Insight

Tax Provisions in the Coronavirus Aid, Relief, and Economic Security (CARES) Act

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Executive Summary

- The CARES Act includes substantial – in excess of $100 billion – individual tax rebates and a delay in the April 15 tax-filing deadline, among other relief provisions.
- The Act also includes business tax provisions, including a change to the tax treatment of business losses, delays in estimated tax payments, and some technical corrections to the Tax Cuts and Jobs Act.
- Combined, the individual and business tax provisions provide a substantial fiscal response to the COVID-19 pandemic.

Introduction

On March 19, the Senate majority introduced "phase 3" of the legislative response to the COVID-19 pandemic, the Coronavirus Aid, Relief, and Economic Security (CARES) Act. The Act includes forgivable loans to small businesses, direct payments and tax relief for individuals, tax relief for businesses, financial assistance for vulnerable industries, additional health funding and policy, and additional assistance for financial markets. With respect to the tax provisions, the bill provides direct payments, among other provisions, to individuals at a time when millions of Americans will likely face disruptions to their employment. The bill also provides business tax relief, including the delay of certain tax payments, as well as a number of adjustments and technical corrections to changes made by the Tax Cuts and Jobs Act (TCJA).

Individual Tax Provisions

Direct Payments

The CARES Act provides direct payment to individuals and families. For individuals with incomes up to $75,000, the Act provides a $1,200 payment, phasing out at a rate of 5 percent for every $100 in income above $75,000. The payment is thus phased out entirely for an individual making $99,000. Married couples with combined incomes up to $150,000 would receive $2,400, subject to the same phaseout as that applying to individuals. Thus, for married couples making $198,000, the payment would be phased out. The provision also provides an additional $500 per child, though also subject to phaseout. Eligibility and benefit levels would be based on 2018 income tax filings.

For individuals and families with low or zero net tax liabilities – such as low-income retirees – the benefit is more limited. The rebate is limited to the *lesser* of a taxpayer's tax liability, such that an individual with a tax liability of less than the rebate would receive a rebate in the amount of their net tax liability (in 2018), but no less than $600. Individuals must have had at least $2,500 in income in 2018 to be eligible.

According to the Internal Revenue Services' Statistics of Income, there were about 80 million taxpayers with taxable income tax returns in those income brackets in 2017. Accordingly, this policy will cost in excess of $100 billion.

Additional Income Tax Provisions

In addition to the direct payments, the Act provides additional relief to individuals and families. The Act delays the regular tax filing deadline of April 15 until July 15. This provision complements actions already taken by the Treasury to allow taxpayers to delay any tax payments due. Additionally, consistent with other disasters, the Act waives the 10 percent early withdrawal penalty for qualifying individuals, who may withdraw up to $100,000 from retirement accounts without facing penalty. The Act provides for flexible tax treatment of that withdrawal and allows taxpayers to restore any withdrawn funds. Last, the Act would enhance charitable giving, by providing individuals with a new $300 above-the-line deduction on charitable donation and increasing previously enacted limitations on charitable deductions.

Business Provisions

The Act contains nine major business relief tax provisions that broadly hew to three categories: delayed tax payments, relief from certain TCJA provisions, and technical corrections to the TCJA. The Act would allow employers (including the self-employed) to delay the payment of the employer portion of the Social Security payroll tax. Under current law, employers pay a 6.2 percent rate on covered employee payroll. Under the proposal, employers would be able to defer the payment for the remainder of the year and pay back the liability over the next two years. The Social Security trust fund would be made whole from the reduced payments with a general fund transfer – essentially additional borrowing. The Committee For a Responsible Federal Budget estimated that the cost of these forgone payments would amount to $275 billion, but under this provision those payments would ultimately be restored in future years. The Act would allow corporations to delay estimated tax payments until October 15 of 2020. Combined, these provisions should provide firms with additional cash flow as economic conditions further deteriorate.

The Act also provides businesses with additional tax relief by temporarily unwinding some of the revenue-raising reforms in the TCJA. One such reform was the limitation on net operating losses. Prior to the enactment of the TCJA, firms could deduct net operating losses (NOLs) to smooth out income tax payments both in the recent past (two years) and in the future. The TCJA eliminated the ability of firms to "carry-back" losses and offset prior years' income taxes, and thus receive a rebate. The TCJA further limited the share of taxable income that can be offset by NOLs. The proposal would allow businesses to carry-back an NOL from 2018, 2019, or 2020 for 5 years – thus a firm could use a loss realized in 2020 to reduce a tax liability as far back as 2015. The proposal also eliminates the income limitation on the deduction. In sum, this proposal, which was also expanded to include pass-through entities, is designed to enhance firms' liquidity during the COVID-19 crisis.

The CARES Act proposes to temporarily unwind two additional TCJA provision. The TCJA eliminated the corporate alternative minimum tax (AMT). Payment of the corporate AMT had generated credit against future payments. When the corporate AMT was repealed, these credits – $10.2 billion – were made refundable over the next several years. The CARES Act allows firms to accelerate recovery of these payments. Last, the Act would loosen one of the larger revenue raisers in the TCJA. Prior to the TCJA, firms could deduct interest on loans. The TCJA reduced the deductibility of interest to 30 percent of a firm's taxable income, raising about $250 billion over the next 10 years. The CARES Act would relax that limitation to 50 percent for the next two years.

Finally, the CARES Act includes three technical corrections to the TCJA. Specifically, the Act would correct an error that requires certain firms to depreciate investment over a longer period than was intended by Congress. The Act would allow firms to collect refunds due from overpayments of the Section 965 deemed repatriation tax. The Cares Act would also correct an error that leads to undue over-taxation of certain foreign subsidiaries. As technical corrections, these fixes would not have a "scorable" cost.

Conclusion

The CARES Act is the third phase of Congress's response to the COVID-19 pandemic. In addition to significant other interventions, the Act provides significant tax relief – including at least $100 billion in payments to individuals and families. The CARES Act provides significant administrative and liquidity enhancements for firms. While the costs are substantial, this is likely not the last fiscal intervention Congress will need to enact as the United States grapples with the current crisis.