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To Our Clients and Friends:

THE CONSOLIDATED APPROPRIATIONS ACT

INTRODUCTION

On December 20, 2019 President Trump signed the Consolidated Appropriations Act, 2020 (the Act). The Act includes numerous tax provisions. For example, the Act extends retroactively several tax provisions that expired after 2017, one that expired after 2018, and some provisions scheduled to expire after 2019. In addition, the Act incorporates the SECURE Act which makes extensive changes to retirement plan provisions, including new required minimum distribution (RMD) requirements. Lastly, the Act contains pro-taxpayer provisions for victims of Presidentially Declared Disasters where the disaster declaration occurred after 2017 and within 60 days after December 20, 2019. This obviously includes losses from Hurricane Florence, Hurricane Michael and California wildfires. The Act also modifies provisions of the Affordable Care Act.

The Act is also notable for what it does not include. The Act does not include a technical correction to the Tax Cuts and Jobs Act of 2017 (TCJA) reducing the recovery period for Qualified Improvement Property (QIP) from 39 years to 15 years as intended by Congress. Therefore, QIP (according to the statute as written) does not qualify for the 100% 168(k) depreciation deduction.

Be Careful! We suggest you call our firm before implementing any tax planning techniques discussed in this letter. You cannot properly evaluate a particular planning strategy without calculating your overall tax liability with and without that strategy. This letter contains highlights of recent tax law changes and is not a comprehensive list. In addition, this letter contains ideas for Federal income tax planning only. **State income tax issues are not addressed.**

AFFORDABLE CARE ACT CHANGES.

- **Repeals Excise Tax On "Cadillac" Employer Health Plans.** The Act repeals the 40% excise tax that was to apply to high cost employer-sponsored health coverage beginning in 2020.

- **Repeals Fee On Health Insurance Providers.** The fee on health insurance providers that was to go into effect in 2020 is repealed by the Act.

- **Repeals Medical Device Excise Tax.** The 2.3% excise tax on the manufacture or production of medical devices is repealed for sales after 2019. The tax was scheduled to apply to sales after 2019.

TCJA CHANGES.

- **Kiddie Tax Reverts To Pre-TCJA Law.** The Act repeals the provision taxing the unearned income of children subject to the Kiddie tax at the tax rates for trusts and estates. Children subject to the Kiddie tax will be subject to tax on unearned income at their parents' tax rates as provided prior to the Tax Cuts and Jobs Act (TCJA).

  Reduced AMT Amount Repealed. The Act eliminates the reduced AMT exemption amount for children to whom the kiddie tax rules apply and who have net unearned income, effective for taxable years beginning after 2017.

  Effective Date. Generally, the revision of the Kiddie Tax to the pre-TCJA rules is effective for tax years beginning after 2019. However, **taxpayers can elect to apply the pre-TCJA Kiddie Tax rules retroactively to tax years beginning in 2018, 2019, or to both years.** The reduced AMT exemption amount is effective for tax years beginning after 2017.

529 PLAN CHANGES.

- **Higher Education Expenses Include Certain Expenses Associated With Registered Apprenticeship Programs, Effective for distributions after 2018.** The Act adds that "Qualified Education Expenses" include fees, books, supplies, and equipment required for the participation of a designated beneficiary of the §529 plan in an apprenticeship program registered and certified with the Secretary of Labor under section 1 of the National Apprenticeship Act.

- **Higher Education Expenses Include Up To $10,000 Of Qualified Education Loan Repayments, Effective for distributions after 2018.** The Act modifies the definition of "Qualified Higher Education Expenses" to include up to $10,000 **paid as principal or interest** on any qualified education of the designated beneficiary of the §529 plan or a sibling of the designated beneficiary. The $10,000 limitation is a lifetime limitation for any one individual. The designated beneficiary of the §529 plan and such designated beneficiary's brother, sister, stepbrother, and stepsister each have a separate $10,000 limitation. **Observation!** It appears, the Act allows a student loan distribution to be made from a §529 plan to a sibling of the account's designated beneficiary without changing the designated beneficiary.

  Any interest on qualified student loans otherwise deductible (before applying the $2,500 limit), must be reduced by the amount of the distribution from the §529 plan which would have been taxable but for the treatment of "Qualified Education Loan" principal or interest payments as "Qualified Higher Education Expenses."

NEW RULES FOR RETIREMENT PLANS.

- **Individuals No Longer Prohibited From Contributing To Traditional IRAs After 70½, Effective for contributions made for tax years beginning after 2019.** Under pre-Act law, no contribution was allowed to a traditional IRA for the benefit of an individual who had attained age 70½ before the close of the tax year for which the contribution was made. **Effective for contributions made for tax years beginning after 2019,** the Act provides that individuals may contribute to a traditional IRA after 70½ (i.e., for contributions made for tax years beginning after 2019, there is no age limitation on contributions to a traditional IRA or a Roth IRA).

- **Tax-Free Portion Of "Qualified Charitable Distributions" (QCDs) For IRA Owners Who Have Reached Age 70½ Reduced By Deductible IRA Contributions Made After Age 70½, Effective for distributions for tax years beginning after 2019.** The Act generally retains the existing provision allowing individuals who have reached **age 70½** to exclude from income annual transfers of up to $100,000 directly from their IRA to a charity. However, effective for distributions made for tax years beginning after 2019**,** the Act requires the **amount of any** such Qualified Charitable Distributions **(QCDs)** from an individual's IRA that **would otherwise be excludible from** the individual's **income,** to be **reduced by any deductible contributions to a traditional IRA after age 70½**.

- **RMDs Delayed Until Age 72 For Individuals Who Attain Age 70½ After 2019, Effective for distributions required to be made after 2019, with respect to individuals who attain age 70½ after 2019.** Under pre-Act law, participants in employee-provided retirement plans and IRA owners were generally required to begin taking Required Minimum Distributions (RMDs) from their plan by April 1 of the year following the year they reached age 70½ **("Required Beginning Date").** However, for distributions required to be made after 2019 with respect to individuals who attain age 70½ after 2019, the Act changes the age for the **"Required Beginning Date"** from **age 70½** to **age 72.**

- **Distributions From An IRA Or A Qualified Plan Generally Must Be Made Within 10 Years After Account Owner's Death, Generally effective for individuals dying after 2019.** The following is a summary of these new distribution rules:

  a. **Designated Beneficiaries Other Than "Eligible Designated Beneficiaries."** A decedent's entire remaining IRA or defined contribution plan account balance must be distributed to a designated beneficiary **who is not an** "Eligible Designated Beneficiary" by December 31 of the 10th year following the year of the decedent's death.

  b. **10-Year Rule Does Not Apply To "Eligible Designated Beneficiaries."** Generally, "Eligible Designated Beneficiaries" continue to have the distribution options available before the Act (e.g., distributions over the Eligible Designated Beneficiary's life expectancy).

  "Eligible Designated Beneficiaries." The term "Eligible Designated Beneficiary" means **1)** the surviving spouse of the decedent, **2)** a child of the decedent who has not reached majority, **3)** a disabled individual (i.e., an individual who is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or to be of long-continued and indefinite duration), **4)** a chronically ill individual, **or 5)** an individual who is not more than 10 years younger than the decedent. Following the death of an Eligible Designated Beneficiary, the account balance must be distributed by December 31 of the 10th year following the year of the Eligible Designated Beneficiary's death.

  Special Rules For Minor Children. Once a minor child who is a designated beneficiary reaches

majority, the balance in the retirement account for such child must be distributed within 10 years of the child reaching majority.

- **Up To $5,000 Penalty-Free Withdrawals From Retirement Plans For Child Birth Or Adoption Expenses, Effective for distributions made after 2019.** The Act exempts up to $5,000 of withdrawals from IRAs and qualified defined contribution plans from the 10% early distribution penalty where amounts are withdrawn during the 1-year period beginning on the date a child is born or the date a legal adoption is finalized. The $5,000 limitation applies to each qualified birth or adoption. For a married couple, each spouse may receive a **maximum aggregate amount** of $5,000 for a qualified birth or adoption from retirement plans in which each spouse participates or holds accounts. In addition, qualified distributions because of a child birth or adoption may be rolled over into a qualified retirement account eligible to accept rollovers.

- **May Adopt Qualified Retirement Plans By Due Date Of Return Including Extensions, Effective for plans adopted for taxable years beginning after 2019.** The Act allows the adoption of a stock bonus, pension, profit-sharing, or annuity plan for a taxable year after the close of the taxable year as long as the plan is adopted by the due date of the employer's tax return, including extensions. Previously, only a SEP could be adopted for a taxable year after the end of the taxable year.

- **Increased Penalties For Failing To File Certain Returns, Etc., Effective for returns due after 2019 including extensions.** The Act increases the minimum penalty for failure to file an income tax return to the lesser of $435 or the tax due with the return.

- **Revised Requirements For Multiple Employer Plans, Effective for plan years beginning after 2020.** Effective for plan years beginning after 2020, the Act revises the requirements for multiple employer pension plans and pooled employer plans. It provides that failure of one employer in a multiple employer retirement plan to meet plan requirements will not cause all plans to fail and that assets in the failed plan will be transferred to another plan. The Act also provides for the establishment of pooled employer plans that do not require a common characteristic.

- **Increase In 10% Cap For Automatic Enrollment Safe Harbor, Effective for plan years beginning after 2019.** The Act increases the maximum cap on the default rate under an automatic enrollment safe harbor plan from 10% to 15% of employee compensation, but only for the years after the participant's first deemed election year.

- **Rules Relating To Election Of Safe Harbor 401(k) Status, Effective for plan years beginning after 2019.** The Act limits the annual safe harbor notice to matching contribution plans and permits amendments to nonelective status at any time before the 30th day before the close of the plan year. An amendment may be made after that date if the amendment provides for a nonelective contribution of at least 4% of compensation for all eligible employees and the plan is amended no later than the last day for distributing excess contributions for the plan year.

- **Increased Tax Credit For Small Employer Retirement Plan Startup Costs, Effective for tax years beginning after 2019.** The Act increases the credit for plan startup costs of employers with 100 or fewer employees who received at least $5,000 of compensation from the employer for the preceding year. The credit is generally equal to 50% of the qualified startup costs paid or incurred during the taxable year. The credit is available for the first three years of the plan and cannot exceed the **greater of** **1) $500** or, **2) the lesser** of **a) $250** for each employee eligible to participate in the plan who is not a highly compensated employee, or **b) $5,000.** Qualified startup costs are expenses connected with the establishment or administration of the plan or with retirement-related education for employees with respect to the plan. The credit is available for qualified start-up costs of an eligible employer plan, including: qualified pension, profit sharing, or stock bonus plans;

qualified annuity plans; simplified employee pension plans; and simple plans.

- **New Three-Year Tax Credit For Small Employers Where Employer Sponsored Plan Includes Automatic Enrollment, Effective for tax years beginning after 2019.** The Act creates a new $500 credit for employers with 100 or fewer employees who received at least $5,000 of compensation from the employer for the preceding year. Qualifying employers only include employers that have an automatic employee contribution arrangement in a qualified cash or deferred plan. The credit is only available for the year the employer sponsored plan first includes an automatic contribution feature and for the two subsequent years. Thus, an eligible employer is allowed a credit of $500 per year for up to three years for the start-up costs for new 401(k) plans and SIMPLE IRA plans that include automatic enrollment, in addition to the plan start-up credit allowed under pre-Act law. The credit is also available to eligible employers that convert an existing plan to an automatic enrollment design.

- **Taxable Stipends And Non-Tuition Fellowships Treated As Compensation For Contributing To An IRA, Effective for tax years beginning after 2019.** The Act treats taxable stipends and non-tuition fellowships paid to aid an individual in the pursuit of graduate or postdoctoral study, as qualified compensation for making an IRA contribution.

- **Trustee-To-Trustee Transfers of Lifetime Income Options From One Retirement Plan To Another Or Distribution In The Form Of Qualified Plan Distribution Annuity, Effective for plan years beginning after 2019.** Under the Act, if a lifetime income investment (an annuity-type investment) is no longer permitted to be held as an investment option under a qualified defined contribution plan, §403(b) plan, or governmental §457(d) plan, except as otherwise provided in guidance, the plan does not fail to satisfy the Code requirements applicable to the plan solely by reason of **1)** allowing a direct trustee-to-trustee transfer to another eligible retirement plan of a lifetime income investment, **or 2)** distributions of a lifetime income investment in the form of a "qualified plan distribution annuity." This distribution must be made within the 90-day period ending on the date when the lifetime income investment is no longer authorized to be held as an investment option under the plan.

- **Clarification Of Coverage Rules For Church-Controlled Organizations, Effective for years beginning before, on, or after 12/20/19.** The Act clarifies that a retirement income account under a §403(b) plan may cover **1)** a duly ordained, commissioned, or licensed minister of a church in the exercise of his or her ministry, regardless of the source of the minister's compensation; **2)** an employee of an organization, whether a civil law corporation or otherwise, that is exempt from tax under §501 and is controlled by or associated with a church, or a convention or association of churches; **and 3)** an employee who is included in a church plan under certain circumstances after separation from the service of a church, a convention or association of churches, or other organization described in item **2)**.

- **Plans Allowing Elective Deferrals Must Allow Employees Who Work At Least 500 Hours For Three Consecutive Years To Make Elective Deferrals, Generally effective for plan years beginning after 2020.** Section 401(k) plans (i.e. plans allowing cash or deferred arrangements) must allow employees working more than 500 hours for at least three consecutive years who are at least age 21 by the end of the three consecutive year period to make elective deferrals. These employees are called "Long-Term Part-Time Employees."

- **Nontaxable Difficulty Of Care Payments Treated As Compensation, Effective for plan years beginning after 2015.** The Act treats difficulty of care payments to healthcare workers as earned income for retirement plan purposes. Contributions made to an IRA or a qualified plan based upon difficulty of care payments are treated as nondeductible contributions.

MISCELLANEOUS CHANGES.

- **2020 Income Exclusion For Qualified Payments To Volunteer Firefighters Or EMS Personnel. For 2020 calendar years only,** the Act provides that if a State or political subdivision of a State provides a reduction or rebate of taxes described in §164(a)(1), (2), or (3) (such as property taxes) to a member of a volunteer firefighting or volunteer emergency medical services organization, those amounts are excluded from the gross income of the member. The Act also excludes from the gross income of the member an expense reimbursement or other payment made by the State or political subdivision to the member for the volunteer services (qualified payments). This exclusion for qualified payments is limited to $50 for each month that the member performed services.

EXTENSION OF EXPIRED AND EXPIRING PROVISIONS.

The Act extends numerous tax provisions that had **expired at the end of 2017, one** provision that **expired after 2018,** and some that **were to expire after 2019.**

SELECTED TAX PROVISIONS THAT PREVIOUSLY EXPIRED AFTER 2017

- **Income Exclusion For Discharge Of Up To $2,000,000 Of Qualified Principal Residence Indebtedness.** The exclusion for discharge of *"qualified acquisition indebtedness"* on a principal residence ***applies to DISCHARGES*** *of qualified principal residence debt* ***OCCURRING THROUGH 2020.***

- **Deduction For Qualified Higher Education Expenses.** The "for AGI" deduction for qualified higher education expenses (up to $4,000) ***APPLIES THROUGH 2020.***

- **Premiums For Mortgage Insurance Deductible As Qualified Residence Interest.** The deduction for ***"qualified mortgage insurance premiums"*** as qualified residence interest ***applies to AMOUNTS PAID THROUGH 2020 and not properly allocable to any period after 2020.***

- **Credit For Qualified Energy-Efficient Home Improvements.** The 10% credit for qualified energy-efficient home improvements with a ***lifetime limit*** of $500 (reduced by any credits claimed after 2005*)* ***applies to PROPERTY PLACED IN SERVICE BEFORE 2021.***

- **Credit For Builders Of Energy-Efficient New Homes.** Contractors and manufacturers receive a credit for the construction of qualified energy-efficient new homes that achieve a 30% or 50% reduction in heating and cooling energy consumption relative to a comparable dwelling. The credit equals $1,000 for manufactured homes meeting a 30% efficiency standard and $2,000 for homes meeting a 50% standard. This credit ***applies to HOMES ACQUIRED FROM THE CONTRACTOR OR MANUFACTURER BEFORE 2021.***

- **Up-Front Deduction For Energy Efficient Improvements To Commercial Buildings**. The up-front deduction of up to $1.80 per square foot for the cost of qualifying energy-efficient property installed in a commercial building ***applies to PROPERTY PLACED IN SERVICE BEFORE 2021***.

- **Credit For Alternative Fuel Vehicle Refueling Property.** The credit for qualified alternative fuel vehicle refueling property ***applies to PROPERTY PLACED IN SERVICE BEFORE 2021.***

- **Credit For New Qualified Fuel Cell Motor Vehicles.** The credit for qualified fuel cell motor vehicles ***applies to VEHICLES PURCHASED BEFORE 2021.***

- **Credit For Electric Motorcycles.** Provides a 10-percent credit for qualifying plug-in electric motorcycles with a battery capacity of at least 2.5 kilowatt-hours and capable of achieving speeds of at least 45 miles per hour. The maximum credit for any qualifying vehicle is $2,500. The Consolidated Appropriations Act, 2020 extends the credit for electric motorcycles ***PLACED IN SERVICE BEFORE 2021.***

SELECTED TAX PROVISIONS THAT EXPIRED AFTER 2018

- **Decrease In Medical Expense Deduction Subtraction From 10% To 7.5%.** The *medical deduction subtraction amount is* ***7.5%-of-AGI*** for ***all individuals*** for tax years beginning ***after 2016 and BEGINNING BEFORE 2021.***

- **Elimination Of Deduction For Alimony.** Generally, effective for any "*Divorce or Separation Instrument" **executed after 2018,*** the deduction for alimony and separate maintenance payments is eliminated and such payments will not be includible in the income of the payee. ***NO CHANGE*.**

- **Shared Responsibility Tax (SR Tax).** The SR Tax for an individual failing to carry ACA approved health insurance is reduced **to ZERO after 2018.** ***NO CHANGE.***

SELECTED TAX PROVISIONS SCHEDULED TO EXPIRE OR BE REDUCED AFTER 2019

- **The Work Opportunity Tax Credit.** The Work Opportunity Tax Credit (WOTC) is available on an elective basis for employers hiring individuals from one or more of certain targeted groups. The WOTC is **ALLOWED FOR EMPLOYEES BEGINNING WORK BEFORE 2021.**

- **30% Individual Energy Credit For "Qualified Fuel Cell Property," "Qualified Small Wind Energy Property," "Qualified Solar Electric Property," "Qualified Solar Water Heating Property," And "Qualified Geothermal Heat Pump Property".** These 30% credits apply to property placed in service ***through 2019.*** The credit is reduced to a **26%** credit for qualified property placed in service in **2020** and **22%** for qualified property placed in service in **2021.** ***NO CHANGE.***

- **30% Business Energy Credit For Qualified Fuel Cell Property, Small Wind Energy Property, Qualified Solar Energy Property, And Fiber-Optic-Distributed Solar Property.** These 30% business credits are **reduced to 26%** for qualified property **where** the **construction** of the property **begins after 2019 and before 2021** and to **22%** for qualified property where the **construction** of the property **begins after 2020 and before 2022.** "Qualified Solar Energy Property" is qualifying solar equipment installed to generate electricity, to heat or cool (or provide hot water for use in) a structure, or to provide solar process heat. ***NO CHANGE.***

- **Health Coverage Tax Credit.** The health coverage tax credit or HCTC allows eligible individuals a refundable credit equal to 72.5% of the premiums paid by the individual for coverage of the individual and qualifying family members under qualified health insurance. An eligible individual is an individual who is **1)** an eligible Trade Adjustment Assistance ("TAA") recipient, **2)** an eligible alternative TAA recipient, **or 3)** an eligible Pension Benefit Guaranty Corporation pension recipient. This credit **EXPIRES AFTER 2020.**

- **Employer Credit For Paid Family And Medical Leave.** The credit for paid family and medical leave is **EXTENDED TO TAXABLE YEARS BEGINNING BEFORE 2021.** Employers may claim an elective general business credit based on eligible wages paid to qualifying employees with respect to qualifying family and medical leave. The credit is equal to 12.5% of eligible wages, if the rate of payment is 50% of such

wages, and is increased by 0.25 percentage points (but not above 25%) for each percentage point that the rate of payment exceeds 50%.

The Act **did not change the tax credit** of up to $7,500 for the purchase of a **"new" Qualified Plug-In Electric Drive Motor Vehicle.** The credit begins to phase out **for a manufacturer's vehicles after at least 200,000 qualifying vehicles manufactured by that manufacturer have been sold for use in the United States** (determined on a cumulative basis for sales after 2009).

RELIEF FOR VICTIMS OF HURRICANE FLORENCE, HURRICANE MICHAEL, AND OF OTHER PRESIDENTIALLY DECLARED DISASTERS AFTER 2017 AND WITHIN 60 DAYS AFTER DECEMBER 20, 2019.

Some benefits provided by the Consolidated Appropriations Act, 2020 are available only to individuals living in and businesses located in "Qualified Disaster Zones" while other benefits are available to individuals and businesses located in a "Qualified Disaster Area."

INCREASED CASUALTY LOSS DEDUCTIONS FOR "QUALIFIED DISASTER-RELATED PERSONAL LOSSES".

Generally, individuals who incur personal Federally declared disaster losses **1)** must itemize deductions in order to take the loss, **2)** must reduce the losses from each separate casualty by $100, **and 3)** the total personal disaster casualty losses for a year are not deductible unless they exceed 10% of adjusted gross income (AGI). **The Act changes these requirements for Federally declared casualty losses within a "Qualified Disaster Area."**

- **"Qualified Disaster-Related Personal Losses" ("Qualified Disaster Losses").** "Qualified Disaster Losses" are those personal Federally declared casualty losses which arise in a Qualified Disaster Area to the extent they exceed personal casualty gains (i.e., from any involuntary conversion of property arising from fire, storm, shipwreck, or other casualty, or from theft).

- **Those Taking Standard Deduction May Deduct "Qualified Disaster Losses."** The Act allows individuals with "Qualified Disaster Losses" who do not itemize deductions to increase their standard deduction by a "Qualified Disaster Loss." In addition, even though the standard deduction is not allowed in calculating AMT, a **"Qualified Disaster Loss" will be allowed in computing AMT.**

- **Reduction Of $100 Per Casualty Increased To $500 Per Casualty.** The $100 reduction in losses related to a particular casualty is increased to $500 for "Qualified Disaster Losses."

- **"Qualified Disaster Losses" Not Subject To 10% AGI Threshold.** "Qualified Disaster Losses" are not subject to the 10% of AGI threshold that normally applies to casualty losses.

SPECIAL RULES FOR LOANS AND DISTRIBUTIONS FROM IRAs AND QUALIFIED RETIREMENT PLANS.

The Act provides tax-favored benefits for disaster distributions from IRAs and qualified retirement plans.

FINAL COMMENTS

We have discussed only selected provisions from The Consolidated Appropriations Act that we believe will have the greatest impact on the largest number of our clients. If you have heard of a provision in the New Law that we did not address in this letter (or if you want additional information on a topic we did discuss), please contact us. In addition, please call us before implementing any planning ideas discussed in this letter, or if you need additional information. **Note!** The information contained in this material represents a general overview of selected provisions in The Consolidated Appropriations Act and should not be relied upon without an independent, professional analysis of how any of the items discussed may apply to a specific situation.

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