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**INDIVIDUAL TAXATION**

**2022 EDITION**

**Pratt-Kulsrud-Burton**

**Changes introduced by the**

**American Rescue Plan Act of 2021**

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**INTRODUCTION**

At this writing, August 31, 2021, the United States and most of the world continues to grapple with the far-reaching effects of the Covid-19 pandemic. While health officials are doing what they can to contain the spread of the disease, the federal government also is trying to address the drastic toll the pandemic has had on the U.S. economy. During 2020, Congress and President Trump worked together to enact five pieces of legislation that impact the tax laws. They include:

1. March 6, 2020: *Coronavirus Preparedness and Response Supplemental Appropriations Act of 2020* (CPRSAA).
2. March 18, 2020: *Families First Coronavirus Response Act* (FFCRA) and two of its component parts, the *Emergency Paid Sick Leave Act* (EPSLA) and the *Emergency Family and Medical Leave Expansion Act* (EFMLEA)
3. March 27, 2020, *Coronavirus Aid, Relief, and Economic Security Act* (CARES).
4. April 24, 2020, *Paycheck Protection Program and Health Care Enhancement Act* (PPP).
5. June 5, 2020, *Paycheck Protection Program Flexibility Act of 2020* (PPFA)
6. December 27, 2020, *Consolidated Appropriations Act of 2020* (CAA), which included the *Taxpayer Certainty and Disaster Tax Relief Act of 2020* (TCDTRA)

The relevant changes of the 2020 legislation are incorporated in the 2022 edition. However, certain provisions are included in this supplement for reference.

More recently, on March 11, 2021, President Biden signed into law the *American Rescue Plan Act of 2021* (ARPA). ARPA provides $1.9 trillion of aid, slightly larger than the previous year’s most generous package, the CARES Act of 2020, that provided $1.8 trillion. ARPA, like the CARES Act, contains many provisions with tax ramifications that are discussed in this supplement.

As we complete this document, President Biden released his 2022 tax proposal, the *American Jobs Plan and the American Families Plan*. These proposals include:

(1) a return to the pre-TCJA top income tax rate of 39.6% (for 2022, the proposed 39.6% rate would affect married filing joint taxpayers with taxable income over $509,300 (over $452,700 for single taxpayers, over $481,000 for heads of households, and over $254,650 for married filing separate);

(2) more generous child tax credits, expansion of the earned income tax credit and the child and dependent care tax credit, and more generous premium tax credits;

(3) taxing capital gains of high-income earners at ordinary rates to the extent income exceeds $1 million; increase the maximum tax on long-term capital gains and qualified dividends from 20% to the top rate on ordinary income (39.6%), which when factoring in the 3.8% net investment income tax, effectively raises the tax rate on long-term capital gains and qualified dividends to 43.4%;

(4) elimination of the like-kind real estate preference for those with the highest incomes; similarly caps the amount of gain that can be deferred in a like-kind exchange at $500,000 per taxpayer, per year ($1 million for joint return);

(5) treating certain transfers of appreciated property by gift or on death as realization events (i.e., as if they sold the property transferred for its fair market value); taxpayers would have a $1 million (adjusted for inflation after 2022) per-person exemption available. The proposed change would be effective for property transferred by gift after 12/31/2021, and for property owned at death by decedents dying after that date;

(6) tax appreciation on certain assets held in a trust, partnership or other noncorporate entity. An entity would be subject to tax if the assets it holds have not been subject to a recognition event within the prior 90 years. The 90-year period begins 1/1/1940, making 12/31/2030 the earliest date that a taxpayer might have to recognize gain in this situation.

(7) increasing the rates on C corporations from 21% to 28% as well as a 15% minimum tax on corporations with book income of more than $2 billion;

(8) eliminating all fossil fuel tax subsidies;

(9) expanding tax incentives that encourage clean energy sources. The document is available online at <https://home.treasury.gov/policy-issues/tax-policy/revenue-proposals>

(10) creation of a new general business credit of up to 10% of the eligible cost of *onshoring* a trade or business (onshoring refers to reducing or eliminating a trade or business (or a line of business) currently conducted outside the U.S. and starting up, expanding, or otherwise moving the same trade or business to the U.S. and creating jobs in the process;

As always, as new legislation is enacted, we will do our best to provide a timely supplement.

**Table of Contents.** The changes made by the recent legislation are discussed in the following pages and are referenced to the 2022 edition by chapter and page. A Table of Contents can be found on **page 5** of this supplement.

**Special Thank You:** The editors would like to acknowledge and thank Professors Jim Angelini of Suffolk University and Ramon Fernandez of the University of St. Thomas-Houston. Their thoughtful insights and comments helped not only us, but hopefully you, gain a better understanding of how this new legislation with all of its complications affects individuals and businesses.

Tax Highlights of the

*Coronavirus Preparedness and Response Supplemental Appropriations Act* (P.L. 116-123, 3/6/2020)

*Families First Coronavirus Response Act*  (P.L. 116-127, 3/18/20)

*Coronavirus Aid, Relief, and Economic Security Act* (P.L. 116-136, 3/27/20),

*Paycheck Protection Program and Health Care Enhancement Act* (P.L. 116-139, 4/24/20)

*Paycheck Protection Program Flexibility Act* (P.L. 116-142, 6/5/20)

*Consolidated Appropriations Act of 2021* (P.L. 116-260, 12/27/20)

*American Rescue Plan Act of 2021* (P.L. 117 1, 3/11/2021)

The legislation above made numerous changes designed to provide relief to individuals and businesses affected by the coronavirus pandemic. Many have tax ramifications. The legislation:

* Establishes the Paycheck Protection Program that provides federal loans to help struggling businesses. Moreover, in most cases, businesses are not required to repay these loans. Additional funding was provided by the Enhancement Act. ARPA made it clear that expenses paid with these are deductible notwithstanding the fact they are paid with tax-exempt funds.
* Reduces or eliminates payroll taxes for businesses (i.e., their share of FICA). Any employer, self-employed individual or nonprofit whose activity was fully or partially suspended in 2020 due to government orders associated with COVID-19 or that experienced a significant decline in gross receipts may be eligible for relief. The CARES Act creates an employee retention credit of as much as $5,000 per employee to offset payroll tax costs (i.e., the 6.2% tax on wages or self-employment income) paid after March 12, 2020, and before January 1, 2021. If the credit amount exceeds the employer’s liability, the excess is refundable to the employer. The estimated benefit was about $54.6 billion. The credit is not available for 2021.
* Requires businesses to make sick and family leave payments for up to 10 weeks. Exceptions exist for businesses that have (1) more than 500 employees or (2) 50 or fewer employees.
* Allows penalty-free access to retirement accounts if for virus-related financial hardships.
* Provides that employer payments of student loans of their employees are nontaxable.
* Gives nonitemizers a charitable deduction of up to $300 (i.e., for AGI in 2020 but a deduction of up to $600 from taxable income in 2021).
* Suspends the required minimum distribution (RMD) rules for retirement plans for 2020.
* Allows taxpayers to withdraw up to $100,000 from retirement plans without the 10% additional tax penalty for early distributions if they are coronavirus-related.
* Temporarily suspends the 80% taxable income limitation for NOLs.
* Eliminates the carryforward rule for NOLs arising in 2018, 2019, and 2020 so they can be carried back to the five previous tax years to provide immediate relief.
* Suspends the excess business loss rules.
* Accelerates refunds of previously generated corporate alternative minimum tax credits.
* Relaxes the business interest limitation of §163(j), increasing it from 30% to 50% of income.
* Makes a technical correction so that “qualified improvement property” (QIP) is now properly classified as MACRS 15-year assets and, therefore, eligible for 100% bonus depreciation.
* Provides an “employee retention credit” to encourage employers to retain employees even if employees cannot report to work because of issues related to the coronavirus.
* Includes a variety of non-tax provisions to assist with mitigation and response as follows:
* Expansion of unemployment benefits; funding for health care providers; aid to state and local governments
* Large supplemental funding package for agencies of the federal government

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**CHAPTER 1: AN OVERVIEW OF FEDERAL TAXATION**

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**Stimulus Payments (also known as Recovery Rebates or Economic Impact Payments).** As noted in the introduction, taxes affect virtually everything Americans do. In that regard, Congress turned to the tax system to provide financial aid to individuals suffering due to the coronavirus. From the outset of the pandemic, Congress has provided several direct payments from the government to individuals. ARPA, like the CARES Act, added another round of stimulus payments. Under ARPA, eligible individuals may receive up to $1,400 each. That number is doubled to $2,800 for married taxpayers who file jointly (§ 6428B). In addition, taxpayers also could receive a $1,400 payment for each qualifying dependent. None of the payments received constitute taxable income to the recipient. See the complete discussion for Chapter 4.

**Employee Retention Credit.** To help employers and employees during the pandemic, Congress has created several special tax credits. Among these is one for businesses and nonprofit organizations that were forced to suspend or close its operations due to COVID-19 but nevertheless continued to pay its employees during the shut-down in hopes of retaining them. Qualified employers were entitled to the “employee retention credit” (ERC), a refundable credit intended to eliminate the employer’s share of FICA (6.2% share of Social Security taxes) in 2020. In effect, employers impacted by COVID-19 were not required to not pay their share of FICA. See Chapter 13 for details.

At this writing, it appears that employee retention credit (ERC) may have a short life. Although ARPA continues the credit through 2021, Biden’s infrastructure bill known as the Infrastructure Investment and Jobs Act, which passed the Senate on August 10, 2021, would end it. The infrastructure bill would make wages paid after September 30, 2021, ineligible for the credit (except for wages paid by an eligible recovery startup business). Only time will tell the fate of the credit and what might replace it. Regardless of the outcome, it appears that the credit will be available for wages paid through September 30, 2021.

**Page 1-22**

**Employment Taxes: Deferral of Payment of Employer Share of Payroll Taxes.** The CARES Act generally allowed most employers and self-employed individuals to defer payment of the employer share of Social Security taxes (the 6.2% portion up to the maximum wage base of $137,700 for 2020 (up to $8,537.40)) incurred between the date the CARES Act was enacted and December 31, 2020. The CARES payroll tax deferral does not include the employer’s portion of the Medicare tax or any amounts withheld from employees (income tax withholdings and employee’s share of Social Security and Medicare).

According to the deferral provisions, employment taxes that were due to be submitted on March 27, 2020, or later are eligible for deferral. There is no maximum on the amount of qualifying payroll taxes that can be deferred. Such amounts are to be paid over the following two years, with half due on December 31, 2021, and the other half due on December 31, 2022. (Act §2302(a)(1) and (b)). Unlike other provisions in the CARES Act, the size of the employer (e.g., number of employees) is irrelevant.

**Example 1.** For the period, March 27 – December 31, 2020, FXG Corporation paid its employees total wages of $400,000. Its share of Social Security taxes on these wages was $24,800 (6.2% x $400,000). The corporation is allowed to postpone payment of the tax over the next two years: $12,400 (50% x $2,480) due on December 31, 2021, and the remaining $12,400 due on December 31, 2022.

**Example 2.**  For the period, March 27 – December 31, 2020, Andrea, a self-employed taxpayer, has $100,000 of net profit from a Schedule C business and her employer share of the social security tax is $5,726 tax (6.2% x .9235 x $100,000). Under the deferral provision, if elected, she can choose to pay 50% of this tax by 12/31/21 and the other 50% by 12/31/22 (i.e., without incurring any interest or penalties).

As the examples above illustrate, the benefits of postponing payment of the payroll taxes are potentially huge. Initially, there was uncertainty about certain aspects of the calculation. As discussed below, employers generally are allowed to reduce the payroll taxes they must pay by the amount of any sick pay they are required to pay under FFCRA (i.e., the payroll tax credit). In addition, employers are entitled to a credit based on employee retention (i.e., the employee retention credit mentioned above). The question in computing the amount of employment taxes that could be deferred (above) was whether such taxes had to be reduced by these credits. The IRS has explained that such credits are not taken into account.

***Effect of Paycheck Protection Program Loans (PPP Loans) on Deferral of Payroll Taxes*.** Special rules may impact the employer’s deferral of payroll taxes. As discussed in Chapter 6, businesses may apply and receive loans from the Small Business Administration to help them stay afloat during the pandemic. Generally, a business is not required to repay these loans as long it does not layoff employees and uses the funds for qualified expenses (e.g., salaries, rent, mortgage interest, or utilities), Although, the cancellation of these loans does produce cancellation of indebtedness income, such income is not taxable.

Employers that have applied for a PPP loan can continue to defer the payment of its payroll taxes until that point when they receive a decision from their lender that its PPP loan is forgiven. At that point, the employer is no longer able to defer additional payroll taxes. However, the payroll taxes that were deferred until that time continue to be deferred and are due on the applicable dates described above. If the application for a PPP loan is denied, the employer can continue to defer any obligation for employment taxes under the rules above.

***Reduction of Payroll Taxes for Payments of Qualified Sick Pay and Medical Leave Wages.***

As discussed in Chapter 7, the CARES Act allows employers to reduce their payroll tax obligations by a credit for the amount of qualified sick pay and family and medical leave wages paid. For a complete discussion see Chapter 7.

**Page 1-30 and 6-27**

**Unemployment Benefits Increase.** To aid the unemployed, the Cares Act expanded unemployment benefits and ARPA continued this approach. For 2021, ARPA increased the amount of the weekly unemployment checks as well as the total number of weeks that benefits are paid. The new law added $300 to weekly unemployment payments through September 6, 2021. Self-employed and gig economy workers are eligible for the increase as well.

**Unemployment Benefits Exclusion**. As discussed in Chapter 6, prior to 1979, unemployment benefits were not considered taxable income. But that changed when Congress made the benefits fully taxable in 1979. However, in light of the hardships brought about by the pandemic, Congress allowed certain taxpayers to exclude a portion of their unemployment benefits. ARPA retroactively makes the first $10,200 of unemployment benefits received in 2020 tax-free but only for taxpayers with *modified AGI* less than $150,000 per year (§ 85). If married, each spouse receiving unemployment compensation may exclude up to $10,200 or a total of $20,400 for both. For example, if a husband received $25,000 in benefits and his or her spouse received $7,000, they could exclude $17,200 of unemployment benefits on their joint 2020 return ($10,200 husband and $7,000 wife). Note that the $150,000 threshold is the same regardless of filing status (e.g., single taxpayer, head of household, or jointly). In addition, the law does not provide for any phaseout mechanism. For taxpayers with $150,000 or more of AGI, their unemployment benefits would be fully taxable. Perhaps Congress (or, the IRS) will act to clarify this provision, but at this point that is how the new law reads.

Modified AGI for this purpose is determined after including taxable Social Security and railroad retirement benefits; excluding U.S. savings bond interest and the nontaxable portion of qualified adoption assistance; and deducting qualified retirement plan contributions, student loan interest, and qualified tuition and related expenses (which was repealed for tax years beginning after 2020).

Another problem concerns taxpayers whose unemployment benefits were delayed and not received until after December 31, 2020. If the taxpayer were to receive benefits for a week in 2020, but did not receive the payment until 2021, such amounts would be taxable. Only time will tell whether Congress addresses this inconsistency.

Note that the treatment of unemployment benefits for state tax purposes can differ, depending on where the taxpayer lives. In some states, such as California, benefits are not taxed at all. However, many other states follow federal law, so that the first $10,200 of benefits may be excluded on state tax returns, as well.

**CHAPTER 4: TAX CONSIDERATIONS FOR DEPENDENTS;   
 FILING STATUS; DETERMINATION OF TAX FOR AN INDIVIDUAL; FILING REQUIREMENTS**

**Payments to Individuals (Stimulus Payments).**

For 2020, the CARES Act provided for a special payment to most Americans, generally referred to as a “recovery rebate.” Such payments were subject to phaseout at higher levels of AGI. Technically, the payments were an advanced payment of the “recovery rebate” credit that phased out at higher AGI levels. Importantly, the payments were not taxable. Under CARES, in 2020, individual taxpayers received a first round of payments of $1,200 while joint filers received $2,400 with another $500 for child under age 17.

For 2020, the Consolidation Appropriations Act (CAA) provided a second round of payments. Under the CAA, in 2020, individual taxpayers received a payment of $600 while joint filers received $1,200 with another $600 for each child under age 17. Similar to the payments of the CARES Act, the CAA payments were technically an advance payment of the recovery rebate credit that phased out at higher income levels. Like the CARES payments, the CAA payments were not taxable.

For 2021, ARPA, like both the CARES Act and the CAA Act, provided for a third round of stimulus payments. Moreover, under ARPA (§ 6428B), the amounts are increased. For 2021, ARPA provides individuals with a payment of $1,400 ($2,800 for married taxpayers filing jointly) plus another $1,400 for each dependent (as defined in Code §152). Moreover, for this purpose, ARPA expands the definition of dependents to include college students and “qualifying relatives” who are claimed as dependents. The inclusion of all dependents is significant. Unlike last spring when only $500 went to dependents for which the $2,000 child tax credit could be claimed (i.e., those dependents under age 17 as of the last day of the tax year), this round of $1,400 stimulus checks goes to all dependents. Like its predecessors, the credit is fully refundable so taxpayers will receive this amount of rebate credit when filing their 2021 Form 1040 regardless of whether any tax is ultimately owed. Like the 2020 payments, the 2021 payments are not taxable.

The amount of ARPA stimulus payments that a person receives phases out based on the individual’s filing status and AGI. Fewer individuals are likely to qualify for the payment this time around. The AGI thresholds start at the same income levels, but the phase-out range is much narrower than with prior stimulus payments. The payment amounts and phase out for the 2021 are shown below.

2021 Stimulus Payment 2021 AGI  
 Status Amount Phase-out

Single or head of household $1,400 $ 75,000 - $ 80,000  
 Eligible to file jointly 2,800 150,000 - 160,000  
 Each dependent 1,400 112,500 - 120,000

For example, a married couple with four dependents and AGI less than $150,000 would receive a payment of $8,400 ($2,800 + (4 x $1,400 = $5,600). If the couple’s AGI exceeded $160,000, all $5,600 would be phased out and the family would have received nothing at all. From a planning perspective, those who can, might want to take steps to lower their income (e.g., maximize the deduction for contributions to Individual Retirement Accounts).

As suggested above, technically, the payments are an advanced payment of a refundable credit against taxes that will otherwise be due for the tax year (§ 6428(b)). For example, assuming a taxpayer receives the advanced payment of the credit to which he or she is entitled for 2021, no credit is claimed on the 2021 tax return. However, as noted above, taxpayers will not have to wait until they file their returns for 2021 to obtain this credit. An advance rebate of the credit will be deposited directly in the taxpayer’s account or mailed in the form of a check. As discussed further below, when the IRS computes the stimulus payment, it uses the AGI that they have available when it computes the credit (i.e., 2020 if the 2020 return has been filed, otherwise 2019).

Since the payment represents a refundable credit, taxpayers receive a check regardless of whether they actually have a tax liability for the year equal to (or greater than) the amount of the check received. As noted above, the payment will not need to be repaid, nor is it includible in the recipient’s gross income (i.e., it is not taxable). As the IRS website suggests, individuals who have no income at all, as well as those whose income is entirely derived from “non-taxable means-tested benefit programs” such as Supplemental Security Income (SSI) benefits, are nevertheless eligible for the advance rebate (or credit).

**Page 4-3**

**Child Tax Credit and ARPA**

*Credit Increase and Phaseout Rules.* For 2021,ARPA substantially increases the child tax credit. The credit amount has been increased from $2,000 to $3,600 for each qualifying child under age 6 and from $2,000 to $3,000 for each qualifying child age 6 through 17, which is an additional $1,600 and $1,000 respectively. For 2021, the child tax credit is subject to two separate sets of phaseout rules. The increased credit amount (i.e., the additional $1,000 or $1,600) phases out for taxpayers with modified AGI (MAGI) over $150,000 for married taxpayers filing jointly, $112,500 for heads of household, and $75,000 for others. The expanded portions of the credit (i.e., $1,000 or $1,600 increase in contrast to $2,000 overall under prior law) is reduced by $50 for each $1,000 of MAGI over those limits. Those who are not eligible for the additional $1,000 or $1,600 amounts because of their MAGI can still claim the $2,000 credit under the pre-ARPA rules for each qualifying child 16 and under. The pre-ARPA rules allow the $2,000 credit amount for taxpayers with MAGI up to $200,000, or $400,000 for married filing jointly.

Example 1: S1 and S2 are married filing jointly in 2021. They have a qualifying child, who is 5 years old. Their MAGI is $160,000. Of the additional $1,600 credit, the phaseout amount would be $500 ([($160,000 - $150,000) / $1,000] x $50). As a result, their child tax credit would be $3,100 ($2,000 +($1,600 - $500 = $1,100).

Example 2: Same facts as in the previous example, except the couple’s MAGI is $190,000.

The phaseout amount would be $2,000 ([($190,000 - $150,000) / $1,000] x $50), which

would completely phaseout the $1,600 amount. However, since their MAGI is under

$400,000, they would receive the regular $2,000 credit.

An additional enhancement for 2021 only is that the credit is fully refundable. This is designed to help taxpayers financially during the COVID-19 pandemic. Taxpayers can receive half of their estimated total child tax credit in advance in six payments spread over the last half of 2021. The estimated amount is based on their 2019 (or 2020, if filed) income tax return. However, taxpayers who receive advance payments in excess of their allowable 2021 child tax credit must pay back the excess by increasing their 2021 tax liability. Taxpayers with MAGI below specified modest income thresholds meeting certain safe-harbor specifications are exempted from having to pay back the excess.

*Revised Definition of Qualifying Child.* ARPA also expands the Code §24 child tax credit in several ways. In addition, it provides that taxpayers can receive the credit in advance of filing a return. ARPA also makes 17-year-olds eligible as “qualifying children” (i.e., as opposed to those children under age 17 as of the last day of the tax year). A “qualifying child” is now defined under the ARPA as an under-age-18 child, whom the taxpayer could claim as a dependent (i.e., a child related to the taxpayer who, generally, lived with the taxpayer for at least six months during the year), and who was a U.S. citizen or national, or a U.S. resident.

ARPA also makes the credit fully refundable for 2021 (i.e., in contrast to $1,400 of the overall $2,000 credit refundable under prior law as noted on page 4-13 and discussed in Chapter 13 page 13-59). However, the amount reverts back to $1,400 in 2022.

For the 2021 tax year, taxpayers can claim a $500 nonrefundable credit for a dependent who does not meet the ARPA’s expanded definition of a qualifying child (for example, a dependent child who will be age 18 or older as of 12/31/21).

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**Due Dates for Filing Returns (2019, 2020 and 2021 Returns).**

To keep dollars in the hands of individuals during the pandemic, the government temporarily moved the due dates of the individual tax returns (Form 1040). The due date of the 2019 individual tax return tax return was moved from the traditional April 15, 2020, to July15, 2020. The 2020 return due date was moved from April 15, 2021, to May 17, 2021. An extension could be obtained until October 15, 2021. However, the due dates for other returns remained unchanged. At this juncture, it appears that the normal filing dates for 2021 returns will apply.

**CHAPTER 6: INCLUSIONS AND EXCLUSIONS**

**Page 6-35**

**Educational Assistance Plans: Employer Payment of Student Loans.**

Under current law (§ 127), an employee may exclude up to $5,250 of tuition payments made by an employer sponsored educational assistance program. The exclusion is not available for payment of the education for the employee’s spouse or dependents. In addition, the payment is not only excluded for income tax purposes but also is exempt from payroll taxes (employer and employee). The CARES and the CAA Acts expanded the reach of this program to include employer payments of existing student loan debt. Thus, if an employer agrees to pay a student’s loans and did it before 2021, the benefit is not taxable. The limitation of $5,250 was not changed. The provision is effective for student loan payments made before January 1, 2026. Obviously, this rule provides a potentially huge benefit for employers and employees but it is not available for payments after 2025.

**Example 3**. An accounting firm pays $3,000 for an MST course taken by one of its employees during 2020. In addition, the firm pays off $4,000 of the employee’s outstanding student loans. Given the $5,250, the employee can exclude $5,250 while the remaining $1,750 ($3,000 + $4,000 = $7,000 - $5,250 = $1,750) would be included in the employee’s wages. The employer can deduct the payment just like compensation except it is not subject to employment taxes.

“Eligible student loan repayments” are payments by the employer of principal or interest with respect to any “qualified higher education loan” for the education of the employee (but not of a spouse or dependent). The payment may be paid to the employee or directly to a lender. See  
§ 221(d)(1) and § 127(c)(1)(B).

As discussed in Chapter 11 (page 32), § 221 allows a deduction for up to $2,500 of interest on student loans per year. To prevent a double benefit, a taxpayer cannot deduct interest on a student loan that is paid by an employer for which the exclusion is allowable. Note that the deduction for student loan interest starts to phase out once the taxpayer’s AGI (computed with certain modifications) exceeds $140,000 for joint returns or $70,000 for all other returns.

As noted above, the CARES Act allows federal-income-tax-free treatment for payments made by employer-sponsored § 127 educational assistance plans towards student loan debts of participating employees. Between March 28, 2020 and December 31, 2020, up to $5,250 per employee could be paid out (towards principal or interest) with no federal income tax hit for the employee. Employers can deduct the payments. The TCDTRA (included in the CAA) extends this break to cover qualifying student loan debt payments made under § 127 plans through December 31, 2025.

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**Cancellation of Indebtedness**

Add to the list of exclusion situations (discussed further below):

* The cancelation of student loans
* The cancellation of Economic Injury Disaster Loans
* The cancellation of Paycheck Protection Loans

**Student Loan Forgiveness.** ARPA amends Code §108(f) to specify that gross income does not include any amount (i.e., apparently regardless of how large that amount might be) that would otherwise be included in income due to the discharge of any student loan after December 31, 2020, and before January 1, 2026. It should be emphasized that ARPA does not forgive student loan debt per se. Rather, it anticipates a possible development that may occur in the future. The “student loan discharge” exclusion applies to these types of loans:

(1) Loans provided expressly for post-secondary educational expenses if the loan was made, insured, or guaranteed by a federal, state, or local governmental entity or an eligible educational institution.

(2) Private education loans.

(3) Any loan made by any educational institution qualifying as a 50% charity (i.e., for purposes of the income tax charitable deduction) if the loan is made under an agreement with any governmental entity (as described in item (1) above) or any private education lender that provided the loan to the educational organization, or under a program of the educational institution that is designed to encourage its students to serve in occupations with unmet needs or in areas with unmet needs and under which the services provided by the students (or, former students) are for or under the direction of a governmental unit or a tax-exempt charitable organization.

(4) Any loan made by an educational organization qualifying as a 50% charity or by an tax-exempt organization to refinance a loan to an individual to assist the individual in attending any educational organization but only if the refinancing loan is under a program of the refinancing organization which is designed as described in item (3) above).

However, the discharge of a loan made by either an educational institution or a private education lender is not excluded under the above rules if the discharge is on account of services performed for either the organization or for the private education lender.

**Economic Injury Disaster Loans (EIDLs).**

Beginning March 30, 2020, businesses that suffered due to the pandemic could seek financial assistance by applying to the Small Business Administration (SBA) for a so-called Economic Injury Disaster Loan (EIDL or disaster loan). Such loans were added by CPRSAA, the first piece of legislation concerning COVID-19. Only businesses with 500 or fewer employees are eligible to apply. Before the coronavirus, these loans were intended for businesses that have suffered due to natural disasters (e.g., hurricanes) but the CARES Act extends them to businesses that can show they have suffered severe economic hardship because of the coronavirus pandemic. In the past, a business was required to prove that it was unable to obtain loans elsewhere. However, this requirement has been waived.

The EIDL program allows eligible businesses to borrow up to $2 million dollars at an interest rate of 3.75% or less. One of the attractive features of a disaster loan is that borrowers are eligible to request an emergency advance while their application is being processed. Originally, the SBA would advance the business up to $10,000. However, on April 14, 2020: the SBA reduced the amount of the advance to $1,000. More importantly, the $10,000 (or $1,000) advance does not have to be repaid even if the application is ultimately denied. The SBA tries to provide the advance within three days of receipt of a borrower’s application.

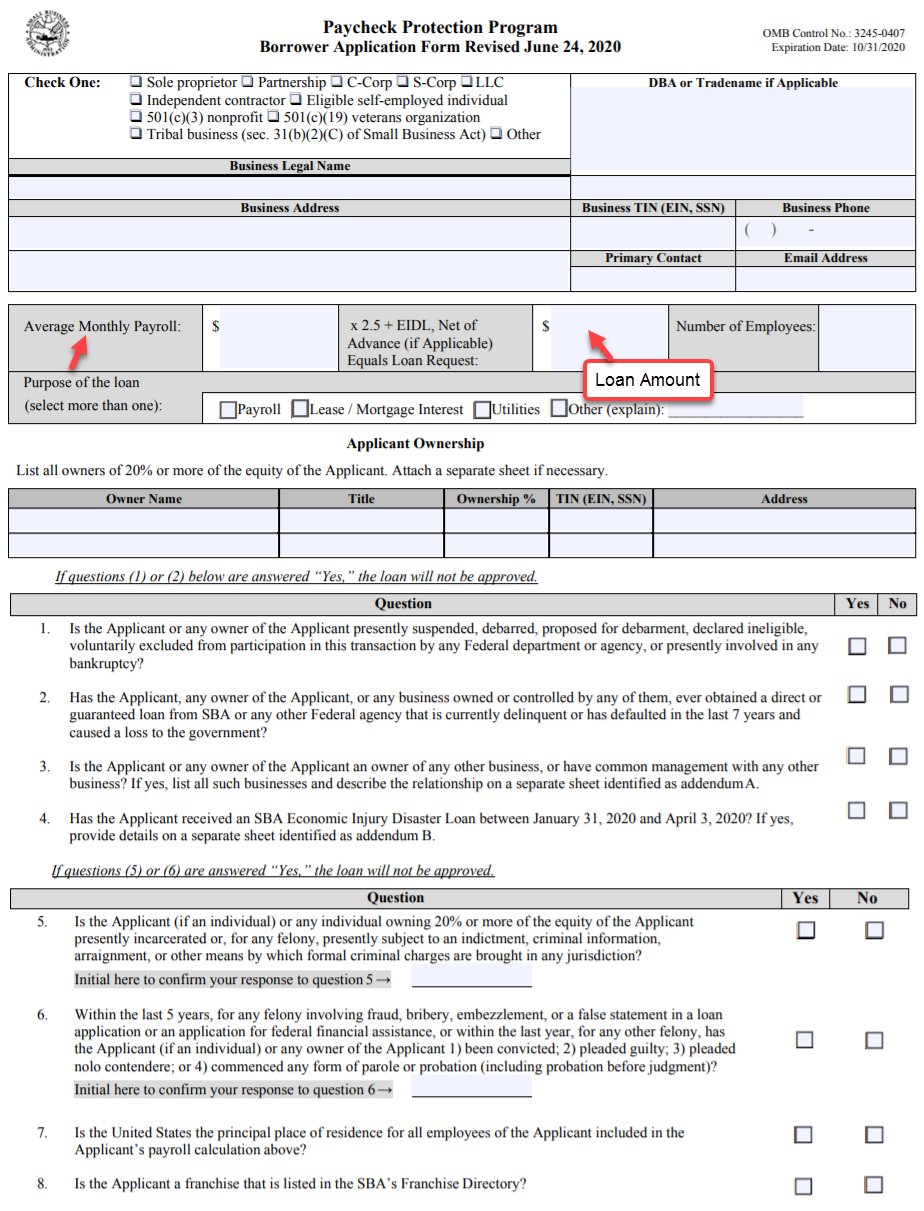
Independent contractors who work for a separate business (e.g. real estate brokers) can qualify for an EIDL if they are able to prove they are separate from that business (e.g. the brokerage firm). Businesses that have obtained a disaster loan must take these loans into account when applying for a loan under the Paycheck Protection Program as discussed below.

**Paycheck Protection Program (PPP Loans)**

**PPP Loans in General.** At this juncture, it is clear that the pandemic has devastated many small businesses and other organizations. Many have struggled and were forced to close their doors and layoff their employees. To help them survive and help their employees keep their jobs, Congress provided a loan opportunity through the so-called Paycheck Protection Program (PPP) (Act § 1102 amending the Small Business Act § 7(a)). As the name of the Act suggests, the purpose of the law is to ensure that people’s paychecks are protected. This government loan—up to $10 million per business—was intended to help companies cover eight weeks of their payroll costs.

The PPP loans were run through the Small Business Administration (SBA). The SBA approved the loans according to certain criteria. However, the actual loan was made by authorized lenders (e.g., federally insured depository institutions (banks), or lenders approved by the SBA).

Businesses started the application process by contacting a lender and submitting an application form by June 30, 2020 (a deadline extended to August 8, 2020). The application form (as revised on June 24, 2020) is shown below and can be found at <https://www.sba.gov/sites/default/files/2020-07/PPP-Borrower-Application-Form-508.pdf>.



The primary advantage of PPP loans is that amounts borrowed could turn out to be a loan in name only. As explained below, if an employer meets certain standards, e.g., it keeps its employees on the payroll (i.e., it does not fire or layoff employees) and uses the funds for qualified expenses (e.g., salaries, rent, mortgage interest, or utilities), the employer is not required to repay the loan. Moreover, unlike the normal rule, the forgiveness of debt is nontaxable and, as clarified by ARPA, the expenses paid with such funds are still deductible.

The normal treatment of debt cancellation is found in § 61(a)(11). It provides that the reduction or cancellation of indebtedness results in cancellation of debt (COD) income to the debtor. Such income normally is taxable. An "identifiable event" determines when a debt has been reduced or canceled. For example, an identifiable event includes a creditor accepting less than full payment as a complete discharge of a debt or events or simply circumstances result that remove the likelihood that a debt will be paid. The PPP program creates a significant exception to this basic rule, generally providing that the debt forgiveness is not considered taxable income. The PPP program provides special rules for determining the amount of eligible forgiveness.

At first glance, it may appear that the PPP is too good to be true. However, this cloud does indeed have a silver lining. Tony Nitti, the famous tax-guru who writes for Forbes, summed up the PPP perfectly. According to Nitti, “free money is hard to pass up, and so last week, businesses were clamoring for Friday to arrive so they could grab their piece of the pie.” (See Tony Nitti, “Paycheck Protection Program Loans: Three Things The SBA And Banks Need To Agree On Now.” *Forbes*, April 5, 2020) <https://www.forbes.com/sites/anthonynitti/2020/04/05/paycheck-protection-program-loans-three-things-the-sba-and-banks-need-to-agree-on-now/#573860c21a32>.

Nitti was right. The rush for the loans was so great that the money—about $349 billion—quickly ran out. According to Treasury Secretary Steven Mnuchin and SBA Administrator Jovita Carranza there were “more than 14 years’ worth of loans in less than 14 days,” before the funds ran dry. But, on April 24, 2020, Congress agreed for another round of funding and enacted the Paycheck Protection Program and Health Care Enhancement Act that added $321 billion. (See Anne Sraders, “14 years in 14 days: Inside the chaotic rollout of the SBA’s PPP loan plan to save America’s small businesses.” *Fortune*, April 29, 2020. See <https://fortune.com/2020/04/29/sba-ppp-paycheck-protection-program-loans-small-business-administration-inside-chaos/>

There is a long list of requirements that police the road to tax-free forgiveness under the PPP. To get a sense of these requirements, see the discussion below and loan application form in full at <https://home.treasury.gov/system/files/136/Paycheck-Protection-Program-Application-3-30-2020-v3.pdf>.

**PPP Loans: Eligible Recipients: Who Can Apply for a PPP Loan?** The Paycheck Protection Plan (PPP) loans are available to eligible recipients, including businesses (e.g., corporations, partnerships, self-employed persons), nonprofits, veterans’ organizations, and Tribal businesses. Only loan applications from small businesses are considered , i.e., the applicant has no more than 500 employees at any time during the 25 weeks starting on the date the loan was originated (when the taxpayer and the bank sign the loan agreement). The organization can apply only if it meets the following requirements (Act § 1102(a)(2)(A)(iv) and ((v)):

(1) The business was operational as of February 15, 2020;

(2) The principal place of business is in the U.S. and

(3) The qualified organization has no more than 500 employees (subject to certain exceptions).

The 500-employee limit was intended to restrict the loans to small businesses but initially it was applied to each location. This approach did not necessarily restrict loans to small businesses since a company might have multiple locations, none of which had more than 500 employees (e.g., Ruth’s Chris Steak House has over 100 restaurants in different locations and each location employs no more than 500), (Act §1102(a)(1)(D)(i)(I) and §1102(a)(1)(D)(iii)).

The implementation of this rule sparked significant controversy (see Davis and Haddon, “How Ruth’s Chris Got an Extra Helping of Small Business Aid Money.” *Wall Street Journal*, April 4, 2020 and Pcheco and Francis, “Public Companies Got $500 Million in Small Business Loans.” *Wall Street Journal*, April 20, 2020). According to SEC filings, 424 publicly traded companies received PPP loans (e.g., Ruth Chris, Shake Shack, Potbelly; for a complete list see <https://factba.se/sba-loans> ). Apparently, Treasury Secretary Steven Mnuchin objected, explaining that the “intent of this money was not for big, public companies that have access to capital.” No doubt succumbing to public pressure, Ruth Chris, Shake Shack and other companies ultimately returned $20 million (see Sarah Hansen, “Ruth’s Chris Steak House Returns $20 Million PPP Loan As Treasury Issues New Guidance.” *Forbes,* April 23, 2020).

But Mnuchin had more to say On May 5, 2020, he announced that any company that received a PPP loan of more than $2 million would be audited for compliance with the program’s terms before any loan forgiveness would be permitted. Apparently, five *publicly* held companies were given a specific deadline to return their money, May 14, to give the money back with no questions asked. Otherwise, Mnuchin wanted them to explain why they should be allowed to keep the money. After the uproar, the SBA issued new guidance making it less likely that publicly traded companies could access the second round of funding created by the Enhancement Act (see <https://home.treasury.gov/system/files/136/Paycheck-Protection-Program-Frequently-Asked-Questions.pdf>.

**PPP Loans: Authorized Uses.** As seen in the application form above, the loans can be used for

• Payroll costs (see below), including benefits but not federal taxes;

• Interest on mortgage obligations, incurred before February 15, 2020;

• Rent, under lease agreements in force before February 15, 2020; and

• Utilities, for which service began before February 15, 2020.

The SBA also cautioned, that the loan application should not include any costs for health benefits, retirement benefits or state and local taxes on income.

It is worth noting, the Inspector General reported that the SBA ignored certain Congressional mandates in implementing the loan program. The report chastised the SBA for failing to issue guidance to lenders that should have instructed them to give priority to borrowers in underserved and rural markets, including minority and women owned businesses. Moreover, the report found that the SBA issued rules that required borrowers to use the majority of their loan funds (75%) on payroll costs to receive full forgiveness even though the Act did not mandate any specific amount be dedicated for payroll expenses. See Amara Omeokwe. “SBA Veered From Guidelines on Small Business Loans, Report Says.” *Wall Street Journal*, May 8, 2020 <https://www.wsj.com/articles/sba-veered-from-guidelines-on-small-business-loans-report-says-11588971101>

**PPP Loans: Computation of Amount and Maximum.** Under the CARES Act (§1106(b)), the taxpayer’s PPP loan is limited. As seen in the application form above, the loan cannot exceed ***2.5 times the employer’s average monthly payroll costs*** (see calculation below) plus any disaster loans obtained after January 31, 2020 that are refinanced into a PPP loan. The maximum loan is $10 million. Note that prior to the SBA guidance, a single company could obtain the maximum loan for each business location so a business with multiple locations could obtain multiple loans.

The average monthly payroll normally is calculated based on the employer’s 12 months of payroll costs prior to the application date—although some applicants have reported that they have used and the banks have accepted the 2019 calendar year average. That *average* monthly payroll number is then multiplied by 2.5. The multiplier of 2.5 or 250% represents the fact that the loan is designed to cover 2 ½ months of payroll costs. For example, assume the employer’s total payroll cost for the year was $240,000, in which case the average monthly payroll cost for the prior 12 months would be $20,000 ($240,000/12). As a result, the employer would qualify for a $50,000 PPP Loan (2.5 x $20,000 average payroll cost).

For purposes of computing the loan, payroll costs are limited to certain expenses incurred during the 8 weeks that begins when the loan originated (the “covered period”).

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Payroll costs include (Act § 1102(a)(1)(A)(viii))

* Wages, salary, or similar compensation to an employee or independent contractor (up to $100,000 plus amounts paid for unemployment taxes, premiums for group health plans, contributions to retirement plans and state or local taxes asses on compensation such as unemployment taxes)
* Cash tips or equivalent
* Vacation, parental, family, medical or sick leave
* Allowances for dismissal or separation

Payroll costs do not include:

* Compensation of any individual employee in excess of an annual salary of $100,000
* Federal payroll taxes
* Compensation of an employee whose principal place of residence is outside the U.S.
* Qualified sick leave or family medical leave for which a credit is allowed under the PPP rules
* Payments to independent contractors

***PPP Loan Amount*.** The maximum amount of a PPP loan is limited to the lesser of (a) or (b):

a. (1) 250% of the employer’s ***average*** ***monthly*** ***payroll costs*** (listed above) for the 1-year period   
 ending on the loan application date

+ (2) Any disaster loan taken out after January 31, 2020 that has been refinanced into a   
 paycheck protection loan.

Payroll costs and disaster loans

b. $10 million

**Example 4.**  THX Inc. (an S or C corporation) applies for a PPP loan from First Bank on April 1, 2020. The business had payroll costs of $600,000 for the prior 12 months (April 1, 2019, through March 31, 2020), a monthly average of $50,000 ($600,000/12). Using the guidelines above, the business is entitled to a fully guaranteed federal loan of $125,000, the lesser of:

(1) $125,000 ($50,000 of average monthly payroll costs x 250%) or

(2) $10 million.

In effect, the loan covers 2 ½ months of payroll costs based on the average of the prior 12 months.

**PPP Loans: Amount of Tax-Free Cancellation.** No doubt the key feature of PPP loans is that borrowers may never have to repay their loans. The SBA generally forgives PPP loans if employers keep their employees on the payroll for eight weeks and the loan proceeds are used for authorized expenses. These expenses include not only the costs of payroll, but also those for rent, mortgage interest, or utilities. Moreover, as noted above, the debt forgiveness is not treated as taxable income to the employer (Act §1106(i)) and ARPA makes the expenses deductible!

Technically, a business (an “eligible recipient”) that seeks forgiveness of the PPP loan must be able to verify that the amount of the loan for which forgiveness is requested “was used to retain employees, make interest payments on a covered mortgage obligation, make payments on a covered lease obligation or to make covered utility payments.” (Act §1106(e)). If the business fails to meet these standards, the business must repay the loan. In that regard, the loan has a modest interest rate of 1% and a maturity of 2 years. (Act §1106(d)(2)).

The CARES Act provides that the amount of the PPP loan that is eligible for forgiveness is the sum of the certain “costs incurred and payments made” during the “covered period” (the 8-week period beginning on the date a PPP loan originates). However, some employers found it difficult to spend all of the proceeds on authorized expenses, thereby forfeiting the forgiveness privilege. Importantly, the PPPFA extended the period for eligible payments to 24-weeks. Qualifying costs include:

* Payroll costs;
* Any payment of interest on any mortgage obligation (not including any prepayment of or payment of principal on a mortgage obligation) that was incurred before February 15, 2020;
* Any payment of rent under a leasing agreement in force before February 15, 2020;
* Any utility payment, including payment for distribution of electricity, gas, water, transportation, telephone, or internet access for which service began before February 15, 2020.

**PPP Loans: Loan Forgiveness Application (Form 3508 Revised July 30, 2021) .**  To compute the amount a borrower must repay, the borrower completes and submits Form 3508 PPP Loan Forgiveness Application Form Revised July 30, 2021 to the banker or lender from whom the loan was obtained (see below). The borrower uses this form to compute the amount of the loan to be forgiven and, at the same time, how much must be repaid. The loan application instructions contain a number of clarifications including, calculation of FTEs, rent, utility expenses, documentation and more.

**PPP Loan Forgiveness Application Form Revised March 18, 2021. See the form below and at** <https://www.sba.gov/sites/default/files/2021-07/PPP%20--%20Forgiveness%20Application%20and%20Instructions%20--%203508%20%287.30.2021%29-508.pdf>

Graphical user interface, application, table

Description automatically generatedThe Application above (Form 3508) reflects the SBA’s three-step approach to compute the amount of forgiveness. In effect, if 100% of the loan was used properly, 100% of the loan is cancelled. To the extent that the loan was not used properly, the forgiveness is reduced proportionately, and repayment is required. As noted earlier, cancellation of the debt is considered nontaxable and, just as important, ARPA allows a deduction for the expenses paid by the loan proceeds. Completion of lines 1-15 and the accompanying schedules yields the amount that is forgiven.

***Computing the Potential Forgiveness Amount (Lines 1-8).***

Consistent with the requirement that the loan must be used for certain expenses, the first step in completing the application is determining the total *payroll and qualifying non-payroll costs* (e.g., interest, rent and utilities) (lines 1-8). These include only such costs that the business has spent over the 8-week period since it received its PPP funds (extended to 24 weeks by the PPPFA). The sum of these costs becomes part of the determination of the “potential forgiveness amount” (lines 12-14). The final Forgiveness Amount is found on line 15.

***Reduction for Cutting Employees and Salary Cuts (Line 5).***

This tentative forgiveness amount is then adjusted to the extent the employer lays off workers or cuts salaries (line 5). The tentative amount to be forgiven is reduced if the employer (1) reduced the pay for returning employees more than 25% or (2) failed to bring back the same number of full-time equivalent employees (FTEs) that it had before the pandemic. The application waives this reduction if the business later brought back the same number of employees by June 30, 2020 (extended to December 31 by the PPPFA). Adjustments are allowed for employees that declined to return to their jobs. The result is the “Potential Forgiveness Amounts (lines 12-14).”

***Reduction for Cutting Payroll (Line 8 -10).***

The third and final step ensures that 75% of loan forgiveness is attributable to payroll costs. To illustrate, assume a business had a PPP loan of $100,000. It secures total forgiveness if it used $75,000 for payroll. However, its actual payroll costs were $70,000 and eligible non-payroll costs were $30,000. In such case, the payroll costs are only 70% of the $100,000 total and do not meet the 75% rule. Thus, the $30,000 in non-payroll costs are reduced so that payroll costs are 75% of the amount forgiven. As a result, the maximum forgiveness is $93,333 ($70,000/75% = $93,333). This calculation effectively trims the non-payroll costs from $30,000 to $23,333 such that the forgiveness request of $93,333 consists of 75% payroll costs ($70,000) and 25% non-payroll costs ($23,333).

**Example 7**. KWL Inc., a C corporation, has payroll costs over the prior 12-month period of $240,000. Its average monthly payroll is $20,000 ($240,000/12). The maximum loan amount is 2.5 times the average monthly payroll or $50,000 ($20,000 by 2.5). The company applied and received a loan of $50,000. For the 8-week period after it received the loan, the company uses $40,000 for payroll costs, $9,000 for rent and $2,000 on utilities for total qualifying expenses of $51,000. In this case, the company has qualifying expenses of $51,000 (including payroll costs that exceed 75% of the loan) that exceed the $50,000 loan. Consequently, the entire loan is forgiven. In addition, the debt forgiveness in this case is nontaxable.

**Example 8.** Same facts as Example 7 above. KWL borrowed $125,000 but incurred only $100,000 in payroll costs (80% of the loan amount), mortgage interest, and utility payments during the 8 week period after the loan origination date. The business is eligible to have only $100,000 of the $125,000 loan forgiven. The forgiveness of $100,000 of the debt does not result in any COD income for tax purposes. Payments on the remaining $25,000 of the loan will not be due for two years. The interest rate on the $25,000 loan remaining cannot exceed 1% annually.

**Example 9.** Same facts as in Example 8 above. If the employer reduced its average workforce during the covered period, the amount of forgiveness is reduced. For example, if the employer employed 80 employees during the covered period and when it normally employed 100, only 80% of the loan would be forgiven. A special calculation is used to determine the average number of employees (Act § 1106(d)(2)(B)).

**PPP Loan Fraud.** As many predicted, the Paycheck Protection Program would be an easy target for crooks. For those who were willing to risk going to jail, all they had to do was find a lender who would fund their PPP loan application and voila, free money. For the most part, the lender had no risk since the loan was backed by the federal government. Lenders were guaranteed that they would be repaid one way or another. However, the SBA recognized the problem early on and issued warnings, promising that it would bring enforcement actions against any engaged in fraud. It didn’t take long. Here are a few examples.

* May 5, 2020: the Criminal Division of the Department of Justice brought the first (of what appears to be many) charges against suspects who made fraudulent loan requests of over $500,000. (See Kelly Phillips Erb, "Feds Announce First Arrests In Country Linked To PPP Loan Fraud." *Forbes*, May 10, 2020 <https://www.forbes.com/sites/kellyphillipserb/2020/05/10/feds-announce-first-arrests-in-country-linked-to-ppp-loan-fraud/#17149dcd59de>).
* May 13, 2020: Federal prosecutors struck again, charging a sole proprietor of a Texas business with “wire fraud, bank fraud, false statements to a financial institution, and false statements to the SBA.” Apparently, the proprietor “allegedly sought $10 million in PPP loan proceeds by fraudulently claiming to have 250 employees with an average monthly payroll of $4 million.” In addition he “sought approximately $3 million in PPP loan proceeds by fraudulently claiming to have 250 employees with an average monthly payroll of approximately $1.2 million.” However, the Texas Workforce Commission had no records of employee wages paid in 2020 by the accused or his business. (See Bruce Brumberg, “Federal Charges Of PPP Loan Fraud Are Here To Remind You These Loans Are Not “Free Money.” Forbes, May 14, 2020 <https://www.forbes.com/sites/brucebrumberg/2020/05/14/federal-charges-of-ppp-loan-fraud-are-here-to-remind-you-these-loans-are-not-free-money/#3bdeecaded53>).
* May 21, 2020: Charges were brought against a Chinese national with trying to fraudulently obtain $20 million in PPP loans. According to numerous reports, Mr. Muge Ma, a 36-year-old known as "Hummer Mars" residing in Manhattan, allegedly presented applications to five banks saying he had two companies with hundreds of employees who needed help. Ma represented himself and one of his companies as a test-kit manufacturer for COVID-19 and a medical supplier, neither of which were true, prosecutors said. The bulk of the loans which were approved before the fraud was found were frozen by investigators before Ma could receive them.

Given how quickly the program was rolled out, there were those who inadvertently did not follow the rules. Unfortunately, these businesses will find themselves trying to distinguish their legitimate claims from those who have committed actual fraud.

**PPP Loans: Payroll Costs for Self Employed Individuals and Partners in General.** Taxpayers can get a PPP loan equal to 250% of their average monthly payroll costs. Payroll costs generally include wages and salary and other benefits up to $100,000 per employee. However, self-employed individuals (sole proprietorships) and partners in partnerships do not receive wages or salaries or a “paycheck” in the normal sense. Consequently, the computation of their payroll cost is a bit different. On April 14, 2020, the SBA issued guidance on how the maximum PPP loans for self-employed individuals and partners are to be computed.

***Payroll Costs for Self-Employed Individuals*.**  In determining the maximum PPP loan that a self-employed person can obtain, the total payroll cost is the sum of two components:

(1) Schedule C net income, not to exceed $100,000, and

(2) Payroll costs for other employees

The computation is shown below.

Schedule C Income for 2019 < $100,000)/12 = Average monthly net profit  
 Outstanding amount of any disaster loan (EIDL) to be refinanced  
+ Payroll costs for other employees/12 = Average payroll cost  
= Total payroll cost   
x 250% or 2.5  
= Maximum PPP Loan for self-employed person not to exceed $10 million

If a self-employed person does not have employees or a disaster loan outstanding, then the total annual payroll cost is simply the individual’s self-employment income reported on Schedule C. Note that the annual limit in computing payroll costs for a self-employed person as well as an employee is $100,000 per person.

**Example 10.** Sam Smart, a CPA, teaches continuing education tax courses for accounting firms and also holds his own workshops. To make ends meet, he also drives for Uber and takes jobs from Taskrabbit. His net income shown on his Schedule C for 2019 was $96,000. He has no employees so there are no additional payroll costs to be considered. His maximum PPP loan is $20,000 [($96,000/12 = $8,000 average payroll cost) x 2.5)].

***Payroll Costs for Partners in Partnerships*.** Unlike self-employed individuals, partners (including LLC members) do not apply for a loan individually. The partnership makes the application. For purposes of computing payroll costs for the partnership loan amount, the partnership includes (1) the net income of the partnership plus (2) the payments made to the partners plus (3) payroll costs for other employees. For this purpose, payments to partners are included only if they are active participants in the business as evidenced by the fact they have self-employment income from the partnership as reported in Box 14 of their K-1. Payments made to partners who are merely passive investors are not included in the calculation. The computation of the PPP loan is shown below.

Partnership net income/12  
+ Average payroll costs for other employees/12)  
= Total average monthly payroll cost   
x 250% or 2.5  
= Maximum PPP Loan for partnership not to exceed $10 million

As seen in the example below, all things being equal, the amount qualifying as payroll costs (and, therefore, the amount of the PPP loan) can differ depending on whether the individual operated as a partnership or an S Corporation.

**Example 11**. Assume a partner has reported at least $100,000 of self-employment income in Box 14 of her K-1 (which is a combination of Box 1 “Ordinary Business Income” and Box 4 “Guaranteed Payments”). On the other hand, assume an owner/employee of an S corporation pays herself $50,000 in wages (i.e., as shown on Form 1120S, Line 7), while having $50,000 in Box 1 “Ordinary Business Income” of the K-1. In this case, the partner and the shareholder both have the same total income of $100,000. However, as calculated below, the partner would have twice the amount eligible for a PPP loan as compared to the S corporation owner/employee who only includes wages in the computation (and may have been trying to minimize the salary amount so as to save on employment taxes).

Partner: [($100,000/12 = $8,333) x 2.5] = $20,833.33 Maximum PPP Loan

S shareholder [($ 50,000/12 = $4,166) x 2.5] = $10,416.67 Maximum PPP Loan

***Deductibility of Business Expenses Paid with PPP Loans.***  See Page 7-43 of this supplement below.

**PPP Loans: Guaranty.** To encourage lenders to make these loans, the loans are fully guaranteed by the federal government through December 31, 2020. Collateral is not required nor are personal guarantees. Thus, if a business defaults on the loan, the government repays the loan.

**PPP Loans: A Final Problem.** While the PPP program seems to be on target, as many have note, there is one major drawback: when businesses receive their loan, they may not be operating. As Mr. Nitti points out, (see Nitti, Tony. “Ten Things We Need To Know About Paycheck Protection Program Loan Forgiveness.” *Forbes*, April 15, 2020 <https://www.forbes.com/sites/anthonynitti/2020/04/15/ten-things-we-need-to-know-about-paycheck-protection-program-loan-forgiveness/#3e3a64603291>

business owners who rushed to get a PPP loan will be faced with the realization that to achieve full forgiveness, they will need to pay employees NOT to work. And given the recent increase to unemployment pay, those same employees may prefer not to be paid by their employer, as in many cases, collecting unemployment will prove more lucrative. Given this reality, many business owners were hopeful that they would have flexibility in choosing their 8-week covered period, allowing them to wait out the shelter-in-place order, get their employees back to work, and maximize the payroll that would be incurred during that stretch, and by extension, the subsequent debt forgiveness.

That won’t be the case. The SBA clarified that the 8-week period begins on the date the borrower receives the disbursement of the loan, and the bank must make the disbursement within 10 days of loan approval. Thus, a business that took out a PPP loan in the past week has to start the clock immediately upon receipt of the funds, regardless of whether their business has even restarted operations.

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**Government Transfer Payments: Exclusion of Employer Disaster Relief Payments (§ 139)**

Employers can help employees who have suffered financial loss due to the pandemic by creating a program that utilizes qualified disaster relief payments. Section 139 and its special rules provide that so-called qualified disaster payments are not taxable. Moreover, the costs of such payments are deductible by the employer as an ordinary and necessary business expenses.

Section. 139(b)(1) defines a qualified disaster relief payment as any amount paid to reimburse or pay reasonable and necessary personal, family, living, or funeral expenses incurred as a result of a qualified disaster (provided amounts are not reimbursed by insurance or otherwise). Under this definition, childcare expenses resulting from school closures and costs incurred to enable an employee to work from home would most likely qualify.

In addition, qualified payments include those for the repair or rehabilitation of a personal residence or repair or replacement of its contents to the extent that the need for such repair, rehabilitation, or replacement is attributable to a qualified disaster,

A qualified disaster eligible for this treatment includes an event declared a major disaster or an emergency under the Robert T. Stafford Disaster Relief and Emergency Assistance Act (Stafford Act) (Rev. Rul. 2003-29). On 3/13/20, President Trump made an emergency declaration under the Stafford Act regarding the COVID-19 pandemic. Therefore, qualified disaster relief payments related to COVID-19 are eligible for tax-free treatment under § 139.

**Certain Benefits Provided to Volunteer Firefighters and Emergency Responders**

For tax years beginning in 2020, any member of a qualified volunteer emergency response organization could exclude from gross income (1) any qualified state and local tax benefit (certain state or local tax relief granted for performing volunteer emergency response services) or (2) any qualified state and local payment (a payment granted by state or local governments for performing volunteer emergency response services). The TCDTRA makes this income exclusion permanent for tax years beginning in 2021 and beyond. (See § 139B, as amended by TCDTRA Sec. 103.)

**CHAPTER 7: OVERVIEW OF DEDUCTIONS AND LOSSES**

**Page 7-9**

# **Compensation for Highly Compensated Employees of Publicly Traded Corporations.**

# For years after 2026, ARPA amends Code §162(m) to add a corporation’s five highest-compensated employees (i.e., besides the employees already covered by Code §162(m)) to the list of individuals subject to the $1 million cap on deductible compensation.

**Family and Medical Leave Payments and Sick Pay.**

In the world of work, the relationship between employers and employees is not always rosy. Indeed, there are labor laws designed to regulate that relationship to ensure that employers observe the rights of their employees and treat them fairly. One area that causes confusion and tension is that of family and medical leaves. The problem is simple: can employees temporarily leave their job due to medical and family circumstances without fear of losing it? Of course, the related question is whether employees should be entitled to paid sick leave.

As mentioned in the text in Chapter 13 (page 13-32), Congress addressed the issue of sick leave with the enactment of the Family and Medical Leave Act (FMLA) in 1993. The FMLA generally requires employers with more than 50 employees to allow their employees up to 12 weeks of ***unpaid*** leave for qualified medical and family reasons without fear of losing their jobs. The FMLA did not contain any tax provisions.

It should be noted that the FMLA of 1993 did not require employers to pay employees while they were on leave. To emphasize, it did not require **paid sick leave,** although some employers offered it and some states required it. What it did do was mandate that employers must grant their employees up to 12 weeks of job protected sick leave. As a result, employees legally can take up to 12 weeks of leave due to health reason and not worry about losing their jobs.

Perhaps, the first tax development with respect to sick leave occurred with the enactment of the TCJA of 2017 that created a special credit to help subsidize an employer’s cost of paying for family and medical leave (see page 13-32 of the text). Section 45S allows eligible employers to claim a general business credit equal to 12.5% of the wages paid. In addition, the credit is increased by 0.25 percentage points for each percentage point by which the rate of payment exceeds 50% of the employee’s normal wages (but not more than 25% or a maximum of 37.5%). Employers who claim the credit must reduce their deduction for wages by the amount of the credit.

No doubt some hoped that the credit would encourage more employers to offer paid sick leave programs. The dramatic upheaval brought by COVID-19 prompted Congress to revisit this area in the enactment of FFCRA (*Families First Coronavirus Response Act*), the first piece of legislation in response to COVID-19. FFCRA generally requires certain employers to provide sick pay. ARPA codified the credits for payment of sick pay and family leave. It also increased the credit to $12,000.

**Paid Sick Leave: Background.** As noted above, prior to FFCRA, there was no federal law in the U.S. that required sick pay for the private sector employees (except for an executive order signed by President Obama for businesses that do business with the federal government). Still, it is not uncommon to hear employees say that they are taking a sick day, for which they may or may not be paid. However, payments for sick leave are usually required for public sector workers—both federal and state employees, who are provided paid sick leave as part of their employment agreements.

As reported by Workest, (<https://www.zenefits.com/workest/the-definitive-list-of-states-and-cities-with-paid-sick-leave-laws/>, an analysis in 2018 by the Bureau of Labor Statistics found that about 61 percent of Americans workers in the private sector had sick pay while 39 percent of American did not. In that regard, currently 11 states and Washington D.C., as well as over 30 localities, require paid sick leave. However, things are changing. For example, recently, on April 3, 2020, the state of New York, in response to the millions of jobs lost due to COVID-19, amended its labor laws to require all New York employers to provide paid (or unpaid) sick leave for their employees See <https://www.littler.com/publication-press/publication/new-york-enacts-statewide-sick-leave-law>.

**FFCRA and Required Payment of Sick Leave.**

On the federal front, the enactment of FFCRA was a milestone concerning sick leave. FFCRA now **requires** most employers to provide **paid sick leave** but only if its employees are directly impacted by the COVID-19. As a result, most of America’s nearly 159 million workers will be able to get *paid* time off if they or their families are directly affected by COVID-19. Moreover, FFCRA modifies the tax law to give employers credits for these payments that can be used to reduce their payroll tax liabilities. This arrangement effectively eliminates the employer’s cost of the sick pay that they are required to pay under federal law.

Technically, FFCRA contains two pieces of legislation that require paid sick leave. The new law is confusing because there are two separate programs that concern sick pay and there are subtle differences between them. Note that at the conclusion of this discussion, there are charts that summarize and compare the two programs. The two programs are:

(1) **The Emergency Paid Sick Leave Act** (**EPSLA**, Act § 5101) that requires certain employers to provide up totwo weeks of *paid sick leave*and.

(2) **The Emergency Family and Medical Leave Expansion Act** (**EFMLEA**, Act § 3101), which, in its so-called *family and medical leave*program, expands the Family and Medical Leave Act of 1993 (FMLA) mentioned above. In so doing, the EFMLEA increases the benefits beyond those required by the paid sick leave rules of EPSLA (i.e., two weeks of sick pay). EFMLEA’s family and medical leave program generally requires 12 weeks of leave (10 of them paid) for certain COVID-19 related reasons. [**Note:** the FMLA of 1993 requires up to 12 weeks of *unpaid* leave (see FMLA of 1993 (29 United States Code § 2611(a)(1) that provides that an “employee shall be entitled to a total of 12 workweeks of leaving . . .”)).

These two acts, EPSLA and EFMLEA, work in different ways to assist working families facing health emergencies arising out of the coronavirus.

**Which Employees Are Covered?** The criteria for which employees are covered by EPSLA’s **paid sick leave** requirement and the criteria for which employees are covered by EFMLEA’s **family and medical leave** program are not identical. For the paid sick leave program of EPSLA, all employees are covered, regardless of how long they have worked (even a day) or whether they are part-time. On the other hand, EFMLEA’s expanded family and medical leave program only covers those employees who have worked for at least 30 days. Both Acts, both programs, apply to part-time employees. **Note**: neither program requires employers to provide paid sick leave for employees who are health care providers or emergency responders.

**Which Employers Are Required to Pay Sick Leave?** Generally, FFCRA covers both private employers with less than 500 employees and certain public employers (“covered employers”). However, as discussed below, small businesses (less than 50 employees) who do not want to pay for sick leave can elect to exempt themselves from certain provisions of FFCRA.

***Large Employers (More than 500 Employees)*.** The new legislation does not necessarily reach the nation’s larger companies. Neither EPSLA’s paid sick leave requirement nor EFMLEA’s family and medical leave program apply to employers with more than 500 employees. These businesses, which may or may not already offer paid time off, are not subject to the legislation. However, some large businesses that had not offered these benefits in the past--including Walmart and McDonald’s—have announced temporary coronavirus-related sick pay policies. While the federal rules do not apply to larger companies, a number of states who are adopting their own emergency sick leave statutes are thinking otherwise. Interestingly, some of these states do not exempt large employers. In addition, proposals in Congress would remove this 500-employee cap and force such businesses to pay sick leave. For this reason, experts are cautioning employers with more than 500 employees to monitor potential legislation at the state and federal levels.

***Small Business Exemption.*** Similar to its treatment of large employers, FFCRA does not always reach the workers of the country’s smaller businesses. Under certain circumstances, employers with fewer than 50 employees (small businesses) are *not* required to provide paid leave when an employee’s leave is necessary to care for a child whose school or place of care is closed, or whose childcare provider is unavailable due to COVID–19 related reasons. In other words, these businesses are exempt from having to pay sick pay in these situations. However, this exemption is available only if the leave payments would jeopardize the viability of the business as a going concern. If businesses wish to avoid paying sick leave based on the viability argument, the regulations of the Department of Labor indicate that an officer of the business must document that one or more of the following is true:

(1) The requested leave causes the business’s expenses and financial obligations to exceed its available revenues and prevents the business from operating at even a minimal capacity;

(2) The absence of the employees requesting leave would entail a substantial risk to the financial health or operational capabilities of the business because of their specialized skills, knowledge of the business, or responsibilities; and

(3) There are not sufficient workers who are able, willing, and qualified, and who will be available at the time and place needed, to perform the labor or services provided by the employee or employees requesting leave, and this labor or services are needed for the small business to operate at a minimal capacity.

To emphasize, the exemption for small businesses is only an exception from the obligation to provide paid leave to an employee who requests leave due to school or childcare closures (e.g., so the employee can be home to take care of his or her child because the child’s school or facility that provided childcare is closed). Small businesses must still provide paid sick leave to an employee who needs leave because he or she: (1) is subject to a quarantine or an isolation order; (2) has been advised by a health care provider to self-quarantine; (3) is experiencing COVID-19 symptoms and is seeking a medical diagnosis; or (4) is caring for an individual subject to a quarantine order or has been advised to quarantine. There is no exception for small businesses in these situations. They are required to pay sick leave. They are only exempt from paying sick leave to those where schools or daycare facilities have closed.

***Number of Employees*.** The number of employees is critical since the small business exemption is available only if the employer has less than 50 employees. Moreover, FFCRA does not apply to employers with more than 500 employees. For these purposes, the following employees are counted: all full- and part-time employees, employees on leave, temporary employees who are jointly employed by the employer and another employer (a staffing company), and day laborers supplied by a temporary agency when the employee’s leave is taken.

**Sick Pay Required.** For employers with 50 but not more than 500 employees, the small business exemption is not available and sick pay is required. FFCRA’s paid sick pay program (i.e., EPSLA (FFCRA Act § 5101(a))) *requires* covered employers (those with at least 50 and less than 500 employees) to provide all **eligible** employees up to **2 weeks** (10 days or 80 hours) of **paid sick leave** at **full** **pay**, up to a **specified cap ($511/day) or a total of $5,110 (10 days x $511/day)**, An employee is **eligible** for sick leave payments if he or she is unable to work (or telework) because he or she:

(1) is subject to a Federal, State, or local quarantine or isolation order related to COVID-19,

(2) has been advised by a health care provider to self-quarantine due to concerns related to COVID-19,

(3) is experiencing symptoms of COVID-19 and seeking a medical diagnosis,

(4) is caring for an individual who is subject to a Federal, State, or local quarantine or isolation order related to COVID-19,

(5) is caring for a son or daughter under 18 because the child’s school or place of care has been closed or the child care provider is unavailable due to COVID-19, or

(6) is experiencing any other substantially similar condition specified by Health and Human Services

**Family and Medical Leave Payments and Sick Pay.** FFCRA’s family and medical leave program (i.e., EFMLEA (FFCRA Act § 3101)) expands the benefits from 2 weeks (per EPSLA) to 10 weeks for an employee in one particular situation, i.e., he or she is unable to work (or telework) due to a need for leave to care for a son or daughter under 18 years if the school or place of care has been closed, or the child care provider of such son or daughter is unavailable. (The IRS generally refers to wages in this case as “qualified leave wages.”)

Unlike the sick pay program of EPSLA, the Medical and Family Leave program provides that the first two weeks of leave (usually ten workdays) are unpaid. However, an employee may get paid sick leave under EPSLA, which requires two weeks of paid sick leave. Alternatively, an employee may be able to obtain sick pay provided to the employee pursuant to the employer’s preexisting policies for these two weeks of unpaid leave (e.g., vacation pay).

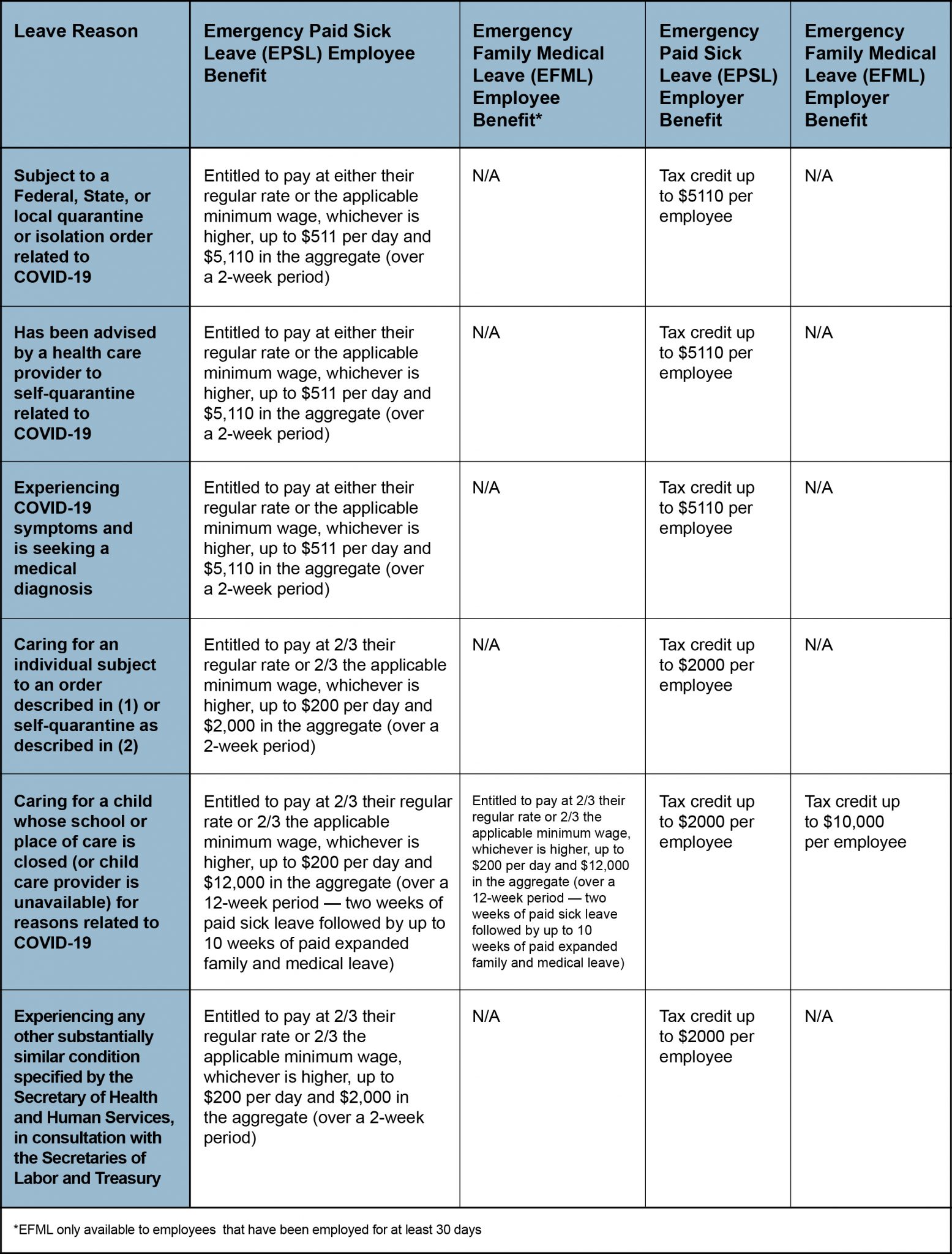
While the Medical and Family Leave program of EFMLEA does not provide paid sick leave for the first two weeks of leave, it does provide payment for the following period of up to ten weeks. The employee must be paid sick leave at **2/3 of the employee’s regular rate of pay** ***up to $200 per******day****.*  The total EFMLEA payment per employee for this ten-week period is **capped at $10,000** in the aggregate. As a result, assuming the employee could obtain two weeks of paid leave taken under EPSLA (10 days x $200 = $2,000) and $10,000 under EFMLEA, the total potential sick pay is $12,000. As noted above, an eligible employee may elect to use (or an employer may require that an employee use), expanded family and medical leave concurrently with any leave offered under the employer’s other policies that would be available for the employee to take to care for his or her child, such as policies for vacation or personal leave or paid time off.

***Employer Social Security Taxes on Qualified Wages.***  The qualified family leave wages are not subject to the employer portion of social security tax.

**Summary Tables.** These two programs are summarized below and a similar table on the next page. Note that the table on the following page also identifies the credit that an employer can get for sick pay. This is discussed later below.

|  |  |
| --- | --- |
| **Sick pay** **(EPSLA)** | **Family and Medical Leave (EFMLEA)** |
| Employee unable to work or telework due to | Employee unable to work (telework) due to |
| 1. Federal, state, local quarantine or isolation order | Must be employed (on payroll) for 30 days |
| 2. Self quarantining under advice of healthcare provider due to Covid-19 concerns | 1. Caring for child if school closed |
| 3. Obtaining diagnosis due to Covid-19 symptoms | 2. Caring for child if child care provider closed or unavailable due to Covid-19 |
| 4. Assisting a family member quarantined under order or advice of healthcare provider |  |
| 5. Caring for child if school closed or child care provider closed or unavailable due to Covid-19 |  |
| 6. Additional categories added by HHS |  |

|  |  |
| --- | --- |
| **Amount of  Sick Pay** | **Amount of  Family and Medical Leave Pay** |
| 1. Up to 2 weeks (80 hours) sick leave, maximum of $511 per day capped at $5,110 total. | 1. 2/3 of compensation up to $200/day for 10 weeks capped at $10,000 |
| 2. Care for family member w/coronavirus or child after school or day care closing,  $200/day ($2,000 per employee cap) | 2. Caring for child if child care provider closed or unavailable due to Covid-19, $200/day ($2,000 per employee cap) |



See <https://www.cshco.com/articles/summary-of-families-first-coronavirus-response-act/>)

**Credits for Sick Pay.**

**(Note:** While tax credits are normally addressed with the general discussion of credits, for purposes of this supplement, the credits related to FFCRA’s sick pay requirements discussed above are considered below).

**FFCRA Credits for Sick Pay.** As noted above, FFCRA provides businesses with refundable tax credits to reimburse 100% of the costs of providing employees with required paid sick leave and expanded family and medical leave for reasons related to COVID-19. In effect, these credits operate such that employers should not incur any cost for the payments. The credits include the employer’s share of Medicare taxes as well as expenses to provide and maintain a group health plan (to the extent that the amounts are excluded from the employee’s gross income under § 106(a)). ARPA codifies these credits.

According to the IRS, “Eligible Employers” can obtain the benefit of these payroll tax credits almost immediately by applying them against their federal payroll taxes that normally are paid quarterly (i.e., amounts withheld for employee income taxes, employment taxes including the employee and employer share for Social Security and Medicare). Generally, employers can claim the credits on their federal employment tax returns filed quarterly (e.g., Form 941, Employer's Quarterly Federal Tax Return). Form 941 is due by the last day of the month that follows the end of the quarter as follows:

The Quarter Includes . , , , . . Quarter Ends Form 941 Is Due

1. January, February, March March 31 April 30  
 2. April, May, June June 30 July 31  
 3. July, August, September September 30 October 31  
 4. October, November, December December 31 January 31

Depending on the total taxes withheld, taxes normally are deposited monthly or semi-weekly (every two weeks). If there are insufficient federal employment taxes to cover the amount of the credits, employers may request an advance payment of the credits from the IRS by submitting Form 7200, Advance Payment of Employer Credits Due to COVID-19.

The IRS also explains that “Eligible Employers claiming the credits for qualified leave wages (and allocable qualified health plan expenses and the Eligible Employer’s share of Medicare taxes) must retain records and documentation related to and supporting each employee’s leave to substantiate the claim for the credits.

**Page 7-43**

**Expenses and Interest Relating to Tax-Exempt Income.**

**Deductibility of Business Expenses Paid with PPP Loans.** As discussed earlier in this supplement (material for Page 6-51 of the text), forgiveness of PPP loans is generally nontaxable if the loan is used for qualified expenses (e.g., payroll costs, mortgage interest, rent and utilities.) At first glance, this seemed quite favorable, but there was trouble lingering below the surface. As noted in the text, § 265 provides that no deduction is allowed for expenses related to tax-exempt income. Early in the continuing saga of PPP loans, tax pundits pointed out that if expenses related to PPP loan forgiveness are not allowed, this puts taxpayers in the same position as if their forgiven PPP loan were included in income and they were able to deduct all expenses. On April 30, 2020, Notice 2020-32, IRB 2020-21, 05/01/2020 takes that position. The Notice specifically explains that a taxpayer that receives a loan through the Paycheck Protection Program (PPP) is not permitted to deduct expenses that are normally deductible under the Code to the extent the expenses were reimbursed by a PPP loan that was later forgiven. None of the legislation relating to the COVID-19 addressed the issue (e.g., FFCRA and CARES).

As might be expected, the Notice was met with great hissing and moaning. The AICPA indicated that it believes strongly that the position of the Notice is contrary to Congressional intent. Chris Hesse, CPA, chair of the AICPA Tax Executive Committee, said: “In effect, the IRS guidance means that the taxability provision [Act § 1106(i)] has no meaning. Why waste the ink to say that for purposes of the Code, the loan forgiveness is not includible in income, if the government will just take away deductions in the same amount?” See Sally P. Schreiber. "AICPA Challenging Nondeductibility of PPP-Related Expenses.” *Journal of Accountancy*, May 1, 2020, <https://www.journalofaccountancy.com/news/2020/may/expenses-reimbursed-by-ppp-not-tax-deductible-paycheck-protection-program.html> In a letter dated August 4, the AICPA joined over 170 organizations to urge Congress to “include a technical correction addressing the tax treatment of loan forgiveness.”

The outcries worked. ARPA provides a deduction for expenses paid out of PPP loan proceeds. In Rev. Proc. 2021-20, the IRS allows taxpayers who filed a tax year 2020 return on or before December 27, 2020, to deduct those expenses on their 2021 tax return rather than file amended returns or administrative adjustment requests.

**CHAPTER 8: EMPLOYEE BUSINESS EXPENSES**

**Page 8-37**

**100% Deduction for Food and Beverages**

The IRS issued new guidance for deductions of the costs of food or beverages obtained from restaurants and bars. The TCDTRA (2020) added a temporary exception to the 50% limit on the amount that businesses may deduct for food or beverages. Beginning in 2021 through 2022, the new exception allows a 100% deduction for food or beverages from restaurants, if the business owner (or an employee of the business) is present when food or beverages are provided, and the expense is not lavish or extravagant under the circumstances. Under the temporary provision, restaurants include businesses that prepare and sell food or beverages to retail customers for immediate on-premises and/or off-premises consumption. However, restaurants do not include businesses that primarily sell pre-packaged goods not for immediate consumption, such as grocery stores and convenience stores. See News Release IR 2021-79 and Notice 2021-25.

**CHAPTER 9: CAPITAL RECOVERY: DEPRECIATION, AMORTIZATION   
 AND DEPLETION**

**Page 9-6**

**Depreciation of Motorsports Entertainment Complex Property.**

Before the TCDTRA, a seven-year depreciation recovery period applied to motorsports entertainment complex property placed in service before 2021. A motorsports entertainment complex is a racing track facility that is permanently situated on land and that hosts one or more racing events within 36 months of the month it is placed in service.

The TCDTRA extends the seven-year recovery period to cover qualifying property placed in service in 2021–2025. [See § 168(i)(15)(D), as amended by TCDTRA § 115.]

**First-year Expensing for Entertainment Productions**

Pre TCDTRA, taxpayers could elect to claim a first-year write-off for the cost of qualified film, television, and theatrical productions commencing before 2021, subject to a $15 million per-production limit or a $20 million limit for productions in certain disadvantaged areas. The TCDTRA extends this deduction to cover qualifying productions commencing in 2021–2025. [See § 181(g), as amended by TCDTRA § 116.]

**Three-year Depreciation for Young Racehorses**

As revised, TCDTRA extends the three-year depreciation recovery period to cover racehorses that are no more than two years old when placed in service in 2021. [See § 168(e)(3)(A)(i), as amended by TCDTRA § 137.]

**Accelerated Depreciation for Indian Reservation Property Extended**

TCDTRA extends shorter depreciation periods for qualified Indian reservation property to cover property placed in service in 2021. To qualify, the property must be predominantly used for business purposes within a reservation, owned by someone unrelated to the previous owner, and unrelated to gaming. [See § 168(j)(9), as amended by TCDTRA Sec. 138.]

**Page 9-22**

**Leasehold Improvements Qualify for Bonus Depreciation**

The CARES Act included a technical correction to the TCJA that allows the interior improvements of buildings (qualified improvement property or QIP as defined in § 168(e)(6)) to qualify for 100% bonus depreciation. The QIP amendments made by §2307 of the CARES Act are retroactively effective for property placed in service after Dec. 31, 2017. In other words, it is as if this QIP provision had been included in the original version of the TCJA.

Technically, the CARES Act provides a correction to the TCJA, and specifically designates QIP as MACRS 15-year property, making it now eligible for bonus depreciation purposes (§ 168(e)(3)(E)(vii)). Also, QIP is assigned a 20-year class life for the Alternative Depreciation System (§ 168(g)(3)(B)). This designation for ADS purposes has implications where the taxpayer has made a “real estate trade or business election” to avoid the interest expense limitation under § 163(j) as discussed in Chapter 11 (see page 11-28). If the taxpayer makes such election, then the real estate involved (i.e., 27.5-year residential or 39-year commercial) as well as the QIP would have to be depreciated under the ADS.

**Example 12.**  JKB LLC, a partnership, purchased a warehouse in 1995 that now stands idle. They (or, their tenants) then proceed to do substantial improvements (i.e., QIP) to the interior of the building as the various units are rented out. These QIP assets would be classified as MACRS 15-year property and would, therefore, be eligible for bonus depreciation.

While this new rule is significant, it should be noted that QIP generally is eligible for immediate expensing under § 179 ($2,590,000 in 2020), if the activity qualified as a trade or business.

Note that § 179 immediate expensing, as well as bonus depreciation, for QIP requires that the commercial building to which these improvements relate must have previously been placed in service before these improvements are made. As a result, a new commercial building in which the improvements are made before receiving, for example, a certificate of occupancy would not be eligible to be classified as 15- year MACRS “qualified improvement property.”

**Page 9-26**

**Deduction for Energy-Efficient Commercial Buildings Made Permanent**

A special rule (not specifically discussed in the text) concerns § 179D containing a special deduction related to expenditures to make commercial buildings energy efficient. Commercial building owners can claim deductions for expenditures for energy-efficient improvements to lighting, heating, cooling, ventilation, and hot water systems and building envelopes. The write-off equals $1.80 per square foot or $0.60 per square foot if certain subsystems meet energy-efficiency standards, but the entire building does not. The TCDTRA makes this deduction permanent and adds an inflation-adjustment feature for tax years beginning in 2021 and beyond.

**Page 9-29**

**Depreciation Limitations.**

The IRS has issued its inflation-adjusted depreciation amount limits for passenger automobiles, vans and trucks placed in service in 2021 (Rev. Proc. 2021-31). For these vehicles for which bonus first-year depreciation is taken, the depreciation limits are $18,200 for the first year (an increase of $100 from 2020); $16,400 for the second year (an increase of $300); $9,800 for the third year (an increase of $100); and $5,860 for each succeeding year (an increase of $100). If bonus first-year depreciation is not taken, the depreciation limit for the first year would be $10,200 (an increase of $100 from 2020); the other years are as above.

Rev. Proc. 21-31 also includes an updated table for the inclusion amounts for passenger automobiles leased beginning in calendar year 2021. The inclusion amounts start for leased automobiles with a fair market value over $51,000.

**CHAPTER 10: CERTAIN BUSINESS DEDUCTIONS AND LOSSES**

**Page 10-13**

**Excess Business Losses (EBLs)**

The TCJA of 2017 created § 461(l) that limits so-called excess business losses (EBLs). This rule was temporarily modified by the CARES Act. The purpose of the EBL rule was to limit the amount of net business losses (e.g., losses of a sole proprietorship, S corporation or partnership) that can be deducted from an active—in contrast to passive—owner’s return. As explained in the text, the maximum loss allowed is $500,000 for joint returns and $250,000 for others. The loss in excess of the allowed amount (the excess business loss) becomes part of the taxpayer’s NOL and carried over under those rules. Generally, the rule (§ 461(l)(3)(A)) provides that an "excess business loss" is the excess of the:

1. Taxpayer's aggregate trade or business deductions for the tax year over

2. The sum of aggregate trade or business gross income or gain plus $250,000 (as adjusted for inflation).

The effect is that only the first $250,000 of loss is deductible without limitation but the remainder is an EBL and becomes part of the taxpayer’s NOL.

**Example 13.**  S, single, has $300,000 of interest income, a $500,000 loss from a partnership and $100,000 of income from an S corporation. The taxpayer materially participates in both the partnership and S corporation activities. Consequently, the passive loss limitations do not apply. Under pre-TCJA rules, the taxpayer would have a net loss of $100,000 ($300,000 interest - $500,000 partnership loss + $100,000 S corporation income). However, under the EBL rules, the two “business interests” are first combined to get an overall loss of $400,000 ($100,000 S corporation income - $500,000 partnership loss = $400,000), which is then limited by the EBL rules to $250,000. The $250,000 loss could offset the $300,000 of nonbusiness interest income for a net positive income of $50,000. The disallowed loss of $150,000 ($400,000 - $250,000), the EBL, is not permanently lost but is instead carried forward as a net operating loss (NOL).

**EBL Limitation Effective Date.** The CARES Act temporarily modified the excess business loss limitation for noncorporate taxpayers so they potentially can deduct a greater amount of excess business losses arising in 2018, 2019, and 2020. In essence, the CARES Act postpones the effective date for the EBL rules retroactively from tax years beginning after December 31, 2017, to tax years beginning after December 31, 2020.

To the extent that a 2018 or 2019 tax return has been filed that reported an EBL (as illustrated in Example 13 above), a taxpayer (i.e., individual, trust, or estate) must evaluate amending the return to claim a refund of taxes or to report a net operating loss under Code §172.

The CARES Act provides several technical corrections to the EBL rules (effective when this provision is once again in effect for 2021 onward). As amended, wage income would not be includible as business income for purposes of the EBL limitation. In addition, deductions for capital losses are not included in the calculation of an excess business loss. Finally, capital gains are only included in the calculation to the extent of the lesser of (1) the net capital gain attributable to a trade or business or (2) capital gain net income. These technical amendments are retroactive to taxable years beginning after December 31, 2017 (i.e., so as if they were included in the original version of the TCJA).

**EBLs and ARPA.** ARPA extends the §461(l) limitation on excess business losses of noncorporate taxpayers for one year, through 2027. As noted above, the rule concerns the $250,000/500,000 limit on business losses (whether passing through on a K-1, or from a Schedule C or F proprietorship) which was part of the TCJA but which was delayed until the 2021 tax year.

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**Net Operating Losses**

**NOL Deduction: Carryback of NOLs for 5 Years Permitted and No 80% Limitation.** The CARES Act addresses several changes made by the TCJA concerning the use of NOLs.

Under the TCJA and as explained in the text, beginning in 2018:

* The 2-year carryback period (except for farming businesses) was eliminated. Therefore, NOLs occurring in 2018 and beyond could only be carried forward.
* NOLs occurring in 2018 and beyond were carried forward indefinitely. The 20-year carryover period was eliminated.
* The NOL deduction for NOLs occurring in 2018 and beyond was limited to 80% of taxable income.  However, NOL carryovers existing prior to 2018 were not subject to the 80% limit.

The CARES Act changed the TCJA rules. As noted above, the TCJA changes, § 172(b)(1)generallyproviding that an NOL for any tax year must be carried *forward*.But, the CARES Actalters that approach and provides that NOLs arising in a tax year beginning *after* Dec. 31, 2017 and *before* Jan. 1, 2021 (i.e., losses for 2018, 2019 and 2020) can now be carried *back* to each of the *five* previoustax years (e.g., a 2018 NOL could be carried back to 2013). The hope of the legislation is that it might help businesses who have suffered due to the coronavirus pandemic.

**NOLs: Temporary Repeal of 80% of Taxable Income Limitation.** As noted above, the CARES Act provides additional relief for businesses affected by COVID-19 by *temporarily* removing the 80% taxable income limitation on the use of NOLs for taxable years beginning *before* January 1, 2021. However, the 80% limitation is reinstated for 2021.

The temporary repeal of the 80% limitation, when coupled with the new 5-year NOL carryback period is aimed at businesses that may struggle given the current economic conditions. The CARES Act gives taxpayers the ability to utilize NOLs in prior taxable years beginning as early as in 2013 (e.g., an NOL incurred in a 2018 tax year could be carried back 5 years) without limitation. In so doing, the CARES Act allows businesses to use NOLs to offset taxable income in those prior years that had been subject to a marginal tax rate as high as 35% for corporations (rather than 21%) and 39.6% for individuals. This, in turn, might provide additional cash flow and liquidity that may help businesses survive.

Although the net effect of easing the NOL rules will be positive for many businesses with applicable losses, that may not be true for all business owners. Some businesses may find that using the new 5-year NOL carryback rule limits their ability to use other deductions or credits based on taxable income that they may have claimed on prior year returns (e.g., foreign tax credits). For this reason, taxpayers that do not want to carry back any NOLs have that option. Taxpayer can make an election (i.e., under §172(b)(3)) to forego this carryback option by the extended due date of their return “for the first tax year ending after the enactment date (i.e., 3/27/20) of this law change.” In other words, an election made for a 2020 calendar tax year return wouldapply to any NOLs arising in either 2018 or 2019 that otherwise would be carried back for five years.

The amendments made by Act § 2303(b) apply to NOLs arising in tax years beginning after December. 31, 2017 and to tax years beginning before, on or after such date to which such NOLs are carried (Act § 2303(d)(2)).

**NOLs: Taxable Income Limitation and § 199A Qualified Business Income Deduction.** The qualified business income deduction is generally limited to 20% of taxable income before any consideration of the deduction for NOLs (except for any portion of the NOL that is attributable to excess business losses as discussed in Chapter 10). As noted above, for taxable years beginning *after* December 31, *2020*, the 80% of taxable income limitation on NOLs is reinstated. When determining taxable income for purposes of calculating the 80% limitation on NOLs, the QBI deduction is ignored.

**Example 14.** The year is 2021 and NOLs are generally limited to 80% of taxable income. A married couple has taxable income in 2021 of $100,000 before considering a QBI deduction of $15,000. They also have a post 2017 NOL of $150,000. With the reinstatement of the 80% of taxable income limitation in 2021, the NOL would be limited to $80,000 (80% x $100,000 of taxable income before the QBI deduction).

**CHAPTER 11: ITEMIZED DEDUCTIONS**

**Page 11-13**

**Health Savings Accounts**

**Qualified Expenses: OTC Drugs, Telehealth and Menstrual Expenses.** As explained in the text, the tax law generally allows taxpayers to pay for medical expenses with pretax dollars through a Health Savings Account (HSA). For example, taxpayers can instruct their employer to withhold amounts from their paycheck that are stored in an HSA. In this way, the amounts are never subject to an income tax nor an employment tax (and most state income taxes). Alternatively, taxpayers can simply make contributions to an HSA and deduct them for AGI.

The predecessor to HSAs was created in 1996 to entice people to be more conscious of health care costs, and thus, use less of it. Advocates of HSAs believe that they are an important tool that help reduce the growth of health care costs and increase the efficiency of the health care system. Some have said that they are the most tax-preferred savings vehicle in American history.

The major drawback of an HSA is that it comes with a qualified High-Deductible Health Plan (HDHP). An HDHP typically has lower premiums but higher deductibles, meaning higher out-of-pocket costs than a traditional health plan. Also, HSAs must be created before old age sets in. Taxpayers enrolled in Medicare Parts A or B, or those that file for Social Security benefits after age 65, cannot make contributions to an HSA.

Payments of medical expenses by an HSA do not impact the individual’s taxable income if the distribution is used for qualified medical expenses (§ 223(d)). If any portion of a distribution is not used for qualified medical expenses, that portion is considered taxable income and is subject to a 20 percent penalty. The CARES Act made several changes to HSAs that are covered in the text but are also noted below.

First, (as noted in the text) the CARES Act eliminated the requirement that medical expenses must be prescribed in order to qualify. This appears to make payment of over-the-counter remedies qualified medical expenses but only for purposes of HSA distributions.

Second, the CARES Act expands the definition of qualified medical expenses to include amounts paid for “menstrual care products” (§ 233(d)(2)). The CARES Act explains that “menstrual care products” include tampons, pads, liners, cups, sponges, or similar products used by individuals with respect to menstruation or other genital-tract secretions. As a result, taxpayers who have a health savings accounts (HSAs), health reimbursement arrangements (HRAs), health flexible spending accounts (health FSAs), and Archer medical savings accounts (Archer MSAs) can contribute to such accounts and use those funds for such expenses on a pretax basis.

Finally, the CARES Act addresses telemedicine. Many employers have utilized telemedicine as a part of their group medical program, either integrated with the group health plan or as a separate benefit. This is particularly true since the arrival of COVID-19. Prior to the CARES Act, the IRS did not allow those expenses (e.g., the cost of telemedicine) to be reimbursed under a high-deductible health plan (HDHP) until the plan’s deductible was satisfied**.** In other words, if the deductible had not been satisfied, the cost of the televisit (i.e., a word so new that it’s not in most dictionaries) would not be a qualified medical expense. In such case, payment for a televisit by the HSA would be considered a taxable distribution and a 20% penalty also would be assessed. In effect, the cost of the televisit would be paid with after-tax dollars plus 20%. The CARES Act alters that approach and allows a high deductible health plan to provide telehealth and remote care services before the deductible is reached for 2020 and 2021.

Note that the IRS has issued Announcement 2021-7, which clarifies that amounts paid for personal protective equipment, such as masks, hand sanitizer, and sanitizing wipes, for the primary purpose of preventing the spread of COVID-19 qualify as deductible medical expenses (provided total medical expenses exceed 7.5% of the taxpayer’s AGI). Such amounts also are eligible to be paid or reimbursed under health Flexible Spending Arrangements (health FSAs), Archer Medical Savings Accounts (Archer MSAs), Health Reimbursement Arrangements (HRAs), or Health Savings Accounts (HSAs).

**Group Health Plans: Required Coverage of COVID-19 Expenses**. The CARES Act requires that all group health plans cover COVID-19 diagnostic testing and related visits at no cost to consumers. The CARES Act expands this coverage to include in vitro diagnostic testing for the detection of SARS, CoV-2 as well as COVID-19 if such tests are approved, cleared, or authorized by the FDA, furnished to a participant during an office visit (in person or by telehealth), urgent care visit, or emergency room visit resulting in an order for or administration of such test. The CARES Act also requires group health plans to cover “qualifying coronavirus preventive service.” A qualifying coronavirus preventive service is an item, service or immunization that is intended to prevent or mitigate COVID-19. The requirement to cover a qualifying coronavirus preventive service takes effect 14 business days after the date on which a recommendation is made relating to such service.

**High Deductible Health Plans**. As noted in the text, in Notice 2020-15, a payment of testing or treatment for COVID-19 by a high deductible health plan (HDHP) without a deductible will not affect such plan’s status as an HDHP, regardless of whether the plan’s deductible has been met (Notice 2020-15 (03/11/20)). As of this writing, the IRS has not provided additional guidance

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**Interest Expense**

**Deduction for Business Interest: Increased Limitation.** As noted in the text, the TCJA of 2017 limits the deduction of business interest to 30% of adjusted taxable income or ATI (§ 163(j)(10)). The total cap is the sum of (1) the taxpayer’s business interest income (if any); (2) 30% of the taxpayer’s ATI; and (3) the taxpayer’s floor plan financing interest expense for the taxable year. Any disallowed interest can be carried over indefinitely.

The text also notes that the CARES Act temporarily modifies this provision for tax years that begin in 2019 or 2020, The CARES Act increases the ATI limitation, from 30% to 50%. In addition, the CARES Act allows corporations to elect to use their 2019 ATI as their ATI in 2020 for purposes of this increased 50% threshold. This ensures that even though their earnings may be harmed by the COVID-19 outbreak, their otherwise increased business interest deduction will not be. As of this writing, there have been no further changes and the 30% limitation is reinstated for 2021.

**Example 15.** CDB Inc. had ATI of $5 million in 2019 but a negative ATI in 2020. It normally would have no deduction for its business interest in 2020 since ATI was negative (50% x ATI $0 = $0). But, under the CARES Act, the business could elect to use its 2019 ATI for 2020. If so, it could deduct $2.5 million of interest expense in 2020 (50% x $5 million ATI from 2019 instead of 2020). This may in turn generate a larger loss, and the company could use the favorable new NOL provisions to carry back the loss to 2019 and receive a refund on some or all of the taxes otherwise paid.

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**Charitable Contributions: Limitations on Deductions**

**Charitable Contributions: $300 Deduction from Taxable Income.** The CARES Actallowed taxpayers to claim contributions of up to $300 of *cash* contributions to public charities as a deduction for AGI (i.e., an above-the-line deduction) in 2020. In short, nonitemizers were allowed to claim up to a $300 deduction. Moreover, a taxpayer choosing to take the standard deduction in 2020 effectively increased this amount by $300 by making $300 of charitable contributions. In 2020, the deduction reduced AGI and, therefore, slightly impacts deductions whose calculation involves AGI (§ 62(a)(22)). The Consolidated Appropriations Act of 2021 continues the $300 deduction; however, it is not a deduction for AGI or an itemized deduction but simply a reduction in taxable income (much like the qualified business income deduction).

**Increase in Limits on Contributions of Food Inventory**: Previously, a donation of “apparently wholesome food inventory” to a charitable organization that was used for the care of the ill, the needy, or infants was deductible. The taxpayer could deduct an amount up to its basis plus half the gain that would be realized had the food been sold (not to exceed twice the basis). In the case of a C corporation, the deduction could not exceed 15% of the corporation's income. In the case of a taxpayer other than a C corporation, the deduction could not exceed 15% of the taxpayer’s aggregate net income for that tax year from all businesses from which those contributions were made, computed without regard to the taxpayer's charitable deductions for the year. § 170(e)(3)(C)).

The CARES Act provides that in the case of charitable contribution of food during 2020, the taxable income limit is also 25% rather than 15%. (Act § 2205(b)). The CARES Act emphasizes that the food donations must be made to a charity. So, it would appear that, for instance, a restaurant that wanted to give excess food that would otherwise spoil would need to donate it first to a church or a school to be distributed, instead of inviting the general public to consume the food at the business’s location (or picking the food up and eating it elsewhere). The Consolidated Appropriations Act of 2021 (§ 213), signed into law on December 28, 2020, maintains and expands the charitable contribution incentives originally enacted by the CARES Act). continues this approach.

**Unlimited Charitable Itemized Deduction for Individuals.** As discussed in the text, for large contributions and contributions of property there is a long list of complex interrelated limitations that can apply (e.g., cash contributions subject to 60% of AGI, non-cash donations subject to 30% of AGI or 20% for certain others and more). However, the CARES Act generally provides that for 2020 the 60% limitation for cash contributions does not apply. In other words, after considering other current charitable contributions that are subject to various AGI limitations, individuals can claim an itemized deduction for charitable contributions of cash equal to 100% of their AGI. Importantly, this 100% of AGI limit applies to cash contributions made directly to charitable organizations, not to contributions to donor advised funds, supporting organizations or private foundations. Moreover, any cash contributions that exceed the taxpayer’s AGI and which, therefore, are not deducted in 2020 generally can be carried forward subject to the 60% of AGI limit in the succeeding 5 years.

***Charitable Deduction******Limitations: Corporations***. Although not discussed in Chapter 11 (except in footnote 114), the charitable contribution deduction for C corporations generally is limited to 10% of taxable income (see Chapter 19). If a corporation's charitable contributions for a year did exceed the 10% limitation, the excess was carried over and deducted for each of the five succeeding years on a FIFO basis. The CARES Act changes the limitation for C corporations to 25% of taxable income for 2020 only. See discussion in Chapter 19.

**CHAPTER 13: THE ALTERNATIVE MINIMUM TAX AND TAX CREDITS**

**Page 13-24**

**Overview of Tax Credits**

**Employee Retention Credit of $5,000 for Employers Closed Due to COVID-19**.

**Note:** At this writing, infrastructure bill known as the Infrastructure Investment and Jobs Act passed by the Senate on August 10, 2021,would end the employee retention credit (ERC) discussed below. Under the CARES Act, only wages paid through September 30, 2021, would be eligible for the credit (except for wages paid by an eligible recovery startup business).

To help employers and employees during the crisis, Congress created several tax credits. Among these is one for businesses and nonprofit organizations that were required to suspend or close its operations due to COVID-19, but that continue to pay its employees during the shut-down in hopes of retaining them. This so-called *employee retention credit* (ERC) and the PPP loans are key elements of the CARES relief package (see Act § 2301 Employee Retention Credit for Employers Subject to Closure Due to COVID-19).

As noted below, the credit reduces or eliminate the employer’s share of FICA taxes attributable to employee wages and other compensation (i.e., 6.2% of wages). In short, it reduces or eliminates the amount of FICA taxes that the employer must pay. However, ***the credit is not available* if the taxpayer has received a PPP loan** (generally a loan equal to 2.5 times the businesses’ average monthly payroll but not to exceed $10 million as discussed in Chapter 6 above). Consequently, the taxpayer must choose between one or the other. Interestingly, it is estimated that the credit will provide an aggregate benefit to businesses of about $54.6 billion**.**

*Eligible Employer.* An employer is eligible for the retention credit if it meets *either* of two tests:

(1) *COVID-19 Shutdown*. The employer’s operations were fully or partially suspended due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purpose) due to the virus or

(2) *Gross-Receipts-Decline (GRD)*. The employer’s gross receipts declined by more than 50% when compared to the same quarter in the prior year. Once an employer becomes an “eligible employer” on account of a “significant decline in gross receipts,” the employer remains an eligible employer for any succeeding calendar quarter until the employer’s gross receipts during that calendar quarter are 80% or more than the gross receipts in the comparable calendar quarter in the preceding year.

For tax exempt organizations, only the “fully or partially suspended operations” condition applies to receive the credit.

*Amount of Employee Retention Credit (ERC).* Eligible employers (e.g., those that shut down or have a significant decline in gross receipts) are allowed a refundable credit against its 6.2% cost of Social Security taxes (IRC § 3111(a)). Note that the credit reduces the amount of wages that can be deducted. The amount of the credit is equal to 5**0% of** ***qualified* *wages*** **up to $10,000 of wages** or a **maximum credit of $5,000 *per employee*** (50% x qualified wages of $10,000). The credit is computed based on qualified wages paid or incurred for each employee between March 13, 2020, and December 31, 2020. The fact that the employee may have been dismissed or furloughed is ignored. The amount of qualified wages taken into account for this purpose differs depending on whether the employer had more than 100 employees. ARPA codified the ERC in § 3134 and extended it through 2021. It also increased the credit from $5,000 to $28,000 in 2021.

*Qualified Wages: More than 100 Employees.* In computing qualified wages, special rules apply if the business had an average of more than 100 full-time employees during 2019. First, qualified wages include *only* the wages of employees “who are furloughed or face reduced hours as a result of their employers' closure or reduced gross receipts.” Second, wages are qualified only if they were paid by the employer during the quarter for the period the business was shut down and the employees were not working due to COVID-19. (Act § 2301)

*Qualified Wages: No More than 100 Employees.* If the business had no more than 100 employees (100 or less) for 2019, the credit is calculated on all qualified wages paid after March 12, 2020. Qualified wages include (1) wages paid to employees during a shut-down and (2) wages paid for each quarter that the business suffered a sharp decline in year-over-year receipts, as described above (see *gross receipts decline)*.

In computing the amount of qualified wages in both situations, qualified wages include any “qualified health plan expenses” allocable to the wages, such as amounts paid to maintain a group health plan. In either case, however, the amount of qualified wages for each employee for all quarters may not exceed $10,000.

The retention credit is subject to numerous rules to prevent double-dipping.

* An employer's deduction for wages must be reduced by the amount of any retention credit.
* An employer may not take into account the following wages:
  + Wages of an employee for whom a work opportunity tax credit is claimed.
  + Wages taken into account under § 45S (income tax credit for paid family and medical leave).
  + Wages taken into account under §§ 7001 and 7003 of the Families First Act, which provides payroll tax credits for paid leave required to be provided by small employers.
  + Wages paid to certain related individuals specified in § 51(i)(1)

The retention credit requires an analysis of how a business has been affected by COVID-19 and if the COVID-19 shutdown or the gross-receipts-decline (GRD) tests have been met. The shutdown test requires that a business has been fully or partially suspended due to government action. If the business does not meet the GRD test, it may be unclear whether a business’ operations has been partially suspended. The GRD test also presents unique challenges. For example, employers must analyze gross receipts across all aggregated entities rather than by location (a change from rules associated with prior employee retention credits related to natural disasters).

The CARES Act requires employers to make a choice: obtain a PPP loan that is potentially forgivable or take the retention credit. In making the choice, there are two aspects of retention credit that deserve special consideration. First, the retention credit may substantially reduce or eliminate the FICA tax. Second, any tax that is due can be postponed to 2021 and 2022 (recall discussion for page 1-22 of this supplement concerning when 2020 payroll taxes are due: 50% due on December 31, 2021, and the other half due on December 31, 2022).

**Example 16.**  Alan Smith, CPA, conducts CPE workshops. He is the sole owner and employee of his own S corporation. This year he had to “partially suspend operations” due to the government-imposed restrictions on group meetings for May and June, 2020. This year the corporation paid him $80,645.16 in wages. Note that the FICA taxes paid exactly equals maximum allowable credit of $5,000 (i.e., 6.2% x $80,645.16 salary = $5,000). The taxpayer must determine whether he should seek a PPP loan or claim the retention credit of $5,000.

The taxpayer computes his retention credit under the rule for businesses with no more than 100 employees. Therefore, qualified wages include not only those paid to employees during a shut-down, but also wages paid for each quarter that the business suffered a sharp decline in year-over-year receipts. In this case, the business was shut down, so the wages are qualified. Thus, the credit is $5,000 (50% x qualified wages up to $10,000 of wages per employee or $5,000). Here, the retention credit of $5,000 is exactly equal to the FICA tax that must be paid and, consequently, would eliminate the expense.

The tax savings increases the company’s profits by a corresponding $5,000. Assuming that the taxpayer is the sole owner and employee of this S corporation and faces a marginal tax rate of 20% for federal income taxes and 5% for state income taxes, this $5,000 of additional profit flowing through on the K-1 would result in an increase of after-tax income of $3,750 (i.e., $5,000 – [(20% + 5% = 25%) x $5,000 =$1,250 in applicable income taxes]).

The taxpayer must determine whether he should obtain a forgivable PPP loan or claim the credit that puts $3,750 in his pocket after tax. Recall that the PPP loan helps cover payroll costs (wages up to $100,000 per employee, employee benefits, and state and local taxes). Employers can also use some of the funds (25%) to cover interest on mortgages, rent, and utilities. If the taxpayer got a PPP loan and uses it to pay the wages, he would not be required to repay the loan. In this situation, it appears that the taxpayer would be better off by seeking a PPP loan.

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**New Markets Tax Credit**

The new markets credit can be claimed by both individual and corporate taxpayers. The credit equals 39% of a taxpayer’s capital investment in a qualified entity that commits to the rules of the new markets tax credit program. In turn, the recipient entity must loan or invest substantially all of the capital in qualified businesses that operate in low-income communities.

Before the CAA, a $5 billion allocation was made to the new markets tax credit program for 2020. The TCDTRA extends the new markets credit to cover allocations made for 2021–2025. The TCDTRA also extends the carryover period for taxpayers to utilize unclaimed new markets tax credits through 2030. (See § 45D, as amended by TCDTRA § 112.)

**Credit for Railroad Track Maintenance**

TCDTRA makes this credit permanent for tax years ending after the 12/27/20. However, the new law also reduces the credit rate from 50% to 40% for tax years beginning in 2023 and beyond. [See IRC § 45G]

**Credit for Mine Rescue Team Training**

TCDTRA extends this credit to cover eligible amounts paid or incurred in tax years beginning in 2021. [See IRC § 45N(e), as amended by TCDTRA § 136.]

**Credit for Energy-Efficient Manufactured Homes Extended**

Under § 45L(g), manufacturers of residential homes can claim a credit of $1,000 or $2,000 for homes that meet applicable energy-efficiency standards. The TCDTRA extends the credit to cover new homes that are acquired from manufacturers in 2021 for use as residences.

**Page 13-30 Work Opportunity Tax Credit**

Before the CAA, the work opportunity tax credit (WOTC) only applied to first-year wages paid to qualifying employees who were hired before 2021. The TCDTRA extends the WOTC to cover first-year wages paid to qualifying employees who are hired in 2021–2025.

**Page 13-32 Credit for Paid Family and Medical Leave**

**Credit for Paid Sick Leave.** See Chapter 7 on changes relating to page 7-9 of the text.

**Page 13-38 Empowerment Zone Employment Credit**

Special federal income tax incentives are available in census tracts designated as empowerment zones. In these zones, taxpayers are potentially eligible for 20% wage credits under § 1396, enhanced first-year depreciation deductions under § 1397A, tax-exempt bond financing under IRC § 1394, and deferral of federal capital gains tax under § 1397B when qualifying assets are sold and sales proceeds are reinvested in other qualifying assets. Before the CAA, 2021, empowerment zone designations were scheduled to expire on 12/31/20.

The TCDTRA extends through 2025 the period for which empowerment zone designations can remain in effect. However, the new law terminates (1) the § 1397A enhanced first-year depreciation rules for property placed in service in tax years beginning in 2021 and beyond and (2) the § 1397B capital gains tax deferral for sales that occur in tax years beginning in 2021 and beyond. (See TCDTRA Sec. 118.)

**Page 13-39 Alternative Fuel Vehicle Credits**

A credit can be claimed for vehicles propelled by chemically combining oxygen with hydrogen to create electricity. The base credit is $4,000 for vehicles weighing 8,500 pounds or less. Heavier vehicles can qualify for bigger credits of up to $40,000. An additional $1,000 to $4,000 credit is available to cars and light trucks to the extent their fuel economy meets federal standards. The TCDTRA extends this break to cover qualifying 2021 purchases. [See § 30B(k)(1), as amended by TCDTRA Sec. 142.]

**New Vehicles Added for Plug-in Vehicle Credit.** With the success of Tesla, it is apparent that many of the car manufacturing companies are getting into the battery powered vehicle game Although the recent legislation does not change the applicable rules, it is worth noting that the IRS has been busy adding new vehicles to the qualified list.

As discussed in the text, § 30(D) provides a credit to the purchaser of a qualified plug-in electric drive motor vehicle, including passenger vehicles and light trucks. The credit allowed is limited to $2,500 plus an additional amount, based on battery capacity, that cannot exceed $5,000. The credit phases out over six calendar quarters beginning when a manufacturer has sold at least 200,000 qualifying vehicles in the U.S.

Recently, the IRS added the following models to its list of vehicles eligible for the credit: the 2021 Mustang Mach-E GT, 2021 Hyundai Ioniq Plug-In Hybrid Electric Vehicle and Ioniq Electric Battery Vehicle, 2021 Porsche Cayenne E-Hybrid and E-Hybrid Coupe, Cayenne Turbo S E-Hybrid and E-Hybrid Coupe, Panamera 4 PHEV which includes the 4 E-Hybrid, 4 E-Hybrid Sport Turismo, 4 S E-Hybrid, 4 S E-Hybrid Sport Turismo, 4 E-Hybrid Executive, Turbo S E-Hybrid, and Turbo S E-Hybrid Sport Turismo. For a full list of vehicles, see [www.irs.gov/businesses/irc-30d-new-qualified-plug-in-electric-drive-motor-vehicle-credit](http://www.irs.gov/businesses/irc-30d-new-qualified-plug-in-electric-drive-motor-vehicle-credit) .

**Page 13-39 Alternative Fuel Vehicle Refueling Equipment Credit**

Under § 30C, a personal and business federal income tax credit can be claimed for up to 30% of the cost of installing non-hydrogen alternative fuel vehicle refueling equipment. The TCDTRA extends this break to cover qualifying 2021 purchases. [See IRC § 30B(k)(1), as amended by TCDTRA § 142]

**Page 13-43 Child and Dependent Care Credit**

ARPA makes several major, but temporary, changes to the child and dependent care credit (§ 21). As noted in the text, the child and dependent care credit helps working families fund the cost of childcare. Note, however, the changes by ARPA are effective only for 2021, including the temporary provision that makes the credit refundable (if the taxpayer lives in the U.S for more than half the year other than temporary absences due to illness, education, business, vacation, or military service).

Before ARPA, the child and dependent care credit was calculated as a percentage (20% - 35%) of qualifying care expenses. The expense amount was limited to $3,000 per qualifying individual, $6,000 for two or more qualifying individuals, resulting in a maximum credit of $1,050 (35% x $3,000), or $2,100 (35% x $6,000) for two or more.

For 2021, the credit is increased from 35% to 50% of eligible expenses. In addition, the amount of expenses taken into account is increased. Under prior law, up to $3,000 of expenses were considered for one qualifying individual (e.g., a child) and $6,000 of expenses for two or more. ARPA increases the limit. Under ARPA, for one qualifying individual the maximum is increased to $8,000 and $16,000 for two or more. Thus, the maximum credit for one qualifying individual for 2021 is $4,000 (50% x $8,000) and for two or more children is $8,000 (50% x $16,000). However, as explained below, the credit is reduced if the taxpayer’s AGI exceeds certain levels. Note also that taxpayer gets no additional benefit having more than two children!

Unlike the pre-ARPA credit that had no complete phaseout, the ARPA credit can phaseout to zero. The phaseout percentage begins at 50% but declines by 1 percentage point for every $2,000 (or fraction thereof) increase in AGI. Once AGI exceeds $183,000, the percentage settles at 20%. In other words, the rate remains at 20% for taxpayers with AGI between $183,000 and $400,000. The 20% rate falls again by 1 point for every $2,000 (or fraction thereof) by which AGI exceeds $400,000. Once AGI exceeds $438,000, the credit percentage becomes 0%, resulting in no dependent care credit.

|  |  |  |
| --- | --- | --- |
|  | Pre-ARPA (pre 2021 | ARPA: 2021 only |
| Qualifying expenses:  1 qualifying individual  2 or more | $3,000  $6,000 | $ 8,000  16,000 |
| Phaseout Level 1  AGI | Rate (35% - 20%)  35% potentially reduced to 20%  1% for each $2,000 AGI above $15,000 | Rate (50% - 0%)  50% potentially reduced to 20%  1% for each $2,000 above $125,000 - $183,001 |
| Phaseout Level 2  AGI | None | 1% for each $2,000 above $400,000;  0% if AGI exceeds $438,000 |
| Refundable | No | Fully refundable for taxpayer whose principal place of abode is in U.S. for half the tax year (either spouse for MFJ) |

Note that under ARPA, the credit is potentially refundable.

**Example 1**: H and W, married, pay $8,400 in qualified employment-related expenses in 2021 to care for their two children while they are working. The children are both qualifying individuals. The taxpayer is entitled to take the entire $8,400 into account in calculating the child and dependent care credit. For tax years other than 2021, the maximum amount of qualified employment-related expenses that this taxpayer could take into account for purposes of determining the credit would be $6,000.

**Example 2**: Assume the same facts as in Example 1 except that the taxpayers have an AGI of $132,000, which exceeds the $125,000 threshold in 2021 by $7,000. Their “applicable percentage” would be reduced by 4 percentage points ($7,000/$2,000 = 3.5 rounded up to 4%) and now only be 46% (i.e., instead of the normal 50%) resulting in a credit amount of $3,864 (i.e., $8,400 x 46%).

**Example 3**: In 2021, M and D are married filing jointly, have AGI of $300,000, and pay $7,000 in qualifying expenses for the care of their qualifying child. They are entitled to a credit of $1,400 (20% x $7,000).

**Example 4**: Same facts as in the previous example except their AGI is $412,500. Their credit amount would be $910. (13% x $7,000); [($412,500 - $400,000) / 2,000 = 6.25%, round up to 7%. 20% - 7% = 13%]. If their AGI had exceeded $438,000, the credit amount would have been $0. Like the 2021 child tax credit, the child and dependent care credit is fully refundable in

2021. But unlike the 2021 child tax credit, it is not subject to advance payment.

**Page 13-51 Lifetime Learning Credit** (2021 and Beyond)

The Consolidated Appropriations Act (CAA), passed on December 27, 2020, increased the maximum Lifetime Learning Credit amount. Beginning in 2021, the Lifetime Learning Credit is increased from $2,000 to $2,500. Since the credit percentage is 20% of qualified tuition and fees, this increases the maximum amount eligible for the credit from $10,000 to $12,500. The CAA also increased the modified AGI phaseout range from $59,000 - $69,000 (as shown in the text) to the new range of $80,000 - $90,000. For married filing jointly, the range is now $160,000 - $180,000, up from the previous $119,000- $139,000. This change makes the phaseout range for high income taxpayers the same as that of the American Opportunity Tax Credit.

**Page 13-56 Earned Income Credit**

ARPA makes several changes to the earned income tax credit, some permanent and some temporary.

**Rules for Taxpayers without Children.** The pre-ARPA requirement that a taxpayer without qualifying children must be over 24 but under 65 years old to claim the earned income credit (EIC) does not apply for 2021. Under ARPA, for 2021 only, the minimum age generally is reduced from 25 to 19 for taxpayers with no qualifying children (unless the taxpayer is a student as discussed below). In other words, the individual claiming the credit need only be 19 years old to obtain the credit, and there is no upper age limit. However, students (other than “qualified foster youths” or “qualified homeless youths”) must be at least 24 years old. Qualified foster youths and qualified homeless youths must be at least 18.

Under the original rules, the maximum tentative EIC for 2021 for a taxpayer with no qualifying children was scheduled to be only $543 ($7,100 × 7.65%). However, ARPA increases the earned income amount and phase-out percentages for people without children, increasing them from $7,100 to $9,820 and 15.3%. Thus, the maximum 2021 EITC is $1,502 ($9,820 × 15.3%). Additionally, the phase-out threshold has increased from an AGI of $8,880 (2020) to an AGI of $11,610 (2021) , completely phasing out the credit at $27,367. This is good news for individuals without kids, as some will see less of their EICs reduced by the phase-out rule.

To calculate the EIC for 2021, taxpayers can use either 2019 or 2021 earned income — whichever yields a larger credit.

**Increased Investment Income Threshold.** Under pre-ARPA law, a taxpayer who had “disqualified income” (certain types of investment income) over an inflation-adjusted amount for the year ($3,650 for 2021) could not claim the EITC. Under ARPA, the threshold amount for disqualified income is permanently increased to $10,000, effective for tax years beginning after 2020. The $10,000 amount will be adjusted for inflation after 2021.

The EIC’s phaseout percentage is increased to 15.3%, and the phaseout amounts are also increased. The EIC also would be allowed for certain separated spouses. Finally, for the time being, taxpayers would be allowed to use their 2019 income instead of 2021 income in figuring the credit amount.

Another permanent change involves married couples. Generally, couples must file jointly to be eligible for the credit. Beginning in 2021, a married taxpayer who lives with a qualifying child for more than half the year may claim the credit as long as (1) he or she does not have the same principal residence as his or her spouse for the last six months of the year, or (2) are under a separation instrument and do not live in the same household as the spouse at the end of the year. In addition, for 2021 and beyond, ARPA explicitly allows taxpayers who have a qualifying child but who cannot provide the child identification information (social security number) to claim the credit under the rules for someone with no qualifying children.

**Elimination of the child identification information requirements**. Under the original EIC rules, taxpayers could not claim the EIC based on a qualifying child unless he or she included the child’s name, age, and taxpayer identification number (Social Security number). For 2021 and thereafter, ARPA permanently removed that rule. So, if a taxpayer is an eligible individual but fails to provide child identification information, the taxpayer can still claim the EIC as a person with no qualifying children.

**CHAPTER 18: EMPLOYEE COMPENSATION AND RETIREMENT PLANS**

**Page 18-7**

**Additional Taxes on Premature or Excess Distributions**

**Penalty-Free Withdrawals for Birth and Adoption Expenses**. The SECURE Act provides that distributions for the birth or adoption of a child (up to $5,000) are penalty-free withdrawals (i.e., not subject to the 10% penalty tax on early withdrawals). It also permits the participant to repay the funds to the plan or IRA. This change is effective for distributions made after 2019 and applies to both IRA distributions and qualified retirement plan distributions.

**Page 18-8**

**Plan Loans**.

Many 401(k)s and other defined contribution plans allow participants to take out a plan loan of up to $50,000 or half of their own vested account balance. Normally, loans are then repaid over a five-year period through payroll deductions. The limit on loans made during the 180-day period beginning on the date the CARES Act is enacted is increased to the lesser of $100,000 or 100% of the participant’s account balance (which doubles the current limit of the lesser of  $50,000 and 50% of the participant’s account balance).  In addition, an individual with an outstanding loan may delay paying off the loan generally for one year. The remaining payments plus interest are re-amortized over the extended period.

**Example 17.** A taxpayer withdraws funds from her IRA or 401(k) plan during 2020 due to being infected by the virus. Not planning to replace these distributed funds back into her IRA or 401(k) plan, she must pay the associated income tax (but, no 10% penalty). She can pay the entire tax when filing her 2020 tax return. Or, instead, she can choose to pay this tax in equal installments in her 2020, 2021 and 2022 returns (presumably, with no interest). What she cannot do is wait to pay the entire tax due (or, one-half each), for example, when she files her 2021 or 2022 tax returns.

**Page 18-21**

**Traditional IRA**

In late 2019, Congress reviewed the rules governing retirement plans and made several changes, hoping to help workers better save for their future. The new law, Setting Every Community Up For Retirement Enhancement Act (the SECURE Act) made a number of changes and are included in the discussion below. Additional changes were made by the CARES Act.

**Deductible Contributions to a Traditional IRA (SECURE Act)**

**Compensation for IRA Purposes: Certain Taxable Tuition**. The contribution to an IRA is normally $6,000 for 2020. However, the deduction cannot exceed the individual’s compensation. The SECURE Act expands the definition of compensation to include certain taxable nontuition fellowship and stipend payments effective 1/1/20.

**Repeal of Maximum Age for IRA Contributions**. The SECURE Act repeals the maximum age limit for traditional IRA *contributions*. Effective for contributions made to a traditional IRA after 12/31/19, there is no maximum age. In prior years, the age limit for contributions to a traditional IRA was age 70½.

**Page 18-25**

**Distribution Requirements**

**Waiver of Required Minimum Distribution Rules.** The start date for any required minimum distribution (RMD) is changed from age 70½ to age 72. This change is effective for any IRA owner who turns 70½ in or after 2020. This will enable individuals to defer distributions (and the taxes due) until age 72. The change applies to both IRA distributions and qualified retirement plan distributions. However, as noted below, the CARES Act suspended the RMD for 2020.

**Limitation on Non-Spouse Stretch IRAs**. When an individual with an IRA or similar retirement plan dies, such plans (and the amounts they contain) pass to one or more beneficiaries identified in the plan document. Prior to the SECURE Act, beneficiaries may have started receiving distributions. In such case, the required minimum distribution (RMD) would be determined by using the beneficiary’s life expectancy. For example, assume that Violet, age 92, died this year with a $100,000 in her IRA. At the time that Violet died, her life expectancy (according to the IRS tables) was about 10 years. In such case, her RMD had she lived would have been about $10,000 per year. However, she named her granddaughter, Jennifer, age 23, as the beneficiary Jennifer had a life expectancy at the time of Violet’s death of about 60 years. Upon Violet’s death, the RMD calculation uses the beneficiary’s (Jennifer) life expectancy of 60 years, in which case, the RMD would drop from about $10,000 per year to about $1,667 per year. In effect, this approach stretches the payout period and postpones the taxes such that the present value is nominal. Moreover, the IRA is growing every year. Obviously, for many, using the so-called stretch IRA has been a valuable tax planning idea.

The SECURE Act changes the "stretch period" applicable for inherited IRAs (other than those inherited by a spouse), from a lifetime distribution period to a 10-year maximum distribution period. There are exceptions to the 10-year maximum distribution period, including distributions to disabled or chronically ill beneficiaries, a beneficiary who is a surviving spouse, and a beneficiary who is no more than 10 years younger than the deceased participant or IRA owner. This change is effective for distributions with respect to participants/IRA owners who die after 12/31/19 and applies to both IRA distributions and qualified retirement plan distributions.

**Wavier of 10% Penalty for Early Withdrawal of Retirement Funds Due to Coronavirus.** As discussed earlier in the text (page 18-7), taxpayers normally must pay a 10% penalty on distributions before age 59 ½. However, there are several exceptions, and the CARES Act adds another. The SECURE Act waives the additional 10% penalty on early distributions of up to $100,000 from IRAs and defined contribution plans (such as 401(k) and 457(b) plans and SEPs) during 2020 but only if the distribution was needed due to the coronavirus—a so-called coronavirus-related distribution. It should be emphasized that distribution must be directly related to COVID-19. While the penalty is waived, an early distribution is fully taxable.

A “coronavirus-related distribution,” (CVD distributions) as defined under the CARES Act, is any distribution from an eligible retirement plan made: (i) on or after January 1, 2020 and before December 31, 2020, (ii) to an individual (a) who is diagnosed with COVID-19, (b) whose spouse or dependent is diagnosed with COVID-19, or (c) who experiences adverse financial consequences as a result of being quarantined, furloughed, laid off, had hours reduced, or other factors as determined by the Secretary of the Treasury during the COVID-19 pandemic. For example, the rule would apply if an individual was unable to work because of lack of childcare due to COVID-19 and experienced adverse financial consequences as a result. In addition, Notice 2020-50 expanded the list of individuals who were eligible to receive CVDs.

There are no restrictions on the use of CVD funds. For example, taxpayers could use the money to pay bills or help their adult children. Once their financial situation improves, they can recontribute the funds within the three-year window. Alternatively, they can keep the CVD money and pay the resulting tax, which may be modest for some individuals. As a results, CVDs can be a useful cash tool for clients who are experiencing a cash crunch in the COVID-19 era. In any event, they avoid the 10% early distributions penalty that applies to IRA distributions taken before age 59 ½.

Coronavirus-related distributions are limited to $100,000 and are included in income ratably over a three-year period beginning with the taxable year in which the distribution is made unless the individual elects to include it in income earlier (or makes a tax-free repayment of the distribution).

**Recontributions.** An individual may recontribute the amount withdrawn to the plan or IRA within three years of taking the distribution and such repayment will be treated as a tax-free rollover. It should be emphasized that “coronavirus-related distributions” are taxable, despite not being subject to the 10% early withdrawal penalty. But if a distributee wants to avoid the current taxation of such distributions he or she will need to pay back these amounts in a timely manner, specifically within the above-mentioned 3-year period. This is similar to the “60- day rollover rule” except the taxpayer instead has three years to recontribute the funds in order to avoid taxation of these distributions.

**Example 15**. V, suffering from the virus decides to withdraw funds from his IRA and 401(k) plan during 2020. The withdrawals are exempt from the 10% early withdrawal penalty. However, he must pay income tax on the distribution when filing his 2020 tax return. However, in 2023 (i.e., within three years of the original distribution date) he is able to recontribute an amount equal to the previously distributed amount back into his IRA or 401(k) plan. It appears that he could then file an amended tax return for the 2020 tax year and claim a refund (plus interest) allocable to the tax originally paid with regard to this “coronavirus-related distribution.”

**CHAPTER 19: TAXATION OF BUSINESS FORMS AND THEIR OWNER**

**Page 19-4**

**Introduction**

**Overview of Changes**. Most of the legislative changes discussed in this supplement relating to an individual’s *business activities* are applicable to *all* businesses, including sole proprietorship, partnerships and both C and S corporations. The changes are summarized briefly below.

***Economic Impact Payments for Individuals.*** The new stimulus payments (see revisions in this update for Chapter 4, page 9 of this supplement) are reserved solely for individuals. The legislation did not provide any similar stimulus device for businesses.

***Paycheck Protection Program (PPP Loans)*.** This program is available to all businesses. Normally, only small businesses (no more than 500 employees) can obtain a PPP loan. See revisions in this update for Chapter 6, page 6-50.

***Sick Pay Requirements***. The legislation requiring businesses to provide sick pay as well as family and medical leave generally applies to all businesses. However, the requirements do not apply to small businesses (fewer than 50 employee if payments would jeopardize the viability of the business). Nor do they apply to large businesses with more than 500 employees. For those corporations required to provide sick pay, they are eligible for the credits that reduce their payroll taxes. See revisions in this update for Chapter 7.

***Payroll Tax Deferral*.** Employers can defer payment of the employer portion of payroll taxes on wages paid through December 31, 2020.

***Employee Benefits*.** Businesses can take advantage of some of the changes to provide benefits to their employees (e.g., tax-free payments of student loans as well as those for disaster relief).

***Leasehold Improvements Qualify for Bonus Depreciation***. See discussion on this topic in this update for Chapter 9, page 9-22.

***Limitation on Deduction of Interest of Businesses*.** See discussion on this topic in this update for Chapter 11, page 11-28.

***Net Operating Losses*.** See discussion on this topic in the update for Chapter 10, page 10-14.

**Pages 19-18 and 19-19**

**Minimum AMT Credit.** As noted in the text, the Tax Cuts and Jobs Act of 2017 eliminated the alternative minimum tax for C corporations, starting in 2018. Although not discussed in this chapter, upon repeal of the AMT, C corporations were allowed to utilize any unused minimum tax credits for the AMT to reduce their tax liability over a four-year stretch through 2021. The CARES Act goes one step further, letting companies immediately claim a refund of any unused AMT credits on their return for either 2018 or 2019, rather than having to wait.

**Employee Retention Credit.** See discussion in the update for Chapter 13, page 13-25.

**Page 19-36**.

**Charitable Contributions of Corporations.** See update for Chapter 11, page 11-41 and below.

**Contributions of Ordinary Income Property by Corporations.** See discussion of contributions on food inventory in the update for Chapter 11, page 11-41.

**Corporations: Charitable Deduction Increased to 25% for Cash Contributions.** Previously, a corporation's charitable deduction was *not* permitted to exceed 10% of its taxable income, as computed with certain modifications (§ 170(b)(2)(A)). If a corporation's charitable contributions for a year did exceed the 10% limitation, the excess was carried over and deducted over each of the *five* succeeding years on a FIFO basis, to the extent the sum of carryovers and contributions for each of those years did *not* exceed 10% of taxable income.The CARES Act temporarily modifies §170(b)(2)(A) to increase a corporation’s limitation on a deduction for its aggregate amount of cash contributions made during 2020 from 10% to 25% of the corporation’s taxable income.

**Page 19-37**

**Net Operating Losse**s **of C Corporations**. See discussion on this topic in the update for Chapter 10, page 10-14

**Corporate Alterative Minimum Tax.** As noted in the text, the Tax Cuts and Jobs Act of 2017 eliminated the alternative minimum tax for C corporations, starting in 2018. Although not discussed in this chapter, upon repeal of the AMT, corporations were allowed to utilize any unused minimum tax credits for the AMT to reduce their tax liability over a four-year stretch through 2021. The CARES Act goes one step further, letting companies immediately claim a refund of any unused AMT credits on their return for either 2018 or 2019, rather than having to wait.

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