

# Selected tax topics from the Consolidated Appropriations Act (CAA), 2021

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## **Extension of COVID-19 credits**

The Consolidated Appropriations Act (CAA), 2021 extends the refundable payroll tax credits for paid sick and family leave, enacted in the Family's First Coronavirus Response Act (FFCRA), through the end of March 2021. It also modifies the tax credits, so they apply as if the corresponding employer mandates were extended through the end of March 2021. This provision is effective as if included in FFCRA.

The CAA also extends the Employee Retention Credit (originally scheduled to expire December 31, 2020) until July 1, 2021.

**Please note:** It is unclear how COVID-19 payroll credits will be reconciled on the 2020 and 2021 income tax returns. The Internal Revenue Service posted FAQs indicating tax treatment FFCRA and Employee Retention Credit prior to the passage of the CAA. Additional guidance from the Treasury will need to be issued on reconciliation of COVID credits.

## **Extension of deferral of employee payroll tax**

In an August 8, 2020 executive order, President Trump issued a moratorium to allow employers to defer withholding employee shares of Social Security taxes or railroad retirement tax-equivalent from September 1, 2020, through December 31, 2020, and required employers to increase withholding and pay the deferred amounts ratably from wages and compensation paid between January 1, 2021, and April 31, 2021. Beginning on May 1, 2021, penalties and interest on deferred unpaid tax liability will begin to accrue.

The new provision extends the repayment period through December 31, 2021. Penalties and interest on deferred unpaid tax liability will not begin to accrue until January 1, 2022.

## **Net Operating Loss (NOL) changes**

Farmers who elected a two-year net operating loss carryback prior to the CARES Act may elect to retain that two-year carryback rather than claim the five-year carryback provided in the CARES Act. This section also allows farmers who previously waived the election to carry back a net operating loss to revoke the waiver. These clarifications eliminate unnecessary compliance burdens for farmers. The provision applies retroactively as if included in Section 2303 of the

CARES Act.

This fixes two dilemmas facing farmers with net operating losses. First of all, if the producer did a two-year carryback, they can leave the two-year carryback in place. The CARES Act basically did away with the two-year carryback, and producers that had a two-year carryback were not sure what they could or could not do. The other option now available is that the producer can waive the NOL carryback option. Some producers may have opted not to do a two-year carryback. However, the five-year carryback would have been advantageous. Now producers have the option to waive the carryback and do a five-year carryback.

### **Changes to the deductibility of business meals**

The Tax Cuts and Jobs Act limited the deductibility of business meals. In 2020, the IRS issued both proposed and final regulations addressing the deductibility of business meals. As part of this guidance, in most cases, business meals were limited to 50 percent deductibility until 2025, when the business meal deduction will go away.

The CAA clarifies 100% deductibility for **business meals provided by a restaurant**. This change is temporary for amounts paid or incurred after December 31, 2020, and before January 1, 2023. The author expects additional guidance from the IRS sometime in the calendar year 2021.

### **Reconciliation of credits from Employee Retention Credit, Families First Coronavirus Response Act, and CARES Act**

Until recently, most of the educational focus on these credits has been on administering the credits with taxpayers. Very little has been shared about what needs to happen when the taxpayer reconciles these credits on the 2020 Income Tax Return.

IRS has posted a series of FAQs (Frequently Asked Questions) addressing special issues for employers who have utilized the COVID-19 employer credits.

These FAQs are not included in the Internal Revenue Bulletin, and therefore may not be relied upon as legal authority. This means that the information cannot be used to support a legal argument in a court case. While FAQs are not substantial authority, FAQs do provide some direction in regards to IRS's position. The author anticipates formal guidance on this issue in the future. However, in the meantime, these FAQs will need to serve as our guide.

### **Employee Retention Credit (ERC) under the CARES Act**

Here is a link to the [IRS FAQ page for Employee Retention Credit under the Cares Act](#).

**“85. Does the Employee Retention Credit reduce the expenses that an Eligible Employer could otherwise deduct on its federal income tax return?”**

Yes. Section 2301(e) of the CARES Act provides that rules similar to section 280C(a) of the Internal Revenue Code (the "Code") shall apply for purposes of applying the Employee Retention Credit. Section 280C(a) of the Code generally disallows a deduction for the portion of wages paid equal to the sum of certain credits determined for the taxable year. Accordingly, a similar deduction disallowance would apply under the Employee Retention Credit, such that an employer's aggregate deductions would be reduced by the amount of the credit as result of this disallowance rule.

**“86. Does an Eligible Employer receiving an Employee Retention Credit for qualified wages need to include any portion of the credit in income?”**

No. An employer receiving a tax credit for qualified wages, including allocable qualified health plan expenses, does not include the credit in gross income for federal income tax purposes. Neither the portion of the credit that reduces the employer's applicable employment taxes, nor the refundable portion of the credit, is included in the employer's gross income.”

**Employee tax credits under the Families First Coronavirus Response Act (FFCRA)**

Here is a link to the [IRS FAQ page for FFCRA credits](#).

**“49. What amount does an Eligible Employer receiving tax credits for qualified leave wages (and allocable qualified health plan expenses and the Eligible Employer's share of Medicare tax on the qualified leave wages) need to include in income?”**

An Eligible Employer must include the full amount of the credits for qualified leave wages (and any allocable qualified health plan expenses and the Eligible Employer's share of the Medicare tax on the qualified leave wages) in gross income.

**“50. May an Eligible Employer deduct as a business expense an amount paid to an employee for qualified leave wages (and allocable qualified health plan expenses and the Eligible Employer's share of Medicare tax on the qualified leave wages) for which it expects to claim the tax credits?”**

“Generally, an Eligible Employer's payments of qualified leave wages (and any allocable qualified health plan expenses and the Eligible Employer's share of the Medicare tax on the qualified wages) are deductible by the Eligible Employer as ordinary and necessary business expenses in the taxable year that these wages are paid or incurred. An Eligible Employer may deduct as a business expense the amounts paid to an employee for qualified leave wages (and any allocable qualified health plan expenses and the Eligible Employer's share of Medicare tax on the qualified leave wages) for which the Eligible Employer expects to claim the tax credits under sections 7001 or 7003 of the FFCRA, if the Eligible Employer is otherwise eligible to take the deduction.”

From the FAQs listed above, we see that the FFCRA credits have different rules than the ERC. Please see the following table.

Table 1: Tax Treatment Comparison of Employee Retention Credit (ERC) and Families First Coronavirus Response Act (FFCRA).

	<b>ERC</b>	<b>FFCRA</b>
<b>Employer includes credit in taxable income</b>	<b>No</b>	<b>Yes</b>
<b>Does the employer need to reduce expenses for the amount of credit the employer received?</b>	<b>Yes</b>	<b>No</b>

In the FAQs for the Employee Retention Credit (ERC), the employer does not need to add the credit to taxable income. However, the employer does need to reduce expenses by the amount of the credit received.

In the FAQs for the credits related to FFCRA, the treatment is the opposite of that for ERC. For FFCRA, the employer includes the credit amount in taxable income and does not need to reduce expenses.

As mentioned before, in this fact sheet, the IRS has not issued any formal guidance on this topic to date. The author expects some form of direction after the new year.

Source information used for this post included [The House Committee on Appropriations H.R. 133 – Division-by-division summary of COVID-19 relief provisions](#), as well as the [final H.R. 133 text](#) as passed, and IRS FAQs.

<i><b>This information is educational in nature and is not tax or legal advice.</b></i>
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