BENNETT THRASHER LLP

2021 Consolidated Appropriations Act: Tax Provisions and Impact

After several days of negotiation, the Consolidated Appropriations Act, 2021 (the "CAA") was passed by Congress on December 21, 2020 and signed by the president on December 27. The legislation includes numerous provisions intended to provide additional relief in response to the ongoing COVID-19 crisis. Many of the provisions contained within the CAA are either modifications or extensions of changes made by the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act") enacted on March 27, 2020. Key individual and business tax provisions and their impacts are summarized below.

Direct Stimulus Payments

The CARES Act provided for direct stimulus payments to individual taxpayers whose incomes fell below certain thresholds, up to a maximum of $1,200 ($2,400 if married) with an additional $500 payment per child. Under the CAA, eligible individuals can receive an additional $600 ($1,200 if married) as well as a $600 payment per qualifying child. Individuals with income below $75,000 ($150,000 if married) are eligible to receive the full stimulus payment, with the amount being phased out completely at an income level of $87,000 ($174,000 if married).

The stimulus payment is treated as a credit on an eligible individual's 2020 tax return, and the amount actually received will be reconciled against the allowable amount per the tax return. If an individual is entitled to an amount larger than the stimulus check they received, the difference will be treated as a refundable credit on their 2020 tax return. However, if the stimulus check they received is greater than the credit allowable on the 2020 tax return, they are not required to repay the excess.

Charitable Contribution Deductions

To incentivize charitable giving during the COVID-19 crisis, the CAA extends two of the provisions of the CARES Act that provided for increased deductibility of charitable contributions. The original CARES Act provisions and the extensions made by the CAA are as follows:

- Allows individuals who do not itemize deductions to take up to $300 of cash contributions to qualified charitable organizations as an above-the-line deduction in both 2020 and 2021 ($600 if married filing jointly in 2021).
- Removes the percentage limitation on adjusted gross income for individuals making cash contributions to public charities for both 2020 and 2021. As a result, an individual can reduce taxable income to zero in these years through qualifying contributions.

Tax Treatment of PPP Loan Expenditures

Under the CARES Act, the recipient of a Paycheck Protection Program ("PPP") loan can use the proceeds for several qualifying uses, including payroll costs, employee healthcare benefits, mortgage interest, rent and utilities. PPP loan funds used for these purposes are eligible for loan forgiveness. The IRS initially indicated that expenditures paid for using a PPP loan that was subsequently forgiven would not be deductible. However, the CAA clarifies that qualifying expenditures paid with forgiven PPP loan proceeds are fully deductible. In addition, the tax basis and other tax attributes of the loan recipient will not be affected by the loan forgiveness.

Business Meals Deduction

Meal expenses are generally allowable as a deduction provided that the expense serves a bona fide business purpose; however, there has been a 50 percent "disallowance" on the deduction amount since 1993. In response to the economic difficulties faced by the restaurant industry, the CAA has removed the 50 percent deduction limit on business meals in 2021 and 2022, but only for food and beverages provided by a restaurant. Other business meals that are not provided by a restaurant remain subject to the 50 percent limitation. The IRS will presumably issue additional guidance in the future clarifying which establishments qualify as restaurants for purposes of the new law.

Tax Credits

The employee retention tax credit, originally enacted as part of the CARES Act, provides for a refundable payroll tax credit of 50% of qualified wages paid from March 13, 2020 through December 31, 2020, for certain qualifying employers. The CAA extends and significantly modifies this tax credit for the period from January 1, 2021 through June 30, 2021 as follows:

- Increases maximum per-employee qualified wages from $10,000 per **year** to $10,000 per **quarter**.
- Increases the credit rate from 50 percent to 70 percent of qualified wages.
- Reduces the threshold to qualify as having experienced a substantial reduction of gross income from 50 percent to 20 percent year-over-year.
- Creates a safe harbor so that employers can use prior-quarter gross receipts in determining eligibility.
- Modifies the definition of qualifying wages to include all wages paid by eligible employers with up to 500 employees (previously limited to those with up to 100 employees). For businesses with more than 500 employees, qualified wages only include

those paid to employees during the period when they are not providing services to the employer.

- Clarifies that new employers, not just those in existence during 2019, are eligible for the credit.
- Extends the credit through June 20, 2021.

In addition, the employer credit for paid sick and family leave, which was included in the Families First Coronavirus Response Act, is extended by the CAA from December 31, 2020 through March 31, 2021. The law also provides for an equivalent credit for self-employed individuals, who can elect to use average daily self-employment income from 2019 in computing the credit.

Other Tax Provisions

Several other changes are made effective by the CAA to provide tax relief to individuals and businesses:

- **Deferred Payroll Taxes:** Employers who chose to defer employees' share of payroll taxes during the period from September 1, 2020 through December 31, 2020, now have until December 31, 2021 to pay back those amounts.
- **Teacher Expenses:** Personal protective equipment and other supplies used by teachers to slow the spread of COVID-19 and purchased after March 12, 2020 are eligible for an above-the-line deduction of up to $250.
- **CTC/EITC Flexibility:** In determining the child tax credit and earned income tax credit for 2020, an individual can elect to use 2019 earned income in determining the credit amounts. This will allow taxpayers whose incomes decreased in 2020 to receive greater refunds.
- **FSA Changes:** Amounts remaining in a health flexible spending arrangement at the end of the year may be used to cover expenses of up to $550 incurred during the following year for plan years ending in 2020 and 2021.
- **Income Exclusion for Grants/Loan Forgiveness:** College students who received emergency financial aid under the CARES Act, as well as small businesses that received Economic Injury Disaster Loans (EIDL) grants, are not required to include these amounts in taxable income.
- **Residential Rental Depreciation:** A real property trade or business that elected out of the business interest deduction limitations of Internal Revenue Code Sec. 163(j) can now depreciate residential rental property placed in service before 2018 over 30 years instead of 40 years.

- **Disaster Tax Relief:** Individuals and businesses located in a federally declared disaster area during 2020 are eligible for several forms of relief, including the forgiveness of early-withdrawal penalties for retirement plan distributions, an increase in the amount of allowable loans from a retirement plan, an additional employee retention credit and expanded use of casualty losses.

Tax Break Extensions

Finally, the CAA addresses several tax breaks that were set to expire at the end of 2020 by extending them per the table below:

Provision	CAA Extension
7.5 percent of AGI floor on medical expense deduction	Permanent extension
Above-the-line deduction for qualified tuition expenses	Not extended, expires after 2020
Mortgage insurance premiums treated as qualified residence interest	Extended through 2021
Exclusion from income of benefits provided to volunteer firefighters and emergency medical responders	Permanent extension
Exclusion from income of discharge of qualified principal residence indebtedness	Extended through 2025 (with modifications)
Exclusion from income of certain employer payments of student loans	Extended through 2025
Special expensing for film, TV and theatrical productions	Extended through 2025
Energy efficient commercial buildings deduction	Permanent extension (with modifications)
Residential energy efficient property credit	Extended through 2022
Nonbusiness energy property credit	Extended through 2021
Credit for new qualified fuel cell motor vehicles	Extended through 2021
Credit for alternative fuel vehicle refueling property	Extended through 2021
Two-wheeled plug-in electric vehicle credit	Extended through 2021
New markets tax credit	Extended through 2025

Work opportunity tax credit	Extended through 2025
Credit for paid family and medical leave	Extended through 2025
Empowerment zone tax incentives	Extended through 2025 (with modifications)
Look-through rule for related controlled foreign corporations	Extended through 2025

Contact Us

While most of the tax provisions of the Consolidated Appropriations Act, 2021 were simply modifications or expansions of existing provisions, they do provide potential tax savings opportunities for many individuals and businesses. Taxpayers should analyze the new provisions in consultation with their tax advisor to determine how to best take advantage of these relief measures, as many are set to expire by the end of 2021.

If you have questions regarding the changes discussed above and how they will affect your tax situation, please contact your Bennett Thrasher tax advisor by calling 770.396.2200.