Wolters Kluwer

Tax Briefing

American Rescue Plan Act of 2021

February 27, 2021

Highlights

- $1.9 Trillion Bill Includes Aid for Schools, State and Local Governments
- $1,400 "Recovery Rebate" Provided for Most American Adults and Their Children
- Extension and Modification of Popular Payroll Tax Credits
- Use of Reconciliation Process to Assure Passage in Senate Limits Contents of Bill

Inside

SPECIAL REPORT

House Passes $1.9 Trillion Stimulus Bill to Aid Recovery From COVID-19 Pandemic

Early on February 27, 2021, the House of Representatives approved the American Rescue Plan Act of 2021. The bill passed by the slimmest of margins, 219 to 212, almost entirely along party lines. The legislative package now moves on to the Senate, where an even slimmer margin is expected to approve the bill and send it to President Joe Biden's desk for signing. Legislators have announced a goal of passing the bill by March 14, when many relief provisions expire after their extension by the Consolidated Appropriations Act, 2021 in late December, 2020.

In order to secure approval in the evenly divided Senate, the bill is being passed under budget reconciliation rules which will require only a simple majority for approval in the upper chamber. With Vice President Kamala Harris providing a tiebreaking vote, the bill can afford no Democratic defectors. Also, in order to use the reconciliation process, the contents of the bill must adhere to specific rules, and must be approved by the Senate Parliamentarian. Before the House could even vote on the package, the Parliamentarian has already announced that the bill's $15 minimum wage provision does not meet the rules.

COMMENT. *In response to the decision of the Parliamentarian, Sen. Ron Wyden (D-Ore.), Chairman of the Senate Finance Committee, has proposed an amendment that would impose a five percent tax penalty on large corporations paying employees an hourly wage less than a specified amount. Wyden believes that the provision would satisfy the reconciliation rules. The details of the proposal were not available at the time of publication.*

The bill largely aligns with the framework put forth by President Biden before his inauguration on January 20. It includes extensions of enhanced unemployment relief, increased funding for COVID-19 testing and vaccination programs, aid to state and local governments, and assistance to schools to help get students back into classrooms.

The bill also includes a number of tax provisions, including a third round of direct stimulus payments, enhancements of many personal credits meant to benefit people with lower incomes and children, extensions of highly popular payroll tax credits for employers first instituted at the beginning of the pandemic, and changes related to retirement plan funding.

INDIVIDUAL TAX RELIEF

Recovery Rebates

The bill includes a third round of direct stimulus payments for taxpayers. The Coronavirus Aid, Relief, and Economic Security (CARES) Act signed into law in March, 2020 included the first round, with $1,200 for individuals and $500 for qualifying children. In December, 2020, the Consolidated Appropriations Act, 2021, provided an additional $600 stimulus payment, for taxpayers and children. At the time of the second payment, many lawmakers, as well as former President Trump and then President-Elect Biden, stated that the amount should be increased to $2,000.

> *"The bill largely aligns with the framework put forth by President Biden before his inauguration on January 20."*

The American Rescue Plan Act of 2021 provides a $1,400 stimulus payment. The payments are essentially credits against 2021 taxes, but fully refundable and payable in advance (similar to the prior payments). Also like previous stimulus payments, this third round is subject to income limitations. The amount of the payment phases out ratably for single filers with adjusted gross income over $75,000 ($112,750 for heads of households and $150,000 for joint filers). The stimulus amount phases down to $0 for single filers with $100,000 of adjusted gross income ($150,000 for heads of households and $200,000 for joint filers). Adjusted gross income amounts for the 2020 tax year are used in applying the phaseout, but 2019 amounts will be used in lieu of 2020 amounts for taxpayers who have not yet filed 2020 returns.

As was the case with the last two stimulus payments, amounts to which taxpayers would have been entitled but did not receive will be creditable when preparing 2021 tax returns in 2022. Also, amounts received based on 2019 or 2020 returns that would have been lower when 2021 returns are prepared do not have to be repaid.

COMMENT. *If the bill stays on track to become law by March 14, taxpayers who have an increase in adjusted gross income in 2020 as compared to 2019 may want to hold off filing 2020 returns until the filing deadline. This will maximize the amount of stimulus payments received because their stimulus payment will not be potentially reduced by the higher 2020 adjusted gross income.*

The $1,400 is available for all persons for whom a Social Security Number is associated, and is $1,400 for taxpayers, children, and non-child dependents. The Treasury and IRS are granted authority to provide payments to nonfilers based on available information.

Child Tax Credit

The bill includes a significant overhaul of the child tax credit, but only for the 2021 tax year. Under current law, the amount of the child tax credit is equal to $2,000 per child, but only $1,000 of that amount is refundable (meaning that the taxpayer receives the credit even if there is an insufficient amount of taxes to be credited against). The bill increases the amount to $3,000 per child (or $3,600 for a child under the age of six) and makes the credit amount fully refundable. The bill also increases the maximum age of qualifying children to include 17-year old children.

The excess of the amount of the credit over the present-law $2,000 amount is phased out by $50 for every $1,000 of modified adjusted gross income in excess of the threshold amount ($150,000 for joint filers, $112,500 for head of household filers, and $75,000 for single filers). Once the excess amount is eliminated, the amount of the credit remains at $2,000 until the present law phaseout thresholds are reached ($400,000 for joint filers, $200,000 for all other filers).

The Treasury and IRS are directed by the bill to issue advance payments of half of the credit amount beginning on July 1, 2021. The advance payments are to be issued monthly, if feasible, or as frequently as possible if monthly payments are not feasible. The remaining half of the credit not paid in advance is received when filing 2021 returns, as the full amount is claimed on the return but reduced by the aggregate amount received in advance.

In the case of a taxpayer who received advance payments in error (for example, where a 2019 or 2020 return indicated a dependent child who is no longer a dependent in 2021), the bill provides a "hold-harmless" provision, protecting taxpayers from having to pay back overpayments of up to $2,000 per child. The full $2,000 amount is ratably reduced for taxpayers with income above a threshold amount ($40,000 for single filers, $50,000 for head of household filers, and $60,000 for joint filers). The $2,000 is completely eliminated for taxpayers with income double the applicable threshold amounts, and the entirety of the overpayment must be paid back.

The IRS and Treasury are directed to create a website for taxpayers to opt out of receiving advance payments, or to provide information on status changes that would impact the amount of the credit.

Earned Income Tax Credit

The bill includes several enhancements to the earned income tax credit (EITC). Under the bill, for 2021 only, the amount of the credit is significantly increased for filers without children. The changes cause the childless EITC amount for 2021 to increase from $543 to $1,502, increase the amount of income at which the credit is maximized to $9,820 (currently set at $7,100) and increase the threshold for the phaseout of the credit for non-joint filers to $11,610 (currently set at $8,880). The minimum age for childless claimants of the EITC is also reduced from 25 to 19 (except in the case of full-time students).

The bill also allows taxpayers to substitute 2019 earned income for 2021 earned income in claiming the EITC on 2021 returns if 2021 earned income was less than 2019 earned income.

COMMENT. *A similar provision was included in the Consolidated Appropriations Act, 2021, applicable to 2020 claims of the EITC.*

Other changes to the EITC are made permanent. This includes the elimination of the prohibition against filers claiming the childless EITC solely because they are unable to claim the EITC for filers with children due to the lack of identification requirements. Additionally, a married but separated individual can claim the EITC as an unmarried person as long as certain requirements relating to children are satisfied. Finally, the amount of disqualifying investment income for purposes of the EITC is increased to $10,000, adjusted for inflation after 2021. The current amount of disqualifying investment income is $3,650 for 2021.

Dependent Care Assistance

The amount of the child and dependent care credit is significantly enhanced under the bill for 2021 only. Under current law, the amount of the credit is equal to 35 percent of qualified expenses for care of a qualifying individual up to $3,000 for one qualifying individual or $6,000 for two or more qualifying individuals. However, the credit percentage is reduced by one point for every $2,000 of adjusted gross income in excess of $15,000, until reaching 20 percent, at which point it is no longer reduced.

The bill increases the credit to 50 percent of qualified expenses, and reduces the credit percentage by one point for each $2,000 of adjusted gross income in excess of $125,000. The credit percentage is then not further reduced below 20 percent until adjusted gross income reaches $400,000, at which point the reduction of credit percentage continues until reaching zero. Additionally, the amount of eligible expenses qualifying for the credit are increased to $8,000 for one individual and $16,000 for two or more individuals. Finally, the credit is made fully refundable.

In addition to the changes to the credit, the maximum exclusion of employer-provided dependent care assistance is also increased for 2021 to $10,500, or $5,000 in the case of a married taxpayer filing separately. These amounts are double the maximum exclusion under current law.

COMMENT. *These changes are applicable to 2021 only.*

EMPLOYER TAX RELIEF

Paid Sick and Family Leave Credits

One of the first relief measures provided by Congress in the early days of the pandemic was the payroll tax credit for employers providing paid sick and family leave, as well as a similar credit for self-employed workers. The period for which the credit could be claimed was originally set to expire on December 31, 2020, but was extended to March 31, 2021. The bill extends the applicable period to September 30, 2021. The bill also increases the limit on applicable wages for which the credit can be claimed to $12,000 from $10,000, effective after March 31, 2021.

The leave for which a credit can be claimed is also expanded by the bill to include time off to receive a COVID-19 vaccine, or to recover from a vaccine-related illness or injury. The bill will also make the credit applicable to the hospital insurance (HI) tax, and not just the old-age, survivors, and disability insurance (OASDI) taxes, effective March 31, 2021.

The bill would also reset the ten-day per employee limitation on claiming the credit. The original bill limited employers to claiming the credit for a total of ten days' leave for an employee, and that ten-day period applies from the original start date through March 31, 2021. Under the bill, effective after March 31, 2021, a new ten-day period is available.

For self-employed persons looking to claim the credit, the number of days for which the credit can be claimed is increased to 60 days (from 50 days) under the bill, retroactively effective after December 31, 2020.

Employee Retention Tax Credit

Another highly popular provision of the original COVID-19 relief legislation is the payroll credit for employee retention. The credit was extended through June 30, 2021 by the Consolidated Appropriations Act, 2021. The bill extends the credit through the end of 2021, and, like the paid sick and family leave credit, makes it available to apply to HI taxes in addition to OASDI taxes after June 30, 2021.

RETIREMENT PLAN FUNDING

The bill includes several changes meant to help employers meet funding obligations for pension plans. For multiemployer plans, the bill provides delays in having to apply changes to funding plans or schedules, as well as providing extended improvement and rehabilitation periods for plans that entered critical or endangered status in 2020 or 2021. The bill also provides a longer investment loss amortization period for multiemployer plans, effective for plan years ending on or after February 29, 2020.

For single-employer plans, the bill provides a longer period for amortizing funding shortfalls, effective for plan years beginning after December 31, 2019. Under the bill, the amortization period is extended to 15 years, from the current seven years. The bill also provides for an extension of funding stabilization measures for single employer plans, also effective for plan years beginning after December 31, 2019.

Perhaps most significantly, the bill provides for a freeze beginning in 2030 to the inflation-adjusted increases to the annual contribution limit to defined contribution plans, the annual defined benefit limit, and the maximum limit on compensation that that may be taken into account when determining the limit on contributions and benefits of an employee. For 2021, these amounts are $58,000, $230,000, and $290,000, respectively. The annual inflation adjustments would continue normally until 2030.

MISCELLANEOUS RELIEF

A handful of other tax provisions are included in the bill, with some aimed at making health care more affordable and ensuring that pandemic-related aid does not create tax burdens on businesses receiving them.

Premium Tax Credits

The bill makes changes to the premium tax credit. For 2021 and 2022, the bill modifies affordability percentages used in calculating the premium tax credit to make credits available for individuals with incomes below 400 percent of the federal poverty line and increases credit amounts for those already qualified. For 2021, the bill makes advance premium tax credits available for individuals receiving unemployment compensation. And the bill eliminates the recapture provisions applicable to 2020 for taxpayers receiving excess premium tax credits.

Tax Treatment of COVID-19 Relief

The bill provides that Targeted Economic Injury Disaster Loans (EIDL) and Restaurant Revitalization Grants received from the Small Business Administration will not be subject to income tax, and the exclusion will not result in the denial of a deduction reduction of tax attributes, or denial of increase in basis.

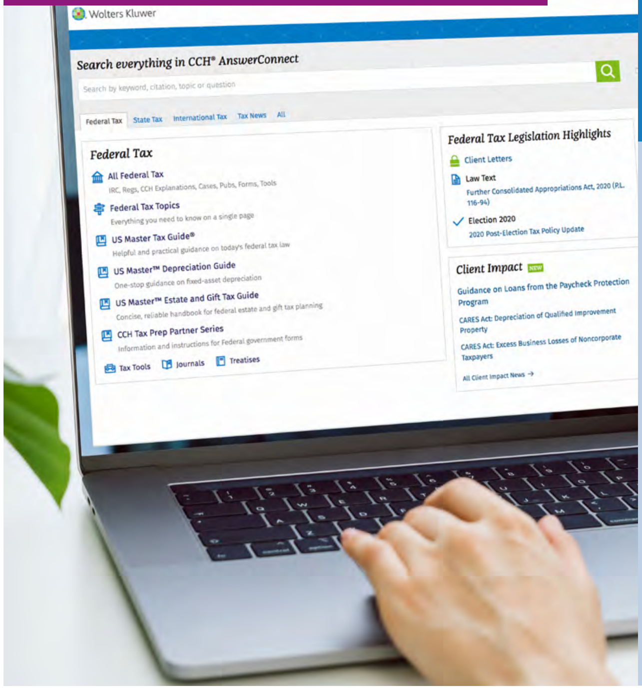
COMMENT. *The Consolidated Appropriations Act, 2021 included similar provisions applicable to EIDL grants, grants to entertainment venues, educational grants, etc.*

Worldwide Allocation of Interest

Finally, the bill includes a repeal of the one-time election available to an affiliated group of corporations to determine foreign-source taxable income of the group by allocating and apportioning interest expense of the domestic members of a worldwide affiliated group on a worldwide-group basis, as if all members of the worldwide group were a single corporation. The election was to be available for the first time in 2021, but the bill provides that treatment of such income will continue under pre-2021 rules.

RESOURCES *from Wolters Kluwer*

COMPLIMENTARY ACCESS



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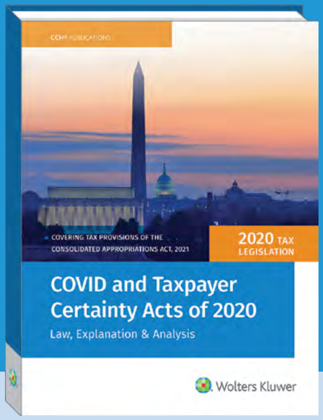

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