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Dear Clients and Friends:

I hope that you have enjoyed a good start to 2021 and are continuing to keep yourself, your loved ones, and your community safe from COVID-19 (the Coronavirus).

The purpose of this letter is to update you on key tax provisions in recent COVID relief legislation that affect individuals and businesses. The legislation is the COVID-related Tax Relief Act of 2020 (the "COVID Act" or COVIDTRA) and the Taxpayer Certainty and Disaster Tax Relief Act of 2020 (the "Relief Act" or TCDTR), both of which are part of the Consolidated Appropriations Act of 2021 (signed into law at the beginning of the year).

TAX CHANGES WHICH IMPACT INDIVIDUAL TAXPAYERS:

Direct-To-Taxpayer Recovery Rebate. The COVID Act provides for a refundable recovery rebate credit for 2020. This recovery rebate credit is in addition to the direct taxpayer payments / rebates provided for in earlier Federal legislation, the 2020 Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act"). The amount of the recovery rebate credit is $600 per taxpayer ($1,200 for married taxpayers filing jointly), plus $600 per qualifying child. Nonresident aliens, persons who qualify as another person's dependent, and estates or trusts don't qualify for the recovery rebate credit. The recovery rebate credit is phased out at a rate of $5 per $100 of additional income starting at $150,000 of modified adjusted gross income for marrieds filing jointly and surviving spouses, $112,500 for heads of household, and $75,000 for single taxpayers.

The Treasury was directed to pay this recovery rebate credit in advance to eligible individuals in 2021. The Treasury has already completed its advance payments of this recovery rebate credit (based on taxpayers' information on 2019 tax returns). If a taxpayer did not receive advance payment of their full recovery rebate credit, the taxpayer can claim the remaining balance of the recovery rebate credit on their 2020 tax return. If the amount of the recovery rebate credit determined on the taxpayer's 2020 return exceeds the amount of the advance payment previously paid to the taxpayer, the taxpayer will receive the difference as a refundable tax credit.

Taxpayers who receive an advance payment that exceeds the amount of their eligible recovery rebate credit (as later calculated on the 2020 return) will not have to repay any of the advance payment.

Internal Revenue Service Treasury Regulations require that I inform you that, to the extent that this communication or its attachments concern federal tax issues, any advice contained in this communication or any attachment thereto is not intended or written to be used, and cannot be used, to avoid penalties under the Internal Revenue Code.

Advance payments of the recovery rebate credit are generally not subject to offset for past due federal or state debts, and they are protected from bank garnishment or levy by private creditors or debt collectors.

Pro-Taxpayer Changes To CARES Act Economic Impact Payment Rules. As noted above, the CARES Act also provided for direct taxpayer payments/rebates (known as "Economic Impact Payments"). The COVID Act makes the following changes to the rules for Economic Impact Payments under the CARES Act:

- Provides that the $150,000 limit on adjusted gross income (for joint returns) before the Economic Impact Payment starts to phase out still applies to joint returns filed by surviving spouses. This change may allow surviving spouses who qualify to file a joint return to claim a larger Economic Impact Payments on their 2020 returns.

- Makes the requirement to provide the IRS with the taxpayer's identification number identical to the taxpayer identification number requirement under the new recovery rebate credit described above.

$250 Educator Expense Deduction Applies To PPE And Other COVID-Related Supplies. The COVID Act provides that eligible educators (i.e., K-12 teachers, instructors, etc.) can claim the existing $250 above-the-line educator expense deduction for personal protective equipment (PPE), disinfectant, and other supplies used for the prevention of the spread of COVID-19 that were bought after March 12, 2020. The IRS is directed to issue guidance to that effect by February 28, 2021.

7.5% AGI "Floor" On Medical Expense Deductions Is Made Permanent. The COVID Act makes permanent the "7.5% of adjusted gross income" threshold on medical expense deductions. The lower threshold will allow more taxpayers to take the medical expense deduction in 2021 and later years.

Mortgage Insurance Premium Deduction Is Extended By One Year. The COVID Act extends the deduction for qualifying mortgage insurance premiums through 2021. The deduction is subject to a phase-out based on the taxpayer's adjusted gross income.

Above-The-Line Charitable Contribution Deduction Is Extended Through 2021; Increased Penalty For Abuse. For 2020, individuals who don't itemize deductions can take up to a $300 above-the-line deduction for cash contributions to "qualified charitable organizations." The COVID Act extends this above-the-line deduction through 2021 and increases the deduction allowed on a joint return to $600 (it remains at $300 for other taxpayers). Taxpayers who overstate their cash contributions when claiming this deduction are subject to a 50% penalty (previously it was 20%).

Extension Through 2021 Of Allowance Of Charitable Contributions Up To 100% Of An Individual's Adjusted Gross Income. In response to the COVID pandemic, the limit on cash charitable contributions by an individual in 2020 was increased to 100% of the individual's adjusted gross income. The COVID Act extends this rule through 2021. The usual limit is 60% of adjusted gross income.

Exclusion For Benefits Provided To Volunteer Firefighters And Emergency Medical Responders Made Permanent. Emergency workers who are members of a "qualified volunteer emergency response organization" can exclude from gross income certain state or local government payments received and state or local tax relief provided on account of their volunteer services. This exclusion was due to expire at the end of 2020, but the COVID Act made it permanent.

Exclusion For Discharge Of Qualified Mortgage Debt Is Extended, But Limits On Amount Of Excludable Discharge Are Lowered. Usually, if a lender cancels a debt, such as a mortgage, the borrower must include the discharged amount in gross income. But under an exclusion that was set to expire at the end of 2020, a taxpayer can exclude from gross income up to $2,000,000 ($1,000,000 for married individuals filing separately) of discharge-of-debt income if "qualified principal residence debt" is discharged. The COVID Act extends this exclusion through the end of 2025, but lowers the amount of debt that can be discharged tax-free to $750,000 ($375,000 for married individuals filing separately).

Extension Of Exclusion For Certain Employer Payments Of Student Loans. Qualifying educational assistance provided under an employer's qualified educational assistance program, up to an annual maximum of $5,250, is excluded from the employee's income. The CARES Act added "eligible student loan repayments" made after March 27, 2020, and before January 1, 2021, to the types of employer payments that are eligible for this exclusion. Qualifying payments (which are subject to the overall $5,250 per employee limit for all educational payments) include payments of principal or interest on a qualified student loan by the employer, whether paid to the employee or a lender. The COVID Act extends the exclusion for eligible student loan repayments through the end of 2025.

10% Early Withdrawal Penalty Does Not Apply To Qualified Disaster Distributions From Retirement Plans. A 10% early withdrawal penalty generally applies to, among other things, a distribution from employer retirement plan to an employee who is under the age of 59½. The COVID Act provides that the 10% early withdrawal penalty doesn't apply to any "qualified disaster distribution" from an eligible retirement plan. The aggregate amount of distributions received by an individual that may be treated as qualified disaster distributions for any tax year may not exceed the excess (if any) of $100,000, over the aggregate amounts treated as qualified disaster distributions received by that individual for all prior tax years.

Increased Limit For Plan Loans Made Because Of A Qualified Disaster. Generally, a loan from a retirement plan to a retirement plan participant cannot exceed $50,000. Plan loans over this amount are considered taxable distributions to the participant. The COVID Act increases the allowable amount of a loan from a retirement plan to $100,000 if the loan is made because of a qualified disaster and meets various other requirements.

Individuals May Elect To Base 2020 Refundable Child Tax Credit (CTC) And Earned Income Credit (EIC) On 2019 Earned Income. If a taxpayer's child tax credit (CTC) exceeds the taxpayer's tax liability, the taxpayer is eligible for a refundable credit equal to 15% percent of that portion of the taxpayer's taxable "earned income" for the tax year in excess of $2,500. In addition, the earned income credit (EIC) equals a percentage of the taxpayer's "earned income." For both of these credits, earned income means wages, salaries, tips, and other employee compensation, if includible in gross income for the tax year. But for determining the refundable

CTC and the EIC for 2020, the COVID Act allows taxpayers to elect to substitute the earned income for the preceding tax year if that amount is greater than the taxpayer's earned income for 2020.

Health Coverage Tax Credit (HCTC) For Health Insurance Costs Of Certain Eligible Individuals Is Extended By One Year. A refundable credit (known as the health coverage tax credit or "HCTC") is allowed for 72.5% of the cost of health insurance premiums paid by certain individuals (i.e., individuals eligible for Trade Adjustment Assistance due to a qualifying job loss, and individuals between 55 and 64 years old whose defined-benefit pension plans were taken over by the Pension Benefit Guaranty Corporation). The HCTC was due to expire at the end of 2020, but the COVID Act extended it through 2021.

New Markets Tax Credit Extended. The New Markets credit provides a substantial tax credit to both individual and corporate taxpayers that invest in low-income communities. This credit was due to expire at the end of 2020, but the COVID Act extended it through the end of 2025. Carryovers of the New Markets credit were extended, as well.

Nonbusiness Energy Property Credit Extended By One Year. A credit is available for purchases of "nonbusiness energy property" (i.e., qualifying energy improvements to a taxpayer's main home). This nonbusiness energy property credit was due to expire at the end of 2020, but the COVID Act extends this credit through 2021.

Qualified Fuel Cell Motor Vehicle Credit Extended By One Year. The credit for purchases of new qualified fuel cell motor vehicles (which was due to expire at the end of 2020) was extended by the COVID Act through the end of 2021.

2-Wheeled Plug-In Electric Vehicle Credit Extended By One Year. The 10% credit for highway-capable, two-wheeled plug-in electric vehicles (capped at $2,500) was extended until the end of 2021 by the COVID Act.

Residential Energy-Efficient Property (REEP) Credit Extended By Two Years, Bio-Mass Fuel Property Expenditures Included. Individual taxpayers are allowed a personal tax credit, known as the residential energy efficient property (REEP) credit, equal to the applicable percentages of expenditures for qualified solar electric property, qualified solar water heating property, qualified fuel cell property, qualified small wind energy property, and qualified geothermal heat pump property. The REEP credit was due to expire at the end of 2021, with a phase-down of the credit operating during 2020 and 2021. The COVID Act extends the phase-down period of the credit by two years-through the end of 2023. The REEP credit won't apply after 2023. The COVID Act also adds qualified biomass fuel property expenditures to the list of expenditures qualifying for the credit, effective beginning in 2021.

TAX PROVISIONS WHICH EFFECT BUSINESSES:

Clarifications Of Tax Consequences Of PPP Loan Forgiveness. The COVID Act clarifies that the non-taxable treatment of Payroll Protection Program (PPP) loan forgiveness that was provided by the 2020 CARES Act also applies to certain other forgiven obligations. Also, the COVID Act clarifies that taxpayers whose PPP loans or other obligations are forgiven are still

allowed to take deductions for otherwise deductible expenses paid with the PPP loan proceeds and that the tax basis and other attributes of the borrower's assets won't be reduced as a result of the forgiveness.

Waiver Of Information Reporting For PPP Loan Forgiveness. The COVID Act allows IRS to waive information reporting requirements for any amount excluded from income under the exclusion- from-income rule for forgiveness of PPP loans or other specified obligations. Note: IRS had already waived information returns and payee statements for loans that (before enactment of the COVID Act) were guaranteed by the Small Business Administration under section 7(a)(36) of the Small Business Act.

Extensions And Modifications Of Earlier Payroll Tax Relief. The Relief Act extends the CARES Act credit allowed against the employer portion of the Social Security (OASDI) payroll tax or of the Railroad Retirement tax for qualified wages paid to employees during the COVID-19 crisis. Under the extension, qualified wages must be paid before July 1, 2021 (instead of January 1, 2021). Additionally, beginning on January 1, 2021, the credit rate is increased from 50% to 70% of qualified wages, and qualified wages are increased from $10,000 for the year to $10,000 per quarter. The Relief Act makes some retroactive clarifications and technical improvements to the credit as initially enacted and relaxes other rules to claim the credit.

The COVID Act also extends (i) the credits provided by the Families First Coronavirus Response Act (FFCRA) against the employer portion of OASDI and Railroad Retirement taxes for qualifying sick and family paid leave, and (ii) the equivalent FFCRA-provided credits for the self-employed against the self-employment tax. Under the extension of the employer credits, wages taken into account are those paid before April 1, 2021 (instead of January 1, 2021). Under the extension of the credits for the self-employed, the days taken into account are those before April 1, 2021 (instead of January 1, 2021).

The COVID Act also makes retroactive clarifications of (i) the employer (but not self-employed equivalent) FFCRA paid leave credits that were extended as discussed above, (ii) the exclusion of qualifying paid leave in calculating the employer portion of Railroad Retirement taxes, and (iii) the increase in the amount of the FFRCA paid leave credits against the employer portion of Railroad Retirement taxes by the amount of the Medicare payroll taxes on qualifying paid leave. Additionally, the COVID Act directs IRS to extend the Presidentially ordered deferral of the employee's share of OASDI and Railroad Retirement taxes. As first provided by IRS, the deferral was of taxes to be withheld and paid on wages and other compensation (up to $4,000 every two weeks) paid in the period from September 1, 2020 to December 31, 2020 so that the taxes were instead withheld and paid ratably in the period from January 1, 2021 to April 30, 2021. Under the deferral, the period over which the deferred-from-2020 taxes are ratably withheld and paid is extended to all of 2021 (instead of the four-month period ending on April 30, 2021).

Employee Benefits And Deferred Compensation. The Relief Act provides that expenses for business-related food and beverages provided by a restaurant are fully deductible if they are paid or incurred in calendar years 2021 or 2022, instead of being subject to the 50% limit that generally applies to business meals. The Relief Act temporarily allows (i) carryovers and relaxed grace period rules for unused flexible spending arrangement (FSA) amounts, whether in

a health FSA or a dependent care FSA, (ii) the raising of the maximum eligibility age of a dependent under a dependent care FSA from 12 to 13, and (iii) prospective changes in election limits set forth by a plan (subject to the applicable limits under the Code).

With a view to layoffs in the current economic climate, the Relief Act relaxes rules that would otherwise cause a partial qualified retirement plan termination if the number of active participants decreases.

Because of market volatility during the COVID-19 pandemic, the COVID Act relaxes (if certain conditions are met) the funding standards that allow a defined benefit pension plan to transfer funds to a retiree health benefits account or retiree life insurance account within the plan. The CARES Act's relaxed rules for "coronavirus-related distributions" are retroactively amended by the COVID Act to additionally provide that a coronavirus-related distribution that is a during-employment withdrawal from a money purchase pension plan meets the distribution requirements of Code §401(a).

And under a provision of narrow applicability, the Relief Act lowers to 55 years (from the usually applicable 59½ years) the age at which certain employees in the building or construction trades can, though still employed, receive pension plan payments under certain multiple employer plans without affecting the status of trusts that are part of the pension plans as qualified trusts.

Residential Real Estate Depreciation. For tax years beginning after December 31, 2017, the Relief Act assigns a 30-year ADS depreciation period to residential rental property even though the property was placed in service before January 1, 2018 (when the 2017 TCJA first applied the more-favorable 30-year period) if the property (i) is held by a real property trade or business electing out of the limitation on business interest deductions, and (ii) before January 1, 2018 wasn't subject to the ADS.

Farmers' Net Operating Losses. The COVID Act allows farmers who had in place a two-year net operating loss carryback before the CARES Act to elect to retain that two-year carryback rather than claim the five-year carryback provided in the CARES Act. It also allows farmers who, before the CARES Act waived the carryback of a net operating loss, to revoke the waiver.

Low-Income Housing Credit. The Relief Act provides a 4% per year credit floor for buildings that aren't eligible for the 9% per-year low-income housing credit floor. (Both floors are alternatives to the calculation under which the per-year credit is generally a percentage, prescribed by IRS, that is intended to result in a credit that, in the aggregate over the 10-year credit period, has a present value of 70% of the qualified basis for certain new buildings and 30% of the qualified basis for certain other buildings.)

Life Insurance. The Relief Act changes the interest rate assumptions that determine whether a contract meets the cash value and premium caps for qualifying as a life insurance contract. The change is to designated floating rates from the respective 4% and 6% rates fixed by prior law.

Disaster Relief. The Relief Act includes several provisions targeted at "qualified disaster areas," some of which affect individuals and some which affect businesses as described below. "Qualified disaster areas" are areas for which a major disaster was presidentially-declared during

the period beginning on January 1, 2020 and ending February 25, 2021. The incidence period of the disaster must begin after December 27, 2019 but not after December 27, 2020. Excluded are areas for which a major disaster was declared only because of COVID-19.

The relief includes relief for retirement funds that consists of the following: (i) waiver of the 10% early withdrawal penalty for up to $100,000 of certain withdrawals by individuals living in a qualified disaster area and that have suffered economic loss because of the disaster (qualified individuals), (ii) a right to re-contribute to a plan distributions that were intended for home purchase but not used because of a qualified disaster, and (iii) relaxed plan loan rules for qualified individuals. Changes to plan amendment rules facilitate the relief.

The Relief Act also provides to employers in the harder-hit parts of a qualified disaster area an employee retention credit (in an amount up to $2,400 per employee), subject to coordination with certain other employer tax credits. Generally, tax-exempt organizations can take it as a credit against FICA taxes.

Corporations are provided with relaxed charitable deduction rules for qualified-disaster-related contributions, and individuals are provided with relaxed loss allowance rules for qualified-disaster-related casualties.

The low-income housing credit is modified to allow, subject to various limitations, increases in the state-wide credit ceilings to the extent allocations are made to harder-hit parts of qualified disaster areas.

Other Tax Credits and Provisions Extended. The Relief Act also extends a multitude of special or industry-specific tax deductions and credits which were slated for expiration. Most notable are extensions affecting deductions and credits for energy-efficient commercial buildings, the energy and alternative energy industries, low-income housing, the film, theater and live performance industry, the motor sports industry, and empowerment zones.

CALIFORNIA COMFORMITY ON TAX PROVISIONS:

Finally, California still has not conformed the majority of its tax laws to include changes to federal tax laws from 2017 onwards, but it appears that some relief is on the way:

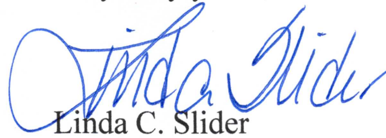
- In March, 2020, California passed legislation to conform state law to the federal CARES Act in a few specific areas, most notably (i) to waive the requirement that taxpayers take their required minimum distribution (RMD) from retirement accounts for 2020, (ii) to permit retirement plan distributions for specific COVID-related distributions, and (iii) to address the tax impact of Payroll Protection Program (PPP) loan forgiveness for taxpayers with tax years starting on or after January 1, 2020. However, the provisions regarding California's PPP loan forgiveness needed further clarification.

- As of the date of this letter, California has not passed legislation to conform state law to any of the provisions contained in either the COVID Act or the Relief Act.

- On February 18, 2021, Governor Newsome and the leaders of the California legislature announced that they have reached an agreement on a package of COVID-relief benefits, including certain tax provisions conforming to federal law and provisions to clarify the treatment of PPP loan forgiveness. However, the text of the actual bill has not been released yet. Taxpayers may want to delay filing of their California returns, pending further clarity on the provisions to be included in this new California COVID-relief bill.

If you or your accountant would like more details about any item discussed in this letter, please do not hesitate to call.

Very truly yours,



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