

Key Federal Tax Relief for Businesses Operating in Puerto Rico

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In response to the COVID-19 pandemic, Congress has enacted sweeping legislation, including measures intended to alleviate its monetary cost and expected impact on the economy.

In the following paragraphs we address the key Federal tax relief measures available to businesses operating in Puerto Rico.

■ **Paid Sick Leave and Family Medical Leave Tax Credits under the Families First Coronavirus Response Act (FFCRA)**

- The FFCRA requires certain eligible employers (businesses and tax-exempt organizations) with fewer than 500 employees (“Eligible Employers”) to pay sick or family leave wages to employees who are unable to work or telework due to certain circumstances related to COVID-19.
- The tax credits under the FFCRA cover 100% of the amounts required to be paid as “qualified sick leave wages” and “qualified family leave wages” (and any qualified health plan expenses allocable and the employer’s share of Medicare tax imposed on those qualified wages), up to 10 days (10 weeks under certain circumstances), subject to certain cap limitations.
- Eligible Employers are entitled to receive a credit in the full amount of the qualified paid sick leave and qualified family leave paid against the employer’s portion of Social Security taxes due for all the wages paid for all of its employees on a given quarter.
- In order to accelerate the benefit of the credit, the Eligible Employer may apply the credit against the *employer’s federal employment taxes* due on any given quarter. When the amount of the credit exceeds the employer’s federal employment taxes, the Eligible Employer may request a refund to the IRS using Form 7200, Advance Payment of Employer Credits Due to COVID-19, or wait to obtain a refund when it claims the credits on the employment tax return. For these purposes, *employer’s federal employment taxes* include withheld federal income taxes, the employee share of social security and Medicare taxes, and the employer share of social security and Medicare taxes with respect to all employees.

Key Federal Tax Relief for Businesses Operating in Puerto Rico

- Eligible Employers may claim tax credits for leave taken beginning on April 1, 2020, and ending on December 31, 2020.
- **Employee Retention Credit for Employers Subject to Closure Due to COVID-19 under the Coronavirus Aid, Relief and Economic Security Act (CARES Act)**
 - The CARES Act provides an employee retention credit to eligible employers that keep employees on their payroll, despite experiencing economic hardship related to COVID-19.
 - Eligible Employers (“CARES Eligible Employers”) are those that carry on a trade or business during calendar year 2020, regardless of their business size, including tax-exempt organizations, and which either:
 - Fully or partially suspended operation during any calendar quarter in 2020 due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to COVID-19; or
 - Experienced a significant decline in gross receipts during the calendar quarter, defined as their gross receipts during such quarter being below 50% of the comparable quarter in 2019. Once the employer's gross receipts go above 80% of the comparable quarter's in 2019, it will no longer qualify as a CARES Eligible Employer after the end of that quarter.
 - The employer may not receive the Employee Retention Credit if it receives a Small Business Interruption Loan under the Paycheck Protection Program that is authorized under the CARES Act (“Paycheck Protection Loans”).
 - The tax credit is equivalent to 50% of the qualified wages (including qualified health plan expenses), up to \$10,000 in total. Accordingly, the maximum tax credit for qualified wages paid to any employee is \$5,000.
 - The definition of qualified wages depends, in part, on the average number of full-time employees during 2019:
 - If the employer had 100 or fewer employees on average in 2019, the tax credit is based on wages paid to all employees, regardless if they worked or not.
 - If the employer had more than 100 employees on average in 2019, the tax credit is based only on wages paid to employees who did not work during the calendar quarter.

Key Federal Tax Relief for Businesses Operating in Puerto Rico

- Qualified wages do not include wages for which the employer receives a credit for sick or family leave under FFCRA.
- CARES Eligible Employers may offset the corresponding tax credit for qualified wages against the employer's portion of social security tax due for all the wages paid for all of its employees on a given quarter.
- In order to accelerate the benefit of the credit, a CARES Eligible Employer may apply the credit against the *employer's federal employment taxes* due on any given quarter. When the amount of the credit exceeds the employer's federal employment taxes, the CARES Eligible Employer may request a refund to the IRS using Form 7200, Advance Payment of Employer Credits Due to COVID-19, or wait to obtain a refund when it claims the credits on the employment tax return. For these purposes, *employer's federal employment taxes* include withheld federal income taxes, the employee share of social security and Medicare taxes, and the employer share of social security and Medicare taxes with respect to all employees.
- CARES Eligible Employers may claim the Employee Retention Credit for qualified wages paid after March 12, 2020, and before January 1, 2021.
- **Delay of Payment of Employer Payroll Taxes**
 - Subject to certain limitations, eligible employers and self-employed taxpayers can delay payment of the employer portion of payroll taxes through the end of 2020. Fifty percent of any payroll taxes deferred under this provision must be paid by December 31, 2021, with the remaining 50% paid by December 31, 2022.
- **Tax Treatment Applicable to Loans and Grants Provided under CARES Act (Small Business Administration Loans)**
 - The CARES Act provides Paycheck Protection Loans to fund eligible payroll costs, certain mortgage payments, rental payments, and utilities payments. A portion of the loan would be eligible for forgiveness, subject to certain requirements.
 - Cancellation of indebtedness under the CARES Act will not be considered gross income for federal income tax purposes, and is therefore exempt from Federal income taxation. Currently, the Puerto Rico Internal Revenue Code does not provide correlative treatment.
 - For federal income tax purposes, loans made or guaranteed by the U.S. Treasury Department will be treated as indebtedness and stated interest

Key Federal Tax Relief for Businesses Operating in Puerto Rico

on such loans will be treated as qualified stated interest and, subject to the applicable limitations, deductible under the U.S. Code.

- Equity investments under these loans will not result in an ownership change for purposes of U.S. Code Section 382. Thus, the NOLs of businesses receiving direct federal investments in the form of stock, warrants, options or other equity should not be limited under Section 382 as a result of such investments.

■ Other Federal Tax Benefits

- There are other tax benefits granted to U.S. taxpayers that file U.S. Income Tax Returns, as follows:
 - *Extension of Certain Federal Filing Due Dates*
 - The Internal Revenue Service provided an extension of time for a Reporting Model 2 FFI or a Participating FFI to file the FATCA Report (Form 8966) with the IRS. The filing deadline for the FATCA Report (Form 8966) will be extended from March 31, 2020 to July 15, 2020. Form 8809-I, Application for Extension of Time to File FATCA Form 8966, will not be required for this extension.
 - The 2019 income tax filing and payment deadlines for all taxpayers who file and pay their Federal income taxes on April 15, 2020, are automatically extended until July 15, 2020. This relief applies to all individual returns, trusts, and corporations. This relief is automatic, taxpayers do not need to file any additional forms or call the IRS to qualify. This relief also includes estimated tax payments for tax year 2020 that are due on April 15, 2020.
 - *Modification of the Rules Relating to Net Operating Losses and Excess Business Losses*
 - For tax years before 2021, net operating losses can fully offset income rather than being limited to 80% of taxable income. Net operating losses generated in 2018, 2019, and 2020 can be carried back five years (real estate investment trusts (REITs) are not allowed such carrybacks). The rules disallowing the deduction for excess business losses derived by non-corporate taxpayers do not apply for tax years 2018, 2019 and 2020.
 - *Increase of the Business Interest Deduction*
 - For tax years beginning in 2019 and 2020, the deduction for business interest expense is limited to the sum of (i) business interest income,

Key Federal Tax Relief for Businesses Operating in Puerto Rico

(ii) 50% of adjusted taxable income (increased from 30%), and (iii) floorplan financing interest expense. For partnerships, this rule only applies for 2020. However, certain excess business interest allocated to a partner in 2019 may be treated as excess business interest paid or accrued by that partner in 2020.

- *Acceleration of AMT Credits*
 - The Tax Cuts and Jobs Act repealed the corporate alternative minimum tax but allowed refundable AMT credits for taxable years beginning in 2018, 2019, 2020 and 2021. The CARES Act amends such rule to allow corporations to accelerate the recovery of such AMT credits, including by requesting a tentative refund of such amounts on or before Dec. 31, 2020.
- *Bonus Depreciation of Qualified Improvement Property (QIP)*
 - QIP is included as 15-year property for depreciation purposes and eligible for 100% bonus depreciation retroactive as of the enactment of the Tax Cuts and Jobs Act. Any improvement to the interior portion of a non-residential building made after it has been placed into service generally is qualified improvement property. This increases businesses' access to cash, as it allows them to amend prior year returns to claim the 100% bonus depreciation for this property.

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