Consolidated Appropriations Act, 2021: PPP and Tax Provisions

By Melissa Ostrower and Robert R. Perry

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The Consolidated Appropriations Act, 2021 (Act) generally provides the annual funding for the federal government and contains several important rules giving further COVID-19 relief. These include, among other things, revisions to the Paycheck Protection Program (PPP), expansion of the employee retention tax credit and changes to other employer-related tax provisions.

The Act was passed by Congress on December 21, 2020, and signed by President Donald Trump on December 27, 2020.

This article highlights some of the PPP and tax provisions we believe will be of interest to employers.

PPP Changes

Title III of the Act, called the "Economic Aid to Hard-Hit Small Businesses, Non-Profits and Venues Act," makes material changes to the PPP enacted under the Coronavirus Aid, Relief, and Economic Security (CARES) Act and subsequently amended.

The changes that Title III of the Act makes to the PPP are based in many respects on the Continuing Small Business Recovery and Paycheck Protection Program Act that was part of the Health, Economic Assistance, Liability Protection and Schools (HEALS) Act introduced by Senate Republicans this past summer.

Expansion of Loan Uses Eligible for Forgiveness

Title III expands the permitted (and potentially forgivable) uses of PPP loan proceeds to include (in addition to the payroll expenses and covered utilities and covered rent permitted under the CARES Act):

- Covered operations expenditures (*e.g.,* payment for any software, cloud computing, and other human resources and accounting needs);
- Covered property damage costs (*e.g.,* related to property damage and vandalism or looting due to public disturbances during 2020 not covered by insurance);
- Covered supplier costs (*e.g.,* expenditures pursuant to a contract for goods in effect prior to the PPP loan covered period and that are essential to the current operations of the entity when made); and
- Covered worker protection expenditures (*e.g.,* expenditures for personal protective and other equipment needed to help a borrower comply with federal health and safety guidelines related to the COVID-19 pandemic during the period between March 1, 2020, and the date on which COVID-19 no longer qualifies for federal emergency status).

Change in Covered Period

The covered period for a PPP loan is 24 weeks (or 8 weeks for borrowers who received their loans prior to June 5, 2020, and elect to use an 8-week covered period). Title III would allow borrowers to select *any* covered period between 8 weeks after loan origination and 24 weeks after loan origination in length.

Simplified Forgiveness Application

Title III significantly simplifies the loan forgiveness application and documentation process for many borrowers as follows:

- Loans up to $150,000 will be forgiven in full if the borrower signs and submits a certification (of not more than one page) that provides minimal information (number of employees retained due to PPP loan, estimated amount of loan spent on payroll expenses, and total loan value) and agrees to retain relevant records for a period of four years (employment records) or three years (all other

Meet the Authors

Melissa Ostrower

Principal
New York Metro
New York City 212-545-4000
Email

Robert R. Perry

Principal
New York Metro
New York City 212-545-4000
Email

Practices

Employee Benefits

Services

COVID-19

records).

- Loans over $150,000 will be subject to the Small Business Administration's (SBA) current loan forgiveness procedures and would remain subject to SBA audit.
- The controversial necessity certification applicable to loans over $2 million (SBA Forms 3509 and 3510) appears to be unaffected by the Act.

Economic Injury Disaster Loans (EIDL) Advances

The $10,000 EIDL advance provided by the SBA will no longer (as under prior law) reduce the amount of PPP loan forgiveness.

Group Insurance Payments as Payroll Costs

Title III clarifies that employer-provided group insurance benefits other than healthcare benefits (*e.g.,* group life, dental, vision, or disability) fall within the definition of forgivable payroll costs.

PPP Loan Cap

Title III caps any future PPP loans (including the "second draw" loans discussed below) at $2 million.

Second PPP Loan Availability

Title III allows eligible entities to receive a second PPP loan, referred to as a "second draw."

To qualify as an *eligible entity*, a prospective PPP borrower must:

- Employ *not more than 300 employees*; and
- Demonstrate at least a 25% reduction in gross receipts in any quarter of 2020 relative to the same 2019 quarter.

Special rules apply for the determination of whether entities that did not exist for some or all of 2019 meet this revenue loss requirement.

Ineligible entities include entities with certain relationships to the People's Republic of China or the Special Administrative Region of Hong Kong, including those created, organized or having significant operations in these areas or having directors who are residents of the People's Republic of China.

Generally, the second draw loan amount is calculated on the same basis as the original PPP loans (up to *2.5 times average total monthly payroll costs* in the one year prior to the loan), but is capped at $2 million. Special rules apply to entities that are assigned a NAICS code beginning with 72 (generally, hotels and restaurants); these entities can borrow up to *3.5 times* their average monthly payroll costs, but the loan amount is still capped at $2 million.

Loan Forgiveness

Borrowers would be eligible for loan forgiveness equal to the sum of their payroll costs, covered mortgage, rent, utility payments, covered operations expenditures, covered property damage costs, covered supplier costs, and covered worker protection expenditures incurred before the end of the covered period (as modified by the Act). The current spending requirement of 60/40 minimum on payroll costs for full forgiveness would continue to apply.

Increased Loan Amount Flexibility

Under Title III, PPP borrowers who are eligible for an increased covered loan amount as a result of any interim final rule that allows for covered loan increases may submit a request for an increase in the covered loan amount (regardless of whether the initial covered loan amount has been fully disbursed or the lender of the initial covered loan has submitted Form 1502 [a form required to be completed by lenders] to the SBA). Additionally, an eligible recipient that returned all or part of an original covered loan or did not accept the full amount of an original covered loan may reapply or request a modification of an existing loan (as applicable).

Tax-Related Changes

Revised and Expanded Retention Tax Credit

The Act extends and expands the availability of the retention tax credit through June 30, 2021, however, certain provisions of the Act apply only after December 31, 2020.

The Act amends the employee retention credit to be equal to 70% of qualified wages paid to employees after December 31, 2020, and before July 1, 2021.

During the first two quarters of 2021, a maximum of $10,000 in qualified wages for each employee per calendar quarter may be counted in determining the 70% credit. Therefore, the maximum tax credit that can be claimed by an eligible employer in 2021 is $7,000 per employee per calendar quarter.

With respect to a calendar quarter during this period (and during which an employer is carrying on a trade or business), (i) if the employer's operations were fully or partially suspended due to orders from an appropriate governmental authority for specified reasons due to COVID-19 OR (ii) the gross receipts of such employer for the calendar quarter are less than 80% of the gross receipts of such employer for the same calendar quarter of 2019, the employer is eligible for the credit that quarter. The Act provides a special rule that allows employers to determine gross receipts based on the prior calendar quarter.

For eligible employers that averaged 500 or fewer full-time employees ("Small Employers"), the tax credit available in 2021 is based on the qualified wages paid to all employees after December 31, 2020, and before July 1, 2021, regardless of whether the wages were paid for services performed. For eligible employers that averaged more than 500 full-time employees, the credit is based on qualified wages paid to those employees not providing services due to the suspension of operations or decline in gross receipts.

Advance payment of credits to Small Employers are permitted under the Act, provided that such advance payments do not exceed 70% of the average quarterly wages paid by the employer in 2019.

Qualified wages taken into account in calculating the 2021 credits are not limited to what the employer paid to the employees in any specific prior period.

The Act provides that qualified wages taken into account in determining the employee retention credit may not be counted as payroll costs under the PPP, but that employers may elect not to have wages count as qualified wages for purposes of the employee retention tax credit. If a PPP loan is ultimately not forgiven, such election will not prevent the wages from counting as qualified wages for purposes of the employee retention credit. In short, the Act allows employers who received PPP loans to remain eligible for the employee retention credit with respect to wages that are not counted as forgiven payroll costs under the PPP.

Additionally, the Act clarifies that qualified wages include amounts paid to maintain a group health plan (but only to the extent excluded from employees' gross income) and such amounts count as qualified wages even if no cash wages are paid to employees.

Employer Takeaway: The employee retention credit has been significantly expanded (in certain cases retroactively and in others only with respect to qualified wages paid in 2021). Employers should review their employee counts and operations to determine the extent to which they may be eligible for enhanced and/or increased credits.

Clarification of Tax Treatment of Forgiveness of Covered Loans

The Act permits employers to deduct expenses paid with forgiven loan proceeds expressly reversing the position previously taken by the Internal Revenue Service. This provision significantly increases the value of the forgiven PPP loans to employers.

By way of background, the IRS held in Notice 2020-32 that no deduction is allowed for an eligible expense that is otherwise deductible if the payment of the eligible expense results in forgiveness of a covered PPP loan. The IRS then reaffirmed and elaborated on this position in Revenue Ruling 2020-27. The Act reverses this IRS position, providing that no deduction may be denied, no tax attribute may be reduced, and no basis increase may be denied due to the exclusion from gross income of debt forgiveness under the PPP. This right to a deduction applies to both existing and new loans under the PPP.

Extension of Credits for Paid Sick and Family Leave

The Act extends until March 31, 2021, the period during which credits for emergency paid sick leave and paid family leave under the Families First Coronavirus Response Act (FFCRA) are available. Essentially, the credits are available as if the emergency paid sick leave and paid family leave provisions under the FFCRA (subject to all applicable limitations) had been extended through March 31, 2021.

Extension of Deferred Payroll Taxes

Pursuant to IRS Notice 2020-65, which provided guidance on the employment tax deferral that was the subject of President Trump's August 8, 2020, Memorandum on Deferring Payroll Tax Obligations in Light of the Ongoing COVID-19 Disaster, the due date for the withholding and payment of the employee share of Social Security taxes on certain wages was postponed until the period beginning on January 1, 2021, and ending on April 30, 2021. The Act extends the deadline for employees to repay these deferred taxes until December 31, 2021.

Temporary Allowance of Full Deduction for Business Meals

The Act temporarily allows a 100% deduction for business expenses for food or beverages provided by a restaurant that are paid or incurred between January 1, 2021, and December 31, 2022.

Exclusion of Certain Employer Payments of Student Loans

The CARES Act amended Section 127 of the Internal Revenue Code (which permits employers to provide certain educational assistance to employees on a tax-free basis) to allow the payment by an employer of principal or interest on certain employee qualified education loans through December 31, 2020. The Act expands this provision to permit the tax-free payment of principal or interest on qualified education loans by employers through December 30, 2025 (subject to applicable limits under Section 127).

Employer Takeaway: There was little employer interest in this special rule in 2020 due to the uncertainties of the pandemic. As the emergency subsides, employers may want to consider amending their Section 127 plans to provide this valuable tax-free benefit.

Please contact the authors or the Jackson Lewis attorney with whom you regularly work if you have questions or need assistance.

Related:

- Consolidated Appropriations Act, 2021: Employer-Sponsored Retirement Plans
- Consolidated Appropriations Act, 2021: Employer-Sponsored Health and Welfare Plan Components
- Consolidated Appropriations Act, 2021: Unemployment Relief
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