BENNETT THRASHER LLP

American Rescue Plan Act of 2021
Summary of Tax Provisions

A full summary of tax provisions related to the American Rescue Plan Act of 2021 is below.

Tax Relief for Individuals

Recovery Rebate Payments: the American Rescue Plan Act (ARPA) includes a third round of direct stimulus payments for taxpayers. The legislation provides for payments of up to $1,400 for eligible individual taxpayers, $2,800 for married couples filing jointly and $1,400 for each qualifying dependent (both children and adults). An "eligible individual" is any individual other than a nonresident alien or an individual who is a dependent of another taxpayer for the tax year. The provisions that apply to this third round are similar to those that applied to the first two rounds. The payments are essentially credits against 2021 taxes, but fully refundable and payable in advance, and subject to income limitations. The relevant provisions under the ARPA include the following:

- Phase-out for economic impact payments: the $1,400 payment will begin to ratably phase out when adjusted gross income (AG) reaches $75,000 for single taxpayers, $112,500 for heads of household and $150,000 for joint filers. Payments will be fully phased out when AGI reaches $80,000 for single taxpayers, $120,000 for heads of household and $160,000 for joint filers.
- The payments will be based on AGI and filing status reported for the 2020 tax year, but 2019 tax information will be used for taxpayers who have not yet filed their 2020 returns.
- Taxpayers who receive an advance payment that exceeds their maximum eligible credit amount based on their 2021 tax return will not be required to repay the excess amount. Conversely, if the advance payment based on either their 2019 or 2020 tax information is less than the maximum eligible credit amount based on their 2021 tax return, the taxpayer will be allowed to claim the difference on their 2021 tax return.
- *Note*: all dependents, regardless of age, will qualify for the extra payment, whereas for the first two rounds of stimulus payments dependents were limited to those under the age of 17.
- *Note*: if you will qualify for a higher payment based on your 2019 income and/or filing status compared to 2020, you may wish to delay filing your 2020 tax return until the filing deadline to maximize the amount of your stimulus payment.

Child Tax Credit: the ARPA significantly enhances this credit, but only for the 2021 tax year, and the following are the pertinent provisions:

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- The maximum credit increases from $2,000 to $3,000 per child (or $3,600 for a child under the age of six).
- The credit amount is made fully refundable.
- The maximum age of qualifying children is increased to include 17-year old children.
- The increased per-child credit amounts will be reduced by $50 for every $1,000 of modified AGI exceeding $150,000 for joint filers, $112,500 for heads of households and $75,000 for other filers.
- The credits for 2021 will be partially advanceable:

    - The Treasury and IRS are directed to issue advance payments of half of the credit amount beginning on July 1, 2021 which are to be issued monthly, if feasible, or as frequently as possible if monthly payments are not possible.
    - These advance payments will be based on taxpayers' 2020 tax returns, or if they are not yet filed, their 2019 returns.
    - The IRS has been directed to create an online portal to allow taxpayers to update information or elect out of advance payments.
    - The remaining half of the credit not paid in advance is received when filing the 2021 tax return. Taxpayers will reconcile their advance payments with their allowable credit on their tax returns and will be required to repay any excess advance payments. However, a special rule will prevent taxpayers below a certain income threshold from being required to repay overpayments of up to $2,000 per child. The full $2,000 amount is ratably reduced for taxpayers with income above a threshold amount ($40,000 for single filers, 50,000 for head of households and $60,000 for joint filers.

<u>Earned Income Tax Credit (EITC)</u>: the ARPA includes several enhancements to the earned income tax credit, including the following:

- For 2021 the maximum age limitation for being eligible to receive the credit is eliminated, and the minimum age to be eligible to receive the credit is reduced from 25 to 19 (except that the minimum age is 24 in the case of full-time students).
- The credit percentage has been expanded, and the phase-out thresholds are increased.
- A special rule has been permanently created that allows separated spouses to claim the EITC on an individual basis.
- The threshold for disqualifying investment income is also permanently increased from $3,650 for 2021 to $10,000, adjusted for inflation after 2021.
- Taxpayers are temporarily permitted to substitute their 2019 earned income for 2021 earned income when claiming the EITC on 2021 tax returns, if 2021 earned income was less than their 2019 earned income.

Child and Dependent Care Tax Credit: this credit is significantly enhanced for 2021 only, as the ARPA temporarily increases the amount of the credit by increasing the allowable expenses, the credit percentage, and the phase-out. The enhancements for 2021 include the following:

- The amount of eligible expenses qualifying for the credit are increased from $3,000 to $8,000 for one qualifying individual, and from $6,000 to $16,000 for two or more qualifying individuals.
- The credit has been made fully refundable.
- The maximum credit rate is increased from 35% to 50% of qualified expenses.
- The 50% credit rate will begin to phase out at AGI of $125,000 and will remain at 20% for households with income between $185,000 and $400,000.
- A separate provision increases the maximum exclusion for employer-provided dependent care assistance for 2021 from $5,000 to $10,500, or from $2,500 to $5,250 in the case of a married taxpayer filing separately.
- *Note:* for taxpayers with AGI of $125,000 or less, the maximum amount of the credit is $8,000 ($16,000 x 50%) for taxpayers with two or more qualifying individuals.

Tax exclusion for certain unemployment insurance benefits: the enhanced federal supplement to state-level unemployment benefits, set to expire on March 14, is extended through September 6, 2021 at a rate of $300 per week. Significantly, up to $10,200 in unemployment insurance benefits received in 2020 will be excluded from income for households with income below $150,000. This same phase-out cliff apples to all taxpayers.

- *Note*: the ARPA does not provide for a phase-out based on AGI. Therefore, if a taxpayer has income of at least $150,000, all the taxpayer's unemployment compensation will be included in gross income.
- *Note*: the same $150,000 limit applies to returns filed jointly, as head of household, or with single status. However, in the case of a joint return, the $10,200 exclusion applies separately to each spouse.
- *Note*: this income exclusion may require individuals who have already filed their 2020 returns to file an amended return to claim the benefit.

Gross income exclusion for forgiven student loan indebtedness: student loan indebtedness forgiven after December 31, 2020 and before January 1, 2026 will be excluded from gross income.

ACA Premium Tax Credits: for 2021 and 2022, the ARPA will reduce an individual's or a family's share of premiums used in determining the amount of the premium tax credit under the Patient Protection and Affordability Care Act (ACA) and make the credit available to taxpayers with incomes above the present-law limitation of 400 percent of the federal poverty line for the applicable family size.

Business Tax Relief

Employee Retention Credit (ERC): the ARPA expands and extends this credit, which was extended by the Consolidated Appropriations Act (CAA) through June 30, 2021, through the end of 2021. This will double the maximum credit for 2021 from $14,000 to $28,000 per employee ($7,000 per employee per quarter). Other provisions applicable to the ERC include the following:

- Startup employers: because many startup businesses had difficulty establishing their eligibility for the ERC under the prior rules, the American Rescue Plan provides a special, limited version of the ERC to businesses that began operations after Feb. 15, 2020, have less than $1 million in annualized gross receipts, and would not otherwise satisfy the employer eligibility tests (based on gross receipts decline or suspension of operations due to a governmental order). The credit for startups is calculated under the normal ERC rules based on per-employee qualified wages but is capped at $50,000 per quarter per employer.
- Severely financially distressed employers: employers that suffered severe financial distress, defined as a 90% or greater decline in gross receipts as compared to the same quarter in 2019, will not be subject to the large employer rule limiting qualified wages to amounts paid to employees that aren't providing services. As a result, eligible employers may claim the credit on wages paid to employees that continued to work during the applicable calendar quarter.
- The credit will apply to the employer's share of Medicare taxes after June 30, 2021.
- Qualified wages do not include wages taken into account as payroll costs under certain SBA programs.
- *Note*: with this extension of the ERC a business may potentially claim a maximum credit of $33,000 per employee ($5,000 for 2020 and $7,000 per quarter for 2021).

Paid Sick and Family Leave Credits (FFCRA Credits): the ARPA extends the applicable period for claiming payroll credits for COVID-19-related paid sick leave and paid family leave from March 31, 2021 to September 30, 2021, but employers are not required to provide such leave. Other changes made by the ARPA:

- The limit on applicable wages for which the credit can be claimed is increased from $10,000 to $12,000, effective after March 31, 2021.
- The number of days for which the credit can be claimed by self-employed persons is increased from 50 days to 60 days, retroactively effective after December 31, 2020.
- The leave for which a credit can be claimed is expanded to include time off to receive a COVID-19 vaccine, or to recover from a vaccine-related illness or injury.

- The 10-day limitation on the maximum number of days for which an employer can claim the paid sick leave credit with respect to wages paid to an employee is reset. The current limitation runs from the start of the credit in 2020 through March 31, 2021. The new limitation applies to sick days after March 31, 2021, while the limitation for self-employed persons resets on January 1, 2021.
- The credit will be applicable to Medicare taxes effective March 31, 2021.

Tax treatment of COVID-19 relief: targeted Economic Injury Disaster Loans (EIDL) and Restaurant Revitalization Grants received from the Small Business Administration will not be subject to income tax, similar to the provisions included in the CAA applicable to EIDL grants, grants to entertainment venues, educational grants, etc. This exclusion from gross income will not result in a denial of a deduction, reduction of tax attributes, or denial of a basis increase, which mirrors the tax treatment of forgiven PPP loans.

COBRA Premium Assistance Credits: the program allowing individuals who are terminated from employment to retain their health insurance through the former employer by paying the premiums themselves is enhanced by providing that individuals receiving COBRA coverage are not required to make premium payments for coverage between April 1, 2021 and September 30, 2021. Because the employer or plan sponsor will need to fund the cost of this coverage, the ARPA provides a tax credit equal to the amount of the premiums. Like the employee retention credit and FFCRA credits, the COBRA premium assistance credit is a refundable credit that is applied against certain payroll taxes.

Revenue-Raising Tax Provisions

Extension of excess business loss limitation: the “excess business loss” rule, which generally limits certain current losses attributable to trades or businesses for noncorporate taxpayers to $250,000 ($500,00 for joint filers), is extended by one year through 2026. This limitation was enacted in the Tax Cuts and Jobs Act but was suspended for taxable years beginning in 2018, 2019 and 2020 by the CARES Act.

Repeal of worldwide interest allocation election**:** the election that allows members of a worldwide affiliated group of corporations to allocate and apportion their combined interest expense among their members is repealed, effective for tax years beginning after 2020. This provision retroactively repeals this optional election which became effective on January 1, 2021.

Compensation deductions for publicly traded companies: the rules limiting executive compensation deductions to publicly traded companies are extended. Specifically, this provision prohibits deductions exceeding $1 million for the five highest compensated employees other than the CEO and CFO.

Action Items

The following are a few immediate steps to consider, depending on individual circumstances:

- Consider delaying filing your 2020 tax return until the filing deadline to maximize the amount of your stimulus payment if you will qualify for a higher payment based on your 2019 income and/or filing status compared to 2020.
- If your 2020 income was below $150,000 and you already filed your 2020 tax return which included taxable unemployment insurance benefits, the IRS posted a statement on March 12, 2021 recommending that you do not file an amended return until the IRS issues additional guidance.
- Consider if your business will now qualify for the Employee Retention Credit after reviewing the new provisions that have been added targeting start-ups and severely financially distressed employers.

Contact Us

We will continue to monitor legislative developments affecting our clients. For further questions regarding how the American Rescue Plan Act will impact your personal or business taxes, please contact your Bennett Thrasher advisor by calling 770-396-2200.