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AMERICAN RESCUE PLAN ACT PASSES WITH MANY TAX COMPONENTS

From the Journal of Accountancy by Alistair M. Nevius, J.D.

The House of Representatives passed the American Rescue Plan Act, H.R. 1319, on Wednesday, March 10, by a vote of 220–211. It now goes to President Joe Biden for his signature. He is expected to sign it quickly.

H.R. 1319 was first passed by the House on Feb. 27. The Senate made several amendments and passed its version of the bill on March 6. The bill then came back to the House for a final vote on Wednesday, March 10.

Among the act's many provisions are several tax items. Most of the tax provisions that were in the House version of the bill were unchanged in the Senate's version, but the tax treatment of 2020 unemployment benefits, the phaseout ranges for economic impact payments, and the treatment of student loan debt forgiveness were changed by the Senate.

Here is a look at the final version of the tax provisions:

Unemployment benefits

The act makes the first $10,200 in unemployment benefits tax-free in 2020 for taxpayers making less than $150,000 per year.

Recovery rebates

The act creates a new round of economic impact payments to be sent to qualifying individuals. The same as last year's two rounds of stimulus payments, the economic impact payments are set up as advance payments of a recovery rebate credit. The act creates a new Sec. 6428B that provides individuals with a $1,400 recovery rebate credit ($2,800 for married taxpayers filing jointly) plus $1,400 for each dependent (as defined in Sec. 152) for 2021, including college students and qualifying relatives who are claimed as dependents. As with last year's economic impact payments, the IRS will send out the advance payments of the credit.

For single taxpayers, the credit and corresponding payment will begin to phase out at an adjusted gross income (AGI) of $75,000, and the credit will be completely phased out for single taxpayers with an AGI over $80,000. For married taxpayers who file jointly, the phaseout will begin at an AGI of $150,000 and end at AGI of $160,000. And for heads of household, the phaseout will begin at an AGI of $112,500 and be complete at AGI of $120,000.

The act uses 2019 AGI to determine eligibility, unless the taxpayer has already filed a 2020 return.

COBRA continuation coverage

The act provides COBRA continuation coverage premium assistance for individuals who are eligible for COBRA continuation coverage between the date of enactment and Sept. 30, 2021. The act creates a new Sec. 6432, which allows a COBRA continuation coverage premium assistance credit to taxpayers. The credit is allowed against the Sec. 3111(b) Medicare tax. The credit is refundable, and the IRS may make advance payments to taxpayers of the credit amount.

The credit applies to premiums and wages paid after April 1, 2021, and through Sept. 30.

Under new Sec. 6720C, a penalty is imposed for failure to notify a health plan of cessation of eligibility for the continuation coverage premium assistance.

Taxpayers who receive the COBRA continuation coverage premium assistance credit are not also eligible for the Sec. 35 health coverage tax credit.

Under new Sec. 139I, continuation coverage premium assistance is not includible in the recipient's gross income.

Child tax credit

The act expands the Sec. 24 child tax credit in several ways and provides that taxpayers can receive the credit in advance of filing a return. The act makes the credit fully refundable for 2021 and makes 17-year-olds eligible as qualifying children.

The act increases the amount of the credit to $3,000 per child ($3,600 for children under 6). The increased credit amount phases out for taxpayers with incomes over $150,000 for married taxpayers filing jointly, $112,500 for heads of household, and $75,000 for others, reducing the expanded portion of the credit by $50 for each $1,000 of income over those limits.

The IRS is directed to estimate taxpayers' child tax credit amounts and pay monthly in advance one-twelfth of the annual estimated amount. Payments will run from July through December 2021.

The IRS must set up an online portal to allow taxpayers to opt out of advance payments or provide information that would be relevant to modifying the amount.

The taxpayer in general will have to reconcile the advance payment amount with the actual credit amount on next year's return and increase taxable income by the excess of the advance payment amount over the actual credit allowed. But taxpayers whose modified AGI for the tax year does not exceed 200% of the applicable income threshold ($60,000 for married taxpayers filing jointly) will have the increase for an excess advance payment reduced by a safe harbor amount of $2,000 per child.

Earned income tax credit

The act also makes several changes to the Sec. 32 earned income tax credit. It introduces special rules for individuals with no children: For 2021, the applicable minimum age is decreased to 19, except for students (24) and qualified former foster youth or homeless youth (18). The maximum age is eliminated.

The credit's phaseout percentage is increased to 15.3%, and the phaseout amounts are increased.

The credit would be allowed for certain separated spouses.

The threshold for disqualifying investment income would be raised from $2,200 to $10,000.

Temporarily, taxpayers would be allowed to use their 2019 income instead of 2021 income in figuring the credit amount.

Child and dependent care credit

The act makes various changes to the Sec. 21 child and dependent care credit, effective for 2021 only, including making it refundable. The credit will be worth 50% of eligible expenses, up to a limit based on income, making the credit worth up to $4,000 for one qualifying individual and up to $8,000 for two or more. Credit reduction will start at household income levels over $125,000. For households with income over $400,000, the credit can be reduced below 20%.

The act also increases the exclusion for employer-provided dependent care assistance to $10,500 for 2021.

Family and sick leave credits

The act codifies the credits for sick and family leave originally enacted by the Families First Coronavirus Response Act (FFCRA), P.L. 116-127, as Secs. 3131 (credit for paid sick leave), 3132 (credit for paid family leave), and 3133 (special rule related to tax on employers). The credits are extended to Sept. 30, 2021. These fully refundable credits against payroll taxes compensate employers and self-employed people for coronavirus-related paid sick leave and family and medical leave.

The act increases the limit on the credit for paid family leave to $12,000.

The number of days a self-employed individual can take into account in calculating the qualified family leave equivalent amount for self-employed individuals increases from 50 to 60.

The paid leave credits will be allowed for leave that is due to a COVID-19 vaccination.

The limitation on the overall number of days taken into account for paid sick leave will reset after March 31, 2021.

The credits are expanded to allow 501(c)(1) governmental organizations to take them.

Employee retention credit

The act codifies the employee retention credit in new Sec. 3134 and extends it through the end of 2021. The employee retention credit was originally enacted in the Coronavirus Aid, Relief, and Economic Security (CARES) Act, P.L. 116-136, and it allows eligible employers to claim a credit for paying qualified wages to employees.

Under the act, the employee retention credit would be allowed against the Sec. 3111(b) Medicare tax.

Premium tax credit

The act expands the Sec. 36B premium tax credit for 2021 and 2022 by changing the applicable percentage amounts in Sec. 36B(b)(3)(A). Taxpayers who received too much in advance premium tax credits in 2020 will not have to repay the excess amount. A special rule is added that treats a taxpayer who has received, or has been approved to receive, unemployment compensation for any week beginning during 2021 as an applicable taxpayer.

Student loans

The act amends Sec. 108(f) to specify that gross income does not include any amount that would otherwise be included in income due to the discharge of any student loan after Dec. 31, 2020, and before Jan. 1, 2026.

Miscellaneous tax provisions

The act amends Sec. 162(m), for years after 2026, to add a corporation's five highest-compensated employees (besides the employees already covered by Sec. 162(m)) to the list of individuals subject to the $1 million cap on deductible compensation.

The act extends the Sec. 461(l) limitation on excess business losses of noncorporate taxpayers for one year, through 2027.

The act also repeals Sec. 864(f), which allows affiliated groups to elect to allocate interest on a worldwide basis.

The act provides that targeted Economic Injury Disaster Loan (EIDL) grants received from the U.S. Small Business Administration (SBA) are not included in gross income and that this exclusion from gross income will not result in a denial of a deduction, reduction of tax attributes, or denial of basis increase. Similar treatment is afforded SBA restaurant revitalization grants.

The act temporarily delays the designation of multiemployer pension plans as in endangered, critical, or critical and declining status and makes other changes for multiemployer plans in critical or endangered status.

For more on the nontax provisions in the act, see "House Gives Final Approval to $1.9 Trillion Pandemic Aid Bill."