Coronavirus Aid, Relief and Economic Security CARES Act

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In the last two months our personal lives and our business lives have been completely altered. All of the closely held businesses and the industries that we work with have been devastated financially because of this COVID-19 worldwide pandemic. In this article we have tried to outline briefly ideas that can be used by businesses, business owners, business employees, and others affected by this coronavirus.

The index below outlines ideas for business owners and employees that you need to read immediately pertaining to the new law that was passed by Congress last week and signed by the president on Friday. In order to implement sections of this new law and all of our business planning ideas you need to consult with several individuals.

First, make sure that your business accountant has read the CARES Act. Your accountant is going to be a very important source of information for you to qualify for different sections of the new tax law outlined below.

Second, your corporate attorney can also be helpful in preparing any documents to qualify for parts of the new tax law.

Third, for all of the industries that Castle Wealth Advisors specializes in, we will make ourselves available to talk with business owners and association leaders about ideas that will help everyone through this pandemic disaster with financial ideas to implement.

Fourth, there are a lot of national organizations that have quickly gotten themselves ready to help you. Consider asking your local Chamber of Commerce if they have someone on staff who can help you apply for benefits from this new CARES Act. Consider contacting the National Federation of Independent Businesses and find out if they have a local office that can help you. Also, you might think about the SCORE Association which has offices in many cities and states.

Fifth, contact your state Small Business Administration (SBA) and find out if they have a local field office near you. Many of the CARES Act provisions for small businesses will be handled by the SBA.

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I. IDEAS FOR BUSINESSES

PAYCHECK PROTECTION PROGRAM & FORGIVABLE LOANS

A significant benefit included in the CARES Act for small business owners is the paycheck protection program, a partially forgivable loan program offered through the Small Business Administration. Such loans must be issued by December 31, 2020 and can have a maximum maturity of 10 years. They may be provided through existing approved SBA lenders, (local banks) as well as lenders who are otherwise certified by the SBA to offer such loans. Furthermore, such loans will be 100% guaranteed by the SBA.

QUALIFYING FOR THE PAYCHECK PROGRAM

Businesses, including Sole-Proprietors that have fewer than 500 employees are eligible for this relief (food service businesses also qualify if they employ fewer than 500 people per physical location).

Under this paycheck protection program, lenders will generally be able to issue 7(a) small business loans up to a maximum of the lesser of $10,000,000 or 2.5 times the average payroll cost per month over the previous year (excluding annual compensation of amounts over $100,000 per person). The proceeds of such loans may be used to pay a variety of costs including:

- Payroll costs
- Group health insurance premiums and other healthcare costs
- Salaries and/or commission
- Rent
- Mortgage interest
- Utilities
- Other business interest incurred prior to February 15, 2020

SBA Emergency Loan Checklist

Step One: Go to SBA.com

Step Two: Go to SBA Disaster Loan

Step Three: Read and download the application

Step Four: Fill out the application

Step Five: Submit application to SBA or your bank

BENEFITS OF LOANS ISSUED UNDER THE PAYCHECK PROTECTION PROGRAM

The single largest benefit of a loan issued under the Paycheck Protection Program is the possibility of having all, or a portion of the loan forgiven. The amount eligible to be forgiven is the amount spent, during the first eight weeks after the loan is made, on:

- Payroll costs, excluding prorated amounts for individuals with compensation greater than $100,000
- Rent pursuant to a lease in force before February 15, 2020.
- Electricity, gas, water, transportation, telephone, or internet access expense for services which began before February 15, 2020
- Group health insurance premiums and other healthcare costs

There is a catch to these provisions. In order for the above amounts to be forgiven the business must maintain the same number of employees (or equivalents) from February 15, 2020 through June 30, 2020 as it did during either the same period in 2019, or from January 1, 2020 until February 15, 2020. To the extent this requirement is not met, the amount eligible for forgiveness will be reduce ratably. Additional reductions in the amount to be forgiven will be incurred if employees with under $100,000 of compensation have their compensation cut by more than 25% as compared to the most recent quarter. Good news, any debt forgiven pursuant to this provisions is not included in taxable income for the year.

Finally, payments from loans made under the Paycheck Protection Program will be deferred for a period of not less than six months, and no longer than one year.

QUALIFYING FOR EMPLOYEE RETENTION CREDIT

The “trigger” for a company to begin to be eligible for the credit is either that operations of the company have

been fully or partially suspended during a quarter as a result of governmental authority, or a quarter in which the revenue in 2020 that has less than 50% of the revenue from the same quarter in 2019. Remember when calculating the business income for the quarter the Act refers to the revenue for the quarter and not profit.

CALCULATING THE EMPLOYEE RETENTION CREDIT

For business planning purposes, it is important for employers to not only understand that they are eligible for a credit, but also to know how much of a credit they are eligible for, as this will help you make better business decisions. In the simplest terms, the credit is equal to 50% of the wages paid to each employee, up to a maximum of $10,000 of wages per employee.

For small businesses (100 or fewer employees), all wages (up to the $10,000 maximum limit per employee) are eligible to count towards the credit.

DEFERRAL OF PAYMENT OF PAYROLL TAXES

Section 2302 of the CARES Act provides employers with another payroll relatedtax break. With the exception of employers who have debt forgiven by the CARES Act for certain loans provided by the SBA, employers are eligible to defer payroll taxes from the date of the enactment, through the end of the year until the end of 2021 and 2022.

More specifically, 50% of the payroll taxes that would otherwise be due during this period, may be deferred until December 31, 2021. The remaining 50% is due on December 31, 2022.

Good news for self-employed persons. This relief applies to them also, at least with respect to the employer equivalent portion of their self-employed taxes. Accordingly, 50% of an individual's self-employment taxes from the date of enactment through the end of 2022 may be deferred, with 50% of that amount (so 25% of the 2020 self-employment taxes) due December 31, 2021 with the remaining deferral amount due on December 31, 2022.

NET OPERATING LOSS RULES HAVE CHANGES

This could be a very important benefit for business owners in 2020. Please discuss this idea in great detail with your outside accounting firm.

Section 2303 of the CARES Act amends the rules for corporations with net operating losses (NOLs). For many years, NOLs were allowed to be carried back up to two years, and forward up to 20 years. The Tax Cuts and Jobs Act of 2017 changed those rules, however, for 2018, 2019 or 2020, to allow such losses to be carried back

five years and forward indefinitely. In theory, this should allow companies to reduce prior years tax bills, allowing them to claim refunds of amounts previously paid, to provide further liquidity to get them through this coronavirus crisis.

The CARES Act further enhances the ability of companies to use their NOLs to offset prior years tax liabilities by amending another rule put into place by the TCJA. Under this act, NOLs were only able to offset up to 80% of taxable income. Section 2303 of the CARES Act amends the law to allow for up to 100% of taxable income to be offset for 2018, 2019, and 2020.

II. IDEAS FOR TAXPAYER/FAMILY

CALCULATING THE AMOUNT OF A TAXPAYER'S RECOVERY REBATE ADVANCE

The CARES Act provides a refundable income tax credit against 2020 income of up to $2,400 for married couples filing a joint return, while all other filers begin with a refundable credit of up to $1,200. The credit amount then increased by up to $500 for each child the taxpayer has under the age of 17.

Thus, a single taxpayer with one child would be eligible for up to $1,200 plus $500 equals $1,700 refundable credit. A married couple with one child and who file a joint return would be eligible for up to $2,400 plus $500 equal $2,900 credit.

There is an income limit to these taxpayer credits. As a taxpayers income begins to exceed their applicable threshold, their potential recovery rebate payment begins to phase out. Specifically, for every $100 a taxpayer's income exceeds their credit, their potential recovery rebate will be reduced by $5.

The applicable AGI threshold amounts are as follows:

- Married joint: $150,000
- Head of Household: $112,500
- All other filers: $75,000

HOW WILL RECOVER REBATES BE DISBURSED?

This may be complicated. The initial amount paid will be based on either a taxpayers 2018 or 2019 income tax return (whichever is the latest return that the IRS has on file), while it will ultimately be corrected if the taxpayer is owed money based on their actual 2020 income.

In other words, Congress is going to "front" taxpayers an estimated amount based on their 2018/2019 incomes, but if your 2020 return shows they really deserved it, they will get it later.

Income is far from the only thing that may change over time. For example, there were about 3.8 million children born in 2019 that won't show up on a 2018 tax return. The parents would not be getting the $500 recovery rebate for that new child. Marriages and divorces have occurred and people have died in the last six to 12 months. All of these changes will impact these families' recovery rebate payments.

<u>WHEN AND HOW THE RECOVERY REBATE ADVANCES WILL BE PAID?</u>

The urgency with which some taxpayers need income cannot be overstated. For them, the recovery rebate cannot come quickly enough. Unfortunately, it's likely to be at least a month, if not more before such payments will actually be received. The CARES Act requires that these payments be made as soon as possible, but the Treasury Department says that it may not happen until May.

How the recovery rebate payments will be made depends. It appears that individuals receiving social security benefits will receive their recovery rebate in the same account they receive the social security benefits. The CARES Act also authorizes Recovery rebate payments to be made to the account into which a taxpayer's 2018/2019 refund was deposited. Other payments will be sent to the last known address on file. Talk with your outside accounting firm and ask them to help you quickly get your business checking account or personal checking account on file with the IRS or the Social Security Administration. If you have recently changed banks or moved to a different state, talk to your accounting firm as soon as possible.

<u>INCREASED ACCESS TO RETIREMENT FUNDS</u>

For those of you that have a traditional IRA, SEP IRA, SIMPLE IRA, 401(k), 403(b), and government 457(b) plans, read this section carefully. We recommend that you not withdraw funds from any type of qualified account except as the last choice. The Coronavirus Related Distributions are distributions of up to $100,000 made from IRA's, employer-sponsored retirement plans, or a combination of both, which are made in 2020 by an individual who has been impacted from the coronavirus because they:

- Have been diagnosed with COVID-19, or
- Have a spouse or dependent that have been diagnosed with COVID-19, or
- Experienced adverse financial consequences as a result of being quarantined, or
- Furloughed, being laid-off, or having work hours reduced because of the disease, or
- Are unable to work because they lack childcare as a result of the disease, or
- Own a business that has closed or operated under reduced hours because of the disease, or
- Meet some other reason that the IRS decides to say is okay.

Given the long list of potential individuals who may qualify for relief under this provision, it seems rather clear that congressional intent was to make the provision broadly available. The IRS will likely operate in-kind and take a liberal view of who has been impacted by the coronavirus enough to qualify for a Coronavirus Related Distribution.

There are a number of potential tax benefits associated with Coronavirus Related Distributions. These benefits include:

- Exempt from the 10% penalty – individuals under the age of 59.5 may access retirement funds without the normal penalty that would otherwise apply.
- Not subject to mandatory withholding requirements – typically eligible rollover distributions from employer sponsored retirement plans are subject to mandatory federal withholding of at least 20%. Coronavirus Related Distributions, however, are exempt from this requirement. Plans can rely on a participant's self-certification that they meet the requirements of a Coronavirus Related Distribution when processing a distribution without mandatory withholding.
- Eligible to be repaid over three years – beginning on the day after an individual receives a Coronavirus Related Distribution, they have up to three years to roll or any portion of the distribution back into a retirement account.
- Income may be spread over three years - by default, the income from a Coronavirus Related Distribution is split evenly over 2020, 2021, and 2022. A taxpayer can, however, elect to include all of the income from a Coronavirus Related Distribution in their 2020 income. This may be a good idea if the taxpayer's income is close to zero this year. However, as I stated above, we do not recommend dipping into one of your retirement accounts unless you absolutely have to. Remember, most retirement accounts are down in value at this time. If possible, leave these retirement accounts alone and let them rise in value over time.

EMPLOYER-SPONSORED RETIREMENT PLANS

Many employer-sponsored retirement plans, such as 401(k)s, and 403(b)s offer participants the option of taking a loan of a portion of their retirement assets. For individuals who have been impacted by the coronavirus, the CARES Act enhances the regular plan loan rules in the following three ways:

- Maximum loan amount is increased to $100,000 – in general the maximum amount that may be borrowed from an employer plan is $50,000. The CARES Act doubles that amount for affected individuals.
- 100% of the vested balance may be used – in general, once an individual has a vested plan balance that

exceeds $20,000 they are only eligible to take a loan of up to 50% of that amount, normally not to exceed $50,000. The CARES Act amends this rule for affected individuals allowing them to take a loan equal to their vested plan balance, dollar for dollar, up to the $100,000 maximum amount.

- Delay of payments – any payments that would otherwise be owed on the plan loan from the date of enactment through the end of 2020 may be delayed for up to one year.

REQUIRED MINIMUM DISTRIBUTIONS (RMDs) ARE WAIVED IN 2020

This is a very interesting provision for all taxpayers over the age of 70.5, or under the new law age 72. If you are currently eligible for RMDs then you should read this carefully.

Section 2203 of the CARES Act amends IRC Section 401 (a) (9) to suspend required minimum distributions (RMDs) during 2020. The relief provided by this provision is broad, and applies to traditional IRA's, SEP IRA's, SIMPLE IRA's as well as 401(k)s, 403(b)s, and 457(b) plans. Furthermore, the relief applies to both retirement account owners, themselves, as well as to beneficiaries taking distributions.

If you need to take some income from a retirement account to pay your bills, we recommend that you take the bare minimum and leave as much cash in your retirement accounts so that it can grow for the future. This idea only applies to 2020.

RETURNING UNWANTED 2020 RMDs THAT HAVE BEEN DISTRIBUTED

We are only through the first quarter of the year, but some individuals have already taken their RMD for 2020. Now in light of the CARES Act these individuals may wish to "return" unwanted and no longer necessary RMDs.

For IRA's and 401(k) plans and other retirement account owners, this may be possible two different ways. If the RMD distribution has taken place within the last 60 days, the distribution won't be prevented from being rolled over due to the once per year rollover rule. In such instances, an individual can simply write a check, or otherwise transfer an amount equal to the RMD back into a retirement account before the end of the 60-day rollover window.

For retirement account owners who took their RMD early in the year and the 60-day rollover window has now expired, there is another potential approach. If it can be shown that the individual has been impacted by the COVID-19 crisis enough to qualify under the liberal guidelines outlined earlier for a Coronavirus Related Distribution, then the rollover can still be completed, anytime for the next three years (from the date the distribution was received).

2020 IS IGNORED FOR PURPOSES OF THE FIVE YEAR PAYOUT RULE

The CARES Act suspends RMDs for 2020 and it also impacts the five-year payout rule that applies to non-designated beneficiaries, for example, charities, estates, and non-see through trusts. This applies to individuals who inherit a retirement account from a decedent who died prior to reaching their required beginning date for RMDs.

In general, such beneficiaries must distribute the entirety of their inherited assets by the end of the fifth year after the retirement account owner's death. The CARES Act, however, allows 2020 to be ignored, or simply not counted as one of those five years. The five-year rule effectively becomes a six-year rule.

The new SECURE Act now imposes a 10-year payout rule for non-eligible designated beneficiaries of retirement accounts. 2020 is the first year that an individual could have died with and had a beneficiary subject to the 10-year rule. The 10 year rule does not actually begin until the year after the year of death. Therefore, 2020 already doesn't count as one of the 10 years for purposes of the 10-year rule.

AGI LIMIT FOR CHARITABLE CONTRIBUTIONS

Section 2205 of the CARES Act temporarily increases the AGI (Adjusted Gross Income) limit on cash contributions made to charities from a maximum of 60% of AGI, to a maximum of 100% for qualified contributions. As such, an individual can completely wipe out their 2020 tax liability with charitable contributions.

UNEMPLOYMENT COMPENSATION

Section 2104 of the CARES Act provides states with the ability to increase their unemployment benefits by up to $600 per week with federally funded dollars, for up to four months. This provision dramatically increases the amount of money an individual can receive temporarily via unemployment compensation benefits.

RELIEF FOR STUDENT LOAN BORROWERS

Section 3513 suspends required payments on federal student loans through September 30, 2020. During this time, no interest will accrue on this debt. While required payments are suspended, voluntary payments are not prohibited. And, by default, payments will continue unless the individual takes proactive measures to contact their loan provider and pause the payments.

III. IDEAS FOR THE BUSINESS OWNER

A new date to remember. Any person with a federal income tax return or payment due on April 15, 2020 is eligible for relief under notice 2020-18 from the Treasury Department. A "person" includes any type of taxpayer, such as an individual, a trust, an estate, a corporation, or any type of unincorporated business entity. The payment due refers to both 2019 federal income tax payments, including payments of tax on self-employed income, and 2020 estimated federal income tax payments, including payments of tax on self-employed income regardless of the amount owed. The return or payment must originally be due on April 15, 2020. This relief does not apply to federal income tax returns and payments due on other dates. The Treasury notice postpones those 2019 return filings and payments due on April 15, 2020 until July 15, 2020.

IV. IDEAS FOR BUSINESS SURVIVAL

Now is the time to make hard decisions about your company and prepare it to become lean and strong quickly. Outlined below are some ideas that you should consider for your company:

- Renegotiate loans with lenders and vendors. Now is the time to ask for lower interest rates and longer terms.
- If you pay rent on your buildings, now is the time to ask for several months of rent deferral or possibly reducing the rent by 50%. The rent not paid can be added to the tail end of the lease.
- Take a hard look at your payroll costs as you enter the second and third quarters of the year. Talk with your accountants, attorneys, and bankers about using all of the government loan programs available for the next several months, but long-term make decisions about where the payroll should be in the last half of 2020. Talk to your national associations and get industry guidelines about what is normal for payroll and rent in your industry. Also, those of us at Castle Wealth Advisors have a lot of that information.
- Sell old inventory. Have a tent sale and get rid of old or obsolete inventory that has been lying around for more than two or three years. Now is the time for you to accumulate cash and build up your war chest rather than leaving old inventory laying on the top shelf or in the warehouse.
- Start being more aggressive on collecting your accounts receivable.
- Maintain your gross margins at their highest levels based on your industry averages. In the next six to 12 months when this coronavirus is over, you need to have the highest gross margins possible going into an economic recovery.

- Be aggressive on depreciation and write-offs in 2020. Previously, in this article, we talked about net operating losses, (NOL's) and you should read that section carefully.
- Look at each item on your profit and loss statement and start cutting unnecessary costs. Cut out the fat and get lean. Make all the cuts now that you have been thinking about for the last five years.
- Make a new business priority. Promise yourself that for the next three months you will spend at least two hours per week working "**on**" the business and continue to improve the profit and loss statement and the balance sheet. In the second quarter, coming up, you need to make several financial changes so that your company comes back quickly in the third and fourth quarter of 2020.

This long article was prepared for every business owner that we have ever met and all industries that we work with every year.

Business owners need to quickly contact their accountants, bankers, SBA regional office, and get details on how to apply for different sections of the CARES Act.

If Castle Wealth Advisors can be of any help to you, please call or email us anytime.

This coronavirus disaster will come to an end and we will all be stronger on the other side. Be safe and stay healthy.

Gary Pittsford, CFP®, is President and CEO of Castle Wealth Advisors, LLC. Castle specializes in helping families and closely-held business owners with valuations, succession planning, estate and income tax analysis and retirement income projections. Castle's senior partners work with clients throughout the country in making logical decisions that help them fulfill their personal and business financial goals. For more information visit www.Castle3.com, call 1-888-849-9559 or e-mail Gary directly at Gary@Castle3.com.