

Initial Overview

Consolidated Appropriations Act 2021

As of December 23, 2020

The Consolidated Appropriations Act, 2021, H.R. 133, passed both houses of Congress late on December 21, 2020, but President Donald Trump said Tuesday night that he might not sign the bill immediately, if at all.

There is a lot going on in this bill which is very heavily weighted in both tax and financial provisions. The total bill consists of 5,593 pages with \$900 billion in Coronavirus stimulus relief along with an additional \$1.4 trillion in omnibus spending to prevent a government shutdown.

As we await, President Trump's signature we have put together the following selective, high-level overview of the bill's major tax and relief provisions. This bill is not law as of this writing. Additionally, since this law is in its initial drafting, we expect significant regulations as it becomes law and begins being implemented.

Paycheck Protection Program (PPP) Changes

Deductibility of Paycheck Protection Program Expenses

One of the most widely-discussed aspects of the PPP process in recent months related to potential tax implication of loan forgiveness, specifically with regards to the deductibility of expenses PPP borrowers paid out of PPP funds that had already been, or were expected to be, partially or fully forgiven. The Act addressed this issue and explicitly clarified the original intent of Congress to provide that PPP-funded expenses of borrowers are fully deductible for federal income tax purposes, whether or not the PPP loan is or will be forgiven. The Act further clarifies that these deductibility provisions apply both to initial PPP loans funded earlier in 2020, as well as PPP Second Draw Loans authorized under the Act that are discussed further below.

In addition to the clarification about the deductibility of expenses paid with PPP funds, the bill clarifies that gross income does not include forgiveness of certain loans, emergency Economic Injury Disaster Loan grants, and certain loan repayment assistance, each as provided by the CARES Act. The provision also clarifies that deductions are allowed for otherwise deductible expenses paid with the amounts not included in income by this section



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and that tax basis and other attributes will not be reduced as a result of the exclusion of those amounts from gross income.

The bill also gives Treasury authority to waive information filing requirements for any amount excluded from income by reason of the exclusion of covered loan amount forgiveness from taxable income, the exclusion of emergency financial aid grants from taxable income, or the exclusion of certain loan forgiveness and other business financial assistance under the CARES Act from income.

PPP Second Draw Loans

Certain entities are eligible to receive PPP second draw loans subject to more restrictive criteria than the original CARES Act provisions for PPP loans. The following is a summary of the provisions under PPP second draw loans:

- Loan terms and provisions will be the same as the CARES Act provisions, with a 5 year term and 1% interest
- PPP second draw loans are available through March 31, 2021
- Entities are eligible if they have no more than 300 employees and have experienced at least a 25% decline in gross receipts in any quarter during 2020 compared to the same quarter in 2019
 - Additional provisions are included in the Act for borrowers that were not in business for all of 2019, but were in business as of February 15, 2020
 - For businesses with more than one physical location with an NAICS code beginning with 72, the 300-employee limit is per location
 - The 72 NAICS code designation includes Accommodation and Food Services businesses, such as hotels, food service contractors, bars, and restaurants
 - Public companies are not eligible
- Certain business types are not eligible, such as entities involved with illegal activities and businesses primarily engaged in political or lobbying activities, or entities with at least 20% ownership by an entity in China or Hong Kong, or entities with a member of the board of directors that is a China resident
- Affiliation rules are waived with respect to eligibility under the same circumstances as the original CARES Act provisions

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- Entities that receive a Shuttered Venue Operator Grant are not eligible
 - This is special grant program for live venue operators or promoters, theatrical producer, live performing arts organization operator, a relevant museum operator, a motion picture theatre operator or a talent representative
- The PPP second draw loan amount is 2.5 times the average monthly payroll costs, using either the calendar year 2019 or the 1-year period prior to applying for the loan, capped at a maximum loan amount of \$2,000,000
 - Seasonal employers have the option to use average monthly payroll costs for any 12-week period between February 15, 2019 and February 15, 2020
 - Additional provisions are included in the Act for applicants that did not exist as of February 15, 2019, which would entail computing the average monthly payroll costs during the time period in which the borrower was in operations
 - Entities with an NAICS code beginning with 72 are eligible for an amount up to 3.5 times the average monthly payroll costs
- Additional eligibility provisions are included in the Act for farmers and ranchers, housing cooperatives, news organizations, and 501(c)(6) organizations
- Like PPP loans obtained under the original CARES Act provisions, the amount forgiven must consist of at least 60% of payroll costs
- PPP second draw borrowers may elect an 8-week or 24-week covered period

Modifications to the Paycheck Protection Program

Additional expenses now eligible as allowable costs with PPP loans, which are in effect as if included in the original CARES Act. Loans that have already been through the PPP forgiveness process are excluded from these modified terms.

- Covered operations expenditures such as payment for any computing software or cloud computing service that facilitates business operations, product or service delivery, the processing, payment, or tracking of payroll expenses, human resources, sales and billing functions, or accounting and tracking of supplies, inventory, records or expenses
- Covered property damage costs including costs related to property damage and vandalism or looting due to public disturbances that occurred during 2020 that was not covered by insurance or other compensation

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- Covered supplier costs including expenditures made by the entity to a supplier of goods pursuant to a contract, order, or purchase order for the supply of goods that are essential to the operation of the entity at the time at which the expenditure is made
- Covered worker protection expenditures including an operating or capital expenditure that is required to facilitate the adaptation of the business activities to comply with requirements established by governmental agencies, such as personal protective equipment and the purchase, maintenance, and renovation of assets (excluding residential real property or intangible property)
- Payroll costs now include not only employer paid health, dental, and vision costs, but group life and disability as well

Simplified application process for PPP loans up to \$150,000, including loans that were obtained under the original CARES Act provisions:

- Eligible borrowers will be required to complete a 1-page forgiveness application to be established by the SBA
- Limited information will need to be provided to the SBA including number of employees retained as a result of obtaining the loan, the estimated amount of the loan spent on payroll costs, and loan value
- Various certifications to be made by the borrower attesting to compliance with the program's requirements
- Supporting documentation is required to be maintained for up to 4 years
- Lenders may still request certain information to be provided by the borrower

PPP loan recipients that have returned all or part of their PPP loan, or did not accept the full amount for which they were eligible, may reapply for an additional amount allowed under the program.

In addition, any PPP borrower that also received an Economic Injury Disaster Loan (EIDL) grant amount from the SBA will no longer have their EIDL grant amount subtracted from the maximum loan forgiveness amount, and this repeal is effective for PPP borrowers regardless of whether or not they have completed the PPP forgiveness process prior to the effective date of the Act.

The SBA will be required to prepare an audit plan and submit this plan to Congress. All PPP loans will be subject to an audit by the SBA.

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“Recovery Rebate” Payments

The bill provides for additional recovery rebates of up to \$600 for most individual U.S. residents. Married individuals who file a joint return are eligible for a rebate of up to \$1,200. The rebate amounts increase by \$600 for each child under age 17. No rebate will be made to anyone who is claimed as a dependent on another taxpayer’s federal income tax return. The rebate, which will be delivered via direct deposit when possible, is not taxable income; it is an advance payment of a refundable tax credit on the taxpayer’s 2020 federal income tax return.

The rebate amounts are reduced for higher income taxpayers and begin phasing-out for taxpayers once adjusted gross income exceeds \$75,000 (the phase-out threshold is \$112,500 for heads of households and \$150,000 for joint filers). For these higher-income taxpayers, the rebate amount is reduced by \$5 for each \$100 that a taxpayer’s adjusted gross income exceeds the phaseout threshold, and it will be completely phased out when adjusted gross income exceeds \$87,000 for single filers (with no children), \$124,500 for heads of households with one child and \$162,000 for joint filers with no children.

The IRS will use the information on the taxpayer’s 2019 federal income tax return to determine rebate amounts. If no 2019 tax return has been filed at the time of determination, the IRS can use information provided by the Commissioner of Social Security, the Railroad Retirement Board, or the Secretary of Veterans Affairs, as appropriate.

The rebates will not be reduced or offset to pay debts owed to other federal agencies, past-due legally enforceable state income tax obligations or unemployment compensation debts. In addition, the rebates will not be reduced or offset by other assessed federal taxes that would otherwise be subject to levy or collection.

The bill requires the Department of the Treasury to coordinate with the Social Security Administration and other relevant federal agencies to conduct a public awareness campaign regarding the availability of the rebates, including information with respect to individuals who may not have filed a federal income tax return for 2019.

Payroll Related Provisions

Payroll tax credits

The bill extends the refundable payroll tax credits for paid sick and family leave, enacted in the Families First Coronavirus Response Act, P.L. 116-127, through the end of March 2021. It also modifies the payroll tax credits so that they apply as if the corresponding employer mandates were extended through March 31, 2021. The bill also allows individuals to elect to use their average daily self-employment income from 2019 rather than 2020 to compute the credit.

Employee retention tax credit modifications

The bill extends the CARES Act employee retention tax credit (ERTC) through June 30, 2021. It also expands the ERTC and contains technical corrections. The expansions of the credit include:

- An increase in the credit rate from 50% to 70% of qualified wages;
- An increase in the limit on per employee creditable wages from \$10,000 for the year to \$10,000 for each quarter;
- A reduction in the required year-over-year gross receipts decline from 50% to 20%;
- A safe harbor allowing employers to use prior-quarter gross receipts to determine eligibility;
- A provision to allow certain governmental employers to claim the credit;
- An increase from 100 to 500 in the number of employees counted when determining the relevant qualified wage base; and
- Rules allowing new employers who were not in existence for all or part of 2019 to be able to claim the credit.

The bill also (retroactive to the effective date of the CARES Act):

- Provides that employers who receive PPP loans may still qualify for the ERTC with respect to wages that are not paid with forgiven PPP proceeds;
- Clarifies the determination of gross receipts for certain tax-exempt organizations; and
- Clarifies that group health plan expenses can be considered qualified wages even when no other wages are paid to the employee, consistent with IRS guidance.

Deferral of employees' portion of payroll tax

In August, Trump issued a memorandum allowing employers to defer the withholding, deposit, and payment of the employee portion of the old-age, survivors, and disability insurance (OASDI) tax under Sec. 3101(a) and Railroad Retirement Act Tier 1 tax under Sec. 3201 for any employee whose pretax wages or compensation during any biweekly pay period generally is less than \$4,000. It applies to payroll taxes on wages paid from Sept. 1 through Dec. 31, 2020. Under the memorandum, employers are required to increase withholding and pay the deferred amounts ratably from wages and compensation paid between Jan. 1, 2021, and April 30, 2021. The bill extends the repayment period through Dec. 31, 2021.

CARES Act extensions and pandemic provisions

Educator expenses for protective equipment

The bill requires Treasury to issue regulations or other guidance providing that the cost of personal protective equipment and other supplies used for the prevention of the spread of COVID-19 is treated as an eligible expense for purposes of the Sec. 62(a)(2)(D)(ii) educator expense deduction. The regulations or guidance will apply retroactively to March 12, 2020.

Money purchase pension plans

The CARES Act temporarily allows individuals to make penalty-free withdrawals from certain retirement plans for coronavirus-related expenses, permits taxpayers to pay the associated tax over three years, allows taxpayers to recontribute withdrawn funds, and increases the allowed limits on retirement plan loans. The bill adds money purchase pension plans to the retirement plans qualifying for these temporary rules. The provision applies retroactively as if included in Section 2202 of the CARES Act.

Farmer NOL carrybacks

The bill allows farmers who elected a two-year net operating loss (NOL) carryback prior to the CARES Act to elect to retain that two-year carryback rather than claim the five-year carryback provided in the CARES Act. This section also allows farmers who previously waived an election to carry back an NOL to revoke the waiver.

Miscellaneous tax provisions

Temporary allowance of full deduction for business meals

The bill temporarily allows a 100% business expense deduction for meals (rather than the current 50%) if the expense is for food or beverages provided by a restaurant. This provision is effective for expenses incurred after December 31, 2020 and expires at the end of 2022.

Certain charitable contributions deductible by nonitemizers

The bill extends and modifies the \$300 charitable deduction for nonitemizers for 2021 and increases the maximum amount that may be deducted to \$600 for married couples filing jointly. However, the Sec. 6662 penalty is increased from 20% to 50% of the underpayment for taxpayers who overstate this deduction.

Education expenses

The bill repeals the deduction for qualified tuition and related expenses but in its place increases the phaseout limits on the lifetime learning credit (so they match the phaseout limits for the American opportunity credit), effective for tax years beginning after December 31, 2020.

Minimum age for distributions during working retirement

The bill modifies Sec. 401(a) to allow certain qualified pensions to make distributions to workers who are 59½ or older and who are still working. For certain construction and building trades workers, the age is lowered to 55.

Temporary rule preventing partial plan termination

The bill provides that qualified plans will not be treated as having a partial termination during any plan year that includes the period March 13, 2020, through March 31, 2021, as long as the number of active participants covered by the plan on March 31, 2021, is at least 80% of the number covered on March 13, 2020.

Temporary special rule for determination of earned income

The bill allows taxpayers to refer to earned income from the immediately preceding tax year for purposes of determining the earned income tax credit and the additional child tax credit for tax year 2020.

Modification of limitations on charitable contributions

This bill extends for one year (through 2021) the increased limit from the CARES Act on deductible charitable contributions for corporations and taxpayers who itemize.

Temporary special rules for health and dependent care flexible spending arrangements

The bill allows taxpayers to roll over unused amounts in their health and dependent care flexible spending arrangements from 2020 to 2021 and from 2021 to 2022. This provision also permits employers to allow employees to make a 2021 midyear prospective change in contribution amounts.

Disaster tax relief

The bill provides disaster tax relief for individuals and businesses in presidentially declared disaster areas for major disasters (other than COVID-19) declared after December 31, 2019, through 60 days after the date of enactment.

Use of retirement funds for disaster mitigation

The bill allows residents of qualified disaster areas (as defined in the bill) to take a qualified distribution of up to \$100,000 from a retirement plan or individual retirement account (IRA) without penalty. Amounts withdrawn are included in income over three years or may be recontributed to the plan.

Employee retention credit for disaster zones

The bill allows a tax credit of 40% of wages (up to \$6,000 per employee) to employers who conducted an active trade or business in a qualified disaster zone (as defined in the bill). The credit applies to wages paid without regard to whether the employee performed any services associated with those wages.

Qualified disaster relief contributions

The bill modifies the CARES Act's modification of the charitable contribution limits for 2020 to allow corporations to make qualified disaster relief contributions of up to 100% of their taxable income.

Qualified disaster-related personal casualty losses

The bill permits individuals who have a net disaster loss (as modified by the bill) to increase their standard deduction amount by the amount of the net disaster loss.

Tax extenders

The bill makes permanent the following provisions:

- Reduction in medical expense deduction floor, which allows individuals to deduct unreimbursed medical expenses that exceed 7.5% of adjusted gross income instead of 10%.
- Sec. 179D deduction for energy-efficient commercial buildings (the amount will be inflation-adjusted after 2020).
- Gross income exclusion for certain benefits provided to volunteer firefighters and emergency medical responders.

There are also a host of smaller tax provisions which were set to expire that were extended for between one and five years.

We will publish additional information once the bill is signed into law and as regulations continue to develop.

If you have any questions regarding this law or strategies regarding your specific situation, please do not hesitate to contact us at 912.353.7800 or at rob@cordasco.cpa