CONSOLIDATED APPROPRIATIONS ACT

Coronavirus Aid Package

The Consolidated Appropriations Act 2021 bill recently signed into law by President Trump on December 27, 2020 is a massive tax, funding, and spending bill contains a nearly $900 billion coronavirus aid package. The emergency coronavirus relief package aims to bolster the economy, provide relief to small businesses and the unemployed, deliver checks to individuals and provide funding for COVID-19 testing and the administration of vaccines. This document highlights the main tax provisions included in the bill.

Paycheck Protection Program

The PPP, one of the stimulus measures created by the CARES Act, provides for the granting of federally guaranteed loans to small businesses, nonprofit organizations, veterans organizations and tribal businesses in an effort to keep businesses operating and retain staff during the COVID-19 pandemic. (PPP loans are administered by the Small Business Administration (SBA)). A recipient of a PPP loan under the CARES Act (the first round) could use the funds to meet payroll costs, certain employee healthcare costs, interest on mortgage obligations, rent and utilities. At least 60% of the loan funds were required to be spent on payroll costs for the loan to be forgiven.

Eligible businesses

Business are eligible for the second round of PPP loans regardless of whether a loan was received in the first round. The bill changes the definition of a “small business.” Small businesses are defined as businesses with no more than 300 employees and whose revenues dropped by 25% during one of the first three quarters of 2020 (or the fourth quarter if the business is applying after January 1, 2021). The decrease is determined by comparing gross receipts in a quarter to the same in the prior year. Businesses with more than 300 employees must meet the SBA’s usual criteria to qualify as a small business.

Borrowers may receive a loan amount of up to 2.5 (3.5 for accommodation and food services sector businesses) times their average monthly payroll costs in 2019 or the 12 months before the loan application, capped at $2 million per borrower, reduced from a limit of $10 million in the first round of PPP loans. The bill also expands the types of organizations that may request a PPP loan. Eligibility for a PPP loan is extended to:

- Tax-exempt organizations described in Internal Revenue Code (IRC) Section 501(c)(6) that have no more than 300 employees and whose lobbying activities do not comprise more than 15% of the organization's total activities (but the loan proceeds may not be used for lobbying activities).

- "Destination marketing organizations" that do not have more than 300 employees.

- Housing cooperatives that do not have more than 300 employees.

- Stations, newspapers and public broadcasting organizations that do not have more than 500 employees.

The following businesses are not eligible for a PPP loan:

- Publicly-traded businesses and entities created or organized under the laws of the People's Republic of China or the Special Administrative Region of Hong Kong that hold directly or indirectly at least 20% of the economic interest of the business or entity, including as equity shares or a capital or profit interest in a limited liability company or partnership, or that retain as a member of the entity's board of directors a China-resident person.

- Persons required to submit a registration statement under the Foreign Agents Registration Act.

- Persons that receive a grant under the Economic Aid to Hard Hit Small Businesses, Nonprofits and Venues Act.

Uses of loan proceeds

The bill adds four types of non-payroll expenses that can be paid from and submitted for forgiveness, for both round 1 and round 2 PPP loans, but it is unclear whether borrowers that have already been approved for partial forgiveness can resubmit an application to add these new expenses:

- Covered operational expenditures, i.e., payments for software or cloud computing services that facilitate business operations, product or service delivery, the processing, payment or tracking of payroll expenses, human resources, sales and billing functions, or accounting or tracking of supplies, inventory, records and expenses.

- Covered property damage, i.e., costs related to property damage and vandalism or looting due to public disturbances that took place in 2020, which were not covered by insurance or other compensation.

- Covered supplier costs, i.e., expenses incurred by a borrower under a contract or order in effect before the date the PPP loan proceeds were disbursed for the supply of goods that are essential to the borrower's business operations.

- Covered worker protection equipment, i.e., costs of personal protective equipment incurred by a borrower to comply with rules or guidance issued by the Department of Health & Human Services, the Occupational Safety and Health Administration or the Centers for Disease Control, or a state or local government.

To qualify for full forgiveness of a PPP loan, the borrower must use at least 60% of the funds for payroll-related expenses over the relevant covered period (eight or 24 weeks).

Increase in loan amount

The bill contains a provision that allows an eligible recipient of a PPP loan to request an increased amount, even if the initial loan proceeds were returned in part or in full, and even if the lender of the original loan has submitted a Form 1502 to the SBA (the form sets out the identity of the borrower and the loan amount).

Expense deductions

The bill confirms that business expenses (that normally would be deductible for federal income tax purposes) paid out of PPP loans may be deducted for federal income tax purposes and that the borrower's tax basis and other attributes of the borrower's assets will not be reduced as a result of the loan forgiveness. This has been an area of uncertainty because, while the CARES Act provides that any amount of PPP loan forgiveness that normally would be includible in gross income will be excluded from gross income, it is silent on whether eligible business expenses attributable to PPP loan forgiveness are deductible for tax purposes. The IRS took the position in guidance that, because the proceeds of a forgiven PPP loan are not considered taxable income, expenses paid with forgiven PPP loan proceeds may not be deducted. The bill clarifies that such expenses are fully deductible—welcome news for struggling businesses. Importantly, the effective date of this provision applies to taxable years ending after the date of the enactment of the CARES Act. Thus, taxpayers that filed tax returns without deducting PPP-eligible deductions should consider amending such returns to claim the expenses.

Loan forgiveness covered period

The bill clarifies the rules relating to the selection of a PPP loan forgiveness covered period. Under the current rules, only borrowers that received PPP proceeds before June 5, 2020 could elect an eight-week covered period. The bill provides that the covered period begins on the loan origination date but allows all loan recipients to choose the ending date that is eight or 24 weeks later.

Loan forgiveness
PPP loan recipients generally are eligible for loan forgiveness if they apply at least 60% of the loan proceeds to payroll costs (subject to the newly added eligible expenditures, as described above), with partial forgiveness available where this threshold is not met. Loans that are not forgiven must be repaid. Currently, PPP loan recipients apply for loan forgiveness on either SBA Form 3508, Form 3508 EZ or Form 3508S, all of which required documentation that demonstrates that the claimed amounts were paid during the applicable covered period, subject to reduction for not maintaining the workforce or wages at pre-COVID levels.

The bill provides a new simplified forgiveness procedure for loans of $150,000 or less. Instead of the documentation summarized above, these borrowers cannot be required to submit to the lender any documents other than a one-page signed certification that sets out the number of employees the borrower was able to retain because of the PPP loan, an estimate of the amounts spent on payroll-related costs, the total loan value and that the borrower has accurately provided all information required and retains all relevant documents. The SBA will be required to develop the simplified loan forgiveness application form within 24 days of the enactment of the bill and generally may not require additional documentation. Lenders will need to modify their systems used for applications to make an electronic version of the new forgiveness application available to eligible borrowers.

Employment Retention Credit and Families First Coronavirus Response Credit

The bill extends and expands the ERC and the paid leave credit under the Families First Coronavirus Response Act (FFCRA).

ERC
The ERC, introduced under the CARES Act, is a refundable tax credit equal to 50% of up to $10,000 in qualified wages (i.e., a total of $5,000 per employee) paid by an eligible employer whose operations were suspended due to a COVID-19-related governmental order or whose gross receipts for any 2020 calendar quarter were less than 50% of its gross receipts for the same quarter in 2019. The bill makes the following changes to the ERC, which will apply from January 1 to June 30, 2021:

- The credit rate is increased from 50% to 70% of qualified wages and the limit on per-employee wages is increased from $10,000 for the year to $10,000 per quarter.

- The gross receipts eligibility threshold for employers is reduced from a 50% decline to a 20% decline in gross receipts for the same calendar quarter in 2019, a safe harbor is provided allowing employers to use prior quarter gross receipts to determine eligibility and the ERC is available to employers that were not in existence during any quarter in 2019. The 100-employee threshold for determining “qualified wages” based on all wages is increased to 500 or fewer employees.

- The credit is available to certain government instrumentalities.

- The bill clarifies the determination of gross receipts for certain tax-exempt organizations and that group health plan expenses can be considered qualified wages even when no wages are paid to the employee.

- New, expansive provisions regarding advance payments of the ERC to small employers are included, such as special rules for seasonal employers and employers that were not in existence in 2019. The bill also provides reconciliation rules and provides that excess advance payments of the credit during a calendar quarter will be subject to tax that is the amount of the excess.
- Treasury and the SBA will issue guidance providing that payroll costs paid during the PPP covered period can be treated as qualified wages to the extent that such wages were not paid from the proceeds of a forgiven PPP loan. Further, the bill strikes the limitation that qualified wages paid or incurred by an eligible employer with respect to an employee may not exceed the amount that employee would have been paid for working during the 30 days immediately preceding that period (which, for example, allows employers to take the ERC for bonuses paid to essential workers).

The bill makes three retroactive changes that are effective as if they were included the CARES Act. Employers that received PPP loans may still qualify for the ERC with respect to wages that are not paid for with proceeds from a forgiven PPP loan. The bill also clarifies how tax-exempt organizations determine “gross receipts” and that group health care expenses can be considered “qualified wages” even when no other wages are paid to the employee.

FFCRA
The FFCRA paid emergency sick and child-care leave and related tax credits are extended through March 31, 2021 on a voluntary basis. In other words, FFCRA leave is no longer mandatory, but employers that provide FFCRA leave from January 1 to March 31, 2021 may take a federal tax credit for providing such leave. Some clarifications have been made for self-employed individuals as if they were included in the FFCRA.

Other Tax Provisions in the CAA

The bill includes changes to some provisions in the IRC:

- **Charitable donation deduction**: For taxable years beginning in 2021, taxpayers who do not itemize deductions may take a deduction for cash donations of up to $300 made to qualifying organizations. The CARES Act revised the charitable donation deduction rules to encourage donations following a decline after the enactment of the Tax Cuts and Jobs Act in 2017.

- **Medical expense deduction**: The income threshold for unreimbursed medical expense deductions is permanently reduced from 10% to 7.5% so that more expenses may be deducted.

- **Business meal deduction**: Businesses may deduct 100% of business-related restaurant meals during 2021 and 2022 (the deduction currently is available only for 50% of those expenses).

- **Extenders**: The bill provides for a five-year extension of the following tax provisions that are scheduled to sunset on December 31, 2020:
  - The look-through rule for certain payments from related controlled foreign corporations in IRC Section 954(c)(6), which was extended to apply to taxable years of foreign corporations beginning before January 1, 2026 and to taxable years of U.S. shareholders with or within which such taxable years of foreign corporations end
  - New Markets Tax Credit
  - Work Opportunity Tax Credit
  - Health Coverage Tax Credit
  - Carbon Oxide Sequestration Credit
  - Employer credit for paid family and medical leave
  - Empowerment zone tax incentives
  - 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
  - Incentive for certain employer payments of student loans (notably, the bill does not include other student loan relief so that borrowers will need to resume payments on such loans and interest will begin to accrue)

- **Permanent changes**: The bill makes several tax provisions permanent that were scheduled to expire in the future, in addition to the medical expense deduction threshold mentioned above:
  - The deduction of the costs of energy-efficient commercial building property (now subject to inflation adjustments)
  - The gross income deduction provided to volunteer firefighters and emergency medical responders for state and local tax benefits and certain qualified payments
  - The transition from a deduction for qualified tuition and related expenses to an increased income limitation on the lifetime learning credit
  - The railroad track maintenance credit
  - Certain provisions, refunds and reduced rates related to beer, wine and distilled spirits, as well as minimum processing requirements for certain craft beverages produced outside the U.S.