

# Tax Incentives in the COVID-Related Tax Relief Act of 2020 ('COVIDTRA')

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**PRACTICES** Tax, Government and Public Policy, Employee Benefits and Executive Compensation

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After months of negotiations, the COVID-Related Tax Relief Act of 2020 (the “Act”) was signed into law by President Trump on December 27, 2020. While the Act grabbed many headlines for its stimulus payments, the Act and the other legislation enacted with it as part of the Consolidated Appropriations Act of 2021 (the “CAA”) also contain several tax incentives designed to help businesses deal with the current economic turmoil caused by COVID-19.

## Deductibility of PPP-Funded Expenses

Prior to the Act, the IRS interpreted the CARES Act (through Notice 2020-32 and Revenue Ruling 2020-27) as disallowing a deduction for an otherwise deductible expense if the funds used to pay the expense were obtained from a PPP loan that was forgiven. The Act now allows businesses to deduct expenses even if the funds used to pay these expenses came from a PPP loan that was forgiven.

## Payroll Tax Credits

The Act extends the refundable payroll tax credits established by Families First Coronavirus Response Act for required paid sick and family leave. The period for which the tax credit can be used now runs through March 31, 2021.

## Employee Retention Tax Credit

The CAA also modified the Employee Retention Tax Credit (the “**ERTC**”) to make it more attractive to businesses. These changes to the ERTC include:

1. Extending the availability of the credit to wages paid after March 12, 2020 but before July 1, 2021;
2. Increasing the number of employees counted when determining the relevant qualified wage base from 100 to 500 (i.e., employers with 500 employees or less will be eligible for the credit, even if the employee is still working);
3. Increasing the credit rate from 50% to 70% of qualified wages;
4. Increasing the limit on per employee creditable wages from \$10,000 for the year to \$10,000 for each calendar quarter; and
5. Decreasing the required year-over-year gross receipts decline from 50% to 20% (i.e., the credit is available for an employer that did not incur a full or partial shutdown due to a COVID-19 related governmental shut down order if its gross receipts are less than 80% of its gross receipts for the same quarter in 2019).

## PPP Loans and Employee Retention Credits

Under the CARES Act, a business could not benefit from both a PPP loan and take ERTCs. The Act retroactively overrides this restriction. Therefore, an employer that received a PPP loan in 2020 and paid qualified wages exceeding the forgiven PPP loan used to pay wages (and is otherwise eligible to claim the credit) should be able to file amended employment tax returns to claim the credit in the relevant quarters. The employer may then continue to take the ERTC in 2021.

Prior to the Act, the ineligibility of a business to benefit from both a PPP loan and an ERTC created complexity in many mergers and acquisitions when the target company had a PPP loan and the acquiror was a beneficiary of the ERTC (or vice-versa). The removal of this restriction should ease this complexity from mergers and acquisitions going forward.

## Extension of Certain Deferred Payroll Taxes

The Act extends the repayment period by eight months for deferred withholdings of employees' share of Social Security taxes due for the last four months of 2020, if an employer elected to defer such amounts pursuant to the August 8, 2020 executive order and related IRS guidance. Any such deferred taxes should be withheld ratably from employees' wages and compensation paid from January 1 through December 31, 2021, rather than through April 31, 2021.

## Miscellaneous

The Act also contains several new temporary modifications to the Internal Revenue Code. For example, the Act allows for a 100% business expense deduction for meals (rather than the current 50%) as long as the expense is for food or beverages provided by a restaurant (for expenses incurred after December 31, 2020 and before December 31, 2022). Similar extensions and modifications have been made to several other provisions, such as allowing corporations to make qualified disaster relief contributions of up to 100% of their taxable income and extending the availability of the Work Opportunity Credit.

Employers should check with their tax advisors about the new tax provisions and the implications to their businesses.

### \*\*\*UPDATE\*\*\*

In response to the COVID-Related Tax Relief Act of 2020 (the "Act"), the IRS has issued Notice 2021-20 (the "Notice") providing 71 questions and answers for the tax changes made by the Act. The Notice is only applicable to qualified wages between March 13, 2020 and December 31, 2020. Some key guidance includes:

1. Rules and examples showing how to determine the portion of Employer Retention Tax Credit ("ERTC") qualified wages based on the amount claimed as payroll costs on the employer's loan forgiveness application. In general, the same wages cannot be counted for both the PPP loan forgiveness and ERTC.
2. Guidance on when an eligible employer may use a special fourth quarter rule provided in the Act (i.e., where an employer has a PPP loan and reported qualified wages paid in the second or third quarter of 2020 as payroll costs with its PPP loan forgiveness application, but

the loan was not forgiven, then the eligible employer may take those qualified wages into account for its ERTC calculation for the fourth quarter of 2020).

3. A list of the records that employers should maintain to substantiate eligibility for the credit.
4. An instruction for taxpayers to reduce their federal income tax deduction for qualified wages, including qualified health plan expenses, by their ERTC amount.

Notice 2021-20 is available [here](#) for additional information.