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PRESIDENT SIGNS COVID RELIEF LEGISLATION

December 28, 2020

Omnibus package includes government funding, COVID relief programs and tax provisions

On December 27, 2020, the President signed into law the Consolidated Appropriations Act of 2021 ("the Act"). The Act is a $2.3 trillion omnibus appropriations measure that is a combination of $1.4 trillion to fund government operations through the fiscal year, $900 billion in emergency COVID relief and several other measures unrelated to COVID. As one of the longest bills to be passed by Congress (5,593 pages), the Act contains numerous appropriation bills and authorizing matters, funding for vaccine distribution, schools, airlines, farmers, broadband and food aid programs, and various forms of relief for individuals, businesses and sectors of the US economy severely impacted by the coronavirus pandemic.

Included among the many tax provisions in the Act are changes and extensions of certain unemployment provisions contained in the Families First Coronavirus Response Act (FFCRA) and the Coronavirus Aid, Relief, and Economic Security (CARES) Act, $600 direct stimulus payments to eligible individuals, an additional $300 a week in federal unemployment insurance benefits, extensions of certain protections from evictions, and tax credit eligibility changes. The new law also provides more than $300 billion in aid to small businesses including, but not limited to, improvements to and an extension of the Paycheck Protection Program (PPP) loan program, deductibility of PPP expenses, changes to the employee retention tax credit, extensions of various tax provisions expiring on December 31, 2020, changes or clarifications to charitable contributions, the low-income housing tax credit rate and residential real property depreciation.

Due to the length and comprehensive nature of the new law, summaries of selected provisions are highlighted below. Additional detailed information and analysis will be provided.

Paycheck Protection Program

PPP Forgiveness Tax Treatment – The Act clarifies that (1) no amount of the PPP loan shall be included in the gross income of the recipient by reason of forgiveness, (2) no deduction shall be denied, no tax attribute shall be reduced and no basis increase shall be denied, by reason of the exclusion from gross income, and (3) in the case of an eligible partnership or S corporation, any amount excluded shall be treated as tax-exempt income for purposes of Sections 705 and 1366 of the Internal Revenue Code except that any increase in the adjusted basis of a partner's interest in a partnership under Section 705 shall equal the partner's distributive share of deductions resulting from costs giving rise to the forgiveness. While this clarification is helpful, a taxpayer must still have sufficient basis/at-risk in order to deduct a resultant loss currently. There are also state considerations in cases where a particular jurisdiction has decoupled from the federal treatment.

Other PPP Loan Provisions – The Act included legislation that made significant changes to the PPP Loan Program including increasing the combined lending authority to $806 billion (from $659 billion), providing $284 billion in direct appropriations (including set-asides for types of lenders, borrowers, areas and programs) and extending the program to March 31, 2021. The new law expands the types of expenses eligible for forgiveness, allows borrowers to elect a covered period between eight and 24 weeks after loan origination, creates a simplified application process for loans under $150,000, and creates a second PPP referred to as a "PPP second draw."

Additional Eligible PPP Expenses – The Act adds four additional allowable PPP expenses (subject to the requirement that 60%of proceeds must be used for payroll costs)

1. Covered Operations Expenditures – Covered operations expenditures include payments for software or cloud computing services that facilitate business operations, delivery of services, payment processing, tracking payroll expenses, human resources, sales and

billing functions, accounting, inventory and records.
2. Covered Property Damage – Costs related to property damage and vandalism or looting that occurred during 2020 that were not covered by insurance.
3. Covered Supplier Costs – These are expenditures that (i) are essential to the operations of the borrower's business at the time the expenditure is made and (ii) made pursuant to a contract, order or purchase order (i) in effect prior before the covered period, or (ii) with respect to perishable goods before or at any time during the covered period.
4. Covered Worker Protection Equipment – An operating or capital expenditure to facilitate the adaption of the business activities to comply with requirements or guidance issued by HHS, CDC or OSHA, or equivalent guidance issued by a state or local government. The Act incudes examples such as installing a drive-thru window, air or air pressure ventilation or filtration systems, physical barriers such as sneeze guards, expansion of business space, and onsite or offsite health screening capability.

Payroll Costs and Group Insurance Payments – The Act clarifies that employer-provided group insurance payments for group life, disability, vision, and dental are included in payroll costs.

Covered Period Elections – The Act allows borrowers to elect a covered period ending anytime between eight and 24 weeks following loan origination. Previously, the covered period options ended at the conclusion of the 24-week covered period beginning on the PPP loan disbursement date or an eight-week covered period if the borrower received its PPP loan prior to June 5, 2020.

Simplified Application Process – Borrowers with loans under $150,000 will receive forgiveness upon signing and submitting a one-page lender certification. The application will ask the borrower to describe the number of employees retained as a result of the loan, amounts spent on payroll costs and provide attestations that the borrower accurately complied with the PPP loan requirements.

Second Draw PPP Loans – The Act creates new second draw PPP loans with more restrictive eligibility requirements than the PPP loans introduced in the CARES Act. These new loans target smaller businesses that have suffered a reduction in revenue. The maximum loan amount is $2 million and eligible entities must:

1. Employ no more than 300 employees (per location if eligible and multiple locations)
2. Have used or plan to use the full amount of their first PPP loan
3. Demonstrate a 25% reduction in gross receipts in Q1, Q2 or Q3 relative to the same 2019 quarter

Loan Terms – In general, the amount borrowed may be up to 2.5 times the sum of the average monthly payroll costs in the one year prior to the loan or the calendar year. An exception is provided for those entities assigned a NAICS code 72 (accommodation and food services) where the loan amount may be 3.5 times average monthly payroll costs.

Eligible and Ineligible Borrowers – The Act extends PPP eligibility to housing cooperatives, FCC license holders and newspapers, TV and radio broadcasters (with certain restrictions and waivers). IRC Section 501(c)(6) organizations are also eligible if (i) the organization does not receive more that 15% of receipts from lobbying, (ii) lobbying activities are not more than 15% of its activities, (iii) the costs of lobbying does not exceed $1 million, (iv) the organization has fewer than 300 employees and (v) professional sports leagues that do not promote or participate in political campaigns or activities. Destination marketing organizations are also eligible and have similar restrictions except there is no provision limiting lobbying costs. In all cases, entities receiving PPP loans are prohibited from using PPP loan proceeds for lobbying activities. Ineligible entities include those that primarily engage in political or lobbying activities, are partially owned by a Chinese entity or have a Chinese resident on the board, and businesses or individuals that are required to register under the Foreign Agents Registration Act.

Bankruptcy and PPP – The Act creates a new bankruptcy procedure for eligible small business debtors that allows court approval for PPP loans. The PPP loan would be permitted only upon a written determination by the SBA that the business is eligible and court approval is obtained. If approved, the PPP loan would be given a superpriority claim.

Assistance to Individuals, Families, and Businesses

<u>Unemployment Insurance</u>

The Act restored and extended certain unemployment provisions contained in both the FFCRA and the CARES Act. The new law provides an additional 11 weeks (from 39 to 50) of $300-per-week pandemic unemployment compensation, and extends pandemic-related unemployment assistance to

March 14, 2021 (or through April 5, 2021 for those receiving benefits and have not reached the maximum number of weeks). The bill also protects individuals who received pandemic-related unemployment benefit overpayments through no fault of their own and are now unable to repay the funds.

COVID-Related Relief

Recovery Rebates - A significant revenue component of the Act is the $600 recovery rebate or "stimulus payment." The provision provides a refundable tax credit in the amount of $600 per taxpayer ($1,200 for married filing jointly) and $600 per qualifying child. The credit begins to phase out at $75,000 of modified adjusted gross income in 2019 ($112,500 for heads of household and $150,000 for married filing jointly) at a rate of $5 per $100 of additional income. A valuable change was also added to allow joint filers where only one spouse has a Social Security number to be eligible for a direct payment under the Act and retroactively under the CARES Act.

Payroll Tax Deferrals - Pursuant to a memorandum issued by President Trump on August 8, employers were allowed to defer an employee's share of payroll taxes from the period beginning September 1, 2020 through December 31, 2020, paying the deferred amounts ratably from wages and compensation increased withholdings through April 31, 2021. The Act extends the repayment period through December 31, 2021. Penalties and interest on deferred unpaid tax liabilities will begin to accrue on January 1, 2022.

Educator Expenses – The Act requires that the Treasury issue regulations to clarify that personal protective equipment, disinfectant and other supplies used to prevent the spread of COVID-19 qualify for the above-the-line educator expense deduction.

Clarifications of Certain Loan Forgiveness – The Act clarifies that certain financial aid received by college students under the CARES Act, loan repayment assistance, forgiveness of Economic Injury Disaster Loan (EIDL) advances or grants for shuttered venue operators are excluded from income.

FFCRA Credits for Paid Sick and Family Leave – The Act made certain changes to the refundable payroll tax credit for paid sick and family leave contained in the FFCRA. The new law extended the covered period from December 31, 2020 to March 31, 2021, allowed individuals to use their daily self-employment income from 2019 rather than 2020 to compute the credit and made technical changes coordinating the definition of qualified ages for paid sick, paid family and medical leave.

Extension of Certain Expiring Provisions

The Act extends many expiring tax incentives that are commonly referred to as "extenders." Many of these provisions, such as the new markets tax credit, the work opportunity tax credit, the exclusion from gross income of the discharge of qualified principal residence debt, and the employer credit for paid family and medical leave, are extended through 2025. Other expiring provisions have been made permanent including the 7.5% floor on the deduction of eligible medical expenses or were temporarily extended for a shorter time period such as the deduction for mortgage insurance premiums, health coverage credits and various energy credits.

Permanent extensions include:	• Reduction in medical expense deduction floor to 7.5% • Exclusion from income for certain benefits provided to volunteer firefighters and emergency medical responders • Lifetime Learning Credit phase-out increase (transition from deduction for qualified tuition and related expenses) • Railroad track maintenance credit • Reduced excise taxes on beer, wine and distilled spirits • Commercial building energy efficiency deduction (179D)
One-year tax extensions include:	• Credit for electricity produced from certain renewable resources • Mortgage insurance premiums as qualified residence interest • Health coverage tax credit for eligible individuals • Indian employment credit • Mine rescue team training credit • Racehorse three-year property • Indian business property depreciation • American Samoa economic development credit

	• Second generation biofuel producer credit • Nonbusiness energy property credit • Fuel cell motor vehicles credit • Alternative fuel refueling property credit • Two-wheeled electric vehicle credit • Indian coal facilities production credit • Energy-efficient homes credit • Alternative refueling property credit • Black lung disability trust fund excise tax
Three-year tax extensions include:	• Energy credit and adjustments to phase-outs • Residential energy-efficient property credit
Five-year tax extensions include:	• Look-thru rule for related controlled foreign corporations • New Markets Tax Credit • Work Opportunity Tax Credit • Exclusion from gross income of discharge of qualified principal residence indebtedness • Seven-year recovery period for motorsports entertainment complexes • Expensing rules for certain productions • Oil spill liability trust fund rate • Empowerment zone tax incentives • Employer tax credit for paid family and medical leave • Exclusion for certain employer payments of student loans

Other Provisions

The “Other Provisions” section in Division EE of the Act contains several tax items including those related to COVID. Some of the provisions include the following:

Low-Income Housing Tax Credit Rate - To support affordable housing and community development, the Act establishes a 4% minimum credit rate for the low-income housing tax credit.

Depreciation of Certain Residential Rental Property Over 30-Year Period – The Act permits in certain circumstances the use of the 30-year ADS depreciation for residential rental property placed in service prior to January 1, 2018 and held by an electing real property trade or business.

IRC Section 48 Energy Credits – The new law expands the IRC section 48 energy credit to include “waste energy recovery property” and extends the credit to January 1, 2026 for offshore wind facilities.

Minimum Rates for Life Insurance Determination – The Act establishes a minimum rate of interest for certain life insurance accumulation tests and guideline premiums rates.

Modifications to Retirement Distributions – A qualified trust of a pension plan will not fail if minimum age distributions are made to an employee who has not separated from employment. The Act also clarifies that partial plan terminations will not occur if the number of active plan participants on March 31, 2021 is at least 80% of active plan participants

Employee Retention Credit – The Act extends the employee retention credit from December 31, 2020 to July 1, 2021 and expands the value of the credit by increasing the credit from 50% to 70% for up to $10,000 in creditable wages per quarter and lowering the reduction in gross receipts test from 50% to 20%. The new law also clarifies that participation in both the employee retention credit and PPP loans are permitted to the extent that a covered loan is not forgiven.

Temporary Allowance of Full Deduction for Business Meals – The Act provides for a full deduction for business meal expenses consisting of food or beverages provided by a restaurant paid or incurred after December 31, 2020 and before January 1, 2023.

Earned Income Credit and Child Tax Credit – The Act provides that lower-income taxpayers may calculate earned income for the 2020 tax year based on income from the 2019 tax year.

Charitable Contributions – The Act extends the temporary provisions in the CARES Act relating to charitable contributions through 2021. Also, taxpayers who do not itemize may claim a $300 above-the-line charitable contribution on 2020 tax returns ($600 for joint filers).

Health and Flexible Spending Arrangements – Temporary rules have been provided in the Act to, among other things, protect a plan's status as a cafeteria plan for carryovers of unused benefits, extensions of grace periods or post-termination reimbursements.

Disaster Tax Relief

The Act also includes disaster tax relief for federally declared disaster areas during 2020. For purposes of the relief in this section, disaster does not include an area where a declaration was based solely on COVID-19 and the relief applies to all declared disasters during the period January 1, 2020 and ending 60 days after the date of enactment of the bill.

The relief provisions in this section includes the following:

Disaster-Related Rules for Use of Retirement Funds – The Act provides for tax-favored withdrawals from retirement plans, forgiveness of early-withdrawal penalties under Code Sec. 72(t) for qualified disaster distributions, the recontribution of amounts withdrawn for home purchases, and an increase in the amount of loans and repayment options from qualified plans.

Employee Retention Credits - An employee retention credit is available in an amount equal to 40% of qualified wages of each eligible employee and the amount cannot exceed $6,000 per employee.

The disaster relief section also provides special rules for qualified disaster relief contributions and personal casualty losses, additional low-income housing credit allocations, and payments to US possessions equal to losses incurred as a result of the disaster relief provisions.

Marks Paneth will continue to monitor developments and will provide updates as they become available. Contact your Marks Paneth advisor if you need additional information or assistance or email responseteam@markspaneth.com.

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