March 20, 2020

Senate Republicans Release a Stimulus Proposal to Combat Economic Impacts of Coronavirus

Introduction

These bullets describe certain key portions of the Senate Republican proposal for Phase 3 of the government's stimulus response, which we think will be of interest to our clients and friends. We cover the return of the money market fund guarantee, lending to and taking equity in distressed companies (including the airlines), small business interruption loans, and tax relief for individuals and businesses. In the interest of time, we are not covering critical portions of the bill, including those that deal with the educational and medical fiscal stimulus, except for the student loan portions.

There are many moving pieces in the current situation. We expect that the proposed bill may change. There will also be proposals put on the table by Senate Democrats and the House. We will be updating these bullets on an ongoing basis, with all updates available on the coronavirus section of the Davis Polk website, and on our Coronavirus Updates Blog, which goes live on Monday, March 23, 2020.

The Senate bill builds on suggestions set forth in the Treasury proposal. The Phase 3 bill is expected to pass sometime next week and is subject to negotiation with Senate Democrats and the House.

Key Elements of the Senate Republican Phase 3 Proposal

1. Temporary Guarantee of Money Market Mutual Funds (MMMFs)

- Currently, the Exchange Stabilization Fund cannot be used to guarantee MMMFs because of a statutory prohibition put in place after the Financial Crisis. Consistent with the Treasury proposal, the Senate Republican bill temporarily lifts this prohibition for the duration of the emergency. Duration of the emergency is defined under the Stafford Act. It would be up to Treasury to determine what the guarantee would entail.

2. Economic Stabilization

- The Treasury is authorized to provide secured loans or loan guarantees via the Exchange Stabilization Fund to air carriers and other "eligible businesses" up to an aggregate amount of $208 billion and to provide subsidy amounts needed for such loans and loan guarantees:
  - $50 billion for passenger air carriers and $8 billion for cargo air carriers
  - $150 billion for other "eligible businesses"
  - "Eligible businesses" are those whose business operations are jeopardized by losses incurred as a direct result of coronavirus and that have not otherwise applied for economic relief
- In issuing loans or loan guarantees, the Treasury Secretary must ensure the government is compensated for the risk it assumes, and the Treasury is accordingly authorized to participate in gains of the borrowers through warrants, stock options, common or preferred stock. This language creates conditions reminiscent of those under the TARP program.
- The Secretary has significant discretion:
  - Can lend to or guarantee loans for any borrower for which (a) credit is not otherwise "reasonably available" at the time of the transaction; (b) the obligation is "prudently incurred"; and (c) the loan is "sufficiently secured"
  - Lending at rate determined by the Secretary, by reference to the "current average yield on outstanding marketable obligations of the United States of comparable maturity"

- Terms to be determined by the Secretary, with lending to occur pursuant to procedures set out by the Secretary within 10 days of legislation going into effect

- Loans and loan guarantees are conditioned on borrowers entering legally binding agreements not to increase for two years the "total compensation" of any executive whose total compensation in 2019 exceeded $425,000
  - "Total compensation" includes salary, bonus, awards, and other benefits
  - Similar restrictions on severance entitlements, which cannot exceed more than two times 2019 compensation
- For air carrier borrowers, Treasury Secretary must coordinate with Department of Transportation on lending, and can require continued service of existing routes "to the extent reasonable and practicable"
- Proposal also includes a holiday from (a) the 7.5% aviation excise tax for the transportation of passengers, (b) the 6.25% aviation excise tax for the transportation of cargo and (c) taxes on certain uses and transportation of kerosene as aviation fuel, in each case until January 1, 2021

3. Small Business Loans

- $300 billion allocation for expansion of existing Small Business Administration Section 7(a) guaranteed lending program to cover any business concern or non-profit[1] with less than 500 employees (rather than just small business concerns)
  - Increases available loan amounts up to the lesser of $10 million or four times average monthly overhead, with special provisions for seasonal businesses
  - Waives all fees to the extent practicable, with 100% of loans guaranteed by the federal government (as compared to no more than 85% under existing program), payments deferred for one year, and no prepayment penalty on payments made prior to December 31, 2020
  - Expands allowable use of loan proceeds beyond capital costs to payroll support, employee salaries, mortgage or rent payments, utility payments, and existing debt obligations
  - Portion of loans used to cover payroll costs and existing debt obligations from March 1, 2020 to June 30, 2020 eligible for forgiveness (with the forgiven amount non-taxable), with reductions in the amount that can be forgiven for employers who lay off employees over the next four months
- Businesses will be eligible for loans through December 31, 2020, with eligibility criteria streamlined. Any business in operation on March 1, 2020 that had employees to which the borrower paid salaries and for which the borrower paid payroll taxes is eligible
- The Small Business Administration would administer the loans, with existing SBA lenders given the authority to make and approve loans under the expanded Section 7(a) program
  - Treasury would be directed to take the lead with other financial regulators to establish criteria for insured depository institutions to participate in offering loans for the duration of the coronavirus national emergency (with exceptions where participation would compromise safety and soundness)
  - Treasury would administer loans under this portion of the program using Treasury, rather than SBA, infrastructure

[1] Excluding non-profits that receive Medicaid reimbursements.

- The proposal also raises the maximum loan available under the existing Express Loan program from $350,000 to $1 million, and includes a grant program for small business development centers to facilitate coronavirus-related entrepreneurial development with priority for women and minority business centers

4. Tax Relief for Businesses

- **Delay of Corporate Estimated Tax Payments**
  - The bill allows corporations to postpone an unlimited amount of estimated income tax payments due at any time after the date of enactment until October 15, 2020. Note that this broadens the relief granted by IRS Notice 2020-17, released on Wednesday, which permitted the deferral of April 15, 2020 tax payments only until July 15, 2020, and was subject to a cap on the amounts that could be deferred
- **Delay of Employer Payroll Tax Payments**
  - The bill allows employers and self-employed individuals to postpone payment of the employer share of Social Security taxes that they would otherwise be required to pay between the date of enactment and January 1, 2021
  - The deferred payments are required to be paid in two installments, with 50% of the deferred amount required to be paid by December 31, 2021 and the other 50% by December 31, 2022
- **Increased Ability for Corporations to Deduct NOLs**
  - The bill permits corporate net operating losses (NOLs) from 2018, 2019, and 2020 (we understand that there will be a fix to an unintentional error in the bill, which otherwise would have meant the provision would apply only to 2018 and 2019) to be carried back five years (under current law, no carryback for NOLs in these years is permitted)
  - The bill also (a) for 2020, allows corporate NOLs to fully offset income in 2020, free of certain taxable income limitations that would otherwise apply, and (b) for 2021 and later years, relaxes in certain respects the taxable income limitations on the use of corporate NOLs that would otherwise apply
  - Both provisions will permit corporations to utilize their NOLs from 2018, 2019 and 2020 to obtain refunds of taxes paid in prior years and/or to reduce their tax payments in 2020 and later years, and enhance corporate cash flow and liquidity
- **Increased Ability of Noncorporate Taxpayer to Deduct NOLs**
  - The bill defers until 2021 the application of certain rules that would limit the ability of noncorporate taxpayers, such as owners of pass-through businesses and sole proprietors, to deduct NOLs from 2018, 2019 and 2020, so that such NOLs are subject to the same rules as described above for corporate NOLs
  - This will permit noncorporate taxpayers to claim refunds and/or reduce their tax payments in respect of their NOLs, enhancing cash flow and liquidity
  - The bill also makes certain technical corrections to the operation of these rules in 2021 and later years
- **Acceleration of Recovery of AMT Tax Credits**
  - The 2017 tax reform act repealed the corporate alternative minimum tax (AMT), and allowed corporate taxpayers to recover certain AMT taxes paid prior to repeal as refundable credits against their regular tax liability, but only over four years starting in 2018
  - The bill accelerates the ability of corporations to recover these credits entirely into 2018

- **Relaxation of Limits on Business Interest Deductions**
  - The ability of a taxpayer to deduct business interest expense is subject to a limitation that is generally equal to 30% of its “adjusted taxable income” for the year, the definition of which is currently roughly analogous to EBITDA
  - The bill increases the limitation from 30% to 50% of adjusted taxable income for 2019 and 2020
  - The bill also permits a taxpayer to elect to determine its deductible interest expense for 2020 based on its adjusted taxable income for 2019
  - These provisions are expected to increase many taxpayers’ ability to deduct interest in 2019 and 2020
- **Amendments to 2017 Tax Reform Provisions**
  - The bill fixes what the Senate Finance Committee summary of the bill describes as an error in the 2017 tax reform law, of importance to the hospitality industry, that will permit taxpayers to immediately write off costs associated with improving their facilities, rather than having to depreciate such improvements over 39 years. The provision is retroactive to the enactment of the 2017 tax reform law
  - The bill fixes what the Senate Finance Committee summary of the bill describes as an error in the 2017 tax reform law that will permit companies that overpaid their taxes in 2017 as a result of the one-time “repatriation” toll charge on untaxed foreign earnings to claim a refund of those taxes. Certain companies were unable to claim a refund because of the interaction of the general provisions governing refunds with the rules that permitted companies to pay the toll charge in installments
  - The bill addresses the treatment of certain foreign corporations as “controlled foreign corporations” (CFCs), limiting some of the unintended consequences of a provision in the 2017 tax reform law that was intended to target certain abusive transactions relating to CFCs. The provision is narrowly drafted and many foreign corporations may continue to be treated as CFCs even though they are outside the intended scope of the changes made in the 2017 tax reform law

5. Tax Relief for Individuals and Families

- **Recovery Rebates for Individuals**
  - The bill provides for an immediately refundable credit for 2020 to eligible taxpayers in an amount up to $1,200 (or $2,400 for married taxpayers filing jointly), subject to income limits. The amount increases by $500 for each child
  - The credit is generally phased out for single taxpayers whose income exceeds $99,000 ($198,000 for joint filers). Specifically, $5 of the credit is reduced for each $100 that a taxpayer’s adjusted gross income exceeds (a) $75,000 in the case of single taxpayers and (b) $150,000 in the case of joint filers. The credit amount will be calculated based on a taxpayer’s 2018 tax return
  - Taxpayers with little or no income tax liability, but at least $2,500 of qualifying income, would be eligible for a minimum rebate check of $600 ($1,200 for joint filers)
  - The U.S. Treasury will issue “refund” checks for such credits “as rapidly as possible”
- **Delay of Deadlines for Filing Returns and Paying Estimated Taxes**
  - The filing deadline for all individual 2019 tax returns is delayed by three months to July 15, 2020, without the need to file for an extension. In a related development, on Friday morning, Treasury Secretary Mnuchin announced via Twitter that the 2019 tax return filing deadline for businesses and individuals would be moved to July 15, 2020. Note that the bill (and Secretary Mnuchin’s tweet) broadens the relief granted by IRS Notice 2020-17, released on Wednesday, which permitted the

deferral of certain tax payments otherwise required to be made on April 15, 2020, but did not extend the time for filing 2019 tax returns

- Individuals are permitted to defer all estimated tax payments otherwise due after the date of enactment until October 15, 2020. There is no cap on the amount that can be deferred

- **Special Rules for Use of Retirement Funds**
  - The bill waives the 10% early withdrawal penalty for certain coronavirus-related distributions up to $100,000 made during 2020 from an eligible retirement plan
  - In addition, any income inclusion attributable to such distributions would be subject to tax only over a three-year period. The amount distributed may be recontributed to an eligible retirement plan within 3 years after the date of such distribution, without regard to the annual cap on contributions
  - The bill also provides flexibility for loans from certain retirement plans for coronavirus-related relief
- **Allowance of Partial Above the Line Deduction for Charitable Contributions**
  - The bill allows for a 2020 tax deduction of $300 for eligible charitable contributions, such as contributions to churches and charities, for taxpayers who do not itemize their deductions
- **Modification of Limitations on Charitable Contributions During 2020**
  - The bill modifies the limitations on deductions for charitable cash contributions in 2020 by individuals that itemize their deductions and corporations. For an individual, the normal limit on certain charitable deductions of 50% of adjusted gross income will not apply. For electing corporations, the normal limit on charitable deductions of 10% of taxable income is increased to 25% of taxable income
  - The bill also increases the limitation on deductions for contributions of food inventory in the case of C corporations, from 15% of taxable income to 25% of taxable income

6. Student Loan Provisions

- The proposal would suspend payments on federal student loans for three months, during which time no interest would accrue, with an option for the Education Secretary to extend the suspension for an additional three months
- The suspension of payments would not impact the ability of borrowers to qualify for federal student-loan forgiveness programs
- The proposal also includes a number of provisions aimed at easing the conditions imposed on federal funds received by higher education institutions

7. Labor Provisions

- The proposal would maintain the paid sick leave requirement imposed on employers by the newly signed H.R. 6201, with some cleanup of the legislative text
- Penalties for failing to make a tax deposit would be waived if the Treasury Secretary determines that any such failure is due to the anticipation of payroll credit for required family leave and certain self-employed individuals under H.R. 6201

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

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