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COVID-19: U.S. Senate Passes US$2 Trillion COVID-19 Stimulus Bill

On March 25, 2020, the United States Senate unanimously voted to pass the *Coronavirus Aid, Relief and Economic Security Act* or the "CARES Act". The House of Representatives is currently expected to vote on the legislation on the morning of Friday, March 27, 2020. The CARES Act is the largest single government stimulus in the history of the United States, comprising an estimated greater than US$2 trillion in relief, which takes the form of a sweeping array of measures including, among others, direct payments, delays of repayment on student loans (without interest), increased benefits, loans, guarantees, government investment and tax relief.

The CARES Act is in addition to two recent emergency measures enacted this month which have been dubbed the "*Coronavirus Preparedness and Response Supplemental Appropriations Act, 2020*" and the "*Families First Coronavirus Response Act*", which included aggregate funding of over US$108 billion and targeted, among other things, emergency health and sick leave, food assistance, unemployment benefits and a supplement to healthcare. The latter measure also exempted companies with over 500 employees from providing paid medical and sick leave.

The following is a brief summary of selected measures under the CARES Act.

I. Financial Aid

<u>Lending Program</u>. Congress additionally allocated US$500 billion in loans, guarantees or investments for distressed companies, which includes:

- US$25 billion for the U.S. airline industry;
- US$25 billion for passenger air carriers;
- US$4 billion for cargo air carriers; and
- US$17 billion for businesses in national security.

Loans will be provided with a maximum term of five years with interest to be determined based on risk and current average yield on comparable outstanding U.S. obligations. Businesses with between 500 and 10,000 employees will have a maximum annualized interest rate of 2% and will not be required to make any payments under these loans for the first six months.

An eligible business must be domiciled and have both significant operations and a majority of its employees in the United States. In addition, the business must be distressed such that it has incurred or is expected to incur significant losses that would put continuing operations in jeopardy. As a condition to these loans, businesses who receive them have restrictions on, among other things, issuing dividends, making capital distributions or purchasing stock listed on a national securities exchange for a year after the loan has been paid off and will also have to retain 90% of their employment levels as of March 24, 2020 through the third quarter of 2020, to the extent practicable. Congress set more stringent rules for mid-sized businesses with between 500 and 10,000 employees, with eligibility requirements including, among others:

- the recipient intends to restore at least 90% of its workforce as at February 1, 2020 by the end of the four-month period following the end of the declared public health emergency;
- the recipient cannot be a debtor in a bankruptcy proceeding;

- for the duration of the loan and two years following termination, the recipient will not outsource or offshore jobs or abrogate any existing collective bargaining agreements; and

- the recipient will remain neutral in any union organizing efforts for the duration of the loan.

In addition to the above requirements, recipients of such loans must also adhere to certain limitations on employee remuneration during the period of the loan and an additional year following its termination. For this period, a recipient employer will be required to agree that it will not:

- increase the compensation of any employee whose total compensation in calendar 2019 exceeded US$425,000 for any consecutive 12-month period;

- pay any severance of other benefits to such employees upon termination that exceed twice the maximum total 2019 compensation received by that employee; and

- pay more than US$3 million plus 50% of the amount an employee who earned more than US$3 million in calendar year 2019 to such employee for any consecutive 12-month period.

Procedures to apply for assistance under this program have not yet been determined and are to be published within 10 days of the enactment of the CARES Act.

The lending program will have an independent congressional oversight committee and will be unavailable to businesses with at least 20% ownership by federally elected officials and certain of their family members.

<u>Small Business Assistance</u>. Congress allocated approximately US$350 billion for small businesses (under 500 employees with some exceptions based on industry standards), independent contractors, sole proprietors and self-employed individuals. Funding will take the form of federally-guaranteed debt. This debt may be forgivable if such businesses maintain certain employment levels through the first half of 2020.

A borrower will need to certify a number of items including that the loan will be necessary to support ongoing operations and provide an acknowledgement that funds will be used to retain workers and maintain payroll or make certain other business payments. In addition, a borrower need not be unable to obtain credit from other sources to qualify to receive a covered loan.

The maximum interest rate under a covered loan is 4% and there will be no prepayment penalties. Covered loans may also be long term, as maturity will be capped at 10 years from the date of an application for forgiveness. In addition, payment of principal and interest will be deferred for a minimum of six months to a maximum of one year.

Loans will be provided up to the lesser of US$10 million or 2.5 times the business's average total monthly payroll cost for the previous year (or for newer businesses, based on payroll from January 1 to February 29, 2020). Such loans will not require any collateral or personal guarantees and use of proceeds will be for wages and other business expenses incurred in a covered period from February 15, 2020, through June 30, 2020. It will not cover prorated salaries for employees making over an annualized US$100,000 or employees with a principal residence outside of the United States.

The CARES Act specifically allows for forgiveness of covered loans. Such amount may be subject to reduction based on average number of full-time employees employed per month for a set period and reductions in salaries. Appropriate documentation will be required.

Implementing procedures will be published within 15 days of enactment.

II. Taxation Changes

Refundable Payroll Tax Credit. The CARES Act provides a quarterly refundable payroll tax credit for half of "qualified wages" paid by those employers (i) whose operations were fully or partially suspended due to a COVID-19 related governmental shutdown order, or (ii) during a period beginning in a calendar quarter where gross receipts declined by more than 50% compared to the same quarter of the previous year and ending with a calendar quarter which gross receipts exceeded 80% of the same quarter of the previous year. For employers with greater than 100 full-time employees, qualified wages are those wages paid when not providing services due to the circumstances above. For employers with 100 or fewer full-time employees, qualified wages include all wages regardless of the circumstances.

The credit is provided for the first $10,000 of compensation including health benefits paid to an eligible employee for wages paid or incurred from March 13, 2020 to December 31, 2020.

Social Security Tax Deferral. Employers and self-employed individuals will be able to defer payment of the 6.2% employer portion of the Social Security Tax on employee wages. Half will become due for the 2021 taxation year with the other half for 2022. This provision may defer payment of a tax for which credits can be currently claimed.

Net Operating Losses (NOLs). Described as a temporary repeal, NOLs arising in a tax year beginning in 2018, 2019, or 2020 can be carried back five years and the Act temporarily removes the taxable income limitation which will allow the NOL to fully offset income.

Pass-through Loss Limitations. The CARES Act modifies the *Tax Cut and Jobs Act* (the "**TCJA**") to halt the limitation on non-corporate tax deductions for excess business and farm losses. In the case of the latter, the TCJA change is removed retroactive to the end of 2017 and accordingly companies may be able to file amended returns to claim a refund.

Alternative Minimum Tax (AMT). Corporate taxpayers subject to the AMT may accelerate and claim a refund of the entirety of its remaining AMT credits. The U.S. Department of Treasury will process such claims within 90 days.

Business Interest Expense Deduction. The limitation on business interest expense deduction increases from 30% of adjusted taxable income to 50% for the 2019 and 2020 tax years. In addition, businesses may elect to use 2019 adjusted taxable income to compute the 2020 deduction. For partnerships, the new 50% limit is unavailable for 2019.

Qualified Improvement Property (QIP). Technical errors in the TCJA were amended so that taxpayers may now file an amended return to expense the cost of QIP as bonus depreciation.

Excise Taxes. Federal excise taxes are waived for distilled spirits used in the production and distribution of hand sanitizer in accordance with 2020 guidelines issued by the U.S. Food and Drug Administration and related to COVID-19 and SARS-CoV-2. Additionally, certain aviation excise taxes are suspended through the date of the CARES Act and the end of 2020.

Retirement Funds. The CARES Act waives early withdrawal penalty for distributions of up to US$100,000 from qualified retirement accounts for coronavirus-related purposes made in 2020. Coronavirus-related purposes are specified as distributions to an individual who (i) either personally or whose spouse or dependent has been diagnosed with SRS-CoV-2 or COVID-19 by a CDC-approved test; or (ii) who experiences adverse financial consequences as a result of being quarantined, furloughed or laid off or having work hours reduced, or being unable to work due to lack of child care or closing or reduction of hours of a business owned or operated by the individual.

Income attributable to such distributions would be subject to tax over three years, and the taxpayer may recontribute the funds to an eligible retirement plan within three years without regard to that year's cap on contributions. Additionally, for 180 days following enactment of the CARES Act, the individual may borrow up to US$100,000 from his or her retirement plan. Finally, the CARES Act waives required minimum distributions for 2020.

Charitable Donations. There is a new US$300 allowance for above the line charitable contribution deductions, regardless that the taxpayer claims the standard deduction. In addition, there is a temporary suspension for 2020 of the 50% adjusted gross income limitation for individuals on charitable contributions for the 2020 taxation year and for corporations, the 10% limitation is increased to 25% of taxable income. The limitation of deductions for charitable contributions of food inventory also increases from 15% to 25%.

Education Assistance. For employer contributions made after passing of the CARES Act, up to US$5,250 made towards an employee's student loans or other educational expenses will not be counted towards the employee's income.

III. Direct Payment

The CARES Act provides for a one-time payment of up to US$1,200 to individuals and an additional US$500 to a parent per each "qualifying child" within the meaning of Section 24(c) of the *Internal Revenue Code of 1986*, as amended (the "**IRC**") (the definition of a qualifying child generally means children, siblings, stepsiblings or their descendants under the age of 17 whom the taxpayer lives with in the same principal abode for at least half of the taxation year and such qualifying child does not provide at least half of his or her own support). The payments are to be made with reference to an individual taxpayer's tax filings, which necessarily means that the US$500 per qualifying child will only be available to one filer whether as a single taxpayer or taxpayers filing jointly.

The amount of direct payment under the CARES Act is effectively set at up to US$1,200 per individual plus US$500 per qualifying child. Such amount is phased out at 5% of adjusted gross income above a set threshold depending on the taxpayer's filing status, being US$75,000 for an individual filer, US$150,000 for a joint filer and US$112,500 for a head of household filer. For an individual filer and a joint filer with no children, this means the amount fully phases out at US$99,000 and US$198,000, respectively. For a head of household filer with one child, full phase out will occur at US$146,500.

Notably, individuals in the above income ranges are above the national median, with estimates that approximately 90% of U.S. individuals will be eligible to receive full or partial payments. The delivery mechanism for the direct payments will be as an advance amount to be based on a taxpayer's 2019 income tax return (which filing deadline has since been postponed to July 15, 2020). If that has not yet been filed, it will be based on the 2018 income tax return. Finally, if neither have been filed, it will be based on the Form SSA-1099, Social Security Benefit Statement or Form RRB-1099, Social Security Equivalent Benefit Statement. Valid social security numbers must be provided for each individual and qualifying child on such forms.

To accomplish the mechanism of an advance amount, the CARES Act treats these direct payments as an advanced credit. This means when a taxpayer files for the 2020 tax year, he or she will go through the same computation that would determine the amount of the direct payment. If the amount the taxpayer would have been owed under the new computed amount exceeds the amount of the direct payment under the CARES Act, the taxpayer will get a credit against 2020 tax liability. Because of such timing, that would mean such taxpayers would not receive a top up on the direct payment until 2021, after filing his or her 2020 income tax return. The CARES Act does not provide for a recapture mechanism in the reverse scenario where the amount that would be owed under the new computed amount is lower than the amount of the actual direct payment.

Of primary concerns under this measure is how quickly individuals will be able to receive funds. The Secretary of the Treasury has indicated distributions would commence around April 6, 2020. However, based on previous similar programs, it may be more realistic to expect payments at a minimum beginning in three weeks for taxpayers who have authorized direct deposit information on file and a minimum of ten weeks for all other individuals.

IV. Unemployment Insurance

Highlights of the unemployment insurance provisions of the CARES Act include:

- up to a maximum of 39 weeks, expanded coverage for workers who are otherwise ineligible to receive unemployment compensation and are unable to work as a direct result of the COVID-19 pandemic;
- through July 31, 2020, an increase in benefits of US$600 per week; and
- an additional 13 weeks of coverage after regular benefits have been exhausted.

Expanded Coverage. A "covered" individual may receive benefits under the CARES Act for up to 39 weeks beginning on or after January 27, 2020 and ending on December 31, 2020. This definition has several requirements, including that he or she:

- must not be eligible to receive regular compensation or extended benefits pursuant to Section 2107 (an extended relief provision after regular unemployment insurance has been exhausted, with express requirement that such individual is not receiving compensation for a given week under Canadian unemployment compensation laws); and
- must provide self-certification of being able and available to work but for being unemployed, partially unemployed, unable or unavailable to work as a result of one of several enumerated conditions which generally relate to COVID-19.

Congress drafted fairly generous breadth for those affected by COVID-19 as the enumerated conditions referenced above include an expansive list of scenarios which would qualify an individual for benefits thereunder. They include and are not limited to situations where (i) the individual has presented symptoms and seeks a medical diagnosis; (ii) the individual, a household member, or a family member for whom the individual cares has been diagnosed with COVID-19; or (iii) a general inability to work or reach work due to COVID-19 related closures. An individual seeking to claim unemployment benefits should refer to the text of Section 2102(a)(3) for more information.

In addition, the CARES Act extends coverage to those who are self-employed, seeking part-time work, do not have sufficient work history or would not otherwise qualify for regular unemployment or extended benefits.

Notably, while Congress included financial support even for those who remain technically employed and retain health benefits through their employer, workers will not qualify for aid where he or she has the ability to telework with pay or receives sick or paid leave benefits.

Larger Payments. Covered individuals will receive an additional US$600 per week for up to four months. Unlike typical unemployment insurance benefits, the additional US$600 is a blanket amount and not tied to a limit based on percentage of previous income. State unemployment insurance prior to this measure ranged from US$200 to US$550 per week.

Extension. Benefits will be extended for an additional 13 weeks past the expiry of applicable state coverage through December 31, 2020. While many states have already begun to extend coverage in the wake of the pandemic, most states currently offer up to 26 weeks of coverage (with a range of between 12 weeks and 30 weeks). Until July 31, 2020, any extension under this provision will include the additional US$600 per week benefit.

Congress also allocated temporary funding for states which have enacted short-time compensation payment programs or will enact such programs through December 31, 2020. Effectively, such programs are those in which an employer will retain its employees but reduce overall hours with the reduction in pay to be covered by state unemployment benefits. More than half of the states have such programs already in place. Under these rules, the federal funding will not be available to replace wages of temporary, intermittent or seasonal workers. These new federal incentives may help to promote such programs as an alternative to layoffs.

The CARES Act is in addition to guidelines and rules regarding eligibility for unemployment insurance which have already been relaxed in the wake of the COVID-19 pandemic. Specifically, the United States Department of Labor (the "**USDOL**") issued guidance that an individual may qualify where (i) an employer temporarily ceases operations due to COVID-19, preventing employees from coming to work; (ii) an individual is quarantined with the expectation of returning to work after the quarantine is over; or (iii) an individual leaves employment due to a risk of exposure or infection or to care for a family member.

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