KPMG Tax Update

COVID-19 Tax Legislation: Pathways for Relief

April 7, 2020

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Notices

The following information is not intended to be "written advice concerning one or more Federal tax matters" subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230.

The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser.

Cash Flow Opportunities: Income Tax

Expanded deductions, including NOLs, and tools under existing law

Opportunities that create refunds

Opportunities for refunds of taxes paid are created by:

- The CARES Act allows for:
  - Expanded deductions (including NOL utilization limits) and AMT credits – some of which can be retroactively applied
  - NOL carryback provisions for 2018-2020 NOLs to offset taxable income in prior years
- There are also existing tools to shift income between tax years, e.g., accounting method changes, elections for losses related to federal disasters.

Each of these reduce taxable income for both current and prior tax years, allowing taxpayers to reassess and potentially recoup taxes previously paid.

Mechanisms for refunds

“Quickie refund” of overpaid estimated taxes if overpayment is at least 10% of expected tax liability

— 2019 and 2020 estimated taxes may be refunded

— **Form 4466 filing for 2019 calendar year is due 4/15/2020…. IRS has 45 days to process Form 4466**

— Potential refunds can be increased by reviewing accounting methods, increased deductions allowed under the CARES Act or electing for disaster losses to be claimed in 2019.

Amended returns

— 2018 and certain 2019 returns (for fiscal years) may be amended to allow for the expanded deductions, including NOL carrybacks and expanded NOL utilization, under the CARES Act

— Potentially a longer process than Form 4466

NOL carrybacks

— 2019 and 2020 returns may provide an opportunity to carry NOLs back up to 5 years

— Potentially the longest route to a refund if via a final return, so consider the use of a Form 1139 for tentative refunds

— Review SPAs to confirm the right to refunds if NOL carrybacks cross ownership changes

For pass through entities, consider impacts on tax distributions and liquidity at the Fund level

Timing of refunds

Tax Claim	Filing Procedure	Timing of Refund	Date of Payment[2]
Excess 2019 Estimated Tax Payments	Form 4466 by April 15, 2020	Refund within 45 days of filing	May 31, 2020
Amended Prior Year Tax Returns (general CARES Act changes for 2018 calendar years and fiscal years ending in 2019)	Form 1120X	No required processing. The IRS instructions note that it can take 3-4 months to process.	Form 1120X – 4-5 months (earliest September 2020)[4]
Carryback of 2019-2020 NOLs	Form 1139[3] or 1120X	Form 1139 required to be filed within the later of 90 days of filing or the last day of the month of the due date (including extension) of the NOL year tax return. Form 1120X has no required processing date.	Form 1139 – 90 days[5] (For example, if 2019 1120 is filed by April 2020, a Form 1139 may be filed and may receive tentative refund as early as July 1, 2020) Form 1120X – 4-5 months after filing (must have filed a Form 1120 for the tax year)[4]
Carryback of 2018 NOLs[5]	Form 1120X	No required processing date. The IRS instructions note that it can take 3-4 months to process.	Form 1120X – 4-5 months (earliest September 2020)[4]

1. Based upon legislation, forms, instructions, and other guidance as of April 1, 2020. Assumes a calendar year taxpayer.
2. Estimates based on past IRS practice. Dates may shift given the current environment and working arrangements.
3. Latest Form 1139 currently limits carrybacks to three preceding tax years, presumably this will be revised. Note that if the NOL carryback impacts a Section 965 liability in the 2017 income tax return, the IRS's position is that a Form 1120X must be used. See Instructions to Form 1139, page 2.
4. Refunds of more than $5 million ($2 million for non-C Corporations) are subject to review and approval of the Joint Committee on Taxation. This can extend the time to receive the refund checks to up to 6-9 months. Threshold is not per year, but per refund. Estimates based on past JCT practice. Tentative refunds requested via Form 1139 will not undergo JCT review prior to initial cash refund.
5. 2018 calendar years losses and taxpayers with fiscal year losses that started in 2018 but ended 1/31/19, 2/29/19, and 3/31/19, can no longer use Form 1139 to carryback NOLs from those periods and must use an 1120X. However, taxpayers with fiscal years that started in 2018 but ended 4/30/19 and thereafter, assuming no 965 inclusion, can use a Form 1139.

CARES Act: Expanded Deductions

Interest Expense Disallowance (163(j))

— Adjusted Tax Income (ATI) limit increased to 50% for tax years beginning in 2019 and 2020
  – For partnerships, 50% only applies to 2020 years, but new rule provides that 50% of any excess business interest carried to 2020 from a 2019 partnership year is available unencumbered for partners in 2020

— Can use ATI from 2019 in the 2020 tax year (likely allowing a higher deduction for companies with reduced 2020 earnings)

Excess Business Loss Limitation (461(l))

— The limitation on the ability of non-corporate taxpayers to deduct business losses in excess of business income plus $250,000, which was imposed by TCJA, is lifted for 2018, 2019, and 2020.

— Taxpayers who were limited in 2018 (or 2019 if filed) can amend.

Qualified Improvement Property (168(k))

— Improvements to the interior of a non-residential building placed in service after the building's initial place-in-service date are now eligible for 168(k) bonus depreciation

— Excludes improvements attributable to elevators, escalators, building enlargement or internal structural framework

— Change is "as if included" in the TCJA on day of enactment, effective for assets placed in service after 2017

— Likely require filing for automatic accounting method change (or possibly corrected with amended return)

Net operating losses: Individuals & Corporations

Temporary suspension of 80-percent-of-taxable income limitation

- Temporary suspension of the limitation on the use of post-TCJA NOLs
  - TCJA imposed an 80-percent-of-taxable-income limitation use of NOLs arising in TYs beginning after 12/31/2017
  - The Act suspends this limitation for TYs beginning before 1/1/2021
    - Suspension is retroactive (thus, applies to TYs 2018 and 2019)

Five-year carryback period for 2018, 2019, and 2020 NOLs

- Applies to NOLs arising in tax years (TYs) beginning after 12/31/2017 and before 1/1/2021
  - Can create rate benefit for carrybacks to 2013-2017
    - Taxpayers might consider adopting various timing strategies, such as changing accounting methods, making a section 165(i) election to claim disaster losses in prior year, adopting a new TY (*i.e.,* a Nov. 30 year end)
  - Carrybacks can require recalculation of carryback year items, e.g., interest expense limitations.

Corporate AMT Credits

Accelerated utilization of remaining minimum tax credits

- Refundable AMT credits were previously limited by 50 percent for TYs beginning in 2018, 2019 and 2020.
- The Act accelerates the refundable credit timetable:
  - Now, a 100 percent credit for 2019
  - Alternatively, taxpayers can elect to have the 100 percent credit for 2018
- The Act contains special procedural rules to claim the refund
  - For 2018 returns, taxpayers can file applications for tentative refunds (note - a 12/31/2020 filing deadline)
  - For 2019 returns, MTCs can be claimed on the return (or on a superseding return if filed before the TY 2019 return's due date, as extended)

Tools Under Existing Law

Losses Related to a Federally Declared Disaster (Section 165(i))

— Eligible losses attributable to a Federally declared disaster to be claimed on a prior year return by election. These include:
  - — Closure of store and facility locations
  - — Abandonment of leasehold improvements
  - — Permanent retirement of fixed assets
  - — Abandonment of pending business deals for which costs have been capitalized
  - — Disposal of inventory, supplies and other property that has become unsaleable
  - — Certain termination payments for executory supply or customer contracts, leases, or licenses
  - — Worthless securities (but not business bad debts)
  - — Impaired securities if the taxpayer uses the mark-to market method, and
  - — Loss from a sale or exchange of property.

— The ability to elect whether those amounts go onto the 2019 or 2020 return may further enhance the benefits of NOL carrybacks, rate arbitrage and accelerated refunds of taxes paid.

Tools Under Existing Law

Accounting Methods

- Method changes can be used to shift income between tax years, e.g., 2019 to 2020 and vice versa.
- Common beneficial method changes include:
  - Accelerating deductions for self-insured medical expenses (particularly relevant currently)
  - Identifying prepaid expenses eligible for immediate expensing
  - Increasing “de minimis” threshold for expensing certain acquisition costs
  - Capitalization methods for indirect costs, including interest expense, related to inventory and self-constructed assets
  - Deferring or accelerating income recognition of certain “advance payments” such as gift card sales
  - Deferring income that is recognized for books but remains contingent for tax
  - Adjusting the method through which certain R&D expenses are claimed, e.g., 10 year amortization.
- As with Section 165 losses, the ability to decide which tax year the benefit is taken can expedite refunds and/or enhance NOL carrybacks.

Practical steps to increase cash flow

Potential to amend returns (2018 and 2019 for fiscal years)

— Review expanded deductions, including NOL limitations, and AMT credits

— Review opportunities to carryback NOLs

— Assess quantum of potential refunds and file amended returns ASAP

Categorize and quantify impact of increased deductions in 2019-2020

— Model impact of:

  — Expanded deductions, including NOL limitations, and AMT credits on the 2019-2020 tax years

  — Changes to accounting methods (acceleration vs deferral) and disaster loss elections, including a comparison as to which year the benefit is taken.

— Examples of key decision points:

  — Faster access to cash via ‘quickie refund’ of 2019 taxes paid?

  — Larger accumulation of a 2020 NOL to carryback to pre-2018 years at a 35% rate?

Filing & Payment Deferrals

Expanded deductions and NOL provisions

Evolving filing and payment guidance

- Stafford Act Emergency Declaration (3/13/20)
- IRS Notice 2020-17 (3/18/20)
- IRS Notice 2020-18 (3/20/20)
- IRS Filing and Payment Questions and Answers (3/25/20)
- IRS Notice 2020-20 (3/27/20)
- Additional guidance is likely

Core guidance

— 2019 Income tax filings and payments due on 4/15/20 are postponed to 7/15/20

— Postponement is automatic – no taxpayer action required

— No limitation on the amount due/postponed

— Penalties and interest disregarded during postponement period

— Extensions beyond 7/15/20 require taxpayer action

Additional guidance

- Income tax returns/payments due on other dates
- Fiscal year returns
- Estimated tax payment issues
- Information returns
- Refund claims

Wrap up:
Key Takeaways & Q&A

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Resources

For additional KPMG updates and insights on the impact of COVID-19, visit:

https://tax.kpmg.us/content/tax/en/index/insights/covid19-tax-impacts.html

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