

Coronavirus: President Trump Signs Consolidated Appropriations Act, 2021; Summary of the Tax Provisions

Tax Talks Blog on **December 29, 2020**

On December 27, 2020, President Trump signed into law the [Consolidated Appropriations Act, 2021 \(the “Act”\)](#). The Act enhances and expands certain provisions of the [Coronavirus Aid, Relief, and Economic Security Act \(the “CARES Act”\) \(H.R. 748\)](#). This blog post summarizes the tax provisions of the Act.

Expenses Related to PPP Loan Forgiveness Are Deductible. The CARES Act included a loan forgiveness program under the Small Business Administration’s Paycheck Protection Program (the “PPP”). A PPP loan may be forgiven if its proceeds are used for “payroll costs” or certain other expenses. Under the CARES Act, the forgiveness of a PPP loan does not give rise to taxable cancellation of indebted income, or a loss of tax attributes. However, the IRS held that expenses that gave rise to PPP loan forgiveness were not deductible.^[1] The Act reverses this rule and permits taxpayers whose PPP loans are forgiven to deduct the expenses relating to their loans to the extent they would otherwise qualify as ordinary and necessary business expenses.^[2] This rule applies retroactively to the effective date of the CARES Act so that expenses paid using funds from PPP loans previously issued under the CARES Act are deductible, regardless of when the loan was forgiven.

Changes to the Employee Retention Tax Credit. The CARES Act provided an eligible employer with a refundable payroll tax credit equal to 50% of certain “qualified wages” (including certain health plan expenses) paid to its employees beginning March 13, 2020 through December 31, 2020 if the employer is engaged in a trade or business in 2020 and the wages are paid (i) while operation of that trade or business is fully or partially suspended due to a governmental order related to COVID-19 (the “suspension test”) or (ii) during the period beginning in the first quarter in which gross receipts for that trade or business are less than 50% of gross receipts for the same calendar quarter of 2019 and ending at the end of the first subsequent quarter in which gross receipts are more than 80% for the same calendar quarter of 2019 (the “gross receipts test”). The employee retention tax credit can be used to offset all federal payroll taxes, including federal withholding tax, and the employer’s and employee’s share of social security tax and Medicare, but not the federal unemployment tax (“FUTA”).

The Act makes several changes to the employee retention tax credit. The changes are effective for calendar quarters beginning after December 31, 2020 except as otherwise indicated below. This chart summarizes the changes; they are explained further below.

	CARES Act	Consolidated
<i>Limitations on credit</i>	50% of qualified wages; \$5,000 annual cap	70% of qualified wages; \$28,000 annual cap
<i>Eligibility of PPP borrowers</i>	Not eligible	Eligible (provided that the wages are not used to pay principal or interest on the loan)
<i>Large employer threshold for additional limitations</i>	100 full-time employees	500 full-time employees
<i>Governmental organizations</i>	Not eligible	Certain governmental organizations are eligible
<i>Availability</i>	Through December 31, 2020	Through December 31, 2021

* Applies retroactively to effective date of CARES Act

Credit increased to 70% of qualified wages; cap on credit increased to

\$28,000. The CARES Act provided for a refundable payroll tax credit of 50% of certain “qualified wages”, capped at \$5,000/employee (50% of up to \$10,000 of qualified wages for all calendar quarters). The Act increases the credit cap from \$5,000 for the year to \$7,000 (70% of \$10,000) for any calendar quarter.^[3] Accordingly, the Act will increase the maximum amount of credit available in 2021 for each employee from \$5,000 to \$28,000.

PPP borrowers may receive the tax credit. The CARES Act denied the employee retention tax credit to any employer that receives a loan under PPP, and defined the term “employer” expansively, potentially causing acquiring corporations with employee retention tax credits to lose or recapture those tax credits if they acquired a target company that had received a PPP loan.[\[4\]](#) The Act permits an employer that receives a PPP loan to receive the employee retention tax credit. However, to prevent any double-dipping, an employer must either exclude “qualified wages” that allowed the employer to claim employee retention tax credits from “payroll costs” for purposes of determining its loan forgiveness under the PPP (so as to reduce the amount of loan forgiveness), or exclude “payroll costs” that qualified for PPP loan forgiveness from “qualified wages” (so as to reduce the employee retention tax credit).[\[5\]](#) This change applies retroactively to the effective date of the CARES Act.[\[6\]](#)

Helpful changes to the gross receipts test. Under the CARES Act, an employer qualified for the employee retention tax credit under the gross receipts test for the period beginning with the first calendar quarter for which gross receipts for the employer’s trade or business were less than 50% of gross receipts for the same calendar quarter of 2019 and ending at the end of the first subsequent quarter in which gross receipts were more than 80% for the same calendar quarter of 2019. Under the Act, in 2021, an employer qualifies for the period beginning in a calendar quarter in which the employer’s gross receipts are **less than 80%** (instead of 50%) of gross receipts for the same calendar quarter of 2019 and ending at the end of the first subsequent quarter in which gross receipts are more than 80% for the same calendar quarter of 2019.[\[7\]](#) Furthermore, employers may elect to apply the gross receipts test based on gross receipts from the prior calendar quarter to determine their eligibility for the credit.[\[8\]](#) The Act also makes the credit available in 2021 to employers that were not in existence in 2019 by permitting them to apply the gross receipts test based on 2020 gross receipts.[\[9\]](#)

Large employer threshold. For an employer with more than 100 full-time employees, the CARES Act imposed an additional restriction: the employee retention tax credit is available only with respect to wages paid to an employee who is not providing services due to circumstances described in (i) the suspension test or (ii) the gross receipts test. The Act increases the threshold for this rule in 2021 to 500 full-time employees (so that employers with between 101 and 500 full-time employees would no longer be subject to this restriction).[\[10\]](#)

Tax-exempt organizations and governmental entities. The Act provides that, for purposes of the employee retention tax credit, the term “gross receipts” of a section 501(c) tax-exempt organization means the amounts the organization receives during its annual accounting period from all sources without subtracting any costs or expenses.[\[11\]](#) This change applies retroactively to the effective date of the CARES Act.[\[12\]](#)

Under the CARES Act, federal, state or local government (and their agencies) were not eligible for the credit. The Act permits federal credit unions, public colleges and universities, and public medical and healthcare providers to receive the employee retention tax credit if they otherwise satisfy the requirements for the credit.[\[13\]](#) For purposes of determining eligibility, public colleges and universities, and public medical and healthcare providers are treated as being engaged in a trade or business.

Health plan expenses. The Act includes health plan expenses in the definition of “qualified wages” for purposes of the employee retention tax credit, including in cases where an employer furloughs employees but continues to provide health benefits to them.[\[14\]](#) This change applies retroactively to the effective date of the CARES Act.[\[15\]](#)

Credit available through July 1, 2021. The Act extends the availability of the employee retention tax credit through July 1, 2021.[\[16\]](#)

Recovery Rebates. The Act provides for a second round of recovery rebates[\[17\]](#) that are available as direct payments to individuals.[\[18\]](#) However, the rebate is reduced from \$1,200 to \$600 per individual. Additional rebates are available for qualifying children (but not adult dependents), and there is no cap on household size. As with the first round of rebates, eligibility is based on 2019 adjusted gross income, and the rebate begins to phase out at \$75,000 for individual filers, \$112,500 for heads of households, and \$150,000 for joint filers with a complete phase out at \$87,000 for individual filers (with no qualifying children) and \$174,000 for joint filers (with no qualifying children).

Extension of Paid Sick and Family Leave Tax Credits. The [Families First Coronavirus Response Act \(H.R. 6201\) \(the “FFCRA”\)](#) provides an “eligible employer”^[19] with refundable payroll tax credits to cover wages paid to employees while they take time off under new paid sick and family leave programs between April 1, 2020 and December 31, 2020.^[20] The Act extends the paid sick and family leave tax credits through March 31, 2021 on a voluntary basis. Employers are not required to provide FFCRA leave between January 1, 2021 and March 31, 2021, but if they do so, they are eligible for the tax credits for wages paid with respect to the leave.^[21]

Temporary 100% Deduction for Business Meals. The Tax Cuts and Jobs Act of 2017 (the “TCJA”) limited the deductibility of business meal expenses to 50% of the cost for food and beverages provided by a restaurant. The Act permits businesses to deduct 100% of these business meals expenses during 2021 and 2022.

Increased Above-the-Line Charitable Contribution Deduction. The Act allows taxpayers that do not itemize deductions to take an “above-the-line” deduction for charitable contributions of up to \$300 (\$600 for joint filers) made to certain section 501(c)(3) public charities.^[22] The Act also provides that taxpayers that overstate the deduction will be subject to increased penalties (from 20% to 50%).^[23]

Corrected 30-Year Cost Recovery Period for Residential Rental Property. A “real property trade or business” may elect out of the limitation on the deductibility of business interest imposed by section 163(j) of the Code that was enacted as part of the TCJA.^[24] If a real property trade or business makes this election, it is required to use the longer cost recovery periods under the alternative depreciation system (“ADS”). When the TCJA was enacted, the ADS cost recovery period for residential rental property was reduced from 40 to 30 years. However, due to a drafting error, this reduction in the cost recovery period for residential rental properties applied only to buildings placed into service or acquired in 2018 or later with the result that a real property trade or business with a residential rental property at the end of 2017 that elected out of the limitation on the deductibility of business interest would be required to use the 40-year cost recovery period. The Act retroactively corrects the error so that the 30-year cost recovery period is available for all residential rental property regardless of when it was placed into service.^[25]

Extension of Look Through Rule for Related Controlled Foreign Corporations

(“CFCs”)[\[26\]](#). Section 954(c)(6) of the Internal Revenue Code (the “Code”) provides that dividends, interest, rents, and royalties received or accrued by a CFC from a related CFC will not be treated as “foreign personal holding company income” currently includible in the income of a United States shareholder[\[27\]](#) under the subpart F regime so long as the source of such payment is not itself subpart F income or income that is effectively connected with a U.S. trade or business. This rule was scheduled to sunset on December 31, 2020, but the Act extends its application to taxable years of CFCs beginning before January 1, 2026 and to taxable years of United States shareholders with or within which such taxable years of CFCs end.

Deferral of Employee-Side Payroll Tax. On August 8, 2020, President Trump issued a [memorandum](#) permitting employers to defer payment of the employee portion of certain payroll taxes (i.e., Old-Age, Survivors, and Disability Insurance tax under Section 3101(a) and Railroad Retirement Act Tier 1 tax under Section 3201(a)) for any employee with pre-tax wages or compensation during any biweekly pay period that were less than \$4,000 during the period between September 1, 2020 and December 31, 2020. The memorandum required the employers to withhold and pay the deferred payroll taxes from wages or compensation paid between January 1, 2021 and April 30, 2021. The Act extends the repayment period to December 31, 2021.[\[28\]](#)

[\[1\]](#) Notice 2020-32.

[\[2\]](#) Section 276.

[\[3\]](#) Section 207(b)-(c).

[\[4\]](#) The IRS previously posted [FAQs](#) providing that an acquisition of the stock or assets of a company that received a PPP loan generally would not cause the acquirer to jeopardize its employee retention tax credits, but this guidance could not be relied upon by taxpayers. For more on this issue, please see our [blog post](#) on the IRS FAQs.

[\[5\]](#) Sections 206(c).

[\[6\]](#) Section 206(g).

[\[7\]](#) Section 207(d)(1).

[\[8\]](#) Section 207(d)(2).

[\[9\]](#) Section 207(d)(1).

[\[10\]](#) Section 207.

[\[11\]](#) Section 206(a).

[\[12\]](#) Section 206(g).

[\[13\]](#) Section 206(d).

[\[14\]](#) Section 206(b).

[\[15\]](#) Section 206(g).

[\[16\]](#) Section 207(a).

[\[17\]](#) For more information on the first round of recovery rebates under the CARES Act, please see our [blog post](#) on the CARES Act.

[\[18\]](#) Section 272.

[\[19\]](#) Eligible employer generally means a private employer or nonprofit organization with fewer than 500 employees that is required to provide paid sick and family leave under the new paid leave programs established by the FFCRA under the Emergency Paid Sick Leave Act and the Emergency Family and Medical Leave Expansion Act.

[\[20\]](#) For more information about these tax credits, please see our [blog post](#) on the FFCRA.

[\[21\]](#) Section 286.

[\[22\]](#) Section 212(a).

[\[23\]](#) Section 212(b).

[\[24\]](#) Section 163(j)(7). A real property trade or business includes any real property development, redevelopment, construction, reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage trade or business. Section 469(c)(7)(C) of the Code.

[\[25\]](#) Section 202.

[\[26\]](#) A foreign corporation is a CFC if more than 50% of the total combined voting power of all classes of stock entitled to vote or the total value of the stock of the corporation is owned directly, indirectly, or constructively by “United States shareholders” on any day during the taxable year of the foreign corporation. Section 957(a) of the Code.

[\[27\]](#) A United States shareholder is a U.S. person that owns 10% or more of the total combined voting power or value of a CFC. Section 951(b) of the Code.

[\[28\]](#) Section 274.

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