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much-needed relief for businesses hindered by a cap on business interest deductions. Icing on the cake: The tax changes are retroactive to 2019.

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The image displays three IRS tax forms. The top form is Form 1065, 'U.S. Return of Partnership Income', for the calendar year 2005. Below it is Form 1120S, 'U.S. Income Tax Return for an S Corporation', also for the calendar year 2005. The bottom form is Form 1120, 'U.S. Corporation Income Tax Return', for the calendar year 2005 or tax year beginning in 2005. Each form includes fields for the taxpayer's name, address, and other identifying information, as well as checkboxes for various filing options and instructions.

The new Coronavirus Aid, Relief, and Economic Security (CARES) Act provides some much-needed relief for businesses hindered by a cap on business interest deductions. Icing on the cake: The tax changes are retroactive to 2019.

Here's a quick recap: Prior to the Tax Cuts and Jobs Act (TCJA), a business entity could generally deduct its business interest expenses without restriction. However,

the TCJA limited the annual net interest deduction to 30% of its adjusted taxable

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- Net operating losses (NOLs);
- The qualified business income (QBI) deduction for pass-through entities; and
- For tax years beginning before 2022, any deduction allowable for depreciation, amortization or depletion. Real estate operations can opt out of this rule.

Any excess may be carried over and offset taxable income in a future year within the allowable limit.

The TCSA did, however, provide an exemption for a qualified small business. The business interest limit doesn't apply to a business with average gross receipts of \$25 or million or less (indexed to \$26 million for 2019) for the three previous tax years.

**New law changes:** The CARES Act raises the limit on business interest deductions from 30% of ATI to 50% of ATI for the 2019 and 2020 tax years. Therefore, a business may amend its 2019 return. In addition, a business can elect to calculate the 50% limit for 2020 based on its ATI in 2019. This could provide a bigger deduction for businesses that expect to have reduced taxable income in 2020 due to the COVID-19 outbreak.

The election may be especially beneficial to a business with a short 2019 tax year. By "grossing up" the deemed ATI based on the entire year, it may be entitled to a more favorable deduction.

**Note:** Due to quirk in the CARES Act, the 50%-of-ATI limit applies to partnerships in 2020, but not in 2019. In other words, the partnership is stuck with the 30% limit for the 2019 tax year. Any business interest expense that is disallowed is passed to the partners and is suspended at the partner level under the TCJA rules.

However, 50% of the suspended business interest is fully deductible at the partner level on a 2020 return. This special tax treatment is automatic unless a partner elects on a 2020 tax return for it not to apply. The remainder from 2019 is suspended until

the partnership generates enough taxable income or excess interest income is passed

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Recommendation: Promptly notify clients affected by these changes. This is especially important for partners in partnerships who should consider their options. They will likely require your expert guidance going forward.

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