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Many tax provisions appear in year-end coronavirus relief bill

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The omnibus spending and coronavirus relief bill passed by Congress includes many tax provisions, including the extension of various expiring provisions, extensions and expansions of certain earlier pandemic tax relief provisions, and much more. The Consolidated Appropriations Act, 2021, H.R. 133, passed both houses of Congress on Dec. 21, and President Donald Trump signed the bill into law on Dec. 27.

Among its general tax provisions, the bill temporarily (through 2022) allows 100% deductibility of certain business meal expenses, extends the $300 charitable contribution deduction for nonitemizers, and enacts various disaster tax relief provisions.

Pandemic relief

The bill provides a refundable tax credit in the amount of $600 per eligible family member by adding a new Sec. 6428A to the Code. The credit is $600 per taxpayer ($1,200 for married taxpayers filing jointly), in addition to $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 taxpayers filing jointly) at a rate of $5 per $100 of additional income. Treasury is authorized to issued advance payments of this credit (economic impact payments) in the same way it made stimulus payments under the Coronavirus Aid, Relief, and Economic Security (CARES) Act, P.L. 116-136.

Deductibility of PPP-funded expenses

The bill clarifies that gross income does not include any amount that would otherwise arise from the forgiveness of a Paycheck Protection Program (PPP) loan. This provision also clarifies that deductions are allowed for otherwise deductible expenses paid with the proceeds of a PPP loan that is forgiven and that the tax basis and other attributes of the borrower's assets will not be reduced as a result of the loan forgiveness. The provision is effective as of the date of enactment of the CARES Act. The provision provides similar treatment for Second Draw PPP loans, effective for tax years ending after the date of enactment of the provision.

While the CARES Act excluded PPP loan forgiveness from gross income, it did not specifically address whether the expenses used to achieve that loan forgiveness would continue to be deductible, even though they would otherwise be deductible. In April, the IRS issued Notice 2020-32, which stated that no deduction would be allowed under the Internal Revenue Code for an expense that is otherwise deductible if the payment of the expense results in forgiveness of a PPP loan because the income associated with the forgiveness is excluded from gross income for purposes of the Code under CARES Act Section 1106(i).

In November, the IRS then expanded on this position by issuing Rev. Rul. 2020-27, which held that a taxpayer computing taxable income on the basis of a calendar year could not deduct eligible expenses in its 2020 tax year if, at the end of the tax year, the taxpayer had a reasonable expectation of reimbursement in the form of loan forgiveness on the basis of eligible expenses paid or incurred during the covered period.

The AICPA disputed this interpretation of the CARES Act loan forgiveness rules, arguing that it was not Congress's intent to disallow the deduction of otherwise deductible expenses. Congress has now agreed with that position.

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 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.

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.

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.

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%) as long as the expense is for food or beverages provided by a restaurant. This provision is effective for expenses incurred after Dec. 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 Sec. 222 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 Dec. 31, 2020.

Minimum low-income housing tax credit rate: The bill establishes a 4% rate floor for calculating credits related to acquisitions and housing bond-financed developments for purposes of the Sec. 42 low-income housing tax credit, effective in 2021.

Depreciation of certain residential rental property over 30-year period: The bill provides that the recovery period applicable to residential rental property place in service before Jan. 1, 2018, and held by an electing real property trade or business is 30 years.

Waste energy recovery property eligible for energy credit: The bill makes waste energy recovery property eligible for the Sec. 48 energy investment tax credit, effective for 2021 through 2023. Waste energy recovery property generates electricity from the heat from buildings or equipment.

Extension of energy credit for offshore wind facilities: The bill extends the Sec. 48 investment tax credit for electing offshore wind facilities that begin construction through 2025.

Minimum rate of interest for certain determinations related to life insurance contracts: The bill updates the Sec. 7702 fixed interest rate for life insurance contracts and ties the rate going forward to benchmark interest rates that are periodically updated.

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 under Sec. 411(d)(3) 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 Sec. 32 earned income tax credit and the Sec. 24(d) 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 Dec. 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:

- Sec. 213(f) 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).
- Sec. 139B gross income exclusion for certain benefits provided to volunteer firefighters and emergency medical responders.
- Sec. 45G railroad track maintenance credit; however, the credit rate is reduced from 50% to 40%.

The bill reduces various excise rates for small brewers and distillers.

Five-year extensions

The bill provides five-year extensions to the following provisions:

- Sec. 45D new markets tax credit.
- Sec. 45S employer credit for paid family and medical leave.
- Sec. 51 work opportunity credit.
- Sec. 108(a)(1)(E) gross income exclusion for discharge of indebtedness on a principal residence.
- Sec. 127(c)(1)(B) exclusion for certain employer payments of student loans.
- Sec. 168(e)(3)(C)(ii) seven-year recovery period for motorsports entertainment complexes.
- Sec. 181 special expensing rules for certain film, television, and live theatrical productions.

- Sec. 954(c)(6) lookthrough treatment of payments of dividends, interest, rents, and royalties received or accrued from related controlled foreign corporations under the foreign personal holding company rules.
- Sec. 1391(d) empowerment zone designation.
- Sec. 4611 Oil Spill Liability Trust Fund financing rate.

The Sec. 1397A increased expensing under Sec. 179 and Sec. 1397B nonrecognition of gain on rollover of empowerment zone investments are both terminated for property placed in service in tax years beginning after Dec. 31, 2020.

The Sec. 1394 empowerment zone tax-exempt bonds and Sec. 1396 empowerment zone employment credit, which expire Dec. 31, 2020, were not extended.

Two-year extensions

The bill provides a two-year extension to the following provisions:

- Sec. 25D residential energy-efficient property credit (the bill also makes qualified biomass fuel property expenditures eligible for the credit).
- Sec. 45Q carbon oxide sequestration credit (through 2025).
- Sec. 48 energy investment tax credit for solar and residential energy-efficient property.

One-year extensions

The Act provides one-year extensions to the following provisions:

- Sec. 25C 10% credit for qualified nonbusiness energy property.
- Sec. 30B credit for qualified fuel cell motor vehicles.
- Sec. 30C 30% credit for the cost of alternative (nonhydrogen) fuel vehicle refueling property.
- Sec. 30D 10% credit for plug-in electric motorcycles and two-wheeled vehicles.
- Sec. 35 health coverage tax credit.
- Sec. 40(b)(6) credit for each gallon of qualified second-generation biofuel produced.
- Sec. 45(e)(10)(A)(i) production credit for Indian coal facilities.
- Sec. 45(d) credit for electricity produced from certain renewable resources.
- Sec. 45A Indian employment credit.
- Sec. 45L energy-efficient homes credit.
- Sec. 45N mine rescue team training credit.
- Sec. 163(h) treatment of qualified mortgage insurance premiums as qualified residence interest.
- Sec. 168(e)(3)(A) three-year recovery period for racehorses two years old or younger.

- Sec. 168(j)(9) accelerated depreciation for business property on Indian reservations.
- Sec. 4121 Black Lung Disability Trust Fund increase in excise tax on coal.
- Sec. 6426(c) excise tax credits for alternative fuels and Sec. 6427(e) outlay payments for alternative fuels.
- The American Samoa economic development credit (P.L. 109-432, as amended by P.L. 111-312).

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