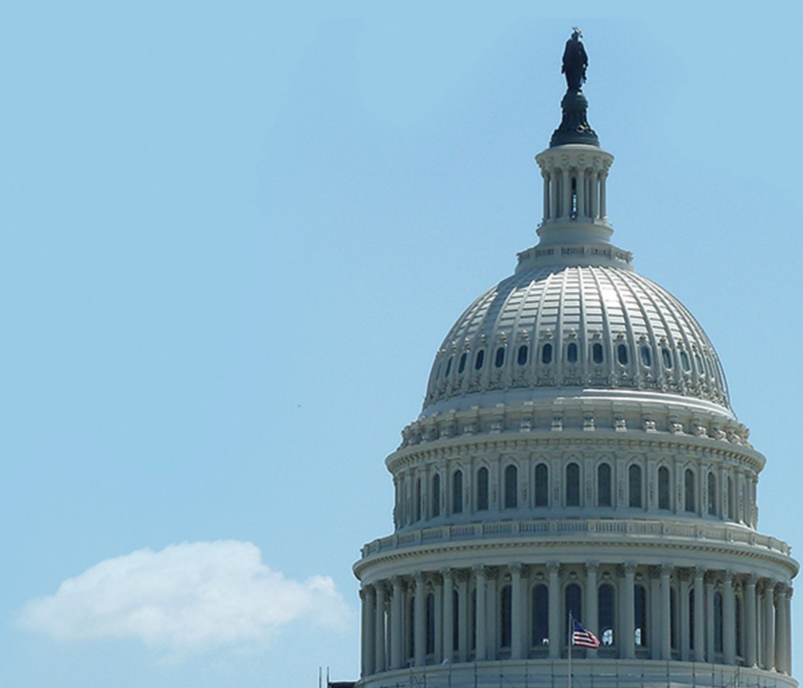
Tax provisions enacted in December 2019 appropriations legislation



December 21, 2019

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President Trump on December 20, 2019, signed into law H.R. 1865 ("The Further Consolidated Appropriations Act, 2020"), a government funding bill that includes significant tax provisions addressing:

- Extensions of 34 expired or expiring provisions—as well as disaster tax relief
- Repeal of the medical device excise tax, the annual fee on health insurance providers, and the excise tax on high cost employer-sponsored health coverage (sometimes referred to as the "Cadillac tax")—as well as an extension of the Patient-Centered Outcomes Research Institute (PCORI) fee under Code sections 4375 and 4376
- Changes to retirement savings and pensions (the "SECURE" Act) as well as to miners' pensions and related matters (the "Bipartisan American Miners Act of 2019")
- Repeal of modifications to the treatment of unrelated business taxable income that had been made by the 2017 tax law commonly referred to as the Tax Cuts and Jobs Act—or TCJA
- Modifications to the excise tax on private foundations
- Modification of rules for determining tax-exempt status of certain mutual or cooperative telephone or electric companies
- Modification of TCJA rules relating to taxation of unearned income of certain children (repeal of Code section 1(j)(4))
- Revenue raisers relating to modification of required distribution rules for designated beneficiaries (relevant to so-called "stretch IRAs"), reduction in minimum age for certain allowable in-service distributions (included in miners' pension provisions), increase in the Code section 6651 failure-to-file penalty, increase in the Code section 6652 penalty for failure to file retirement plan returns, and increased information sharing relating to excise taxes

According to the Joint Committee on Taxation (JCT), the revenue provisions of H.R. 1865 would lose approximately $426 billion (net) over a 10-year period.

As indicated above, the new law includes some substantive changes to TCJA provisions. However, it does not address errors made in drafting the TCJA (i.e., TJCA technical corrections). Thus, for example, it does not correct errors made in drafting provisions relating to the depreciation of qualified improvement property ("QIP"), the effective date of net operating loss ("NOL") deduction changes, or the deduction of legal fees in connection with sexual misconduct.

This report provides more information, as well as preliminary analysis and observations, regarding some of the key tax provisions in the new law.

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Background

H.R. 1865 is one of two appropriations bills enacted December 20, 2019, that fund the government for the 2020 fiscal year. Prior to enactment of the bills, the government was operating at fiscal year (FY) 2019 funding levels under a continuing resolution that was scheduled to expire on December 20, 2019. Enactment of these bills prevents a government shutdown.

H.R. 1865 includes four "divisions" with revenue provisions—Divisions M, N, O, and Q.

Expiring or expired provisions and disaster relief

Division Q is referred to as the "Taxpayer Certainty and Disaster Tax Relief Act of 2019" and was added to H.R. 1865 as an amendment during House consideration.

Extenders—In general

Division Q includes extensions of 34 tax provisions that either had already expired or that were scheduled to expire. Some of the tax provisions extended are:

- The look-through rule for payments between related controlled foreign corporations
- The New Markets Tax Credit
- The Work Opportunity Tax Credit (WOTC)
- The credit for electricity from renewable resources (PTC)
- Reduction in medical expense deduction floor

- Railroad track maintenance credit
- Biodiesel and renewable diesel credit
- Alternative fuel and alternative fuel mixture credit
- Empowerment Zone tax incentives
- TCJA craft beverage provisions

The law generally extends provisions through 2020, although the biodiesel and renewable diesel credit and the credit for short line railroad track maintenance were extended through 2022. The law also delays the phase-out of the energy credit for wind (but not solar) facilities and modifies the wind phase-out percentages.

In addition, incentives that already had expired (some as long ago as the end of 2017) generally are extended retroactively to the date of expiration.

KPMG observation

Given that some of the tax incentives that were extended had expired as of the end of 2017, otherwise eligible taxpayers generally could not use the incentives on their 2018 returns. Although the new law provides specific instructions to the IRS about issuing guidance for taxpayers to obtain one-time payments of the alternative fuel and biodiesel mixture credits, it does not provide a "blanket" rule as to how taxpayers and the IRS should address questions associated with the impact of retroactive extensions on 2018 returns (particularly in situations in which elections needed to be made by the extended due date of such returns). Hopefully, the IRS will issue guidance on these issues.

The JCT estimated that the extension of expired or expiring provisions would cost approximately $39.2 billion in total over 10 years.

Alternative fuel mixture credit "clarification"

The new law makes a "clarification" to the rules regarding the alternative fuel mixture credit. The law provides that the following alternative fuels do not qualify for the alternative fuel mixture credit: liquefied petroleum gas, compressed natural gas, liquefied natural gas, and compressed or liquefied gas derived from biomass.

The effective date of this clarification is for fuel sold or used on or after enactment date, and for fuel sold or used before enactment, but only to the extent that claims for the alternative fuel mixture credit for such sale or use have not been paid or allowed and were made on or after January 8, 2018. The law also provides a "no inference" provision stating nothing in the clarification shall be construed to create any inference as to a change in law or guidance in effect prior to enactment.

KPMG observation

A number of taxpayers filed alternative fuel mixture claims with respect mixtures containing the alternative fuels that are now excluded under the "clarification." The IRS issued Revenue Ruling 2018-02 on January 8, 2018, holding these claims do not qualify for the alternative fuel mixture credit. The validity of the claims for these mixtures is currently being litigated by taxpayers and the

IRS. Should taxpayers prevail in court against the IRS's position in Revenue Ruling 2018-02, the JCT has estimated that the potential payments of refunds for these at-issue alternative fuel mixture claims would be $8.4 billion.

Oil spill excise tax and coal excise tax

The law also includes provisions reinstating the oil spill excise tax imposed on crude oil and imported petroleum products and raising the rates on the coal excise tax. Given the date of enactment, the effective date of these provisions is January 1, 2020.

Disaster relief tax provisions

Division Q also included a number of disaster relief changes. These proposals include an employee retention credit for employers affected by qualified disasters as well as special disaster-related rules for use of retirement funds, personal casualty losses and charitable contributions.

Healthcare-related tax issues

Division N repeals three taxes that were enacted as part of the Patient Protection and Affordable Care Act:

- The medical device excise tax (MDET) is repealed effective for sales after December 31, 2019.
- The 40% excise tax on high-cost employer-sponsored health plans (the so-called "Cadillac" tax) is repealed for tax years beginning after December 31, 2019.
- The annual fee on health insurance providers is repealed, but not until calendar years beginning after December 31, 2020.

The JCT estimated that the 10-year revenue cost of repeal of these taxes is approximately $373.3 billion.

KPMG observation

Repeal of MDET: The MDET was in effect for 2013-2015 but has been suspended under a moratorium for the last four years. Repeal of this tax is welcomed by medical device manufacturers who have been advocating repeal since the MDET's enactment.

KPMG observation

Repeal of the Cadillac tax: When enacted, the excise tax on high-cost, employer-sponsored health coverage was designed to apply to "expensive" health coverage and related expenses paid for by employers at a rate of 40% for such healthcare coverage. Originally scheduled to take effect in 2018, the implementation of the tax had been delayed twice and was scheduled to apply beginning in 2022. In July, the U.S. House of Representatives passed a bill to repeal the excise tax (read ***TaxNewsFlash***), but that bill was not taken up in the Senate.

KPMG observation

Repeal of the annual health insurer fee: The annual health insurer fee was suspended for the 2017 and 2019 fee years, so health insurers were not required to pay the fee in those two years. The fee is in effect in 2020; however, the new law repeals it for calendar years beginning after December 31, 2020. Therefore, health insurers subject to the fee are required to file IRS Form 8963 in April 2020 for the 2019 data year and pay the fee by September 30, 2020.

Division N of the new law also includes an extension of the healthcare inflation-adjusted excise taxes imposed by Code sections 4375 and 4376 (commonly referred to as the "PCORI fee") on health insurance policies and self-insured health plans through 2029. These taxes were originally scheduled to expire for policy years and plan years ending after September 30, 2019. Further, the law includes authorization through 2029 of the transfer of funds raised through these fees to the Patient-Centered Outcomes Research Trust Fund (PCORTF) and authorization for certain expenditures from the fund.

KPMG observation

Affected health insurers and plan sponsors of self-insured health plans need to file a second quarter federal excise tax return (IRS Form 720) and pay the fee in 2020. A similar provision was passed by the House Ways and Means Committee earlier this year (read ***TaxNewsFlash***) but would have only extended the fee through 2026.

In addition, the "extenders" division of the law addresses the medical expense deduction floor. Immediately prior to the enactment of the TCJA, individuals could deduct qualified medical expenses in excess of 10% of adjusted gross income (AGI). The TCJA lowered the threshold for the medical expense deduction to 7.5% of AGI for tax years 2017 and 2018, with the 10% AGI threshold scheduled to resume after 2018. Under the new law, the 7.5% AGI threshold is reinstated for tax years 2019 and 2020 for regular and alternative minimum tax purposes.

SECURE Act retirement savings and pensions provisions

Division O includes the retirement savings changes of the "Setting Every Community Up for Retirement Enhancement Act" (SECURE Act).

In general

The new law includes provisions intended to expand and preserve retirement savings, as well as "administrative improvements." For example, provisions include:

- *Repeal maximum age for allowing contributions to a traditional IRA*. This provision allows working individuals to continue to make contributions to an IRA past age 70.5 (which is the current age limit). This provision is effective for contributions made for tax years beginning after December 31, 2019.

KPMG observation

ROTH IRAs and 401(k) plans already allow participants to continue to make contributions if they continue working past age 70.5, so this change brings traditional IRAs in line with other contributory plans.

- *Required minimum distributions (RMD) would start at age 72 instead of age 70.5*. However, this change only affects those who did not attain age 70.5 by end of 2019. This change allows participants to defer distributions and grow their savings for a longer period. This provision is effective for distributions required to be made after December 31, 2019 for individuals who attain age 70.5 after such date.

- *Increase automatic contribution limits to 15%.* 401(k) plans can provide for automatic employee contributions. However, there are limits on the amount that can be automatically contributed. The limit has been 10%, but this change allows plans to have automatic contributions up to 15%. This provision is effective for plan years beginning after December 31, 2019.

KPMG observation

This change allows for increased participant savings. Increased savings by rank and file employees can help plans pass required nondiscrimination testing as well.

- *Penalty-free distributions for birth of child or adoption*. This provision allows a penalty-free distribution of up to $5,000 from an IRA or certain defined contribution plans after the birth or adoption of a child. Prepayment to the retirement plan is allowed. This provision is effective for distributions made after December 31, 2019.

- *Qualified cash or deferred arrangements must allow long-term part-time employees to participate*. Long-term employees must provide consecutive service for three years and work more than 500, but less than 1,000, hours per year to participate. While these new participants can make contributions, the employer is not required to make matching or non-elective contributions for these part-time participants. Further, participation of part-time employees is not considered for purposes of top-heavy testing or certain other nondiscrimination test. This amendment is effective for plan years beginning after December 31, 2020.

KPMG observation

401(k) plans are usually provided for full-time employees. This provision provides opportunity for certain part-time employees to increase retirement savings. While employers may have additional administrative expenses, this provision does not require employer to extend matching contribution to part-time employees.

- *Pooled multiple employer plans*. This provision allows unrelated, small employers to join a pooled retirement plan. A designed pooled plan provider is selected as the fiduciary and plan administrator responsible for operating the plan. The designed pooled plan provider registers with the IRS. Each employer participating in a pool plan is treated as the plan sponsor for their portion of the plan attributable to their employees. This provision is effective for plan years beginning after December 31, 2020.

KPMG observation

This provision may allow smaller employers an easier opportunity to provide their employees with access to retirement savings.

Revenue offsets, including "stretch IRA" provision

The approximately $16 billion estimated revenue cost of the SECURE Act enhancements is offset by a provision affecting "stretch IRAs" that is estimated to raise a significant amount of revenue, as well as by certain procedural and penalty provisions that raise a smaller amount of revenue. Specifically, Division O includes:

- *Removal of required minimum distribution provisions for stretch IRAs*. Non-spouse designated beneficiaries of an IRA would generally be required to take distributions over 10 years instead of distributions over the designated beneficiary's lifetime. This provision generally is effective for those dying after December 31, 2019. The JCT estimated that this provision would raise approximately $15.75 billion over 10 years.

KPMG observation

This provision does not change rules for an IRA inherited by a spouse.

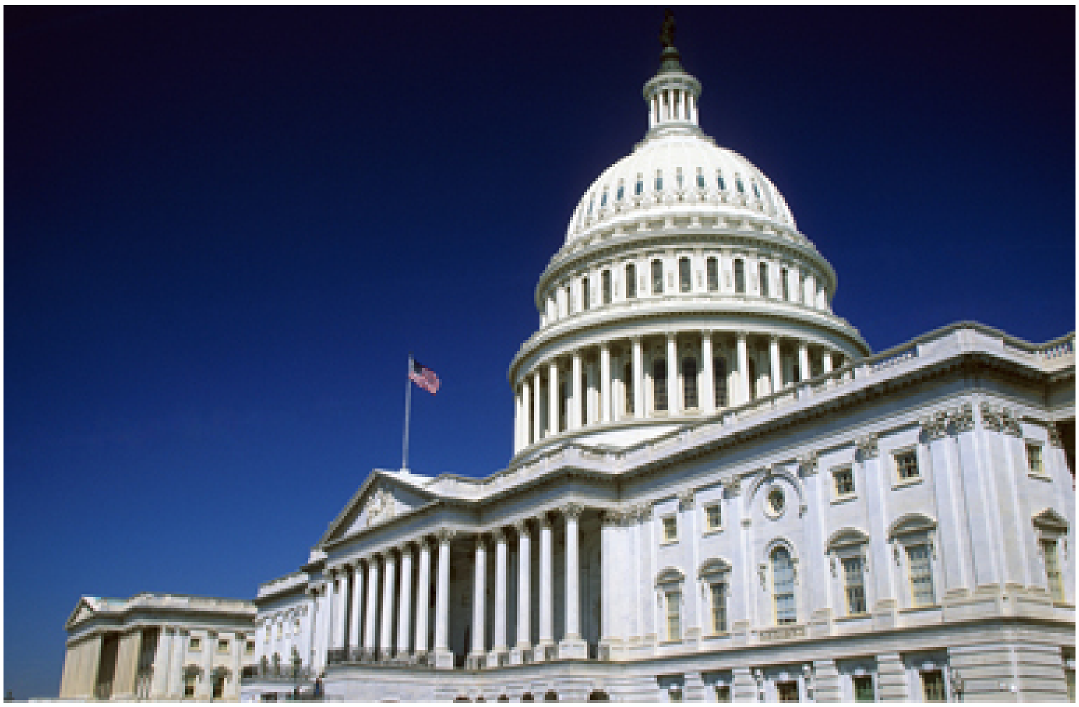
- *Increased failure-to-file penalty*. The law increases the Code section 6651 failure-to-file penalty from $330 to $435, effective for returns the due date of which (including extensions) is after December 31, 2019 (estimated to raise approximately $39 million over a 10-year period).

KPMG observation

The failure-to-file penalty was increased earlier this year as part of an IRS administration bill. Read ***TaxNewsFlash***

- *Increased section 6653 penalty*. The law increases penalties under Code section 6653 for failure to file retirement plan returns (estimated to raise approximately $260 million over a 10-year period).

- *Information sharing*. The law provides for increased information sharing to administer excise taxes (estimated to raise approximately $160 million over a 10-year period).



Miners' pensions

Division M of the new law contains the "Bipartisan American Miners Act of 2019," which provides a number of proposals addressing the 1977 United Mine Workers Association pension plan and other related matters. Division M includes an amendment to Code section 401(a)(36) that reduces the minimum age for allowable in-service distributions. The JCT estimated that this provision would raise approximately $1.3 billion over a 10-year period.

Tax-exempt issues

Division Q of the new law includes provisions relating to tax-exempt organizations.

Repeal of "parking tax"

The legislation repeals what is commonly referred to as the "parking tax"—that is, section 512(a)(7), which requires tax-exempt organizations to include in unrelated business taxable income the amounts they pay or incur on qualified transportation fringe benefits. Section 512(a)(7) was enacted as part of the TCJA.

The repeal takes effect retroactively, as if it had been included in the TCJA.

KPMG observation

Because the repeal of section 512(a)(7) is retroactive back to the date of enactment, organizations that paid UBIT on their employees' qualified transportation fringe benefits presumably may be entitled to a refund of all such UBIT.

Modify rate for excise tax on private foundation investment income

Division Q also includes a provision that would change the current two-tiered excise tax rate applicable to investment income of certain private foundations (Code section 4940(a)) to a single 1.39% rate. This provision applies to tax years beginning after the date of enactment (i.e., beginning after December 20, 2019).

The JCT estimated that this provision would have negligible revenue effect over a 10-year period.

KPMG observation

Changing the private foundation excise tax from a two-tier rate to a flat 1.39% tax is expected to increase the excise tax paid by some private foundations and to decrease the amount paid by others. However, the administrative burden of calculating the tax may be reduced for all private foundations.

Cooperative telephone and electric companies

Division Q also includes a measure modifying the rules for determining the tax-exempt status of certain mutual or cooperative telephone or electric companies. The provision generally allows mutual or cooperative telephone or electric companies to exclude from income certain government grants when applying the requirement under Code section 501(c)(12) that 85% or more of their income must consist of amounts collected from members. The provision is effective retroactive to tax years beginning after December 31, 2017.

The JCT estimated that this provision would lose approximately $34 million over a 10-year period.

KPMG observation

The TCJA amended Code section 118 to provide that contributions after December 22, 2017 "by any governmental entity or civic group" that was not a shareholder could no longer be excluded from income as a contribution to capital. This caused section 501(c)(12) cooperatives to be concerned that they would have to recognize government grants as non-member income, thereby jeopardizing their tax-exempt status. Although the new provision is retroactive to tax years beginning after December 31, 2017, it appears that government grants made after December 22, 2017 and before the first day of a cooperative's first tax year beginning after December 31, 2017 could still adversely affect the cooperative's tax-exemption under section 501(c)(12).

Unearned income of children

Division O includes a provision modifying the taxation of unearned income of certain children (the "kiddie tax"). The provision, sometimes referred to as the "Gold Star Family" proposal, strikes paragraph (4) of Code section 1(j)—a paragraph added by the TCJA that increased the tax rate on certain income of children.

This change is generally effective for tax years beginning after December 31, 2019. However a taxpayer may elect for the change to apply retroactively to tax years beginning in 2018 or 2019.

The JCT estimated that this change would lose approximately $470 million over a 10-year period.

KPMG observation

Concerns had been raised that the change made by the TCJA to the kiddie tax was affecting a broader segment of taxpayers than had been anticipated when the TCJA was enacted—such as surviving children of military members who had been lost in action (i.e. Gold Star families). Gold Star families receive survivor benefits, some of which are payable to the surviving children. Prior to the TCJA's modification of the kiddie tax, these benefits would be taxable to a child at the parent's marginal tax rate. The TCJA provided for taxing these benefits at estate and trust rates, which apply at much lower income thresholds compared to individual rates.

Revenue raisers

Read the **discussion of the SECURE Act** above for a list of revenue raisers used to offset the costs of those provisions. These raisers relate to "stretch IRAs" penalties, and excise tax information sharing.

As also **indicated above**, the miners' pensions part of the bill includes a provision that has been scored as a revenue raiser; this provision relates to reducing the minimum age for allowable in-service distributions.

Documents

- Read the text of **H.R. 1865** [PDF 1.8 MB] [add link]

- Read the **JCT revenue table**

- Read *TaxNewsFlash* for previous House and Senate action on the legislation:
  - **Congress approves government funding, with tax provisions**
  - **House approves government funding bills, including tax provisions**
  - **Government funding bills include some tax provisions**

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