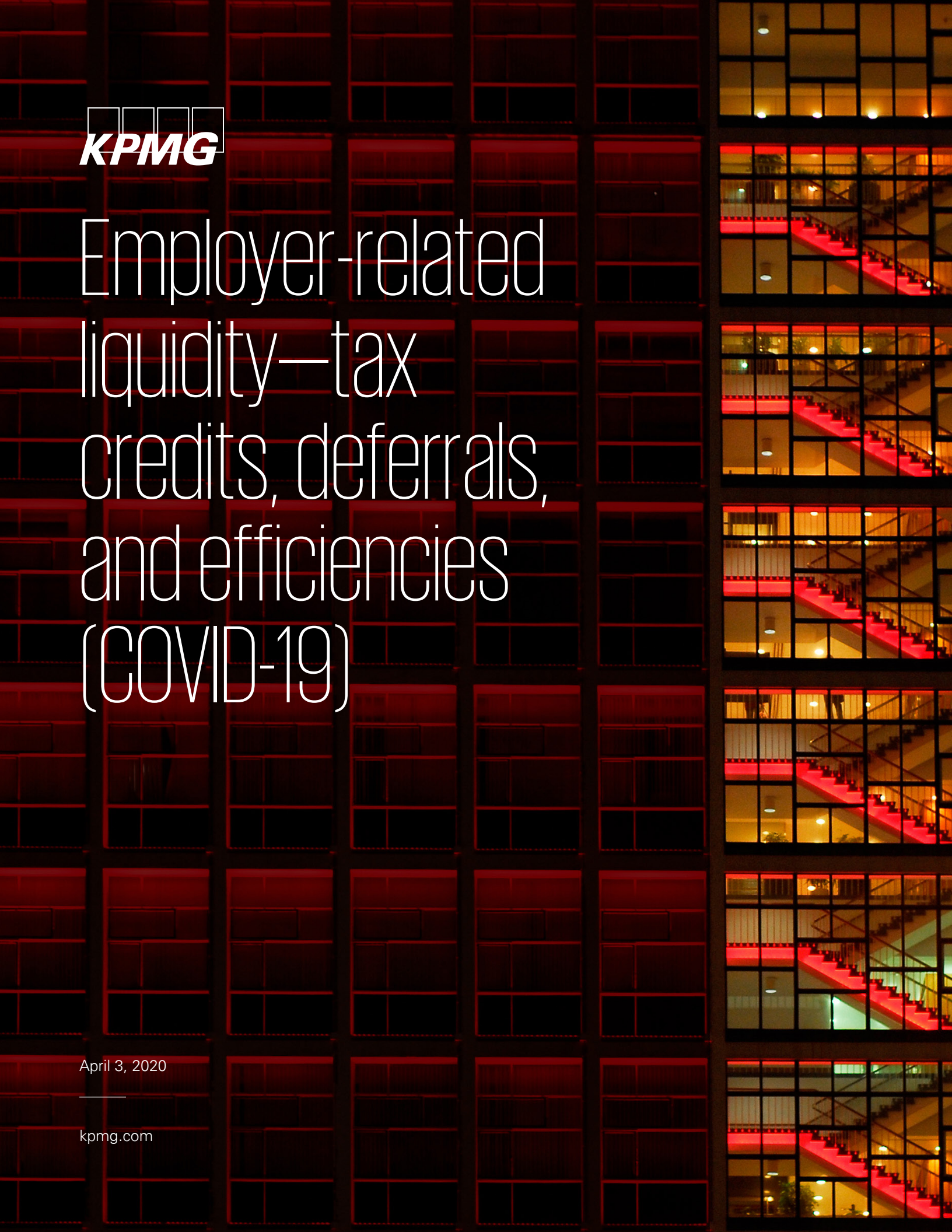

Employer-related liquidity—tax credits, deferrals, and efficiencies (COVID-19)

April 3, 2020

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Introduction

As a result of new U.S. legislation as well as existing rules, there are several employer-related tax credits, deferrals, and efficiencies providing economic stimulus that encourage cash retention and provide additional benefits for businesses affected by the coronavirus (COVID-19) pandemic.

The following is a summary of select labor-related tax provisions of the "Coronavirus Aid, Relief, and Economic Security Act" (CARES Act)[1], the "Families First Coronavirus Response Act (FFCRA)[2] and provisions triggered by the COVID-19 National Emergency Declaration.

- The CARES Act includes a payroll tax credit for qualified wages paid by employers during a partial or full suspension or after significant downturn; the deferral of certain payroll and self-employment taxes; as well as enhanced employee retirement and benefit provisions.
- The FFCRA provides for two new payroll tax credits for paid leave for certain employers with less than 500 employees to offset mandatory paid FMLA and sick leave.

Contents

[1] Pub. L. 116-136, signed by the president March 27, 2020.
[2] Pub. L. No. 116-127, signed by the president March 18, 2020.

Payroll tax deferral

The CARES Act defers the required deposit of certain payroll taxes for employers and self-employed individuals from the date of enactment (March 27, 2020) through December 31, 2020. The deferred taxes are considered timely paid as long as 50% of the deferral is remitted by December 31, 2021, and the remaining 50% is remitted by December 31, 2022.

The deferred payroll taxes are limited to:

- The employer's share of Old-Age, Survivors, and Disability Insurance taxes (Social Security), which is 6.2% of wages up to the $137,700 wage base for 2020.
- Similar rules apply to the portion of the employer's and employee representative's share of Tier 1 Railroad Retirement Tax Act (RRTA) taxes.
- For self-employed individuals, 50% of the Self-Employment Contributions Act (SECA) tax due on net earnings from self-employment under IRC section 1401(a) (i.e., 50% of the 12.4% tax).
    - This portion also exempt from estimated tax payments

The IRS and Treasury have issued guidance[3] to provide penalty relief for deposits of certain federal employment taxes[4] for employers entitled to any of the payroll credits under the FFCRA and CARES Act. Employment taxes include deposits of withheld income taxes, FICA[5], and RRTA taxes.

The guidance provides relief from the section 6656 penalty to timely file such employment taxes to the extent such amounts not deposited are equal to or less than the amount of payroll tax credits for which an employer may be entitled as long as the employer does not also seek an advance credit with regard to the same amount.

In addition, the IRS has issued an advance draft of **Form 7200**, *Advance Payment of Employer Credits Due to COVID-19*, that employers may file with their quarterly payroll tax return to request an advance payment of the tax credits for qualified sick and qualified family leave wages, and the employee retention credit.

According to the draft **Form 7200 Instructions**, eligible employers who pay qualified sick and family leave wages or qualified wages eligible for the employee retention credit should retain an amount of the employment taxes equal to the amount of qualified sick and family leave wages (plus certain related health plan expenses and the employer's share of the Medicare taxes on the qualified leave wages) and their employee retention credit, rather than depositing these amounts with the IRS.

In order to reduce the need for a refund, employment taxes in addition to the employer's portion of social security can be withheld for the credits including federal income tax, the employee share of

[3] Notice 2020-22.
[4] Sections 31.6302-1 or 31.6302-2 of the Employment Taxes and Collection of Income Tax at Source Regulations.
[5] Federal Insurance Contributions Act, which includes Social Security and Medicare.

social security and Medicare taxes, and the employer share of social security and Medicare taxes with respect to all employees.

If there aren't sufficient employment taxes to cover the cost of qualified sick and family leave wages (plus the qualified health expenses and the employer share of Medicare tax on the qualified leave wages) and the employee retention credit, employers can file Form 7200 to request an advance payment from the IRS.

Often, payroll is handled by third-party providers. Accordingly, the CARES ACT permits employers to direct the agent or certified professional employer organization (CPEO) to defer the applicable tax payments. In these cases, the CARES Act provides that employers are solely liable for any untimely deposits deferred under this provision.

Kindly note that the payroll tax deferral is **not** available to a taxpayer that obtains a Small Business Act loan under the Paycheck Protection Program established by the CARES Act in the event such loan is forgiven.

Employee retention credit

The CARES Act provides a refundable payroll tax credit for 50% of "qualified wages" paid by certain employers to employees. The CARES Act provides the credit is available to eligible employers carrying on a trade or business in calendar year 2020 whose:

- Operations were fully or partially suspended, due to the COVID-19 crisis, or
- Gross receipts declined by more than 50% when compared to the same quarter in the prior year.

An employer is not an eligible employer after the end of the calendar quarter in which gross receipts are greater than 80% of gross receipts for the same calendar quarter for the prior year. Tax-exempt entities are eligible if operations are fully or partially suspended due to COVID-19. The trade or business requirement is removed for section 501(c) organizations.

The 50% credit is for "qualified wages." For employers with greater than 100 full-time employees, qualified wages are wages paid to employees when they are not providing services due to COVID-19 circumstances. For eligible employers with 100 or fewer full-time employees, all employee wages qualify for the credit. The average number of full-time employees is determined based on employees employed during 2019 under section 4980H rules. The section 4980H shared responsibility rules under the Affordable Care Act (ACA) provide that a full-time employee includes an employee who is employed on average at least 30 hours per week.[6] Employers may be able to leverage Forms 1095-C for this purpose.

The 50% credit is capped at the first $10,000 of qualified wages (maximum $5,000 credit per employee), including health benefits, paid to the employee. Wages may not exceed amount an employee would have been paid for working an equivalent duration during the 30 days immediately preceding. The credit shall not exceed the employer portion of Social Security taxes (6.2% of wages up to the wage base—$137,700 in 2020) on wages paid with respect to the employment of all employees of the eligible employer for the calendar quarter. Similar rules apply to the portion of the employer's share of RRTA tax. To the extent the credit exceeds the Social Security tax liability, it is treated as an overpayment and a

[6] Section 4980H(c)(4)

refund is available. The provision is effective for wages paid or incurred from March 13, 2020 through December 31, 2020.[7]

The CARES Act prevents double-dipping of the retention credit such that an employer's deduction for wages must be reduced by the amount of the retention credit and an employer may not take into account the following wages for determining the credit:

- Wages providing for payroll tax credits for emergency paid sick leave and emergency FMLA (as discussed below)
- Wages already taken into account for an IRC section 45S income tax credit for certain paid family and medical leave
- Wages paid to certain related individuals specified in IRC section 51(i)(1)
- Wages for any employee for whom a work opportunity tax credit is claimed for qualified veterans
- Wages providing payroll credits under section 41(h) regarding research expenditures

Aggregation for retention credit

The CARES Act applies the sections 52(a) and (b) and 414(m) and (o) aggregation rules to determine which entities are treated as a single employer. Section 52(a) provides that all employees of all corporations which are members of the same controlled group of corporations shall be treated as employed by a single employer.[8] Section 52(b) provides that all employees of trades or business (whether or not incorporated) which are under common control shall be treated as employed by a single employer.

Section 414(m) provides that all employees of the member of an affiliated service group are treated as employed by a single employer.[9] Section 414(o) provides rules related to employee leasing.

The rules look to each organization within a tax-exempt entity as to whether the organizations' operations experience a COVID-19 suspension.

Denial of credit for employers taking small business interruption loan

An eligible employer that receives a covered loan under the Small Business Act (SBA) pursuant to the Paycheck Protection Program (PPP) provisions added under the CARES Act, is not eligible for the employer retention credit.

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[7] For more information on the employer retention credit, see ***CARES Act: Employee Retention Credit FAQs***, prepared by the U.S. Senate Finance Committee, March 31, 2020, as well as ***FAQs: Employee Retention Credit under the CARES Act***, prepared by the Internal Revenue Service.

[8] A controlled group of corporations has the meaning given by section 1563(a) except that "more than 50 percent" shall be substituted for "at least 80 percent" in section 1563(a)(1), and the determination shall be made without regard to subsections (a)(4) and (e)(3)(C).

[9] An affiliated service group is a group consisting of a service organization (first organization) and

- Any service organization which is a shareholder or partner in the first organization, and regularly preformed services for the first organization or is regularly associated with the first organization in performing services for third persons, and
- Any organization is a significant portion of the business of such organization is the performance of services (for the first organization) of a type historically performed in such service filed by employees, and 10% or more of the interests in such organization is held by persons who are highly compensated employees under 414(q) of the first organization.

Treasury guidance

Treasury is instructed to issue forms, instructions, regulations and guidance necessary to:

- Allow the advance payment of the credit
- Provide for reconciliation of the advance payment with the amount advanced at time of filing the return for the calendar quarter or tax year, and
- Provide for recapture of the credit if the credit is allowed to a taxpayer which receives a SBA loan in a subsequent quarter

"Emergency Family and Medical Leave Expansion Act"

The *Emergency Family and Medical Leave Expansion Act* (the Act) enacted under the FFCRA amends the Family and Medical Leave Act of 1993 (FMLA)[10] to create a new category of benefits available from April 1, 2020[11] through December 31, 2020. These benefits generally apply in the case of a qualifying need related to the COVID-19 public health emergency.

A qualifying need related to the public health emergency exists when an eligible employee is "unable to work (or telework) due to a need for leave to care for the son or daughter under 18 years of age of such employee if the school or place of care has been closed, or the child care provider of such son or daughter is unavailable, due to a public health emergency."[12] An eligible employee for this purpose is an employee who has been employed for at least 30 calendar days.

After an initial 10-day leave period (which may be unpaid), a qualifying employee generally is entitled to paid leave at not less than two-thirds of the employee's regular rate of pay for the number of hours the employee would otherwise be scheduled, or would normally be scheduled, to work. However, the Act provides that the paid leave requirement for an employee is limited to $200 per day and $10,000 in the aggregate.

For purposes of applying the new category of leave, the Act modifies the FMLA's employer threshold by using a "fewer than 500 employees" standard.[13] This paid leave provision appears to apply to all government employers, which is consistent with regular FMLA provisions. The Secretary of Labor is given authority to exclude certain health care providers and emergency responders as well as exempt small businesses with fewer than 50 employees in certain cases. In determining whether an employer has fewer than 500 employees, the FMLA rules apply.

Rules for multi-employers

Special rules apply in the case of employment under certain multi-employer bargaining agreements. Employers may fulfill their obligations under the extended FMLA leave provisions by making contributions to a multiemployer fund, plan or program based on the paid leave each of its employee is entitled to, so long as the fund, plan or program provides the expanded FMLA benefits to the employees.

[10] 29 U.S.C. §§ 2601, et seq.
[11] IRS Notice 2020-21.
[12] FFCRA § 110(a)(2)(A).
[13] Whether related businesses' employees are aggregated for purposes of the 500 or more employees threshold is determined under the FMLA "integrated employer" test. See 29 C.F.R. § 825.104.

"Emergency Paid Sick Leave Act"

The FFCRA requires certain employers to provide to employees up to 80 hours (or the average two-week total hours for part-time employees) of paid sick time because the individual is unable to work or telework due to a need for leave for **any** of the following COVID-19-related reasons:

1. The employee is subject to a federal, state, or local quarantine or isolation order relating to COVID-19;
2. A health care provider advised the employee to self-quarantine due to concerns relating to COVID-19;
3. The employee is experiencing symptoms of COVID-19 and is seeking a medical diagnosis;
4. The employee is caring for an individual who is subject to an order described in the first category above, or has been advised by a health care provider as described in the second category above;
5. The employee is caring for a son or daughter of such employee if the school or place of care of the child is closed due to COVID-19 precautions; **or**
6. The employee is experiencing any other substantially similar condition specified by the Secretary of Health and Human Services in consultation with the Secretaries of Treasury and Labor.

The required payment for sick leave is limited for each employee to: (1) full pay up to $511 per day and $5,110 in the aggregate in the case of the first three categories (one through three) described above; or (2) 2/3 pay up to $200 per day and $2,000 in the aggregate for the other categories (four through six). The CARES Act clarified that these are the maximum amounts **required** to be paid; however, there are corresponding credits as discussed below.

This sick leave has no length of employment requirement and is in addition to any regularly-provided annual sick leave. The sick leave is available from April 1, 2020 through December 31, 2020.

The *Emergency Paid Sick Leave Act* provisions apply to "covered employers" as well as certain other entities that are engaged in commerce (including government) or an industry or activity affecting commerce. For this purpose, the FFCRA generally defines a "covered employer" as including a person engaged in commerce or in any industry or activity affecting commerce that: (1) in the case of a private entity or individual, employs fewer than 500 employees; and (2) in the case of a public agency (government) or other entity that is not a private entity or individual, employs one or more employees.

Special rules apply in the case of employment under certain multi-employer bargaining agreements. Similar to the FMLA provisions, the employer could pay into a multi-employer fund, plan or program which would provide the required benefit to the employees.

Further, the Secretary of Labor has the authority to exclude certain health care providers and emergency responders as well as exempt small businesses with fewer than 50 employees in certain cases.

Payroll tax credits

The FFCRA also includes two payroll tax credits relating to the temporary required emergency paid sick leave and FMLA provisions. The credits are available for sick leave and extended FMLA paid from April 1, 2020 through December 31, 2020.

Payroll tax credit for required paid sick leave

The FFCRA provides an employer payroll tax credit equal to 100% of the qualified sick leave wages paid by the employer under the *Emergency Paid Sick Leave Act*, subject to certain limitations. The credit applies against the portion of Social Security taxes imposed by section 3111(a) or the section 3221(a) "Tier 1" excise tax (relating to the RRTA).

The tax credit is applied against 100% of qualified sick leave wages up to either $511 or $200 for each day an individual is paid qualified sick leave, depending upon the category in which the individual falls for purposes of determining the amount required to be paid for sick leave. In addition, the total number of days taken into account in each calendar quarter cannot exceed 10 and is reduced by the number of days taken in preceding calendar quarters.

The amount of the credit for any calendar quarter generally may not exceed the tax imposed under section 3111(a)[14] or section 3221(a) for such quarter. However, the Act provides the credit is refundable for amounts exceeding such tax liability.

Increased credit for health plan expense

The amount of the credit is increased by so much of the employer's "qualified health plan expenses" as are properly allocable to the qualified sick leave wages for which the credit is allowed. For this purpose, qualified health plan expenses generally are amounts paid or incurred by the employer to provide and maintain a group health plan to the extent such amounts are excluded from employee gross income under section 106(a). Such amounts are be allocated to qualified sick leave wages in such manner as the Secretary of Treasury (or delegate) may prescribe.

Special rules

Gross income of employers is increased by the amount of the credit. Further, to prevent double dipping on the credit, any wages taken into account in determining the credit may not be taken into account for purposes of determining the credit under section 45S[15] (relating to paid family and medical leave).

The credit does not apply to the government of the United States, any state, any subdivision of a state, or any agencies or instrumentalities of the foregoing.

Employers may also elect not to apply this new provision for any calendar quarter. The Secretary of the Treasury is responsible for the time and manner of such election.

Finally, the Act provides special rules for payments to possessions of the United States.

The Act provides that the Secretary of the Treasury is to provide regulations and guidance to carry out the purpose of the sick leave credit. Specifically the guidance is to provide information on:

- Preventing the avoidance of the purposes of this credit
- Minimizing compliance and record-keeping burdens

[14] The credit is further reduced to the extent payroll credits were allowed under section 51 for employment of qualified veterans or under section 41(h) regarding research expenditures.
[15] The section 45S credit for paid FMLA leave was extended through December 31, 2020.

- Waving penalties for failure to deposit amounts in anticipation of the allowance of the credit allowed under these provisions
- How to recapture the benefit of credits

Credit for sick leave for certain self-employed individuals

The Act similarly allows an eligible self-employed individual a refundable credit against income taxes with respect to qualified sick leave equivalent amounts. To qualify, an individual generally must regularly carry on a trade or business within the meaning of section 1402 and must have met the criteria that would apply to receive paid leave pursuant to the *Emergency Paid Sick Leave Act* if the individual were an employee of an employer.

The individual is eligible for a credit of the lesser of 100% of average daily income capped at $511 per day for leave covered in the first three categories (one through three) dealing with quarantine, self-quarantine or seeking a diagnosis. The individual is eligible for a credit of the lesser of $200 or 67% of average daily income for leave related to taking care of another as specified in categories four through six.

If the individual is receiving wages or compensation by an employer required to pay emergency paid sick leave, the payments under this section are reduced to the extent that the sum of both amounts exceeds $2,000 or $5,110 depending upon the category of sick leave.

The Act requires the individual to maintain documentation to establish they were a self-employed individual. The Treasury is to provide guidance on required documentation.

This provision expires on December 31, 2020.

Payroll tax credit for required paid family leave

Effective April 1, 2020, and ending December 31, 2020, the Act provides an employer with a payroll tax credit for each calendar quarter generally equal to 100% of the qualified family leave wages paid by the employer to comply with the *Emergency Family and Medical Leave Expansion Act* with respect to such quarter as described above. The credit applies against the employer portion of Social Security taxes imposed by section 3111(a) or the tax imposed by section 3221(a).

The amount of wages taken into account for the credit for each individual cannot exceed $200 for any day for which the individual is paid qualifying family leave wages. In aggregate, a maximum of $10,000 in wages per employee for all calendar quarters is eligible for the credit.

The amount of the credit for any calendar quarter cannot exceed the tax imposed under section 3111(a) or section 3221(a) for such quarter. However, the credit is a refundable credit that allows employers a refund for credits that exceed payroll tax liability.

As with the qualified sick leave program, the amount of the credit for required paid family leave is increased by so much of the employer's qualified health plan expenses as are properly allocable to the qualified family leave wages for which the credit is allowed. The credit is subject to similar "denial of double benefit" rules as the credit for sick leave.

The credit does not apply to the government of the United States, any state, any subdivision of a state, or any agencies or instrumentalities of the foregoing.

Employers may elect not to apply this new provision for any calendar quarter. Further, the Treasury is directed to provide substantially similar guidance as that provided for in the sick leave credit provisions.

Credit for family leave for certain self-employed individuals

The Act provides an eligible self-employed individual a refundable credit against income taxes with respect to qualified family leave equivalent amounts. To qualify, an individual must regularly carry on a trade or business within the meaning of section 1402 and must have met the criteria that would entitle the individual to receive paid leave pursuant to the *Emergency Family and Medical Leave Expansion Act* if the individual were an employee of an employer. The credit is equal to the lesser of 67% of average daily self-employment income or $200.

Payroll provisions under FFCRA

The FFCRA provides that any wages required to be paid by reason of the *Emergency Paid Sick Leave Act* and the *Emergency Family and Medical Leave Expansion Act* are not considered wages for purposes of section 3111(a) or section 3221(a). Thus, leave payments are not subject to the employer portion of social security tax. In addition, the Act provides that the credits for qualified sick leave and family leave are increased by the amount of tax imposed by section 3111(b) (employer portion of Medicare tax) on the qualified sick leave wages or qualified family leave wages for which the credits are allowed.

Other compensation and benefits provisions

Temporary exclusion for student loan repayment benefits from employers

The CARES Act allows employers to provide a tax-free student loan repayment benefit to employees under section 127. The Act allows an employer to contribute up to $5,250 annually toward an employee's student loans and the payment is not included in employee income. The annual limit applies to both the student loan payment as well as other educational assistance traditionally provided under a section 127 plan. The provision disallows the employee's deduction for interest paid on the student loan. This provision would be effective for payments made after March 27, 2020 and before January 1, 2021.

Temporary waiver of early withdrawal penalty for certain withdrawals from qualified retirement plans

The CARES Act provides that the 10% penalty for early withdrawal from a qualified retirement account is waived for distributions up to $100,000 for coronavirus-related purposes. Further, the distribution is taxed over three years, but the taxpayer has the option to repay the amount to the retirement plan within the three-year period. Distributions are coronavirus related if made to an individual:

- Who is diagnosed with COVID-19 with a test approved by the CDC;

- Whose spouse or dependent (as defined by section 152) is diagnosed with COVID-19; or
- Who experiences adverse financial consequences as a result of being quarantined, furloughed, laid off, having work hours reduced, being unable to work due to lack of child care due to COVID-19, closing or reducing hours of a business because of COVID-19, or other factors determined by Treasury.

A plan administrator may rely upon the certification of an employee that a condition was satisfied. This provision applies to distributions made on or after January 1, 2020 and before December 31, 2020.

The bill also provides that the limit on loans from qualified plans is increased from $50,000 to $100,000. The loan is limited to the present value of the nonforfeitable accrued benefit of the employee under the plan. The loan limit is increased for a 180-day period starting on the date of enactment (i.e., March 27, 2020).

Additionally, the CARES Act provides that the repayment due dates with respect to certain outstanding loans from qualified plans made to qualified individuals that were otherwise due between the enactment and December 31, 2020 will be delayed for one year. Further, the Act provides that any subsequent repayments will be adjusted to reflect the delay and any interest accrued during such delay.

Temporary waiver of required minimum distribution rules for certain plans and accounts

The CARES Act waives the required minimum distribution (RMD) rules for calendar year 2020 for certain defined contribution plans and individual retirement arrangements (IRAs). Individuals are usually required to take mandatory distributions starting at age 72[16], but such distributions are not required during 2020. The provision is effective for calendar years beginning after December 31, 2019.

Single-employer plan funding rules

The CARES Act provides single employer pension companies additional time to meet funding obligations. Minimum required contributions to single employer pension plans that would otherwise be due during 2020 may be deposited before January 1, 2021—at which time contributions will become due and if they would have been due earlier, will be due with applicable interest. Further, the Act provides that plan sponsors of single-employer pension plans may elect to treat the plan's adjusted funding target attainment percentage for the last plan year ending before January 1, 2020 as the adjusted funding target attainment percentage for plan years which include calendar year 2020.

The Act does not appear to extend the timing of the deduction for contributions; as such, employers may want to consider if they would like to make contributions earlier to be deductible in the 2019 tax year, including filing extensions as provided in IRS guidance.

[16] In prior years, RMDs began at age 70.5. Starting in 2020, the RMD age is 72.

Application of cooperative and small employer charity pension plan rules to certain charitable employers whose primary exempt purpose is providing services with respect to mothers and children

The CARES Act provides that small employer charity pension plans will include pension plans that as of January 1, 2000 have been maintained by an employer that is described in section 501(c)(3), has been in existence since at least 1938, that conducts medical research directly or indirectly through grant making, and whose primary exempt purpose is to provide services with respect to mothers and children. This amends and expands the definition of cooperative and small employer charity plans. This provision is effective for plan years beginning after December 31, 2018.

Temporary exemption for telehealth services

The CARES Act provides that high deductible health plans, for plan years beginning on or before December 31, 2021, will not fail to be treated as such for purposes of maintaining a Health Savings Account (HSA) for not having a deductible for certain telehealth services. Generally, in order to maintain an HSA, a taxpayer must be covered under a high-deductible health plan that meets certain requirements, including what services may be provided without satisfying a minimum deductible. This provision is effective at the date of enactment (i.e., March 27, 2020).

Inclusion of certain over-the-counter medical products as qualified medical expenses

The CARES Act provides that amounts paid for certain menstrual care products may be treated as paid for medical care for purposes of expenses disbursed from or reimbursed through: HSAs, Archer Medical Savings Accounts, Health Reimbursement Arrangements, and Flexible Spending Accounts. The provision is effective for expenses paid or reimbursements for expenses incurred after December 31, 2019.

KPMG observation

The environment relative to COVID-19 is rapidly evolving. Employers need to consider whether the new leave provisions require any changes to existing arrangements and, if so, what credits, procedures, and payroll adjustments may be available to offset such expenses. Swift implementation and management of these challenges is critical.

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