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CERTIFIED PUBLIC ACCOUNTANTS

The Consolidated Appropriations Act, 2021, (CAA) was passed by Congress and signed into law at the end of last year and provides $900 billion for COVID-19 relief. Highlights of the provisions include:

2020 Tax Consequences:

- **<u>The CARES Act provided Payroll Protection Program (PPP) loans may be forgivable, in whole or in part, if taxpayers use the proceeds for qualifying expenses (i.e., payroll, benefits, mortgage interest, rent and utilities).</u>** However, unlike other debt that is forgiven, the CARES Act also specifically provides that any PPP loan amounts forgiven do not constitute cancellation of debt income and is non-taxable.

- **<u>The CAA ensures tax deductibility for business expenses paid with forgiven PPP loan funds.</u>** In addition, the CAA also ensures that the tax basis and other attributes of the borrower's assets will not be reduced because of the loan forgiveness.

- **<u>The CAA clarifies that gross income does not include forgiveness of EIDL Loans,</u>** emergency EIDL grants, and certain loan repayment assistance, and business expenses paid for by those funds are allowable deductions and that tax basis and other attributes will not be reduced because of those amounts being excluded from income.

- **<u>The CAA provided for $600 economic impact payments to individuals making up to $75,000 per year</u>** and $1,200 for married couple making up to $150,000 per year, as well as a $600 payment for each child dependent, which in most cases was automatically sent to taxpayers who qualified. If a taxpayer did not receive the full payment, they may be eligible to claim the Recovery Rebate

Credit on their 2020 tax return, which effectively increases the amount of their tax refund or decreases the amount of the tax they owe.

- **Individual taxpayers may elect to substitute the earned income for the preceding tax year if that is greater than the taxpayer's earned income for 2020 in calculating refundable child tax credits and earned income credits** under the CAA.

- **The CARES Act provides that Non-itemizers can take up to a $300 above-the-line deduction for cash contributions** to qualified charitable organizations on their 2020 tax return.

- **The percentage limitation rules for individuals making qualified charitable contributions to 50% charities do not apply** to 2020 returns.

- **The CAA allows for unused amounts remaining in a health FSA as of the end of a plan year to be carried over,** rather than forfeited.

- **The CAA made retroactive modifications to the Employee Retention Tax Credit (ERTC) for which employers may be eligible based on 2020 wages paid.** This credit is obtained through the filing of quarterly payroll tax returns, Form 941, so any additional credits will be reported on amended Form 941's for the 2020 quarters affected. Some of the retroactive changes to the credit include eligibility for the credit even if the employer received PPP funds if the same wages were not used for both, and an extension of the period of time employers can support the PPP loan forgiveness for wages paid to April 1st– December 31st, 2020, rather than just the initial 8-week period or extended 24-week period. An employer with more than 100 employees can qualify for the credit if EITHER: 1) governmental orders affected the jobs of employees but the employers still paid the employees for time when the employees were not working or 2) the company had more than a 50% decline in gross receipts for a 2020 quarter, when compared to the same quarter in 2019, resulting in the payment of wages to employees when the employees were not working. A "small" employer, which is an employer with 100 or fewer employees, could use all qualified wages paid to employees, rather than determining the compensation paid to employees for time that they were not working. Payment by the employer of pre-tax health benefits for furloughed employees count toward the ERTC wage calculation. The credit is capped at $5,000 per employee for the entire 2020 period.

2021 Tax Consequences:

- **The CAA permanently extends the unreimbursed medical expense threshold floor of 7.5% of AGI** for itemized deductions.

- **The CAA removes the different phaseout rules for the American Opportunity Tax Credit and the Lifetime Learning Credit and** replaces them with a single phaseout and permanently repeals the Qualified Tuition Deduction.

- **The CAA extends the New Markets Tax Credit,** which is available to both individual and corporate taxpayers.

- **The Work Opportunity Credit** was extended through 2025 by the CAA and provides an elective general business credit to employers hiring individuals who are members of one or more of ten targeted groups.

- **The exclusion from gross income from the Discharge of Qualified Principal Residence Indebtedness** was extended through 2025.

- **The CAA extends the Employer Credit for Paid Family and Medical Leave** which permits eligible employers to claim an elective general business credit based on eligible wages paid to qualifying employees with respect to family and medical leave.

- **Mortgage insurance premiums are allowed to be continued to be treated as personal residence mortgage interest**, subject to phaseout based on adjusted gross income.

- **The percentage limitation rules for individuals making qualified charitable contributions to 50% charities do not apply** to 2021 returns.

- **The CAA allows for 2021 full 100% deduction of ordinary and necessary food and beverage expenses** associated with operating a trade or business, including meals consumed by employees on work travel.

- **The CAA made significant expansions to the Employee Retention Tax Credit (ERTC) for which employers may be eligible based on 2021 wages paid during the first two quarters.** The maximum credit is capped at $7,000 per employee for each of the first two quarters of 2021, resulting in a total $14,000 credit available per employee. The definition of "small employer" was changed to include employers with no more than 500 employees, rather than 100 employees in the 2020 credit. The employer must only have had a 20% decline in gross receipts (as opposed to 50%) for a 2021 quarter, when compared to the same quarter in 2019, to satisfy the gross receipts test, and there is even an election available to use the gross receipts from the immediately preceding quarter and compare these prior quarter gross receipts to the same quarter in 2019, rather than the current quarter. (Example: Company A wants to determine whether they can use the gross receipts test to satisfy the ERTC eligibility regarding qualified wages paid to employees in 2021. Company A can choose to compare the first quarter 2021 gross receipts (once known) to the gross receipts from 1st quarter 2019 or Company A can, instead, use the gross receipts from the fourth quarter of 2020 and compare those gross receipts to the gross receipts to the fourth quarter of 2019. If either test shows a more than 20 percent decline, Company A is eligible for the ERTC in the first quarter of 2021.)

Payroll Protection Program (PPP) Updates:

- **The PPP Loan Forgiveness Application, Form 3508S** has been released and can be used by borrowers that received a PPP loan of $150,000 or less. No supporting documentation is required to be submitted with the application, but borrowers are required to maintain supporting documents in the case of SBA loan review or audit.

- **The Treasury released two other PPP loan forgiveness applications, Form 3508 and Form 3508EZ,** which do require submission of documentation.

- **The CAA provides additional funds available for first-time PPP borrowers,** equal to 2.5 times their average monthly payroll costs (with a cap per employee of $100,000 annualized) in 2019, 2020, or the year prior to the loan. The maximum loan amount is $10 million, the same as in the original PPP. The costs eligible for loan forgiveness in the revised PPP include payroll, rent, covered mortgage interest, utilities, covered worker PPE to comply with COVID-19 federal health and safety guidelines, covered property damage costs related to property damage and vandalism or looting due to public disturbances in 2020 that were not covered by insurance, expenditures to suppliers that are essential at the time of purchase to the recipient's current operations, covered operating expenditures related to software, cloud computing, product or service delivery, processing of payroll expenses, human resources, sales and billing functions, or accounting or tacking of supplies, inventory, records and expenses. To be eligible for full loan forgiveness, PPP borrowers will have to spend no less than 60% of the funds on payroll over a covered period between 8 or 24 weeks.

- **Previous PPP loan recipients may also apply and receive another PPP loan of up to $2 million,** if they have 300 or fewer employees, have used or will use the full amount of their first PPP loan, and can show a 25% gross revenue decline in any

2020 quarter compared with the same quarter in 2019. The costs eligible for loan forgiveness from the second PPP loan received include payroll, rent, covered mortgage interest, utilities, covered worker PPE to comply with COVID-19 federal health and safety guidelines, covered property damage costs related to property damage and vandalism or looting due to public disturbances in 2020 that were not covered by insurance, expenditures to suppliers that are essential at the time of purchase to the recipient's current operations, covered operating expenditures related to software, cloud computing, product or service delivery, processing of payroll expenses, human resources, sales and billing functions, or accounting or tacking of supplies, inventory, records and expenses. To be eligible for full loan forgiveness, PPP borrowers will have to spend no less than 60% of the funds on payroll over a covered period between 8 or 24 weeks.

- **The SBA has released procedural guidance that details requirements for 1st time-PPP borrowers to reapply for a PPP loan or request an increase to a PPP loan**. This applies to borrowers that returned or repaid a PPP loan and whose lender reported to the SBA before December 27, 2020 that a borrower had fully repaid the loan or canceled the loan, or to borrowers that returned or repaid part of their first PPP loan, if the lender had reported to the SBA before December 27, 2020 that the loan had been partially repaid. For example, if a borrower returned $25K of a $100K PPP loan because the borrower could not spend the funds during the covered period, the lender can disburse $25K back to the borrower provided other conditions are met.

- **The new COVID-19 relief bill also repeals the requirement that PPP borrowers deduct the amount of any EIDL advance from their PPP forgiveness amount.**

- **The Treasury Department and SBA have issued guidance related to the computation of the maximum 1st-draw PPP loan amount as well as the maximum 2nd-draw PPP loan amount and the calculation of Revenue Reduction.** These can be found on our webpage as well as the SBA website at https://www.sba.gov/funding-programs/loans/coronavirus-relief-options/paycheck-protection-program