Shumaker

APRIL 2, 2020 | PUBLICATION

Client Alert: CARES Act: Provisions of Potential Interest to Large Manufacturers

INDUSTRY SECTOR

Manufacturing

MEDIA CONTACT

Wendy M. Byrne
wbyrne@shumaker.com

Download Client Alert: The CARES Act: Provisions of Potential Interest to Large Manufacturers

Introduction

The Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act" or "CARES")[1] was signed into law by President Donald Trump on Friday, March 27, 2020 in response to the coronavirus pandemic and its vast economic and social impacts in the United States. Never before has Congress passed such a large and sweeping economic stimulus package. The size of the package – roughly $2.2 trillion – is more than twice the size of the stimulus package signed by President Obama in the wake of the 2008 financial crisis, the "American Recovery and Reinvestment Act of 2009"[2] (at approximately $830 billion).

The CARES Act provides an important lifeline to individual Americans, families, and businesses facing severe economic distress as a result of much of the nation shutting down due to the coronavirus. Much of the attention and discussion on the legislation has been on the small business provisions – in particular, the significant new Paycheck Protection Program (PPP) within SBA's 7(a) program for businesses with less than 500 employees – the direct payments (through the form of "rebates") to individuals and families, and the loans and other benefits to specific industries, including in particular, the airlines. However, the massive bill contains 800-pages of legislative text and many other provisions affecting every industry and virtually every aspect of our economy.

While no aspects of the bill focus on the manufacturing sector per se (other than some smaller provisions specifically targeted in the pharmaceutical and medical device space), there are a number of loan and tax provisions that could be noteworthy to large manufactures. This alert explores those provisions, and then looks ahead at other policy issues and potential next steps. Indeed, there is already talk in Washington, D.C. of a "phase four" stimulus package, as the true breadth and depth of the economic impact of COVID-19 comes into greater focus.

CARES Act Summary – Key Provisions of Interest

A. Loans to Eligible Businesses through Federal Reserve Lending Programs and Facilities. Title IV, "Economic Stabilization and Assistance to Severely Distressed Sectors of the Economy," provides $500 billion to Treasury's "Exchange Stabilization Fund" to support federal lending programs to businesses, states, and municipalities. Much of the attention on this provision has been on the $46 billion for direct lending programs within Treasury for specifically-named industries.[3] However, the provision also provides up to $454 billion to make "loans and loan guarantees" to and "other investments in" programs or facilities established by the Federal Reserve to provide liquidity to eligible businesses, states, and municipalities by:

- Purchasing obligations directly from issuers;
- Purchasing obligations in secondary markets; or
- Making loans, including securitized loans or other advances

An "eligible business" is one that has "not otherwise received adequate economic relief in the form of loans or loan guarantees" under the CARES Act.[4] It is important to note that there are certain conditions placed on lending under this authority, including restrictions on stock repurchases, dividends, and executive compensation, though the Secretary has authority to waive the restrictions if "necessary to protect the interests of the Federal Government." In addition, the program is limited to businesses "created or organized in the United States or under the laws of the United States and that have significant operations in and a majority of its employees based in the United States." The requirements under 13(3) of the Federal Reserve Act regarding loan collateralization, taxpayer protection, and borrower solvency continue to apply. This program is NOT eligible for loan forgiveness.

The statute doesn't provide a great deal of detail on how any of the bigger company credit programs should work, leaving it up to the Federal Reserve and Treasury. Guidance should be forthcoming any day.[5] According to some estimates, the support provided under the bill will allow the Federal Reserve to issue nearly $4 trillion in loans and debt guarantees to U.S. businesses, which should help improve liquidity in distressed parts of the economy.

B. Business Tax Provisions. There are several business tax provisions contained in the CARES Act that are worthy of mention. While the tax provisions would not be considered major tax changes, there are several important provisions designed to enhance liquidity in the short-term and should be of interest to most companies, including manufacturers. The Joint Committee on Taxation (JCT)[6] estimates the total revenue impact of all tax provisions under the bill to be about $600 billion, about half of which is accounted for by the rebate checks sent to individual Americans and families.[7]

1) **Employee retention credit for employers subject to closure due to COVID-19.** Sec. 2301 provides a refundable payroll tax credit for 50 percent of wages paid by employers during the COVID-19 crisis. The credit is available to employers whose: (1) operations were fully or partially suspended, due to a COVID-19-related shut-down order, or (2) gross receipts declined by more than 50 percent when compared to the same quarter in the prior year. The credit is based on "qualified wages" paid to the employee. For employers with greater than 100 full-time employees, "qualified wages" are wages paid to employees when they are not providing services due to the COVID-19-related circumstances described above.[8] The credit is provided for the first $10,000 of compensation, including health benefits, paid to an eligible employee and is provided for wages paid or incurred from March 13, 2020 through December 31, 2020.[9]

2) **Delay of payment of employer payroll taxes**. Section 2302 allows employers to defer payment of the employer share of the Social Security tax they otherwise are responsible for paying to the federal government with respect to their employees. The provision requires that the deferred employment tax be paid over the following two years, with half of the amount required to be paid by December 31, 2021 and the other half by December 31, 2022.[10]

3) **Modifications for net operating losses.** Sec. 2303 relaxes the limitations on a company's use of

losses. Net operating losses (NOL) are currently subject to a taxable-income limitation, and they cannot be carried back to reduce income in a prior tax year. The provision provides that an NOL arising in a tax year beginning in 2018, 2019, or 2020 can be carried back five years. The provision also temporarily removes the taxable income limitation to allow an NOL to fully offset income. These changes will allow companies to utilize losses and amend prior year returns.

4) **Modification of credit for prior year minimum tax liability of corporations.** The corporate alternative minimum tax (AMT) was repealed as part of the Tax Cuts and Jobs Act, but corporate AMT credits were made available as refundable credits over several years, ending in 2021. Sec. 2305 accelerates the ability of companies to recover those AMT credits, permitting companies to claim a refund now and obtain additional cash flow during the COVID-19 emergency.

5) **Modification of limitation on business interest.** Sec. 2306 temporarily increases the amount of interest expense businesses are allowed to deduct on their tax returns, by increasing the 30-percent limitation to 50 percent of taxable income for 2019 and 2020.

C. Other manufacturing-specific provisions. There are a few other provisions in the CARES Act that speak directly to specific segments of the U.S. manufacturing sector.

1) **Report on U.S. Medical Product Supply Chain.** Section 3101 directs the National Academies to study the manufacturing supply chain of drugs and medical devices and provide Congress with recommendations to strengthen the manufacturing supply chain.

2) **Treatment of respiratory protective devices.** Section 3103 provides permanent liability protection for manufacturers of personal respiratory protective equipment, such as masks and respirators, in the event of a public health emergency. This provision expands on the immunity given to manufacturers of certain essential medical devices during a public health crisis under the Public Service Health Act.

3) **Reporting requirements on drug manufacturers**. Section 3112 requires drug manufacturers to submit more information when there is an interruption in supply, including information about active pharmaceutical ingredients (API), if API is the cause of the interruption. It also calls on manufacturers to maintain contingency plans to ensure backup supply of products and to provide information about drug volume.

D. What may be the horizon?

1) **Trade policy.** Trade, and specifically tariff policy, continues to receive attention from some policy makers on Capitol Hill, as well as in within industry, as another possible way to provide economic relief during the COVID-19 crisis. One hundred and sixty businesses and organizations, including many in the manufacturing space, wrote a letter to the president on March 18, 2020, urging him to lift the tariffs – "taxes that Americans pay" – as part of other emergency measures taken in response to the coronavirus. The initial response from the Administration was not positive. Specifically, in response to a question asked about tariffs, President Trump said later at a press briefing, that there was "no reason" to suspend them. However, its likely free trade advocates on the Hill and in the business and agriculture communities, will continue to raise the issue. Of note, according to one report[11] on March 25, 2020, U.S. Customs and Border Protection (USCPB) notified companies that will approve some delays in tariff payments, a move akin to the tax filing and payment relief provided by the IRS in response to COVID-19. Meanwhile, on Wednesday, March 25, a group of Republican senators sent a letter to President Trump asking for new exclusions to existing tariffs and a ban on new ones.[12] Specifically, in the letter led by the Chairman of the Senate Finance Committee, Senator Chuck

Grassley (R-Iowa), and signed by 11 members of the Committee, the senators laid out several trade-related options, including, "expanding and extending tariff relief through the exclusion process for Section 301 tariffs." It's an issue that bears watching.

2) **Coronavirus Stimulus "Phase Four?"** There is already talk in Washington about a potential fourth economic stimulus measure, or "Phase Four." House Speaker Nancy Pelosi reportedly told reporters on Monday, March 30, 2020 that House Democrats are in the early stages of drafting another major bill that will not only shore up health systems and protect frontline health care workers, but could include substantial investments in infrastructure.[13] But other senior House and Senate Republicans have expressed a desire to "let this work," in the words of House Minority Leader Kevin McCarthy. Neither the House nor the Senate are scheduled to return to Washington until April 20, but the respective majority leaders of the House and Senate also both indicated, at the time they made their announcements, that they could return sooner if necessary. Depending on the length and breadth of the crisis, Washington may need to respond again. If so, it will be an opportunity to change, enhance, and/or fix provisions of the third stimulus package, and include provisions that were not addressed or are necessary for continued economic recovery.

3) **China concerns.** One potential issue that will be worth following in the wake of the COVID-19 pandemic is the impact to the U.S.-China relationship going forward. While the entire U.S. Government's focus is on addressing the current crisis, beating the virus, and ensuring a robust economic revival, concerns remain, particularly among conservative lawmakers, about China, and in particular the lack of transparency that contributed to the spread of COVID-19 and the vulnerability to the U.S. supply that has been laid bare by the current crisis, particularly in the pharmaceutical space. In addition to the above-referenced National Academies report, it could lead to questions and continued oversight in the U.S. Congress. It could even lead to legislative action. For example, Senator Tom Cotton (R-AR) recently introduced legislation, the "Protecting our Pharmaceutical Supply Chain from China Act," S. 3537, that would require an FDA registry of certain drugs and active pharmaceutical ingredients (API) produced outside the United States and prohibit federal health agencies, such as the VA and DOD, from purchasing drugs that have APIs from China. Senator Cotton and Wisconsin Congressman Gallagher wrote an op-ed recently explaining their legislation.[14] While the Senate bill was only recently introduced (March 19, 2020), has only two (2) cosponsors, and focuses only on the pharmaceutical supply chain, at the very least, it is a sign of potential increased scrutiny on our international supply chain, specifically reliance on China.

E. Conclusion. Shumaker Advisors will continue to closely monitor developments with the implementation of the CARES Act, and with a possible "Phase Four" package, for Shumaker clients. For the most up-to-date legal and legislative information related to the coronavirus pandemic, please visit our Shumaker COVID-19 Client Resource Center at www.shumaker.com. We have also established a 24/7 Legal & Legislative Helpline at 1.800.427.1493 monitored by Shumaker lawyers around the clock.

---

[1] H.R. 748 (116th Congress).

[2] P.L. 111-5, February 17, 2009.

[3] Specifically, up to $46 billion is allocated for direct loans to specific industries, including passenger air carriers (not more than $25 billion), cargo air carriers (not more than $4 billion), and businesses "critical to maintaining national security" (not more than $17 billion).

[4] Note this program is distinct from the Paycheck Protection Program (PPP) authorized within the Small Business Administration's 7(a) authority, which is targeted to employers with under 500 employees.

[5] Treasury has issued guidance on how the loan program for air carriers and businesses important to national security should work. See here: https://home.treasury.gov/cares.

[6] https://www.jct.gov/publications.html?func=startdown&id=5252

[7] All summary information was pulled from the section-by-section prepared by the Senate Finance Committee. See here: https://www.finance.senate.gov/imo/media/doc/CARES%20Act%20Section-by-Section%20(Tax,%20Unemployment%20Insurance).pdf In addition, anyone interested in learning more about the nuances of the specific tax provisions briefly highlighted here is encouraged to review the Shumaker CARES Act: Shumaker Legal & Legislative Summary.

[8] For eligible employers with 100 or fewer full-time employees, all employee wages qualify for the credit, whether the employer is open for business or subject to a shut-down order.

[9] An employer cannot take this credit if it receives a PPP loan.

[10] The Social Security Trust Funds will be held harmless under this provision with a transfer of appropriated funds.

[11] https://www.wsj.com/articles/u-s-customs-tells-importers-it-will-approve-tariff-delays-on-a-case-by-case-basis-11585144953

[12] https://www.finance.senate.gov/imo/media/doc/2020-03-25%20CEG,%20SFC%20Republicans%20to%20Donald%20J.%20Trump%20(Trade%20Measures%20during%20COVID-19).pdf?mod=article_inline

[13] https://www.politico.com/news/2020/03/30/pelosi-move-fast-rescue-package-155920.

[14] https://www.foxnews.com/opinion/sen-cotton-and-rep-gallagher-china-stole-us-capacity-to-make-drugs-we-must-take-it-back.

Shumaker