tax, the employer may reduce its tax payments for a calendar quarter. There is no special election that must be made. The employer does report the deferred taxes on its Form 941 employment tax return.

[5] https://www.irs.gov/newsroom/deferral-of-employment-tax-deposits-and-payments-through-december-31-2020

Payroll Tax Deferral – Employee Share

On August 8, 2020 the White House issued a presidential memorandum[6] authorizing the Secretary of the Treasury to permit employers to defer the employees' share of Social Security tax on wages or compensation paid during the period from September 1, 2020 through December 31, 2020 on bi-weekly wages or compensation less than $4,000.

Pursuant to that presidential memorandum, on August 28, 2020 the IRS issued Notice 2020-65[7] providing guidance with respect to employee Social Security tax withholding. The guidance provided by the IRS Notice permits, but does not require, employers to defer withholding of the employees' portion of Social Security tax on applicable wages or compensation paid during the September 1, 2020 through December 31, 2020 period. Employers must withhold and pay the total deferred taxes ratably from wages and compensation paid between January 1, 2021 and April 30, 2021. TRA 2020 extends the repayment period through December 31, 2021.

Pandemic Unemployment Assistance

The unemployment provisions of the CARES Act are contained in Title II, Subtitle A in sections 2102 through 2116. The principal provisions of the pandemic unemployment assistance affecting individuals address:

- The amount and duration of benefits;
- Benefit eligibility under the program; and
- The tax treatment of benefits received.

Unemployment Benefits

The Pandemic Unemployment Assistance (PUA) provisions of the CARES Act provide for federal unemployment benefits of $600 per week ***in addition*** to any state-provided unemployment assistance. The federal program also extends the maximum period of unemployment benefits by 13 weeks from the customary 26-week state-provided assistance to a maximum period of 39 weeks. States are not permitted to reduce their unemployment benefits—either in amount or duration—during the extended period provided under the Act.

Department of Labor guidance indicates that employees are eligible for up to an additional 10 weeks of paid expanded family and medical leave at 2/3 the employee's regular pay rate if that employee must care for a child whose school or child care provider is closed or unavailable for COVID-19 related reasons.[8] Eligibility for benefits is far broader than under typical state unemployment laws. Self-employed persons and those with limited employment history are eligible for certain benefits provided under the CARES Act.

Benefits may be available for individuals who may be otherwise able to and available for work but are unemployed, partially unemployed, or unable or unavailable to work because of the need to care for

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[6] August 8, 2020 presidential memorandum may be accessed at https://www.whitehouse.gov/presidential-actions/memorandum-deferring-payroll-tax-obligations-light-ongoing-covid-19-disaster/

[7] IRS Notice 2020-65 may be accessed at https://www.irs.gov/pub/irs-drop/n-20-65.pdf

[8] DOL guidance may be accessed at https://www.dol.gov/agencies/whd/pandemic/ffcra-employee-paid-leave and https://www.dol.gov/sites/dolgov/files/WHD/Pandemic/Quick%20Tip%20Poster%20FFCRA.pdf

family or household members for COVID-19 related reasons. Additionally, primary caregivers for children or other household members may be eligible for PUA due to school or other facility closures.

Both regular unemployment insurance benefits and the unemployment insurance benefits expanded under the CARES Act are includible in gross income and subject to income taxes.

Benefit Eligibility

Eligibility for unemployment benefits under the federal Pandemic Unemployment Assistance program is far broader than under typical state unemployment laws. Although individuals with the ability to telework with pay or who are receiving paid leave benefits are not eligible for benefits, this federal program covers individuals who meet both of the following requirements:

1. They are not eligible for regular compensation or extended benefits under state or federal law or pandemic emergency unemployment compensation (including someone who has exhausted all such benefits); and
2. They are otherwise able to work and available for work but are unemployed, partially unemployed or unable or unavailable to work because –
    a) The individual has been diagnosed with COVID-19 or is experiencing symptoms of the disease and seeking a diagnosis,
    b) A member of the individual's household has been diagnosed with COVID-19,
    c) The individual is providing care to a family member or household member who has been diagnosed with COVID-19,
    d) A child or other household member for whom the individual has primary caregiving responsibility is unable to attend school or another facility closed as a direct result of COVID-19 and such care (provided by the school or other facility) is required for the individual to work,
    e) The individual is unable to reach the place of employment because of a quarantine imposed as a direct result of the COVID–19 public health emergency;
    f) The individual is unable to reach the place of employment because the individual has been advised by a health care provider to self-quarantine due to concerns related to COVID–19,
    g) The individual was scheduled to commence employment and does not have a job or is unable to reach the job as a direct result of the COVID–19 public health emergency,
    h) The individual has become the breadwinner or major support for a household because the head of the household has died as a direct result of COVID–19,
    i) The individual has to quit his or her job as a direct result of COVID–19,
    j) The individual's place of employment is closed as a direct result of the COVID– 19 public health emergency,
    k) The individual meets any additional criteria established by the Secretary for unemployment assistance under this section; or ,
    l) Is self-employed, is seeking part-time employment, does not have sufficient work history, or otherwise would not qualify for regular unemployment or extended benefits under State or Federal law or pandemic emergency unemployment compensation under section 2107 and meets the requirements of subclause (I)

Tax Treatment of Benefits

Both regular unemployment insurance benefits and the unemployment insurance benefits expanded under the CARES Act are includible in gross income and subject to income taxes.

Generally, tax treatment of unemployment benefits depends on the type of program paying the benefits. Unemployment compensation includes amounts received under an unemployment compensation law of the United States or of a state. IRS *Publication 525, Taxable and Nontaxable Income*, provides that "all unemployment compensation" must be included in income. That is, the federal government taxes unemployment income received from federal programs, state programs, and other governmental programs.[9] Note that it is unemployment ***compensation*** that is included.

The recipient generally may elect to have federal income taxes withheld at 10% at the time of receipt.[10] If this election is not made, the recipient should be mindful of quarterly estimated tax payment requirements. Estimated tax payments are paid quarterly by a taxpayer to cover income taxes on amounts not subject to tax withholding.

If a taxpayer repays unemployment compensation in the same year in which it was received, he or she should subtract that repaid amount from the total received. In contrast, if a taxpayer repays unemployment compensation in a subsequent year, that amount can be reported on Schedule A of Form 1040, line 16, if the repaid amount exceeds $3,000. For tax years beginning after 2017, taxpayers cannot claim any miscellaneous itemized deductions; accordingly, if the amount repaid was $3,000 or less, the taxpayer cannot deduct it from income in the year repaid.

Employee Retention Credit

The Employee Retention Credit under the CARES Act encourages businesses to keep employees on their payroll. The refundable tax credit is 50 percent of up to $10,000 in wages and health plan expenses paid by an eligible employer whose business has been financially impacted by COVID-19. The credit covers payments made after March 12, 2020, and before January 1, 2021. The refundable credit is capped at $5,000 per employee and applies against certain employment taxes on wages paid to all employees.

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[9] IRC Section 85.

[10] To make this election, *Publication 525* indicates that the taxpayer must file Form W-V4 and provide it to the paying office.

Chapter 1 Review Questions

1. Which of the following is true with respect to a refundable credit?
   A. A refundable credit reduces a taxpayer’s liability to $0
   B. A refundable credit reduces a taxpayer’s liability, possibly to less than $0
   C. A refundable credit has the same effect on income tax liability as a miscellaneous itemized deduction
   D. A refundable credit has to be paid back by the taxpayer to the Treasury in the first year the taxpayer makes too much money to qualify for the credit
2. If a business receives a loan of $200,000 under the Paycheck Protection Act, how much of this amount must be used for payroll and related purposes in order for the borrower to have the full amount of the loan to be forgiven?
   A. $60,000
   B. $120,000
   C. $75,000
   D. $150,000

Answers to Chapter 1 Review Questions

Answer to question #1

A. This answer is incorrect. A refundable credit may reduce a taxpayer's liability to less than $0, resulting in a payment from the federal government to the taxpayer in the form of a "refund."

B. That is correct! A refundable credit may in some instances reduce a taxpayer's liability to less than $0. If such liability is reduced to less than $0 so that the person receives a payment even if that person owed no tax at all.

C. This answer is incorrect. Credits and itemized deductions do not serve the same purpose and are not treated the same.

D. This answer is incorrect. A taxpayer cannot retroactively lose eligibility for a tax credit due to a change in circumstances (such as earning more money).

Answer to question #2

A. This answer is incorrect. A minimum of 60% of the loan amount must be used for payroll and related purposes.

B. That is correct! A minimum of 60% of such a loan must be used in order for the entire amount to be forgiven. $200,000 × 60% is $120,000. (Note: Forgiveness of a PPP loan of less than $50,000 is generally unaffected by reductions in full-time equivalent (FTE) employees or reductions in employee salary or wages.)

C. This answer is incorrect. The minimum of 60% of the loan amount must be used for such purposes in order to have the entire amount forgivable.

D. This answer is incorrect. Although $150,000 is 75% of the $200,000 loan amount, the minimum required amount is 60% toward payroll and related costs in order to have the full amount forgivable.

Chapter 2 – Charitable Contributions, Retirement Funds, and NOLs

Introduction

The CARES Act makes changes to the ability of non-itemizing taxpayers to deduct charitable contributions, the tax treatment of various transactions involving retirement plans—changes involving qualified plan loans as well as IRA and qualified plan distributions—and net operating loss carryovers. This chapter will consider those CARES Act-related changes.

Learning Objectives

After completing this chapter, students should be able to:

- Identify the changes in deductible charitable contribution rules;
- Describe changes made to qualified plan loans;
- Recognize the early distribution tax penalty changes for coronavirus-related distributions;
- Apply the rules governing the tax treatment of coronavirus-related withdrawals;
- Describe the tax treatment governing repayment of IRA and qualified plan withdrawals;
- Identify the changes to required minimum distributions (RMDs) applicable to 2020; and
- Recognize the net operating loss carryover rules.

Charitable Contributions

The CARES Act temporarily suspends some of the limitations imposed by the Internal Revenue Code with respect to certain individual taxpayer cash contributions. In general, qualified contributions are disregarded in applying IRC section 170 as it pertains to percentage limits[11] and carryovers of excess contributions.[12]

A qualified contribution is allowed as a deduction to the extent the total amount of such contributions doesn't exceed the excess of the taxpayer's contribution base—a taxpayer's adjusted gross income (computed without regard to any net operating loss carryback)—over the amount of all other charitable contributions allowed under the Code. In other words, an individual taxpayer may make a tax-deductible cash contribution of up to 100% of his or her AGI, i.e., an increase from the current 60% of AGI.

Prior to passage of the CARES Act, the 60% limitation had been in place only since 2018 after passage of the 2017 Tax Cuts and Jobs Act (TCJA). The 60% was an increase from the 50% limit applicable before the TCJA changes.

If the aggregate amount of qualified contributions made in the contribution year exceeds the limitation, i.e. it exceeds 100% of the individual taxpayer's AGI, the excess may be carried over to the succeeding five years.

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[11] Section 170(b)
[12] Section 170(d)

Non-cash charitable contributions made by an individual taxpayer may be deducted by up to 50 percent of AGI (without regard to NOL carrybacks). The CARES Act did not provide for a 100%-of-AGI limit for personal property.[13]

The charitable contribution provisions of the CARES Act also increase the percentage of corporations' taxable income that may be deducted as a charitable contribution. In the case of a corporation, the deduction of qualified contributions is increased from 10% to the extent that the total of such contributions does not exceed the excess of 25% of the taxpayer's taxable income over the amount of all other charitable contributions allowed.

As in the case of individual taxpayers, qualified contributions made by the corporation in the contribution year exceeding the limitation, i.e. it exceeds 25% of the corporate taxpayer's taxable income, may be carried over to the succeeding five years.

Qualified Contributions

The term ''qualified contribution'' means a charitable contribution meeting the following two requirements:

1. The contribution is paid in cash during calendar year 2020 to an organization described in section 170 of the Internal Revenue Code,[14] and
2. The taxpayer has elected the application of this section with respect to the 2020 contribution.

However, the term doesn't include a contribution by a donor if the contribution is—

- To a supporting organization described in section 509(a)(3) of the Internal Revenue Code, or
- For the establishment of a new, or maintenance of an existing, donor advised fund.[15]

TRA 2020 extends the period during which an otherwise eligible contribution will be considered a qualified contribution to include 2021.

Let's look a little more closely at Section 509(a)(3) of the IRC.

IRS materials indicate that a "supporting organization" is a charity that supports other exempt organizations (usually public charities).[16] An entity that meets 501(c)(3) ***and*** 509(a)(3) requirements is treated for tax purposes as a public charity rather than a private foundation. Private foundations are subject to more restrictive regulations and receive less tax-favored treatment than public charities do.

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[13] https://www.irs.gov/charities-non-profits/charitable-organizations/charitable-contribution-deductions

[14] Section 170(b)(1)(A)

[15] In general, the term "donor advised fund" means a fund or account—

- Which is separately identified by reference to contributions of a donor or donors,
- Which is owned and controlled by a sponsoring organization, and
- With respect to which a donor (or any person appointed or designated by such donor) has, or reasonably expects to have, advisory privileges with respect to the distribution or investment of amounts held in such fund or account by reason of the donor's status as a donor.

[16] At https://www.irs.gov/charities-non-profits/section-509a3-supporting-organizations

Partial Above-the-Line Deduction for Charitable Contributions

A new charitable deduction is available to taxpayers who do not itemize deductions. Sometimes referred to as a "universal deduction," this CARES Act provision permits a non-itemizing taxpayer to take an above-the-line deduction of up to $300 for charitable contributions made in taxable years beginning in 2020. TRA 2020 extends the above-the-line charitable deduction for taxpayers who do not itemize to include 2021 and increases the maximum deductible limit to $600 for married taxpayers filing jointly.

A deduction that is "above the line" reduces AGI. It is a deduction that is made in calculating AGI in the first place. Such deductions may be taken regardless of whether a taxpayer itemizes deductions. Other above the line deductions include certain retirement plan contributions, health savings account (HSA) and medical savings account (MSA) contributions, HDHP premium payments, self-employment tax, and certain other expenses.

Although the Economic Recovery Act of 1981 included a modest above-the-line deduction for limited amounts of charitable contributions, it was phased out in 1987 and wasn't renewed. Thus, prior to the CARES Act, there was no existing above-the-line charitable deduction.

Retirement Plans

Just as taxpayers and preparers were making sense of the 2019 SECURE Act (Setting Every Community Up for Retirement) retirement rule changes, the worldwide economic collapse captured the immediate attention of lawmakers, taxpayers and tax preparers.

Before we cover the rules applicable under the CARES Act, let's review some of the differences among retirement plan types. It is important to be mindful of the terms "earnings" and "contributions" with respect to retirement accounts. "Contributions" are the funds put into the account. "Earnings" are the income generated by the money in the account.

Employer-Sponsored Qualified Retirement Plans

Employer-sponsored qualified plans fall into two general categories: defined benefit retirement plans and defined contribution retirement plans.

A defined benefit plan is a qualified employee plan that is designed to provide participants with a definite, specified benefit at retirement. The benefits that are provided by the plan determine the contributions that must be made to it. Defined benefit plans are often referred to as "traditional pension plans."

Unlike a defined benefit plan, a defined contribution plan is a qualified employee plan stated in terms of the employer's contribution to it instead of a stated benefit to be provided at retirement. Falling into the category of defined contribution plans are the following employer-sponsored plans:

- Money purchase pension plans;
- Target benefit plans;
- Profit sharing plans;
- Thrift plans;
- 401(k) plans;
- 403(b) tax sheltered annuity plans;
- Stock bonus plans;

- Employee stock ownership plans (ESOPs);
- Simplified employee pensions (SEPs); and
- Savings incentive match plans for employees (SIMPLEs).

Contributions made to the plans are normally made on a before-tax basis, and distributions from them are ordinarily taxable as ordinary income.

SEP IRA[17]

A Simplified Employee Pension (SEP) may be established by an employer or someone who is self-employed. A SEP is nothing more than an employer's agreement to contribute to traditional IRAs that are maintained by employees. The plan can be adopted by an employer by completing a fairly simple IRS form, rather than the much more complicated procedure involved in installing a qualified retirement plan.

Accordingly, SEPs are generally not as expensive to set up or operate as traditional employer-sponsored qualified retirement plans. Employers may make SEP contributions on a discretionary basis and may choose, in any tax year, to make no contribution to the plan. SEPs are treated as defined contribution plans for the overall limits on employer contributions. Employer contributions in 2021 are, therefore, limited to no more than the lesser of 25 percent of compensation and $58,000. Contributions vest immediately, so that the employee owns 100% of the invested money.

SIMPLE IRA[18]

A Savings Incentive Match Plan for Employees (SIMPLE) IRA also allows for higher contributions than permitted in a traditional or Roth IRA. The fundamental concept behind SIMPLEs is also identical to that for SEPs: plan design and administrative convenience resulting in a plan that is relatively inexpensive to implement and produces employer savings when compared to traditional qualified plans.

Eligibility to establish a SIMPLE is restricted to small employers. In the context of SIMPLE plans, a "small employer" is one with 100 or fewer employees earning at least $5,000 annually. For purposes of this small employer limitation, all employees employed at any time during the calendar year are considered, even those employees who are excludable or ineligible to participate.

Contributions to a SIMPLE IRA may come from two sources:

1. Elective contributions by employees; and
2. Employer contributions.

Employee elective contributions are made under a written arrangement with an eligible employer. Employees that are eligible to participate may elect to receive payments in cash or contribute them to a SIMPLE IRA to which the employer may make either matching contributions or nonelective contributions.

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[17] See https://www.irs.gov/retirement-plans/choosing-a-retirement-plan-sep

[18] See https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-simple-ira-contribution-limits

Except for certain catch-up contributions that may be made by employees age 50 or older, elective contributions to a SIMPLE IRA are limited to no more than $13,500 in 2020 and 2021. Participating employees age 50 or older may make an annual catch-up contribution of not more than $3,000.

Traditional IRA[19]

A traditional IRA is a personal retirement savings plan, funded by an annuity or a trust that meets certain requirements and which may permit tax-deductible contributions and tax-deferral of earnings. To be eligible to contribute to a traditional non-spousal IRA, an individual must generally have earned income.

Withdrawals from a traditional IRA are taxed at the ordinary income tax rate applicable at that time, which for many retirees would be lower (due to lower overall income) than the rates applicable at the time of contribution. Note that these withdrawals will be taxed as ordinary income, even if portions attributable to dividends or asset appreciation would otherwise be taxed at, for example, capital gains rates.

As with Roth IRAs, traditional IRA *contribution* limits are set at $6,000 (individual under age 50) and $7,000 (individual 50 or older) for 2020 and 2021, less any contribution made to a Roth IRA for the same year. Although any taxpayer with earned income may contribute to a traditional IRA, contributions are tax-deductible at the time they are made only if the taxpayer is not an active participant in an employer-sponsored retirement plan or, if the taxpayer is an active participant, the taxpayer's 2020 modified adjusted gross income (MAGI) does not exceed $124,000 (married filing jointly) or $75,000 (single or head of household). For 2021, those income limits are increased to $125,000 (married filing jointly) or $76,000 (single or head of household).

Absent the CARES Act's temporary required minimum distribution (RMD) suspension, applicable only to 2020, RMDs would have to begin at age 72.

Roth IRA[20]

A **Roth IRA** is a personal retirement savings plan, funded by an annuity or a trust that meets certain requirements and which may permit non-deductible contributions and tax-deferral of earnings. Rather than distributions being taxable when withdrawn—as they would be from a traditional IRA—Roth IRAs offer possible tax-free distributions instead of deductible contributions. In addition, although virtually everyone may establish a traditional IRA, whose contributions *may or may not be deductible*, not everyone may be eligible for a Roth IRA. And finally, amounts contributed to and accumulating in a Roth IRA can remain in the account as long as the owner wishes; Roth IRAs do not impose required minimum distributions during an owner's life.

Any *earnings* on the invested money is tax-free if the distribution is considered a qualified distribution. When the earnings are withdrawn in a qualified distribution, the tax liability is considered to have been satisfied, and no tax is due at the withdrawal time—the taxpayer has already paid the tax bill so there is generally no tax due upon withdrawal.

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[19] See https://www.irs.gov/retirement-plans/traditional-and-roth-iras
[20] See https://www.irs.gov/retirement-plans/traditional-and-roth-iras

A qualified distribution from a Roth IRA—a distribution that is entirely tax free—is one that is made after the five-taxable year period beginning with the first taxable year for which the individual made a contribution to a Roth IRA and one of the following applies:

- The individual is age 59 1/2 or older;
- The distribution is a qualified first-time homebuyer distribution;
- The individual is disabled; or
- The distribution is made to a beneficiary on or after the individual's death.

As long as a Roth IRA has been in force for the required period, a distribution from it that meets one of the four tests will be entirely income tax free.

*Contribution*s are limited to $6,000 for 2020 and 2021 ($7,000 for taxpayers age 50 or over), less any contribution made to a traditional IRA for the same year. A taxpayer may not contribute more than his or her earned income. Taxpayers with adjusted gross income above certain thresholds cannot contribute to Roth IRAs. For 2020, the phase-out begins at $196,000 modified adjusted gross income (MAGI[21]) for taxpayers with married-filing-jointly (MFJ) status and $124,000 for single filers. The contribution amount is phased out completely at $206,000 and $139,000 for MFJ and single, respectively. For 2021, the phase-out begins at $198,000 modified adjusted gross income (MAGI) for taxpayers with married-filing-jointly (MFJ) status and $125,000 for single filers. The contribution amount is phased out completely at $208,000 and $140,000 for MFJ and single, respectively.

Contributions (not earnings) can be withdrawn tax-free for any reason and at any time from a Roth IRA. Withdrawing *earnings* tax-free is possible only in a qualified distribution.

Relaxation of Retirement Fund Tax Rules

The CARES Act provides for broader distribution options and more favorable tax treatment for up to $100,000 in withdrawals, in aggregate, from retirement accounts (401(k), 403(b), and IRAs). The 10 percent early distribution penalty is waived for these coronavirus-related withdrawals.

Distributions may be included in income ratably over a three-year period unless the taxpayer elects to include the income in the year of distribution. IRA and qualified plan withdrawals may be rolled over within three years of distribution.

As a reminder, the SECURE Act changed IRA distribution rules. Traditional IRAs (but not Roth IRAs) must meet required minimum distribution (RMD) rules during the holder's lifetime. Under pre-SECURE Act law, that initial RMD was required for the year the holder reached age 70½, but the holder could delay receiving the initial RMD until April 1st of the following year, a date referred to as the "required beginning date." The problem in so doing is that the second RMD is required by December 31st of the same year, resulting in the need to include two years' worth of RMDs in the same yearly income.

Under the SECURE Act, RMDs were pushed back to age 72. However, that increase in the age at which RMDs had to begin ***only applied to those traditional IRA holders who reached age 70½ in 2020.*** Traditional IRA holders who were required to begin RMDs at age 72 could defer receipt of their first

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[21] MAGI is not shown on the tax return; it is calculated for the purposes of determining whether a taxpayer qualifies for certain tax benefits, including but not limited to Roth IRA and health care premium credit eligibility. MAGI is AGI with tax-exempt interest income and certain deductions added back.

RMD until April 1st of the year following the year in which they attained age 72. The change to age 72 for the commencement of RMDs was effective for years after December 31, 2019.

To provide temporary relief for the 2020 economic crisis, section 2202 of the CARES Act addresses changes affecting retirement plan funds and sets forth special distribution options, provides for relaxed IRA and other retirement account rollovers, and expands permissible loans from retirement plans.

In short, section 2202:

- Raises the qualified retirement plan loan maximum from $50,000 to $100,000,
- Waives the early distribution tax penalty for qualified plan and IRA distributions up to $100,000,
- Extends over a three-year period the taxation of withdrawals from IRAs and qualified plans,
- Allows rollover of IRA and qualified plan withdrawals within three years of their distribution, and
- Suspends required 2020 minimum distributions (RMDs).

Let's consider each of these changes.

Qualified Plan Loan Maximum Increased

Not all qualified plans permit participants to borrow from the plan, and, under the law prior to passage of the CARES Act, those that offered such loans were required to limit them to the lesser of $50,000 or one half of the present value of the plan participant's vested accrued benefit. In addition to meeting other requirements—formal documentation, loan term, level amortization, etc.—a borrower must meet the specified repayment schedule or risk having the loan considered a taxable distribution and subject to an early distribution tax penalty.

Pursuant to the provisions of the CARES Act:

- The maximum qualified plan loan permitted is increased to the lesser of –
  - $100,000, or
  - The present value of the plan participant's nonforfeitable, i.e. vested, accrued benefit;
- Repayment of the loan is changed as follows –
  - The due date of any repayment occurring during the period beginning on March 27, 2020 and ending on December 31, 2020 is delayed for one year,
  - Subsequent loan principal and interest repayment due dates are adjusted to reflect the delayed repayment(s), and
  - Neither the resulting non-level amortization nor the greater-than-five-year term of the plan loan caused solely by the authorized changes in loan repayment will cause the loan to be considered a taxable distribution.

Early Distributions

Contributions to IRAs and qualified retirement plans are afforded special tax benefits under the Internal Revenue Code—benefits including possible deductibility of contributions, tax-deferred accumulations, possible tax-free distributions—principally to encourage individuals to participate in such plans that will provide them with retirement income. In an attempt to limit the use of such funds to producing retirement income, early distributions—distributions from a qualified plan or IRA before the plan participant or IRA account holder becomes age 59 ½—would generally be subject to a 10% penalty tax.

In recognition of the possibility of emergencies or other conditions that mandate such funds be accessible, the Internal Revenue Code identifies certain exceptions to the imposition of early withdrawal tax penalties in the case of a pre-59 ½ distribution. This penalty is usually waived only in the following circumstances:

- The taxpayer plans to use the funds to purchase a first home;
- The taxpayer becomes disabled before the distribution occurs;
- A beneficiary receives assets after the account owner's death;
- The taxpayer uses the funds for unreimbursed medical expenses, health insurance costs incurred after job loss;
- The taxpayer uses the funds for adoption or higher education expenses;
- The distribution results from an IRS levy;
- The distribution is from returns on non-deductible contributions;
- The taxpayer is in the military and is called to active duty for more than 179 days; or
- The distribution is part of a SEPP program

A SEPP program, or "substantially equal periodic payments" program, is another program allowing for penalty-free IRA and 401(k) withdrawals before age 59 1/2 and is not related to the CARES Act.

In addition to these specified exceptions to imposition of the penalty that traditionally apply, the CARES Act adds coronavirus-related distributions. The 10% tax penalty is waived for any coronavirus-related early distributions or qualified disaster distributions up to $100,000 from an individual's IRA or qualified plan. This $100,000 limit applies to the aggregate of distributions to a single person – not per account. A retirement plan administrator may rely on an employee's certification that the early distribution is related to the coronavirus.

TRA 2020 has further authorized waiver of the tax penalty for qualified disaster distributions.

Taxation of IRA and Qualified Plan Withdrawals Over Three-Year Period

Not only is the tax penalty waived in the case of any coronavirus-related distribution, such a distribution is afforded additional special tax treatment. Under the CARES Act, unless the taxpayer elects to have the entire amount included in income in the year of withdrawal, any withdrawal amount required to be included in gross income for the taxable year—in most cases, the entire amount withdrawn is includible in gross income—will be included ratably over the three-taxable-year period beginning with the taxable year in which the withdrawal was made.

Example

> Tina Taxpayer receives a $12,000 coronavirus-related distribution on May 1, 2020. She must begin including the distribution as income in 2020. Unless she elects to include the entire distribution in 2020 income, she must include at least $4,000 for 2020, at least $4,000 for 2021, and any remainder in 2022. That is, Tina may elect to report the entire $12,000 distribution for 2020 or spread out its reporting over three years, as long as at least $4,000 has been reported for 2020 and $4,000 reported for 2021 (and the remaining $4,000 reported for 2022.)

IRS guidance indicates that although plan administrators may rely on participants' self-certification that they are eligible for CARES Act distributions, a taxpayer who takes such a distribution may owe penalties at a later date if it is shown that he or she made misrepresentations about eligibility for a distribution.

That is, taxpayers may later be disqualified from the 10% penalty waiver and the ability to spread income recognition over three years. Although a particular distribution may be disqualified, a ***plan*** will not be disqualified due to taxpayers' misrepresentations about eligibility for COVID-related distributions.

Rollover of IRA and Qualified Plan Withdrawals Within Three Years of Distribution

Most retirement plan distributions may be rolled over and, thereby, avoid current taxation. Coronavirus-related plan distributions enjoy a similar benefit in that they do not have to be included in income to the extent the taxpayer subsequently redeposits the distribution. In such a case, the redepositing will be treated, for tax purposes, as though the taxpayer had made a direct transfer of the redeposited funds from trustee to trustee.

Any IRA account holder or qualified plan participant who receives such a distribution is permitted to redeposit the distribution. Under the CARES Act, the recipient of a coronavirus-related distribution may make a single contribution or multiple contributions in an aggregate amount not to exceed the amount of the coronavirus-related distribution to an eligible retirement plan.

The repayment must occur during the three-year period beginning on the day after the date on which it was received. The redeposited withdrawals, for tax purposes, will be treated as if the redeposited distribution had been transferred to an eligible retirement plan in a direct trustee to trustee transfer within 60 days of the distribution; in short, it will avoid taxation.

Example

> Tina Taxpayer's May 1, 2020 distribution of $12,000 will be treated as redeposited as long as she makes a direct transfer or transfers on or before May 2, 2023. She may transfer a maximum of $12,000 (the original distribution amount) and keep tax-favored treatment for her funds. Any funds up to that $12,000 that she transfers in this manner will be treated as though it had been repaid within 60 days of the original distribution.[22]

Coronavirus-Related Distribution

The term ''coronavirus-related distribution'' means a distribution not exceeding $100,000 in the aggregate from a qualified retirement plan or IRA made in 2020 to an individual:

- Who is diagnosed with the virus SARS–COV-2 or with coronavirus disease 2019 (COVID– 19) by a CDC-approved test,
- Whose spouse or dependent is diagnosed with such virus or disease by such a test, or
- Who experiences adverse financial consequences as a result of –
  - being quarantined, being furloughed or laid off or having work hours reduced due to such virus or disease, or
  - being unable to work due to –
    - lack of child care due to such virus or disease,
    - closing or reducing hours of a business owned or operated by the individual due to such virus or disease, or
    - other factors as determined by the Secretary of the Treasury.

[22] IRC Section 408(d)(3) covers the otherwise applicable 60-day repayment requirement

IRS Notice 2005-92

In a FAQ, issued in May of 2020,[23] the IRS indicates its plans to release guidance for CARES Section 2202 in the "near future." This FAQ points to the Katrina Emergency Tax Relief Act of 2005 (KETRA) as a source of principles "substantially similar" to those expected for Section 2202 guidance.

To date, much of the relief under the CARES Act is consistent with KETRA provisions. KETRA waived the 10 percent penalty for early withdrawals from certain retirement accounts.

Qualified Disaster Distribution

A ''qualified disaster distribution'' means any distribution from an eligible retirement plan made:

- On or after the first day of the incident period of a qualified disaster and before the date which is 180 days after the date of the enactment of this Act (December 27, 2020), and
- To an individual whose principal place of abode at any time during the incident period of such qualified disaster is located in the qualified disaster area with respect to such qualified disaster and who has sustained an economic loss by reason of such qualified disaster.

The term ''qualified disaster area,'' as used in TRA 2020, means any area with respect to which a major disaster was declared, during the period beginning on January 1, 2020, and ending on the date which is 60 days after the date of the enactment of this Act, by the President under section 401 of the Robert T. Stafford Disaster Relief and Emergency Assistance Act.

Suspension of 2020 Required Minimum Distributions

IRC Section 401(a)(9) requires a retirement plan or IRA owner to take required minimum distributions (RMDs) annually once that person reaches age 72 (formerly age 70 ½ prior to passage of the SECURE Act in the closing days of 2019). The CARES Act suspends this requirement for 2020 for certain types of plans—defined contribution plans and individual retirement plans.

Modifications for Net Operating Losses (NOLs)

A business's profit and loss volatility can cause fundamentally unequal income tax treatment among different business entities. The ability of a firm to carryover net operating losses helps to equalize that treatment.

Example

> Consider the tax treatment of two firms—firm XYZ whose net income is stable from year to year and firm ABC whose net income is characterized by significant variability—but whose net income over two years is identical. Suppose the XYZ firm has $50,000 net income in each of years one and two while the ABC firm has a $100,000 loss in year one and $200,000 net income in year two. Although both firms have the same net income over the two-year period, ABC has a substantially larger tax bill, as shown below:

Firm	Yr. 1 Net Income	Yr. 2 Net Income	Yr. 1 Tax	Yr. 2 Tax	Combined Effective Rate

[23] The IRS indicates that as of a September 19, 2020 review date, this FAQ is current (and no additional guidance has been issued at this point). See https://www.irs.gov/newsroom/coronavirus-related-relief-for-retirement-plans-and-iras-questions-and-answers

ABC	($100,000)	$200,000	$0	$42,000	42%
XYZ	$50,000	$50,000	$10,500	$10,500	21%

However, when ABC takes a net operating loss (NOL) deduction in year two, it equalizes the two-year tax rate between the two firms as shown in the next chart (below):

Firm	**Yr. 1 Net Income**	**Yr. 2 Net Income**	**Yr. 1 Tax**	**Yr. 2 Tax**	**Combined Effective Rate**
ABC	($100,000)	($200,000 - $100,000)	$0	$21,000	21%
XYZ	$50,000	$50,000	$10,500	$10,500	21%

Under the Internal Revenue Code prior to the passage of the CARES Act, firms:

- Could not carry back losses to a previous year,
- Could carry losses forward for an unlimited number of years,
- Were limited to an NOL deduction of up to 80% of their taxable income, and any additional loss needed to be carried forward, and
- Organized as pass-through businesses were limited to using no more than $250,000 ($500,000 for joint filers) of losses to offset taxable income earned outside of the pass-through business.

The CARES Act alleviates some of the inequality for firms with volatile incomes by:

- Providing for a five-year carryback for losses occurring in 2018 through 2020,
- Temporarily removing the 80% NOL deduction limit, and
- Permitting owners of pass-through businesses to disregard the prior $250,000/$500,000 limits to offset non-business income for years 2018 through 2020.

Thus, a NOL arising in tax years beginning in 2018, 2019, and 2020 generally would be carried back, under IRC Section 172, to each of the five years preceding the tax year in which the loss was incurred. A 2018 loss can be carried back as far as 2013, when the highest corporate tax rate was 35%. Prior year returns may be amended and tax refunds collected. A taxpayer may make an irrevocable election to waive the carryback period for the NOL for any tax year.[24]

For the owner of certain pass-through entities, the TCJA had placed a limitation on the amount that could be used for these losses. A single taxpayer was limited to $250,000 and a joint filer was limited to $500,000. These limits were removed, as noted above, so that taxpayers may offset non-business income by greater than those amounts to the extent they had income in the years to which NOLs are carried back.

[24] At https://www.irs.gov/pub/irs-drop/rp-20-24.pdf

Chapter 2 Review Questions

1. Lola Limito asks you: "What is the charitable contributions limit for 2020?" What do you tell her?
   A. 60 percent of AGI
   B. 50 percent of AGI
   C. 100 percent of AGI
   D. There is no limit
2. Kendrick Cuomo makes charitable contributions of personal property which was worth $200,000 when she first bought it and has a fair market value of $20,000 at the time of donation. Assuming her AGI is $180,000, how much is tax-deductible?
   A. An amount based on limits that were not changed by the CARES Act
   B. $180,000
   C. $200,000
   D. $20,000
3. Which of the following is a change made by the CARES Act?
   A. The 10 percent penalty is waived if the taxpayer becomes disabled before the distribution occurs.
   B. The 10 percent penalty is waived if the taxpayer uses the funds for health insurance costs incurred after job loss.
   C. The 10 percent penalty is waived if the reason for a distribution is to satisfy an IRS levy.
   D. The 10 percent penalty is waived for up to $100,000 used to pay for coronavirus-related expenses.
4. Genie Glassware Corporation suffers a $100,000 net operating loss for tax year 2018. Which of the following is true with respect to this NOL under the CARES Act?
   A. The NOL may be carried back for five years (to 2013)
   B. Is subject to an 80% NOL deduction limit
   C. Disallows carrybacks by owners of pass-through entities
   D. Requires carried-back NOLs to be treated as though 2020 tax rates had been in place for carryback years

Answers to Chapter 2 Review Questions

Answer to question #1

A. This answer is incorrect. A 60 percent limit was put in place by the Tax Cuts in Jobs Act, but the CARES Act temporarily suspends this limit.
B. This answer is incorrect. A 50 percent limit was in place before the Tax Cuts and Jobs Act.
C. That is correct! The CARES Act provides that an individual taxpayer may make a tax-deductible cash contribution of up to 100 percent of his or her AGI
D. This answer is incorrect. There is a limit on the tax-deductible contribution a taxpayer can make in 2020.

Answer to question #2

A. That is correct! Kendrick is making a contribution of personal property. The temporary 100 percent deduction does not apply.
B. This answer is incorrect. The temporary 100 percent CARES Act deduction applies only to cash donations.
C. This answer is incorrect. The contribution is of personal property, not cash.
D. This answer is incorrect. Personal property contribution limits were not changed by the CARES Act.

Answer to question #3

A. This answer is incorrect. The 10 percent penalty waiver for taxpayer disability was applicable before the CARES Act was enacted,
B. This answer is incorrect. The 10 percent penalty waiver for use in paying health insurance costs after job loss was in place before the CARES Act.
C. This answer is incorrect. The 10 percent penalty waiver for satisfying an IRS levy was in place before the CARES Act.
D. That is correct! The CARES Act allows for a withdrawal of up to $100,000 by a taxpayer if needed to pay for coronavirus-related expenses.

Answer to question #4

A. That is correct! Under the CARES Act, NOLs incurred in 2018 through 2020 may be carried back for five years from the year incurred.
B. This answer is incorrect. The CARES Act temporarily suspended the 80% NOL deduction limit.
C. This answer is incorrect. The CARES Act provides for disregard of previously in-place limitations of $ 250,000/$500,000 for owners of certain pass-through entities.
D. This answer is incorrect. The CARES Act requires use of the tax rates applicable to the year the NOL is carried back to.

Chapter 3 – Miscellaneous CARES Act and TRA 2020 Provisions

Introduction

The CARES Act and TRA 2020 address a wide range of additional issues. This chapter will consider the changes brought about by the Acts with respect to health savings accounts (HSAs), qualified medical expenses, qualified tuition and related expenses, high deductible health plans (HDHPs), foreign earned income, tax-free exchanges of investment property and certain miscellaneous business provisions. Among the business provisions considered are the correction of the Tax Cuts and Jobs Act of 2017 provision addressing the deductible period applicable to qualified improvement property, changes to the deduction of losses by non-corporate taxpayers, modifications of business interest limitations, employer student loan payments and SBA loans referred to as economic injury disaster loans (EIDLs).

Learning Objectives

After completing this chapter, you should be able to:

- Describe the health savings account (HSA) exemptions for telehealth services,
- Discuss changes made to qualified medical expenses,
- Identify the changes made to high deductible health plans (HDHPs) with respect to first-dollar payment of COVID-19 related testing and treatment expenses;
- Recognize the extension available with respect to Section 911 exclusion of foreign earned income;
- Describe the changes made to the tax treatment of tuition and related expenses;
- Identify the Section 1031 time-sensitive action deadlines; and
- Describe the CARES Act provisions affecting businesses, including the –
    - Correction regarding the deductible period applicable to qualified improvement property,
    - Modification of limitation on losses for non-corporate taxpayers,
    - Changes to the limitation on business interest expense deductions,
    - Exclusion of certain employer payments of student loans, and
    - Expansion of economic injury disaster loans (EIDLs).

Let’s consider each of these provisions individually.

Exemption for Telehealth Services

“Telehealth” is a term that refers to the use of telecommunications—telephone, email, videoconferencing, remote monitoring and other communications services and devices—technology to provide healthcare services. With more people likely to need in-home or other remote health care services during the pandemic, the CARES Act[25] addresses telehealth coverage as it may impact on health savings accounts (HSAs).

Section 223 of the Internal Revenue Code authorizes HSAs and a tax deduction for contributions to them. In order to establish an HSA, a taxpayer must be covered under a high deductible health plan

[25] Section 3701

(HDHP) and ***not covered*** under any health plan—other than specifically identified plans—that is not an HDHP. In short, the statute generally forbids coverage under anything but the HDHP.

Section 3701 of the Cares Act adds telehealth and other remote care services to the list of coverages that can be provided on a first-dollar basis, i.e. with no deductible, without adversely affecting the taxpayer's eligibility to establish and maintain an HSA. Without this provision, a taxpayer receiving first-dollar coverage for such services would be disqualified from establish an HSA or making tax-favored HSA contributions.

Qualified Medical Expenses

Only certain medical expenses are considered "qualified medical expenses" for which a taxpayer may receive a tax deduction and which may be considered qualified medical expenses under various healthcare programs, such as medical flexible spending accounts (FSAs), HSAs and Archer MSAs. Section 3702 of the CARES Act adds certain over-the-counter medical products—specifically menstrual care products—as qualified medical expenses effective after December 31, 2019. Accordingly, such products—expenditures for which would be considered qualified medical expenses—include, among other over-the-counter products:

- Tampons,
- Pads,
- Liners,
- Cups,
- Sponges, and
- Similar products used by individuals with respect to menstruation or other genital-tract secretions.

High Deductible Health Plans and COVID-19-Related Expenses

As noted earlier, Section 223 of the Internal Revenue Code authorizes HSAs and a tax deduction for contributions to them, and it requires that coverage be provided by an HDHP. HDHPs, as the name suggests, impose a high deductible that must normally be met before benefits are paid for covered charges. IRS Notice 2020-15 provides that a taxpayer who is otherwise eligible to establish and maintain an HSA will not be considered ineligible even though the health plan covers testing for and treatment of COVID-19 without a deductible or with a deductible below the minimum HDHP deductible.

Additional Health Care Related Provisions

Section 125 cafeteria plans maintained by employers permit employee-taxpayers to allocate pre-tax income to the plan and to subsequently use those funds to pay certain healthcare and dependent assistance expenses. The operation of a cafeteria plan is characterized by inflexibility with respect to amounts that may be allocated, the expenses that are reimbursable and the general prohibition against making changes during a coverage period.

The CARES Act provides temporarily increased flexibility in making mid-year changes (in 2020) to taxpayers' Section 125 cafeteria plan elections. IRS Notice 2020-29 indicates that taxpayers may change certain elections related to employer-sponsored health insurance coverage, flexible spending accounts for health care, and dependent care assistance. Eligible employees may increase their pre-tax contributions, revoke elections, enroll in plans, and otherwise change their existing elections.

Cafeteria plan administrators may also extend the period of time covered by these accounts as well as the grace period for filing claims for medical and dependent care expenses incurred during calendar year 2020 (and any extended coverage date). Otherwise, a taxpayer would normally otherwise have to forfeit funds not used by the end of the calendar year. To provide further taxpayer flexibility, TRA 2020 also permits taxpayers to roll over any unused FSA amounts from 2020 to 2021 and from 2021 to 2022 as well as to make midyear prospective contribution changes in 2021.

Unreimbursed Medical Expense Threshold Lowered

The threshold for deduction of unreimbursed medical expenses has been scheduled to increase from 7.5% of AGI to 10% of AGI several times but has been forestalled repeatedly by temporary tax extenders and was again expected to increase to 10% again in 2021. However, TRA 2020 makes permanent the 7.5% AGI floor for deduction of unreimbursed medical expenses.

Section 911 Foreign Earned Income

Internal Revenue Code § 911 provides an exclusion from income for a portion of foreign earned income and housing costs for persons living in a foreign country. The permitted exclusion applies to an individual who is a bona fide resident of a foreign country for an uninterrupted period that includes an entire taxable year or is physically present in a foreign country for at least 330 full days during any period of 12 consecutive months.

Because of the COVID-19 pandemic and the travel bans imposed to limit its spread, the Treasury Department and the IRS released Revenue Procedure 2020-27. Revenue Procedure 2020-27 provides that qualification for the foreign earned income exclusion and foreign housing cost amount from gross income will not be impacted as a result of days spent away from a foreign country due to the COVID-19 pandemic.

Pursuant to the Revenue Procedure, the COVID-19 emergency is an adverse condition that precluded the normal conduct of business:

- In the People's Republic of China, excluding the Special Administrative Regions of Hong Kong and Macau, as of December 1, 2019; and
- Globally, as of February 1, 2020.

Absent an extension, the period covered by the Procedure ends on July 15, 2020. Individuals seeking to qualify for the § 911 exclusion because they could reasonably have been expected to have been in a foreign country for 330 days except for the COVID-19 emergency and have met the other requirements for qualification may use any 12-month period to meet the qualified individual requirement.

Section 1031 Timing Relief

A Section 1031 exchange involves selling one investment property and replacing it with another in a manner that allows for capital gains on the sale to be deferred. Most 1031 exchanges will result in no tax (or limited tax) being due at the time of the swapping of properties. The properties have to be like-kind (no swapping of a vacation rental house for a jewelry collection, in other words). The TCJA tightened the like-kind requirement so that the deferral only applies to real estate.[26]

Capital gains may be deferred on the sale of property by rolling over the gains from one property to another like-kind property under an exchange referred to as a *1031 exchange*. The like-kind exchange authorized under § 1031 of the Internal Revenue Code demands that certain actions—referred to as "Specified Time Sensitive Actions"—occur as required in order to accomplish the tax deferral provided for under the statute.

These time sensitive actions are:

1. Within 45 days of the sale of the property, the seller must identify a replacement property; and
2. Within 180 days of the sale the seller must purchase the replacement property.

IRS Notice 2020-23 provides relief from these time sensitive actions that are due to be performed on or after April 1, 2020 and before July 15, 2020. Under the relief provided in the Notice, the due date is extended to July 15, 2020.

When the 45- and 180-day deadlines and other Section 1031 requirements are met, any capital gain on the sold property can be rolled over to the purchased property. Capital gains tax will be avoided until the purchased property is sold. If the replacement property is sold much later, it could qualify for long-term capital gains treatment rather than short-term tax treatment. In many years, the long-term capital gains tax rate is lower than that for short-term capital gains.

Miscellaneous Personal Tax Changes

In addition to those changes already discussed, TRA 2020 has brought about the following:

- The tax deduction for qualified tuition and related expenses has been repealed;
- The phase-out limits applicable to the lifetime learning credit have been increased to equal the phase-out limits applicable to the American opportunity credit;
- Taxpayers are permitted to use the earned income in 2019 to compute their earned income for the child tax credit (CTC) and earned income tax credit (EITC);
- The threshold for deduction of unreimbursed medical expenses has been permanently set at 7.5%; and
- The exclusion from gross income of a discharge of indebtedness on a personal residence was extended for five years.

Miscellaneous Business Provisions

Certain provisions of the CARES Act that affect businesses and which are discussed below include:

- Temporary increase in business meal deductibility;
- Correction regarding qualified improvement property,
- Modification of limitation on losses for non-corporate taxpayers,
- Modifications of limitation on business interest,
- Exclusion of certain employer payments of student loans, and

[26] https://www.irs.gov/newsroom/like-kind-exchanges-now-limited-to-real-property

- Economic injury disaster loans (EIDL).

Temporary Increase in Business Meal Deductibility

TRA 2020 provides for temporarily increased deductions for business meals. Pursuant to TRA 2020, businesses are permitted a 100% tax deduction for business meals—up from the current 50%—if the food or beverages are provided by a restaurant. The increased business meal deduction is available for 2021 and 2022.

Technical Amendments Regarding Qualified Improvement Property

Section 2307 of the CARES Act makes qualified improvement property (QIP) eligible for bonus depreciation. The Tax Cuts and Jobs Act had provided for 39-year depreciation of qualified improvement property (QIP) rather than the intended 15 years. Additionally, the TCJA made such property ineligible for bonus depreciation. Accordingly, the CARES Act sets the depreciable life of qualified improvement property at 15 years, thereby enabling taxpayers to take advantage of bonus depreciation. This correction is retroactive.

Qualified improvement property is any improvement to a non-structural, interior portion of a non-residential building as long as that improvement is placed in service after the building was first placed in service by any taxpayer. Because the CARES Act correction is retroactive, many taxpayers can recapture tax savings. A 2018 return, for example, could be amended so that the depreciation is carried back over five years to years with higher tax rates. For property placed in service during 2019, the taxpayer may claim bonus depreciation for 2019, and possibly claim a refund for overpaid estimated taxes.

Limitation on Losses for Non-Corporate Taxpayers

The Tax Cuts & Jobs Act (TCJA) disallowed the deduction of "excess business losses" for tax years beginning after December 31, 2017 and ending before January 1, 2026 by non-corporate taxpayers. Accordingly, non-corporate taxpayers were generally required to carry forward losses in excess of $250,000 ($500,000 for joint filers) as NOLs. Such carryovers were limited to 80% of net income for tax years beginning after December 31, 2017.

Section 2304 of the CARES Act retroactively defers the effective date of this rule to tax years beginning after December 31, 2020. Because of that deferral, a non-corporate taxpayer now can recognize those losses for the 2018, 2019, and 2020 tax years. CARES Act Section 2303 removes the 80% limitation for tax years beginning before January 1, 2021. The 80% limitation returns for tax years beginning January 1, 2021 and later.

Modifications of Limitation on Business Interest Expense

Internal Revenue Code § 163(j)(1) provides that business interest expense is deductible in an amount not exceeding the sum of the following:

1. The business' interest income for the year,
2. 30% of the business' adjusted taxable income[27] (ATI), plus

[27] Adjusted taxable income (ATI) is the business' taxable income before interest expense, income tax expense, depreciation, amortization and depletion.

3. The business' floor plan financing[28] interest for the year.

Section 2306 of the CARES Act modifies the calculation for determining deductible business interest expense by:

- Increasing item 2 (above) to 50% of the business' ATI for regular (C) corporations and S corporations for taxable years beginning in 2019 and 2020, and
- Increasing item 2 (above) to 50% of the business' ATI for partnerships for taxable years beginning in 2020.

Additionally, the CARES Act permits taxpayers to elect to use their 2019 ATI as their ATI in 2020.

Special Partnership Rules

Rather than increasing the percentage of ATI in 2019 for purposes of determining deductible interest in the case of partnerships, the 2019 excess business interest—the business interest in excess of 30% of the business' ATI, in other words—is split. Half of the 2019 excess business interest is treated as paid or accrued in 2020 and deductible by the partner ***without regard to the § 163(j) limitation***, and the balance is subject to the existing rules.

Exclusion of Certain Employer Payments of Student Loans

The Internal Revenue Code, prior to passage of the CARES Act, permitted employers to assist their employees with tax-free reimbursement up to $5,250 for tuition and books. However, any money in excess of that amount counted as income for the employee. In addition, funds received toward student loans would also be deemed income which means the employee would be required to pay taxes on the amount, and, if the employee's student loan repayment was being repaid in accordance with an income-based repayment plan, the employee's monthly payment could increase due to the resulting higher income.

The CARES Act enables employers to contribute toward the principal or interest on an employee's qualifying student loan, and those student loan payments are tax-free up to $5,250 if made at any time after March 27, 2020 through December 31, 2020. Neither an employer's payroll tax or an employee's income tax is affected by payment of the student loan.

In order for the payment to be tax-free, the employee must not have the option to receive the funds as taxable income. Furthermore, unless the employer's student loan payment is identified as payment of the loan principal only—the interest expense being paid by the employee—the employee will not be able to deduct the loan interest since it would have been paid by the employer. TRA 2020 extended the exclusion for employer payments of student loans for five years.

Economic Injury Disaster Loans (EIDL)

The availability of an Economic Injury Disaster Loans (EIDL) is not the result of a new program. Instead, it is an existing Small Business Administration (SBA) program and is the principal means of federal assistance for repairing and rebuilding non-farm, private sector disaster losses. The SBA may provide up to $2 million under the program for EIDL assistance to small businesses or private non-profit

[28] "Floor plan financing indebtedness" is indebtedness a) used to acquire motor vehicles held for sale or lease, and b) secured by the inventory so acquired, i.e. the motor vehicles.

organizations located in a presidentially-declared disaster area that have sustained economic injury. No front-end fees or early payment penalties apply, and the term of repayment is determined by the borrower's ability to repay the loan.

Although not a new program, the EIDL program has been expanded by the CARES Act and, with the emergency declaration on March 13, 2020 under the Robert T. Stafford Disaster Relief and Emergency Assistance Act, all of the United States has been declared a disaster area. Thus, any small business in the United States that meets the balance of requirements can be eligible.

The CARES Act in § 1110 provides for emergency EIDL grants to eligible entities during the covered period which extends from January 31, 2020 through December 31, 2020.

Eligible entities include:

- Small business concerns,
- Private non-profit organizations,
- Small agricultural cooperatives,
- Businesses with not more than 500 employees[29],
- Individuals who operate under a sole proprietorship, with or without employees, or as an independent contractor,
- Cooperatives with not more than 500 employees,
- ESOPs with not more than 500 employees, and
- Tribal small business concerns with not more than 500 employees.

Certain organizations are ineligible, including:

- Businesses engaged in illegal activities,
- Businesses engaged in lobbying,
- Businesses who derive more than 1/3 of their revenue from gambling,
- Businesses engaged in live performances of a prurient sexual nature or that derive more than de minimis gross revenue from the sale of products or services, or the presentation of any depictions or displays, of a prurient sexual nature.

The CARES Act also waives certain rules and requirements for loans made in response to COVID-19 during the covered period, including:

- Rules related to the need for personal guarantees on advances and loans not exceeding $200,000,
- The requirement that an applicant have been in business for the one-year period before the disaster, except that no waiver may be made for a business not in operation on January 31, 2020, and
- The requirement that an applicant be unable to obtain credit elsewhere.

With respect to small-dollar loans made during the covered period in response to COVID-19, the CARES Act provides for additional flexibility. Pursuant to that additional flexibility, the SBA may:

[29] Restaurants and hospitality businesses may qualify if they have not more than 500 employees per location.

- Approve an applicant based solely on the applicant's credit score, or
- Use alternative appropriate methods to determine an applicant's ability to repay.

Emergency Grants

During the covered period, an eligible entity that applies for an SBA loan under the CARES Act in response to COVID-19 may request that the SBA provide an advance of up to $10,000 within three days of application. An advance provided may be used for any allowable purpose described in the Small Business Act, including:

- Providing paid sick leave to employees unable to work due to the direct effect of COVID-19,
- Maintaining payroll to retain employees,
- Meeting increased costs to obtain materials unavailable from the applicant's original source due to interrupted supply chains,
- Making rent or mortgage payments, and
- Repaying obligations that cannot be met due to revenue losses.

No repayment of an advance provided pursuant to the provisions of the CARES Act is required, even if the applicant is subsequently denied a loan under the program.

Chapter 3 Review Questions

1. Which of the following is *not* part of the increased flexibility the CARES Act provides with respect to Section 125 cafeteria plan elections?

    A. Eligible employees may make a mid-year increase in the pre-tax contributions to flexible spending accounts

    B. Eligible employees may revoke certain elections mid-year

    C. Eligible employees may enroll in plans mid-year

    D. Eligible employees may use 2020 funds through 2026

2. Alexis Alixir, individual taxpayer, has lived in Jamaica since 2010. He had planned to live in Jamaica for all but two weeks in 2020. His plans changed. He had to make an emergency trip back to the United States for a funeral and ended up being in the United States from March 1 through July 10, when he returned to Jamaica for the rest of the year. What will be the federal income tax treatment for Alexis's $250,000 in income earned in 2020 from his Jamaica activities?

    A. Section 911 will not provide him a foreign income exclusion because he did not meet the 330-day requirement.

    B. Section 911 will not provide him a foreign income exclusion because his time in Jamaica was not "uninterrupted."

    C. Section 911 will allow him to exclude the value of his foreign housing but not any of his earned income.

    D. Section 911 provides an exclusion from income for a portion of foreign earned income and housing costs in 2020 because he was absent from Jamaica for Covid-related reasons.

3. Federico is attempting to make a like-kind exchange under Section 1031. He is selling a duplex he owns in Oregon in order to find a duplex in Montana and purchase it. The Oregon duplex has an adjusted basis of $575,000 and he sells it on January 15 for $875,000. In order to defer capital gains tax, what are the requirements for purchasing like-kind replacement property?

    A. Federico has 45 days from the sale of the property to identify and purchase the replacement property.

    B. Federico has 45 days from the sale of the property and 180 days from the sale to purchase that replacement property.

    C. As long as Federico replaces the sold duplex on or before December 31, 2020, he may defer capital gains tax for five years.

    D. As long as Federico identifies the replacement property by December 31, 2020, he may defer capital gains tax until he sells the replacement property.

4. Bobby Crofoot works for a business providing aesthetic skin care services to liberate people from their facial wrinkles. Having gone to law school in his early 20s, he is still paying off his

student debt at age 38. In June of 2020, his employer makes a $7,250 payment ($250 interest, $7,000 principal) toward Bobby's qualifying student loan. What is the income tax treatment of this payment?

A. All $7,250 is treated as taxable income to Bobby.

B. The $7,000 in principal is taxable to Bobby as income, and the $250 toward the interest is deductible.

C. $5,250 is income tax free, but Bobby and the company must both pay payroll taxes.

D. Bobby will be able to deduct $5,250.

Answers to Chapter 3 Review Questions

Answer to question #1

A. This answer is incorrect. Mid-year increases to FSAs are part of the CARES Act's increased flexibility.
B. This answer is incorrect. Revoking elections mid-year is part of the CARES Act's added flexibility.
C. This answer is incorrect. Enrolling in plans mid-year is one of the ways the CARES Act provided increased flexibility.
D. That is correct! Although there may be an extension beyond the beginning of 2021 (as an "extended coverage date"), there is no provision providing for such an extension through 2026.

Answer to question #2

A. This answer is incorrect. The 330-day requirement is waived in 2020, provided certain conditions are met.
B. This answer is incorrect. The requirement that time in the foreign country be "uninterrupted" is waived for part of 2020.
C. This answer is incorrect. Section 911 will allow him an exclusion for a portion of his foreign housing *and* earned income in 2020.
D. That is correct! The Section 911 exclusion applies because he was absent from Jamaica (during the period of 2020 ending July 15).

Answer to question #3

A. This answer is incorrect. It is true that Federico must identify the replacement property within 45 days of the sale, he has longer to purchase that property.
B. That is correct! Section 1031 requires identification of replacement property within 45 days of sale of the original property. Replacement property must be purchased within 180 days.
C. This answer is incorrect. Federico has 45 days from sale to identify replacement property and 180 days to purchase is. Further, there is no statutory deferral for five years
D. This answer is incorrect. Federico must identify his replacement property within 45 days of sale.

Answer to question #4

A. This answer is incorrect. At least a portion of the payment is deductible.
B. This answer is incorrect. Although there can be different treatment for the principal and interest, the payment is not entirely taxable to Bobby.
C. This answer is incorrect. Neither has to pay payroll taxes.
D. That is correct! Student loan payments are tax-free up to $5,250 if made between March 27, 2020 and December 31, 2020. The excess will be taxed as income to Bobby.

Chapter 4 – Additional Economic Stimulus Legislation

Introduction

Before and after passage of the CARES Act, Congress passed other stimulus legislation, and this chapter will briefly look at their principal provisions.

Learning Objectives

After completing this chapter, you should be able to:

- Describe primary objective of the Coronavirus Preparedness and Response Supplemental Appropriations Act;
- Identify the principal intent of the Families First Coronavirus Response Act (FFCRA); and
- Recognize the impact of the Paycheck Protection Program and Health Care Enhancement Act.

Let's discuss each of these pieces of legislation in turn.

Coronavirus Preparedness and Response Supplemental Appropriations Act

The first stimulus law was passed as the economic impact of the virus had just begun noticeably to disrupt the U.S. economy. Public Law 116-123 was passed on March 6, 2020. The $8.3 billion stimulus was directed primarily toward public health funding and vaccine development. Most funding was allocated domestically, with 19 percent being directed internationally to foreign public health systems.

More specifically, the funds were intended to be used for the development, manufacture, and procurement of vaccines and medical supplies; for grants, loans, and evacuation preparedness; and, as noted, for humanitarian assistance for foreign health systems.

Families First Coronavirus Response Act (FFCRA)

Next, the FFCRA provided $105 billion in aid to cover extended sick leave and Family Medical Leave Act (FMLA) leave for people working for companies with fewer than 500 employees. Some federal employers or private employers with 50 or fewer employees were made exempt from the requirement to provide such leave.

Additionally, Medicare and private health insurance plans were required to cover COVID-19 testing.

Paycheck Protection Program and Health Care Enhancement Act (Enhancement Act)

In April, Congress provided additional funds to continue to cover costs of the PPP, small business disaster loans and grants, aid to hospitals and health care providers, and testing costs. The $484 billion allocation was to replenish and/or supplement the CARES Act programs. The Enhancement Act was enacted on April 24, 2020.

Extended Eviction Ban

In September, the Centers for Disease Control and Prevention suspended certain evictions through December 31, 2020. There is also financial aid for residential rental property owners to offset the associated reductions in rent receipts. A landlord or other person with a legal right to pursue eviction must observe a moratorium on evictions. The purpose of the moratorium is to help limit the spread of the coronavirus. Renters remain liable for rent, and landlords may charge fees, penalties, and interest for late payments.[30]

Additional Stimulus Legislation

As the public health and economic crises have extended well beyond April, Congress has considered additional stimulus legislation. The Health and Economic Recovery Omnibus Emergency Solutions Act (HEROES Act) is a $3 trillion bill from sponsors in the House of Representatives. The HEROES Act includes provisions for rental assistance, subsidized child care, hazard pay for front-line workers, extended unemployment eligibility, and extended suspension of federal student loan interest and payment obligations. The Health, Economic Assistance, Liability Protection, and Schools Act (HEALS Act) is a $1.1 trillion Senate bill providing essentially for lesser benefits for many of the same challenges.

Additionally, the Department of Labor's Wage and Hour Division posted FFCRA revisions, summarized in a press release published on September 11, 2020.[31] The revisions were made partially in response to an August decision in the U.S. District Court for the Southern District of New York. In the *State of New York vs. the United States Department of Labor*,[32] New York argued that several of the FFCRA's provisions unduly restricted paid leave. The court agreed with New York on three of its six substantive claims, thereby partially limiting the DOL's attempted reductions in federally subsidized paid leave.

As employers, workers, and every level of government struggle to manage the complex interaction between economic and public health challenges, it will remain especially important for taxpayers and tax preparers to monitor court decisions, legislative actions, and guidance from governmental agencies.

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[30] https://www.federalregister.gov/documents/2020/09/04/2020-19654/temporary-halt-in-residential-evictions-to-prevent-the-further-spread-of-covid-19

[31] At https://www.dol.gov/newsroom/releases/whd/whd20200911-2

[32] 20-CV-3020 (JPO) at https://www.nysd.uscourts.gov/sites/default/files/2020-08/State%20of%20New%20York%20v.%20United%20States%20Department%20of%20Labor%20et%20al%2C%2020-cv-3020%20%28JPO%29.pdf

Chapter 4 Review Questions

1. Out of the following choices, which was the earliest stimulus legislation and how much relief did it provide?

    A. Coronavirus Preparedness and Response Supplemental Appropriations Act, $8.3 billion total

    B. The Families First Coronavirus Response Act (FFCRA), $1 billion total

    C. The Paycheck Protection Program and Health Care Enhancement Act (Enhancement Act), $484 billion total

    D. The HEROES Act, $1 trillion total

2. Which of the following is *false* with respect to the Coronavirus Preparedness and Response Supplemental Appropriations Act?

    A. It provided $8.3 billion in relief

    B. **All funds were allocated domestically

    C. It was directed in part toward vaccine development

    D. It was directed in part toward evacuation preparedness

Answers to Chapter 4 Review Questions

Answer to question #1

A. That is correct! On March 6, 2020, the Coronavirus Preparedness and Response Supplemental Appropriations Act was enacted and provided $8.3 billion in relief.

B. This answer is incorrect. The FFCRA was not the first legislative response, and it provided $105 billion in relief (not just $1 billion).

C. This answer is incorrect. The Enhancement Act was enacted on April 24, 2020, and it was a $484 billion allocation intended to replenish CARES Act programs.

D. This answer is incorrect. There has been a bill introduced under this name, but it has not been approved.

Answer to question #2

A. This answer is incorrect. The Act *did* provide $8.3 billion in relief.

B. That is correct! Funds were allocated mostly domestically, but about 19 percent went abroad.

C. This answer is incorrect. The Act was directed in part toward vaccine development and procurement and for medical supplies.

D. This answer is incorrect. The Act was directed in part toward evacuation preparedness.

Glossary

Cafeteria plan	An employer-sponsored plan under which employees may choose to receive cash or qualified benefits that may be purchased with pre-tax income.
Coronavirus-related distribution	A coronavirus-related distribution is a distribution not exceeding $100,000 in the aggregate from a qualified retirement plan or IRA made in 2020 to an individual affected by the coronavirus and meeting certain conditions.
Defined benefit plan	A defined benefit plan is a qualified employee plan that is designed to provide participants with a definite, specified benefit at retirement.
Defined contribution plan	A defined contribution plan is a qualified employee retirement plan stated in terms of the employer’s contribution to it.
Early distributions	Early distributions—distributions from a qualified plan or IRA before the plan participant or IRA account holder becomes age 59 ½—are generally subject to a 10% penalty tax.
Economic Injury Disaster Loan (EIDL)	A Small Business Administration (SBA) program that is the principal means of federal assistance for repairing and rebuilding non-farm, private sector disaster losses.
Employee Retention Credit	Employee Retention Credit under the CARES Act encourages businesses to keep employees on their payroll. The refundable tax credit is 50 percent of up to $10,000 in wages and health plan expenses paid by an eligible employer whose business has been financially impacted by COVID-19.
Federal poverty level	A measure of income issued every year by the Department of Health and Human Services (HHS). Federal poverty levels are used to determine your eligibility for certain programs and benefits, including savings on Marketplace health insurance, and Medicaid and CHIP coverage.
Health savings account (HSA)	A trust created exclusively for the purpose of paying qualified medical expenses of an account beneficiary. Modeled after an Archer MSA, it requires an account beneficiary to purchase high-deductible health insurance.
High deductible health plan (HDHP)	Health insurance coverage having a high deductible that must normally be met before benefits are paid for covered charges.

Medicaid	Joint federal and state program to provide health insurance coverage to taxpayers whose income does not exceed the federal poverty level.
Pandemic Unemployment Assistance	Pandemic Unemployment Assistance (PUA) provisions of the CARES Act provide for federal unemployment benefits of $600 per week ***in addition*** to any state-provided unemployment assistance.
Paycheck Protection Program	A program managed by the U.S. Small Business Administration (SBA) designed to provide a direct incentive for small businesses to keep workers on the payroll.
Qualified improvement property	Any improvement to a non-structural, interior portion of a non-residential building as long as the improvement is placed in service after the building was first placed in service by any taxpayer.
Qualified medical expenses	Medical expenses for which a taxpayer may receive a tax deduction and which may be considered qualified medical expenses under various healthcare programs, such as medical flexible spending accounts (FSAs), HSAs and Archer MSAs.
Recovery rebate	Direct federal government payment to taxpayers.
Required minimum distribution	Required minimum distributions (RMDs) are distributions from most tax-favored retirement plans required annually once that person reaches age 72.
Rollover	The transfer of tax-deferred funds from a plan or account to another plan or account providing for tax-deferral. Such transfers are effected without the need to recognize any income for tax purposes.
Roth IRA	A **Roth IRA** is a personal retirement savings plan, funded by an annuity or a trust that meets certain requirements and which may permit non-deductible contributions, tax-deferral of earnings and tax-free distributions.
Section 1031 exchange	The sale of an investment property that is replaced by another in a manner that allows for capital gains on the sale to be deferred.
Section 911 Foreign Earned Income	Section 911 provides an exclusion from income for a portion of foreign earned income and housing costs for persons living in a foreign country.
Telehealth	A term that refers to the use of telecommunications technology to provide healthcare services.

Traditional IRA	A traditional IRA is a personal retirement savings plan, funded by an annuity or a trust that meets certain requirements and which may permit tax-deductible contributions and tax-deferral of earnings.

Index

Appendix

Paycheck Protection Program
PPP Loan Forgiveness Application Form 3508S

OMB Control No. 3245-0407
Expiration date: 10/31/2020

A BORROWER MAY USE THIS FORM ONLY IF THE BORROWER RECEIVED A PPP LOAN OF $50,000 OR LESS.
A Borrower that, together with its affiliates, received PPP loans totaling $2 million or greater cannot use this form.

Business Legal Name ("Borrower")	DBA or Tradename, if applicable	
Business Address	Business TIN (EIN, SSN)	Business Phone
		( ) -
	Primary Contact	E-mail Address

SBA PPP Loan Number: ____________________ **Lender PPP Loan Number:** ____________________

PPP Loan Amount: ____________________ **PPP Loan Disbursement Date:** ____________________

Employees at Time of Loan Application: __________ **Employees at Time of Forgiveness Application:** __________

EIDL Advance Amount: ____________________ **EIDL Application Number:** ____________________

Forgiveness Amount: ____________________

By Signing Below, You Make the Following Representations and Certifications on Behalf of the Borrower:

The Authorized Representative of the Borrower certifies to all of the below by **initialing** next to each one.

_____ The dollar amount for which forgiveness is requested does not exceed the principal amount of the PPP loan and:

- was used to pay costs that are eligible for forgiveness (payroll costs to retain employees; business mortgage interest payments; business rent or lease payments; or business utility payments);
- includes payroll costs equal to at least 60% of the forgiveness amount;
- if a 24-week Covered Period applies, does not exceed 2.5 months' worth of 2019 compensation for any owner-employee or self-employed individual/general partner, capped at $20,833 per individual; and
- if the Borrower has elected an 8-week Covered Period, does not exceed 8 weeks' worth of 2019 compensation for any owner-employee or self-employed individual/general partner, capped at $15,385 per individual.

_____ I understand that if the funds were knowingly used for unauthorized purposes, the federal government may pursue recovery of loan amounts and/or civil or criminal fraud charges.

_____ The Borrower has accurately verified the payments for the eligible payroll and nonpayroll costs for which the Borrower is requesting forgiveness, and has accurately calculated the forgiveness amount requested.

_____ I have submitted to the Lender the required documentation verifying payroll costs, the existence of obligations and service (as applicable) prior to February 15, 2020, and eligible business mortgage interest payments, business rent or lease payments, and business utility payments.

_____ The information provided in this application and the information provided in all supporting documents and forms is true and correct in all material respects. I understand that knowingly making a false statement to obtain forgiveness of an SBA-guaranteed loan is punishable under the law, including 18 USC 1001 and 3571 by imprisonment of not more than five years and/or a fine of up to $250,000; under 15 USC 645 by imprisonment of not more than two years and/or a fine of not more than $5,000; and, if submitted to a Federally insured institution, under 18 USC 1014 by imprisonment of not more than thirty years and/or a fine of not more than $1,000,000.

_____ The tax documents I have submitted to the Lender are consistent with those the Borrower has submitted/will submit to the IRS and/or state tax or workforce agency. I also understand, acknowledge, and agree that the Lender can share the tax information with SBA's authorized representatives, including authorized representatives of the SBA Office of Inspector General, for the purpose of ensuring compliance with PPP requirements and all SBA reviews.

_____ I understand, acknowledge, and agree that SBA may request additional information for the purposes of evaluating the Borrower's eligibility for the PPP loan and for loan forgiveness, and that the Borrower's failure to provide information requested by SBA may result in a determination that the Borrower was ineligible for the PPP loan or a denial of the Borrower's loan forgiveness application.

The Borrower's eligibility for loan forgiveness will be evaluated in accordance with the PPP regulations and guidance issued by SBA through the date of this application. SBA may direct a lender to disapprove the Borrower's loan forgiveness application if SBA determines that the Borrower was ineligible for the PPP loan.

______________________________________ ____________________
Signature of Authorized Representative of Borrower Date

______________________________________ ____________________
Print Name Title

SBA Form 3508S (10/20)