Tax Insights

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President Trump Signs COVID Relief Legislation

On Sunday, Dec. 27, President Trump signed into law the Consolidated Appropriations Act, 2021 (CAA 2021), which serves as a vehicle to fund the federal government, as well as provide relief due to the COVID-19 pandemic. Two divisions of the Act that address the main tax changes discussed herein are the Taxpayer Certainty and Disaster Tax Relief Act of 2020 (TCDTR) (Division EE of the CAA 2021) and the COVID-related Tax Relief Act of 2020 (COVIDTRA) (Division N, Title II, Subtitle B of the CAA 2021). (References to the Code below are references to the Internal Revenue Code of 1986, as amended. Section references below are references to sections of the CAA 2021.) See our ongoing coverage of COVID related legislation and guidance, like the Families First Coronavirus Response Act (FFCRA) and the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), here.

Highlights of some of the tax provisions in the CAA 2021 include:

- **Individual Recovery Rebate (COVIDTRA Section 272)** – The section provides a refundable tax credit to eligible individuals in the amount of $600 per eligible family member, for which the U.S. Department of the Treasury (Treasury) is able to issue advanced payments based on a taxpayer's 2019 return. The credit is $600 per taxpayer ($1,200 for married filing jointly), in addition to $600 per qualifying child. The credit starts to phase out at $75,000 of modified adjusted gross income for single taxpayers ($150,000 for married filing jointly). In general, a taxpayer needs to have an eligible Social Security number to receive the payment, except if the taxpayer is married. Married taxpayers filing jointly where one spouse has an eligible Social Security number and one spouse does not are eligible for a payment of $600, in addition to $600 per child with an eligible Social Security number. Taxpayers receiving an advance payment that exceeds the amount of their eligible credit will not be required to repay any amount of the payment. If the amount of the credit determined on the taxpayer's 2020 tax return exceeds the amount of the advance payment, taxpayers will receive the difference as a refundable tax credit.

- **Charitable Contribution Deduction for Itemizers (TCDTR Section 213)** – Prior to the change, under Code Section 170 (as recently modified by the CARES Act), individual taxpayers who itemized their deductions were limited to a deduction of not more than 60% of their contribution base on charitable contributions, of cash, made to 50% charities. For 2020 and 2021, the percentage limitation rules for individuals making qualified charitable contributions, in cash, to 50% charities do not apply.

- **Charitable Contribution Deduction for Non-Itemizers (TCDTR Section 212)** – Under Code Section 170(p), added by the CARES Act, individual taxpayers who do not itemize their deductions were permitted to take up to a $300 above-the-line deduction for cash contributions to qualified charitable organizations on their 2020 tax return. A 20% penalty is applied to underpayments attributable to any overstated cash contribution. This rule now applies to 2021, as well, but the penalty has been increased to 50% for any underpayment.

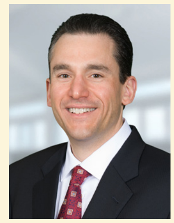
- **Paycheck Protection Program Loans** – The paycheck protection program (PPP) originally established by the CARES Act has been modified and refunded, allowing for additional loans to be paid to qualified borrowers through March 31, 2021. (See Division N, Title III of the CAA 2021 known as the "Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act".) COVIDTRA Section 276 clarifies that taxpayers whose PPP loans are forgiven are allowed to take deductions for otherwise deductible expenses paid with the proceeds of a PPP loan. Also, the tax basis and other attributes of the borrower's assets will not be reduced as a result of the loan forgiveness. Section 276 is effective as of the date of enactment of the CARES Act.

- **Temporary Allowance of Full Deduction for Business Meals (TCDTR Section 210)** – Prior to the law change, under Code Section 274, taxpayers were able to deduct ordinary and necessary food and beverage expenses associated with operating a trade or business, like employee meals while traveling for work. The deduction was limited to 50%. Code Section 274 has been amended to allow for the full deduction of such food and beverage expenses as long as such expenses are provided by a restaurant and paid or incurred before Jan. 1, 2023.

- **Extension of Deferred Payroll Taxes (COVIDTRA Section 274)** – Under the CARES Act, employers were permitted to defer paying the employer portion of certain payroll taxes through Dec. 31, 2020 and repay such wages ratably from Jan. 1, 2021 through April 30, 2021. This section extends the repayment period through Dec. 31, 2021. Penalties and interest on deferred unpaid tax liability will not begin to accrue until Jan. 1, 2022.

- **Extension of Credits for Paid Sick and Family Leave (COVIDTRA Section 286)** – Under the FFCRA, employers were required to provide paid sick leave and expanded family and medical leave to employees for COVID-19 related reasons. Also, it provided refundable paid sick leave credits and paid childcare leave credits for employers who provided qualifying leave through Dec. 31, 2020. Section 286 extends the refundable payroll tax credits for paid sick and family leave (and related employer mandate) through the end of March 2021. This provision is effective as if included in FFCRA.

- **Employer Credit for Paid Family and Medical Leave (TCDTR Section 119)** – The employer tax credit for paid family and medical leave, as created by the 2017 Tax Cuts and Jobs Act (TCJA), allows eligible employers to claim an elective general business credit based on eligible wages paid in 2018 and 2019 to qualifying employees with respect to family and medical leave. The maximum amount of family and medical leave that may be taken into account with respect to any qualifying employee is 12 weeks per tax year. This credit is now extended through 2025 for wages paid in tax years beginning after Dec. 31, 2020.



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- **Employee Retention Credit (TCDTR Sections 206 and 207)** – The CARES Act provided a refundable payroll tax credit for 50% of qualified wages paid after March 12, 2020, through Dec. 31, 2020, by eligible employers. Generally, the credit is available to employers, including nonprofits, whose operations have been fully or partially suspended as a result of a government order limiting commerce, travel, or group meetings and to employers who have experienced a greater than 50% reduction in quarterly receipts, measured on a year-over-year basis. Section 206, which is retroactively effective to March 12, 2020, provides (i) clarification on determining gross receipts for tax-exempt organizations and (ii) that employers who receive a PPP loan may still qualify for the credit for wages that are not paid with forgiven PPP proceeds. Section 207, among other things, increases the rate from 50% to 70% of qualified wages and reduces the gross receipts decline from 50% to 20% for wages paid on Jan. 1, 2021, through June 30, 2021.

- **Exclusion for Certain Employer Payments of Student Loans (TCDTR Section 120)** – Under the CARES Act, eligible student loan repayments made after March 27, 2020. and before Jan. 1, 2021, are excluded from an employee's gross income if such payments are made by the employee's employer. This exclusion is now extended through 2025.

- **Related Controlled Foreign Corporations Look-Thru Rule (TCDTR Section 111)** – U.S. persons who are 10% shareholders of a controlled foreign corporation (CFC) are required to include in income their pro rata share of the CFC's subpart F income, which includes foreign personal holding company income under Code Section 954, whether or not this income is distributed. Under Code Section 954, dividends, interest, rent, and royalties from a CFC that's a related person for taxable years of a CFC beginning after Dec. 31, 2005, and before Jan. 1, 2021, isn't treated as foreign personal holding company income to the extent attributable or properly allocable to income of the related person that isn't subpart F income or income treated as effectively connected with the conduct of a U.S. trade or business. This look-through rule is now extended through 2025 for related CFCs.

IRS Releases Tax Accounting Regulations

The IRS has issued a pre-released version of the final regulations regarding the timing of income inclusion under Code Section 451 for taxpayers using the accrual method of accounting. Code Section 451 was amended by the TCJA to provide that, for an accrual method taxpayer, the all-events test for an item of gross income, or portion thereof, is met no later than when the item, or portion thereof, is included in revenue for financial accounting purposes on an applicable financial statement (AFS Income Inclusion Rule) and that an accrual method taxpayer may use the deferral method of accounting for advance payments. The final regulations adopt the proposed regulations (two sets of which were issued in Sept. 2019 (see our prior coverage here)) with certain changes and clarifications. For example, the final regulations modify the AFS Income Inclusion Rule to provide that the all-events test for any item of gross income, or portion thereof, is met no later than when that item, or portion thereof, is "taken into account as AFS revenue." In determining when an item of gross income is "taken into account as AFS revenue," AFS revenue is reduced by amounts that the taxpayer does not have an enforceable right (as determined by the terms of the contract and applicable law) to recover if the customer were to terminate the contract on the last day of the taxable year. The final regulations also provide an alternative method and two additional adjustments for determining when an item of gross income is taken into account as AFS revenue. The final regulations also modify and clarify the special ordering rule for items of income for debt instruments and the cumulative rule for multi-year contracts, disputed income, special accounting methods to which the AFS Income Inclusion rule generally doesn't apply, and contracts with multiple performance obligations. The final regulations do not change the list of items that are included in the definition of advance payment but do make some clarifications regarding the amount of a payment that must be included in revenue in an AFS. Additionally, despite some commenters' requests, Treasury and the IRS declined to define "realization" since it is a factual determination that has different meanings in different contexts. Lastly, the final regulations provide a cost offset method for advance payments and indicate further guidance may be issued.

ICI Submits Letter Requesting RIC Reporting Relief

In a letter dated Dec. 16, the Investment Company Institute (ICI) has asked that the Treasury Department and the IRS permit regulated investment companies (RICs) to satisfy their reporting requirements with regard to the character of certain dividends by posting such information on their public websites. Under Code Section 852(b)(3), a capital gain dividends must be reported by a RIC as such in "written statements furnished to its shareholders." (Similar rules apply to certain other distributions.) This requirement generally is met by a RIC's filing of Form 1099; however, not all shareholders receive this form. As such, given the lack of clarity on what constitutes a "written statement furnished to its shareholders," most RICs provide this information in their annual reports. The Securities and Exchange Commission is finalizing a proposal to reduce substantially the amount of information that can be included in shareholder reports, where many RICs today provide this dividend information, and beginning Jan. 1, 2021, under Rule 30e-3, RICs will be able to mail a postcard to shareholders indicating that the shareholder report is available on the RIC's website instead of mailing the entire shareholder report. If the proposal is adopted and when the new rule change goes into effect, RICs may need to mail separate statements to shareholders solely for tax purposes. In the letter, the ICI requests asks the IRS and Treasury Department to clarify that RICs can satisfy the distribution reporting requirements by posting capital gains and other dividends on the tax information pages of their public websites. However, at a minimum, the ICI requests that IRS and Treasury confirm that RICs that include the distribution information in their financial statements and comply with the SEC's Rule 30e-3, which becomes effective on Jan. 1, 2021, have satisfied these reporting requirements for tax purposes.

IRS Issues Partnership Practice Units

The IRS has issued practice units on Partnership Liabilities, addressing both recourse and nonrecourse liabilities, and Partnership Liability Allocations, regarding the determination of such allocations.