First Look at the New Covid-Response Stimulus Bill for 2021

By William E. Sigler

The ink is finally drying on the COVID-Related Tax Relief Act of 2020 ("COVIDTRA") and the Taxpayer Certainty and Disaster Tax Relief Act of 2020 ("TCDTR"), both of which are part of the Consolidated Appropriations Act, 2021 ("CAA, 2021") passed by Congress on December 21, 2020, and signed it into law by the President on December 27, 2020.

The CAA, 2021 is a $2.3 trillion spending bill that combines $900 billion in stimulus relief for the COVID-19 pandemic with a $1.4 trillion omnibus spending bill for the 2021 federal fiscal year. The bill is one of the largest spending measures ever enacted, surpassing the $2.2 trillion CARES Act, enacted in March 2020. At 5,593 pages, the legislation is the longest bill ever passed by Congress.

The CCA, 2021 builds on the CARES Act and contains many provisions which are intended to help individuals and business through the COVID-19 pandemic. The new act is extensive, and will affect taxes not only for 2020 and 2021, but in many cases for several years to come.   This article reviews a few of the tax provisions in the act.

I. INDIVIDUAL PROVISIONS

A. Additional 2020 Recovery Rebates.

COVIDTRA provides "additional 2020 recovery rebates" in the amount of $600 ($1,200 for married filing jointly), plus $600 per qualifying child. The credit phases out starting at $75,000 of modified adjusted gross income ($112,500 for heads of household and $150,000 for married filing jointly) at a rate of $5 per $100 of additional income. The credit is not available to nonresident aliens, anyone who qualifies as another person's dependent, estates or trusts.

The credit is available on the taxpayer's 2020 return. Treasury is authorized to issue advance payments based on the information on the taxpayer's 2019 tax return. Eligible taxpayers who were treated as providing returns through the nonfiler portal when they received their economic impact payment under the CARES Act will also receive payments. A taxpayer who receives an advance payment that exceeds the amount of the eligible credit will not have to repay the excess. If the amount of the credit determined on the taxpayer's 2020 tax return exceeds the amount of the advance payment, the taxpayer will receive the difference as a refundable tax credit.

In general, taxpayers without an eligible Social Security number are not eligible for the payment. However, married taxpayers filing jointly where one spouse has a Social Security Number and one spouse does not are eligible for a payment of $600, in addition to $600 per child with a Social Security Number.

Advance payments are generally not subject to administrative offset for past due federal or state debts. The payments are also protected from bank garnishment or levy by private creditors or debt collectors.

B. Selected Other Individual Provisions.

- IRS is directed to clarify that PPE qualifies for the $250 above-the-line deduction available to Kindergarten through 12th grade teachers under IRC §62(a)(2)(D)(iii).
- COVIDTRA excludes certain CARES Act emergency financial aid grants from the gross income of college and university students.
- Certain employees in the building and construction industries who have not separated from employment may take in-service distributions from their qualified plan at age 55.
- In determining the refundable child tax credit and earned income credit for 2020, taxpayers may elect to substitute the earned income for the preceding tax year if greater than the taxpayer's earned income for 2020.
- The rule for 2020 permitting individuals who normally do not itemize deductions to take up to a $300 above-the-line deduction for cash contributions to qualified charitable organizations is extended to 2021.
- The 2020 waiver of the percentage limitation rules for individuals making qualified charitable contributions in cash to 50% charities is extended to 2021. Ordinarily, individuals may not take an itemized deduction of more than 60% of their contribution base for charitable contributions of cash made to 50% charities.

- The special rule for 2020 allowing unused amounts in a health FSA to be used in the following year is extended to 2021. An employee who ceases to participate in the plan during 2020 or 2021 may continue receiving reimbursements through the end of the year. There is a special carry forward rule for dependent care flexible spending arrangements where the dependent aged out during the pandemic.

II. BUSINESS PROVISIONS

A. Paycheck Protection Program ("PPP") Loans.

- COVIDTRA clarifies taxpayers whose PPP loans are forgiven are allowed deductions for otherwise deductible expenses paid with the proceeds of the PPP loan.
- The tax basis and other attributes of the borrower's assets will not be reduced as a result of the loan forgiveness.

B. Economic Injury Disaster Loans ("EIDL").

- COVIDTRA clarifies that gross income does not include forgiveness of EIDL loans, emergency EIDL grants, and certain loan repayment assistance.
- Deductions are allowed for otherwise deductible expenses paid with the amounts not included in income.
- Tax basis and other attributes will not be reduced as a result of those amounts being excluded from gross income.

C. Depreciation of certain Residential Rental Property.

- TCJA allowed real property trade or businesses to elect out of the business interest deduction limitations of Code Sec. 163(j) imposed by the TCJA. In return, for tax years beginning after December 31, 2017, the taxpayer had to treat any elected-for nonresidential real property, qualified improvement property and residential rental property as subject to the alternative depreciation system ("ADS"). TCJA also changed the ADS recovery period for residential rental property from 40 years to 30 years for property placed in service after December 31, 2017.
- For tax years beginning after December 31, 2017, TCDTR assigns a 30-year ADS depreciation period to residential rental property even though it was placed in

service before January 1, 2018, if (i) the property is held by an electing real property trade or business and, (ii) before January 1, 2018, it wasn't subject to the ADS.

D. Selected other Business Provisions.

- Taxpayers may generally deduct the ordinary and necessary food and beverage expenses associated with operating a trade or business, including meals consumed by employees on work travel. The deduction is generally limited to 50% of the otherwise allowable amount. Under TCDTR, the 50% limit won't apply to expenses for food or beverages provided by a restaurant that are paid or incurred after December 31, 2020, and before January 1, 2023.
- COVIDTRA allows farmers who elected a two-year net operating loss 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. It also allows farmers who previously waived an election to carry back a net operating loss to revoke the waiver.

III. TAX EXTENDERS

The TCDTR contains numerous tax extenders. The following highlights a few of them:

- The 7.5% of AGI threshold for itemizing unreimbursed medical expenses is made permanent after December 31, 2020.
- The Work Opportunity Tax Credit is extended through 2025. This is a tax credit available to employers hiring individuals who are members of one or more of ten targeted groups.
- The exclusion from gross income for discharge of indebtedness income from qualified principal residence debt up to a $2 million limit ($1 million for married individuals filing separately) is extended through 2025. Previously, it only applied to qualified principal residence indebtedness discharged pursuant to a binding written agreement entered into before January 1, 2021.
- The employer credit for paid family and medical leave under IRC Section 45S is extended through 2025. It had applied only to tax years beginning before January 1, 2021. The credit is based on eligible wages paid to qualifying employees for family and medical leave. The credit is equal to 12.5% of eligible wages provided

that the paid leave is at least 50% of those wages, and it is increased by 0.25 percentage points (but not above 25%) for each percentage point that the rate of payment exceeds 50%. The maximum amount of family and medical leave that may be taken into account with respect to any qualifying employee is 12 weeks per tax year.

- Under IRC Section 127, educational assistance provided under an employer's qualified educational assistance program up to an annual maximum of $5,250 is excluded from the employee's income. The CARES Act added "eligible student loan repayments" made after March 27, 2020, and before January 1, 2021 as a permissible payment. The CCA, 2021 extends the exclusion for loan repayments through 2025.

IV. PENSION AND HEALTH PROVISIONS

- In-service distribution from a money purchase pension plan can qualify as "coronavirus-related distributions" ("CRD") exempt from the 10% premature distribution penalty. This provision applies retroactively as if included in the CARES Act. Previously, a qualified pension plan (defined benefit ?plan or money purchase pension plan) was not permitted to make a distribution before an otherwise ?permitted distributable event merely because the distribution, if made, would qualify as a CRD. ?Additionally, a qualified pension plan was not permitted to make a distribution in a form other than a ?qualified joint and survivor annuity without spousal consent, even though such distribution, if ?made, could be treated as a CRD. ?
- Due to market volatility caused by the pandemic increasing defined benefit pension plan underfunding, a one-time election is allowed, not later than December 31, 2021, to end transfers under IRC Section 420 from a defined benefit pension plan to a retiree health benefits account and/or a retiree life insurance account within the pension if certain requirements are met.
- A qualified plan won't be treated as having a partial termination (e.g., resulting in full vesting) during any plan year which includes the period beginning on March 13, 2020, and ending on March 31, 2021, if the number of active participants covered by the plan on March 31, 2021 is at least 80% of the number of active participants covered by the plan on March 13, 2020.
- Group health plans are required to implement procedures to prevent surprise medical bills.

V. SELECTED PAYROLL PROVISIONS

A. Paid Sick and Family Leave Credits.

Under the Families First Coronavirus Response Act (“FFCRA”), employers are required to provide employees with Emergency Paid Sick Leave of up to 80 hours (or the number of hours worked over two-week period if part-time) financed through a refundable tax credit provided on a quarterly basis and allowed against the employer’s Social Security and Medicare taxes, payable to the employee at either (i) 100% of pay capped at $511 per day and $5,110 in total if due to the employee’s own condition or quarantine, or (ii) 2/3 regular rate of pay capped at $200 per day or $2,000 in total if the employee is caring for others (or because the employee, personally, is experiencing any other condition substantially similar to one specified by the Secretary of Health and Human Services in consultation with the Secretaries of the Treasury and Labor). In addition, employees who have been employed with a covered employer for at least 30 days are eligible for Emergency Family Medical Leave under which no pay is provided for the first 10 days (unless employer has a different policy or Emergency Paid Sick Leave is paid concurrently) and thereafter at 2/3 regular rate for next 10 weeks capped at $200 per day or $10,000 in total. This leave is also financed through a refundable tax credit provided on a quarterly basis and allowed against the employer’s Social Security and Medicare taxes. These requirements apply to employers with fewer than 500 employees. Employers with fewer than 50 employees may qualify for an exemption from the requirement to provide paid leave due to school closings or the unavailability of child care if the leave payments would “jeopardize the viability of the business as a going concern.”

The Additional Coronavirus Response and Relief (ACRR), part of CAA, 2021, extends the tax credits available for qualifying FFCRA leaves, which employers are no longer mandated to provide but may voluntarily provide through March 31, 2021. It similarly extends the credits available to self-employed individuals, and allows them to use their reported wages from tax year 2019 instead of tax year 2020 to compute the credit. Further, it conforms the definitions of qualified wages for paid sick and family leave with the IRC and excludes leave payments from employer Social Security employment taxes.

B. August 8, 2020, Presidential Memorandum.

On August 8, 2020, the President signed a Presidential Memorandum directing the Treasury Secretary to permit the postponement of the withholding, deposit, and payment of the employee’s share of Social Security tax (6.2%) on wages and compensation paid from September 1, 2020 through December 31, 2020 for employees whose wages or compensation payable during any biweekly pay period generally is less than $4,000. Amounts were to be deferred without any penalties, interest, or additional amounts to the tax. The IRS issued Notice 2020-65 to provide further guidance to employers on postponing the withholding and remittance of the taxes ratably from wages and compensation paid between January 1, 2021 and April 30, 2021. Penalties, interest, and additional amounts would begin to incur on May 1, 2021. The ACRR extends the repayment period of the deferred employee taxes through December 31, 2021. It also provides that penalties and interest will not begin to accrue on the deferred amounts until January 1, 2022.

C. Employee Retention Credit.

The Employer Retention Credit ("ERC") is a refundable payroll tax credit under the CARES Act for 50% of qualified wages (including health care costs) of up to $10,000 per employee for a maximum credit of $5,000 per employee. For eligible employers with more than 100 full-time employees, qualified wages paid to an employee may not exceed what the employee would have been paid for working an equivalent duration during the 30 days immediately preceding the commencement of the full or partial suspension or the first day of the calendar quarter in which the employer experienced a significant decline in gross receipts.

The ERC may be claimed for wages paid after March 12, 2020, and before January 1, 2021. "Eligible Employers" include private-sector businesses and tax-exempt organizations whose operations have been fully or partially suspended as a result of a government order limiting commerce, travel, or group meetings. The credit is also provided to employers who have experienced a greater than 50% reduction in quarterly receipts, measured on a year-over-year basis.

Beginning on January 1, 2021 and through June 30, 2021, the TCDTR extends and expands the following CARES Act provisions:

- Increases the ERC rate from 50% to 70% of qualified wages;
- Expands eligibility for the credit by reducing the required year-over-year gross receipts decline from 50% to 20% and provides a safe harbor allowing employers to use prior quarter gross receipts to determine eligibility;
- Increases the limit on per-employee creditable wages from $10,000 for the year to $10,000 for each quarter;
- Increases the 100-employee delineation for determining the relevant qualified

wage base to employers with 500 or fewer employees;
- Allows certain public instrumentalities to claim the credit;
- Removes the 30-day wage limitation, allowing employers to, for example, claim the credit for bonus pay to essential workers;
- Allows businesses with 500 or fewer employees to advance the credit at any point during the quarter based on wages paid in the same quarter in a previous year;
- Provides rules to allow new employers who were not in existence for all or part of 2019 to be able to claim the credit; and
- Provides for a small business public awareness campaign regarding availability of the credit to be conducted by the Secretary of the Treasury in coordination with the Administrator of the Small Business Administration.

The TCDTR also includes the following provisions which are retroactively effective back to March 12, 2020:

- Clarification on the determination of gross receipts for certain tax-exempt organizations;
- Reaffirmation of prior IRS guidance that group health plan expenses can be considered qualified wages even when no wages are paid to an employee; and
- Employers who receive a PPP loan may still qualify for the ERC for wages that are not paid for with forgiven PPP loan proceeds.

VI. PPP LOAN EXPANSION AND CLARIFICATION

A. Second Draw.

The CARES Act authorized the SBA to establish the PPP, which provides up to 24 weeks of cash-flow assistance through 100% federally guaranteed loans to eligible recipients to maintain payroll during the COVID-19 pandemic and to cover certain other expenses. The Paycheck Protection Program Flexibility (“PPPF”) Act made substantial changes to the PPP, including decreasing the percentage that loan proceeds must be used on payroll costs from 75% to 60%, thereby increasing the percentage that may be used for nonpayroll costs such as rent, mortgage interest and utilities from 25% to 40%. Additionally, the PPPF permits borrowers to defer payments of principal, interest, and fees to 10 months after the last day of the covered period (the earlier of 24 weeks or December 31, 2020). Prior to the PPPF Act, the deferral period would end after six months. The application period closed on August 8, 2020. The SBA began approving PPP forgiveness applications and remitting forgiveness payments to PPP lenders on October 2, 2020.

The CAA, 2021 gives the following kinds of businesses that received a PPP loan the opportunity to take a second draw of up to $2 million:

- Employ no more than 300 employees per physical location;
- Have used or will use the full amount of their first PPP loan; and
- Demonstrate at least a 25% reduction in gross receipts in the first, second, or third quarter of 2020 relative to the same 2019 quarter. Applications submitted on or after January 1, 2021 are eligible to utilize the gross receipts from the fourth quarter of 2020.

Second draws on PPP loans may be for up to 2.5 times the average monthly payroll costs in the one year prior to the loan or the calendar year. However, borrowers in the hospitality or food services industries (NAICS code 72) may receive loans of up to 3.5 times average monthly payroll costs. Only a single second draw is permitted to an eligible entity.

Second draw borrowers of no more than $150,000 may submit a certification, on or before the date the loan forgiveness application is submitted, attesting that the eligible entity meets the applicable revenue loss requirement. Non-profits and veterans' organizations may use gross receipts to calculate their revenue loss standard.

The second draw loan may be forgiven for payroll costs of up to 60% (with some exceptions) and nonpayroll costs such as such as rent, mortgage interest and utilities of 40%. The current safe harbors on restoring full-time employees and salaries and wages are extended.

B. Clarification of Tax Treatment of PPP Loans.

- Gross income does not include any amount that would otherwise arise from the forgiveness of a PPP loan.
- Deductions are allowed for otherwise deductible expenses paid with the proceeds of a PPP loan that is forgiven.
- The tax basis and other attributes of the borrower's assets will not be reduced as a result of the loan forgiveness.
- These provisions are effective as of the date of enactment of the CARES Act, and apply to second draws on PPP loans.

C. Additional PPP Eligible Expenses.

Additional allowable and forgivable uses are provided for PPP loans:

- Payment for any software, cloud computing, and other human resources and accounting needs.
- Costs related to property damage due to public disturbances that occurred during 2020 that are not covered by insurance.
- Expenditures to a supplier pursuant to a contract, purchase order, or order for goods in effect prior to taking out the loan that are essential to the recipient’s operations at the time at which the expenditure was made. Supplier costs of perishable goods can be made before or during the life of the loan.
- Personal protective equipment and adaptive investments to help a loan recipient comply with federal health and safety guidelines or any equivalent State and local guidance related to COVID-19 during the period between March 1, 2020, and the end of the national emergency declaration.

Borrowers with loans made under PPP before, on, or after the enactment of these changes are eligible to utilize the expanded forgivable expenses other than borrowers who have already had their loans forgiven.

D. Simplified Application for Loans under $150,000.

There is a new simplified application process for loans under $150,000. A borrower will receive forgiveness if the borrower signs and submits to the lender a certification that is not more than one page in length, includes a description of the number of employees the borrower was able to retain because of the covered loan, the estimated total amount of the loan spent on payroll costs, and the total loan amount. The borrower must also attest that borrower accurately provided the required certification and complied with PPP loan requirements.

The SBA is required to create this form within 24 days of enactment and may not require additional materials unless necessary to substantiate revenue loss requirements or satisfy relevant statutory or regulatory requirements. Additionally, borrowers are required to retain relevant records related to employment for four years and other records for three years. The SBA may review and audit these loans to ensure against fraud.

E. PPP Miscellany.

- A borrower may elect a covered period ending at the point of the borrower's choosing between 8 and 24 weeks after loan origination.
- Employer-provided group insurance benefits are included in payroll costs. This includes group life, disability, vision, or dental insurance.
- A business or organization that was not in operation on February 15, 2020 is not eligible for an initial PPP loan or a second draw PPP loan.
- A seasonal employer is defined to mean one which (i) operates for no more than seven months in a year, or (ii) earned no more than 1/3 of its receipts in any six months in the prior calendar year.

VII. PARTING THOUGHTS

There would be an understandable tendency to believe that the CCA, 2021 was intended primarily to aggravate tax practitioners. However, its important to keep in perspective that the tax provisions are only part of a larger stimulus bill. When the stimulus will be felt by the economy is another matter. It may not be until the latter half of 2021 when, hopefully, the distribution of COVID-19 vaccines helps both individuals and business return to a sense of normalcy.

In the near term, other drags on the economy include state and local governments, which are struggling with budget shortfalls, and the looming eviction crisis. In the longer term, the U.S. budget deficit soared to a record $3.1 trillion for the fiscal year ended September 30, 2020, which was more than triple that of fiscal 2019 and easily eclipsed the previous record of $1.4 trillion recorded in 2009.

If anything is clear it's that much more work lies ahead . . .