TaxNewsFlash

United States

No. 2020-774
December 22, 2020

Legislative update: Compensation and benefit-related tax provisions in year-end funding and COVID relief legislation

The year-end funding and stimulus legislation includes several compensation and benefit-related tax provisions.

As part of the stimulus legislation, the “Taxpayer Certainty and Disaster Tax Relief Act of 2020” would expand the employee retention credit provisions through June 30, 2021 (from January 1, 2021) as well as allowing for the full deductibility of business meals provided by a restaurant during the next two calendar years.

Employee retention credit modifications

The provision in the legislation would extend and expand the employee retention tax credit (ERC), part of the “Coronavirus Aid, Relief, and Economic Security Act” (CARES Act), for a six-month period from January 1, 2021, through June 30, 2021. The legislation also contains technical corrections to the CARES Act.

For calendar quarters beginning on January 1, 2021, and through June 30, 2021, the legislation includes changes that would:

- Increase the credit rate from 50% to 70% of qualified wages
- Expand eligibility for the credit by reducing the required year-over-year gross receipts decline from 50% to 20% and would provide a safe harbor allowing employers to use prior quarter gross receipts to determine eligibility
- Increase the limit on per-employee creditable wages from $10,000 for the year to $10,000 for each quarter
- Increase the definition of a “large employer” from one with 100 employees to employers with 500 or fewer employees for the purpose of determining the relevant qualified wages

- Expand ERC eligibility to colleges, universities, as well as government entities with a principal purpose or function of providing medical or hospital care
- Provide rules to allow new employers that were not in existence for all or part of 2019, to be able to claim the credit
- Provide for outreach campaign for employers—a special notice and educational materials to be provided to employers with 500 or fewer employees
- Remove the 30-day wage limitation to allow credits for bonus pay

The legislation includes several retroactive provisions regarding the effective date of the ERC provisions under the CARES Act (that is, section 2301 of the CARES Act) to:

- Provide that employers that receive Paycheck Protection Program (PPP) loans may still qualify for the ERC with respect to wages that are not paid for with forgiven PPP proceeds
- Clarify the determination of gross receipts for certain tax-exempt organizations is determined under section 6033
- Clarify that group health plan expenses can be considered qualified wages even when no other wages are paid to the employee (consistent with IRS guidance)

Full deduction for certain business meals

Code section 274 would be amended to provide a 100% deduction for business meal food and beverage expenses provided by a restaurant that are paid or incurred in calendar year 2021 and 2022.

Minimum age for distributions during working retirement

The legislation would allow certain construction and building-trades workers age 55 years or older who are receiving retirement benefits to continue to work and receive such benefits. Generally, distributions cannot be taken out until age 59½ years. This provision would be effective for distributions before, on or after the date of enactment.

Partial plan termination changes for 2020

A partial termination generally occurs when a qualified plan has turnover in excess of 20%. A partial termination can cause significant cost and administrative expenses to the plan sponsor. Due to the high turnover since March 2020, the legislation includes a temporary rule for any plan year that includes March 13, 2020, because of the high workforce turnover since March 2020. The legislation provides that determination of the partial termination could be delayed until March 31, 2021, to give companies time to restore their workforce above 80%and avoid the partial termination.

Health and dependent care flexible spending arrangements

The legislation provides flexibility for taxpayers to rollover unused amounts in their health and dependent care flexible spending arrangements from 2020 to 2021 and from 2021 to 2022. The legislation would allow this extended 12-month grace period. In addition, employers would be permitted to allow employees to make a 2021 mid-year prospective change in contribution amounts.

Expiring tax provisions extended through 2025

- The "family leave credit" under section 45S allows a tax credit for providing paid Family and Medical Leave Act (FMLA) leave. This provision was originally enacted under the 2017 tax law known as the "Tax Cuts and Jobs Act" (TCJA) for a two-year period, but was extended through 2020. This legislation would continue to extend the effective date of the credit through 2025.

- The CARES Act provides an exclusion from income for certain employer-paid student loan payments made through a section 127 educational assistance program. This provision was set to expire after December 31, 2020. However, the legislation would extend the use of section 127 for a student loan payment through December 31, 2025.

Medical expense deduction provision made permanent

The stimulus legislation would make permanent the reduced requirement of 7.5% of adjusted gross income for a medical deduction. Section 213 allows a deduction for medical expenses that exceed a certain percent of adjusted gross income. The requirement had been 10% of adjusted gross income, but the TCJA reduced the percentage to 7.5%. The reduced percentage was set to expire at the end of 2020.

Disaster tax relief (not COVID-19 related but certain declared disasters relating to fires, hurricanes, etc.)

The stimulus legislation includes a provision for disaster tax relief for individuals and businesses in presidentially declared disaster areas for major disasters declared (other than COVID-19) after December 31, 2019, through 60 days after the date of enactment.

- **Use of retirement funds for disaster mitigation:** Would allow residents of disaster areas to borrow or take out a loan of up to $100,000 from a retirement plan or IRA account without penalty. Amounts withdrawn would be included in income, but the income would be spread over three years. Also, the amount may be recontributed to the plan to avoid tax. For new and outstanding plan loans, the repayment period would be extended for one year.
- **Employee retention credit for disaster zones:** Would provide a tax credit of 40% of wages (up to $6,000 per employee) to employers in disaster zones. The credit would apply to wages paid without regard to whether services associated with those wages were performed.

Employee payroll tax deferral repayment extended

In August 2020, the president issued a memorandum directing the Secretary of Treasury to use his authority to defer the withholding, deposit, and payment of certain payroll tax obligations. Employee payroll tax could be deferred from September 1, 2020, through December 31, 2020. Under IRS Notice 2020-65, the amount of this deferral would be repaid from January 1, 2021, through April 30, 2021, with penalties accruing as of May 1, 2021. The stimulus legislation would provide an extended payroll period for employees, and would allow for repayment to be extended from January 1, 2021, through December 31, 2021. Penalties would not accrue until January 1, 2022.

Read a summary of the legislation: ***TaxNewsFlash***

For more information, contact a tax professional with KPMG's Washington National Tax:

Robert Delgado | +1 (858) 750-7133 | rdelgado@kpmg.com

Erinn Madden | +1 (202) 533-3757 | erinnmadden@kpmg.com

Terri Stecher | +1 (202) 533-4830 | tstecher@kpmg.com

Direct comments, including requests for subscriptions, to Washington National Tax. For more information, contact KPMG's Federal Tax Legislative and Regulatory Services Group at + 1 202.533.4366, 1801 K Street NW, Washington, DC 20006-1301.