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## Business-Related Tax Changes Made by the Coronavirus Aid, Relief, and Economic Security Act (CARES Act)

**Legal Update**

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The Coronavirus Aid, Relief, and Economic Security Act (P.L. 116-136) (CARES Act) signed into law on March 27, 2020, makes important changes to certain key tax provisions for businesses affected by COVID-19. Many of these changes are effective retroactive to prior tax years and may impact tax returns for 2019 that are yet to be filed. In addition, some taxpayers may need to file amended tax returns in order to take advantage of these changes. Future IRS guidance will likely be needed to implement many of these changes.

For a summary of the employment-related tax changes made by the CARES Act, please see "COVID-19: What the CARES Act Means to Employers."

### Increase in Business Interest Deductions for 2019 and 2020

The Tax Cuts and Jobs Act of 2017 (TCJA) modified Section 163(j) of the Internal Revenue Code of 1986, as amended (Code), to add a new limitation on deductions for business interest. Under Section 163(j) of the Code, deductions for business interest are generally limited to 30 percent of adjusted taxable income for such year.

Taxpayers engaged in certain real property businesses, such as real estate development, construction, rental, management or brokerage businesses, are permitted to elect out of the limitations of Section 163(j) of the Code. However, taxpayers that make this election are required to use the alternative depreciation system for their nonresidential real property, residential real property and qualified improvement property.

The CARES Act generally increases the Section 163(j) limit on the deductibility of business interest to 50 percent of adjusted taxable income effective for taxable years beginning in 2019 and 2020. In addition, for taxable years beginning in 2020, businesses may elect to use their 2019 adjusted taxable income, instead of 2020 adjusted taxable income (which may be lower than 2019 due to COVID-19) for purposes of computing their business interest deductions.

The CARES Act includes special rules for partnerships. For any taxable year of a partnership beginning in 2019, the business interest expense deduction would generally be limited to 30 percent of adjusted taxable income, and for taxable years beginning in 2020, the limitation would be 50 percent. However, unless a partner elects out, if the partner has interest expense deductions allocated to them for 2019 that are limited by Section 163(j) (so-called “excess business interest”), 50 percent of that excess business interest would be available to be deducted in 2020 without regard to the limitations of Section 163(j) of the Code, and the remaining 50 percent of such excess business interest would be carried forward to 2020 and would be subject to the general limitations of Section 163(j) of the Code.

The special rules for partnerships are likely intended to provide relief to taxpayers without requiring amended tax returns which, under the centralized partnership audit regime that took effect in 2018, partnerships are unable to file.

## Technical Corrections for Qualified Improvement Property

The TCJA increased the deduction for bonus depreciation from 50 percent to 100 percent for certain qualified property with a recovery period of 20 years or less. In addition, the TCJA eliminated definitions for qualified improvement property, qualified restaurant property and qualified retail improvement property, and replaced these definitions with a single category called “qualified improvement property.” Congress intended that qualified improvement property would have a 15-year recovery period. However, this was not reflected in the relevant statutory language. As a result, since the TCJA, qualified improvement property has been treated as nonresidential rental property with a 39-year recovery period and ineligible for bonus depreciation.

The CARES Act corrects the technical error made by the TCJA and provides that qualified improvement property is 15-year property for depreciation purposes, which makes qualified improvement property eligible for bonus depreciation. The technical correction made by the CARES Act is effective retroactively as if included in the TCJA.

If permitted by future IRS guidance, taxpayers engaged in real property businesses that elected out of the limitations of Section 163(j) of the Code may want to reconsider that election if they acquired qualified improvement property that would otherwise be eligible for bonus depreciation as a result of the technical corrections made by the CARES Act.

## Modifications to Net Operating Loss Carrybacks and Carryforwards

As a result of changes made by the TCJA, net operating losses (NOLs) are generally required to be carried forward (i.e., generally may not be carried back) and may only be deducted to the extent of 80 percent of taxable income.

The CARES Act removes the NOL carryback limitation for NOLs arising in taxable years beginning after December 31, 2017, and before January 1, 2021 (i.e., 2018, 2019 and 2020 for calendar year taxpayers), and allows NOLs arising in such years to be carried back to the five taxable years preceding the taxable year of the loss.

The CARES Act also removes the 80 percent of taxable income limitation on NOL deductions for taxable years beginning after December 31, 2017, and before January 1, 2021.

After 2020, the 80 percent of taxable income limitation would apply to deductions for NOLs. The CARES Act clarifies that for purposes of this limitation, taxable income would be determined without regard to deductions under Sections 199A and 250 of the Code and after taking into account any pre-2018 NOL carryforwards. In addition, NOLs arising in a taxable year beginning on or after January 1, 2021, would generally not be eligible to be carried back.

## Modification to Excess Business Loss Limitations

The TCJA generally limited deductions for business losses of noncorporate taxpayers, or excess business losses, to \$250,000, as adjusted for inflation, for taxable years beginning after December 31, 2017, and before January 1, 2026. The CARES Act modified the effective date of the excess business loss limitations to taxable years beginning after December 31, 2020, retroactively to the TCJA effective date. Thus, for calendar year taxpayers, the excess business loss limitations would not apply for 2018, 2019 and 2020. The CARES Act also made certain other clarifying changes to the excess business loss provisions.

## Accelerated Recovery of Corporate Alternative Minimum Tax Credits

The CARES Act allows corporations to claim an accelerated refund with respect to any remaining alternative minimum tax (AMT) credit carryovers. The corporate AMT tax was repealed by the TCJA.

## Next Steps

Taxpayers that may be eligible for relief granted by the CARES Act should seek advice based on the taxpayer's own facts and circumstances. We are closely monitoring tax-related developments relating to COVID-19 and are available to assist clients that may be impacted by COVID-19.

## Contact Us

For further information or inquiries, please contact Mark Salsbury or John Erhart.