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CARES Act: Guidance on Tax Relief for Real Estate Businesses

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The Coronavirus Aid, Relief, and Economic Security Act, P.L. 116-136 (CARES Act), made some important and taxpayer-friendly changes to the allowance for business interest expense and accelerated depreciation for qualified improvement property (QIP), generally including taxpayer improvements to the interior portion of nonresidential real estate. Recent guidance issued by the IRS helps taxpayers take advantage of these changes.

Under the Tax Cuts and Jobs Act, P.L. 115-97 (TCJA), a taxpayer's deduction for business interest expense for taxable years after 2017 was generally limited to 30% of the taxpayer's adjusted taxable income (ATI). A taxpayer engaged in certain real-estate businesses could avoid this limitation by making an election to treat the business as an "electing real property trade or business" (ERPTB Election). This election, however, came at a price: A taxpayer making an ERPTB Election was required to use the alternative depreciation system for residential and nonresidential real estate and QIP. For many, this tradeoff made economic sense, especially given that, under the TCJA, QIP was ineligible for 100% bonus depreciation—the so-called retail glitch.

The CARES Act made two important changes to these rules.

- The business interest limitation was increased from 30% to 50% of a taxpayer's ATI for taxable years beginning in 2019 and 2020. (For partnerships, the increased limitation applies only to taxable years beginning in 2020, although special rules apply for taxable years beginning in 2019.)
- The CARES Act fixed the "retail glitch" by classifying QIP as 15-year property, thus making it eligible for 100% bonus depreciation retroactively to 2017.

A series of newly issued revenue procedures provides much-needed guidance for taxpayers to take advantage of these changes.

- Rev. Proc. 2020-22, issued April 10, 2020, allows a taxpayer to make a late ERPTB Election or, perhaps more significant, withdraw an existing ERPTB Election by filing an amended tax return or, for a taxpayer classified as a partnership, an administrative adjustment request (AAR) or amended IRS Form 1065. This guidance piggybacks off Rev. Proc. 2020-23, issued the same day, which generally allows a partnership to file an amended IRS Form 1065 for taxable years beginning in 2018 and 2019 instead of an AAR, as required by the partnership audit rules. Rev. Proc. 2020-22 also explains how to make various

elections regarding the application of the new business interest limitations.

- Rev. Proc. 2020-25, issued April 17, 2020, allows a taxpayer to elect 100% bonus depreciation for QIP placed in service after December 31, 2017, in taxable years ending in 2018, 2019 or 2020, by filing an amended tax return or an application for a change in method of accounting on IRS Form 3115. A partnership can also file an AAR. In addition, the guidance tells taxpayers how to make various late elections, or revoke or withdraw existing elections, with respect to bonus depreciation and the alternative depreciation system.

Taxpayers desiring to take advantage of these recent changes should consult with their tax advisors to determine which methods provide the best result given the facts and circumstances.

We encourage you to visit Holland & Hart's Coronavirus Resource Site, a consolidated informational resource offering practical guidelines and proactive solutions to help companies protect their business interests and their workforce. The dynamic Resource Site is regularly refreshed with new topics and updates as the COVID-19 outbreak and the legal and regulatory responses continue to evolve. Sign up to receive updates and for upcoming webinars.