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Temporary Individual Tax Provisions (“Tax Extenders”)

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Temporary Individual Tax Provisions (“Tax Extenders”)

Nine temporary individual income tax provisions that expired in 2020 were extended or made permanent by the Taxpayer Certainty and Disaster Tax Relief Act of 2020, enacted as Division EE of the Consolidated Appropriations Act, 2021 (P.L. 116-260). The law repealed an additional provision, while modifying a related permanent provision. In the past, Congress has regularly acted to extend expired or expiring temporary tax provisions. These provisions are often referred to as “tax extenders.” A summary of the changes made by P.L. 116-260 is provided below.

Extended through the end of 2021

Two provisions that had been extended in the past were extended through 2021:

- the mortgage insurance premium deduction; and
- the health coverage tax credit.

Three provisions enacted initially in the Coronavirus Aid, Relief, and Economic Security (CARES) Act (P.L. 116-136) for 2020 were extended through 2021:

- the charitable deduction for nonitemizers;
- the increased income limit for charitable deductions for itemizers; and
- flexible spending account rollovers, a midterms election, and other flexibilities.

Extended through the end of 2025

Two provisions were extended through 2025:

- the exclusion for employer payments of student loans; and
- the tax exclusion for canceled mortgage debt.

The student loan provision was enacted in the CARES Act.

Permanent Changes

Two provisions were made permanent:

- the 7.5% floor for the medical expense deduction; and
- benefits for volunteer firefighters and emergency medical responders.

One provision was repealed, but modifications were made in a related provision to benefit those individuals: the above-the-line deduction for qualified tuition and related expenses was repealed, while the income phaseout level for an education tax credit was increased.

This report provides background information on individual income tax provisions that were extended, made permanent, or replaced by the Consolidated Appropriations Act, 2021. For other reports related to extenders, see

- CRS Report R46627, *Tax Provisions Expiring in 2020 (“Tax Extenders”)*, by Molly F. Sherlock;
- CRS Report R46451, *Energy Tax Provisions Expiring in 2020, 2021, 2022, and 2023 (“Tax Extenders”)*, by Molly F. Sherlock, Margot L. Crandall-Hollick, and Donald J. Marples; and
- CRS Report R46271, *Business Tax Provisions Expiring in 2020, 2021, and 2022 (“Tax Extenders”)*, coordinated by Molly F. Sherlock.

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Introduction

Historically, Congress has regularly acted to extend expired or expiring temporary tax provisions.¹ Collectively, these temporary tax provisions are often referred to as “tax extenders.” There are 25 temporary tax provisions, both individual and business, scheduled to expire at the end of 2021, with additional provisions scheduled to expire in the following years. This report discusses expiring *individual income tax* provisions, including expiring provisions that were made permanent in the most recent tax extenders legislation, the Taxpayer Certainty and Disaster Tax Relief Act of 2020, enacted as Division EE of the Consolidated Appropriations Act, 2021 (P.L. 116-260).

Five provisions discussed in this report expire at the end of 2021. Two of these provisions have been extended in the past as part of the tax extenders: (1) the deduction for mortgage insurance premiums; and (2) the tax credit for health insurance costs. Three provisions that were first enacted in the Coronavirus Aid, Relief, and Economic Security (CARES) Act (P.L. 116-136) and originally scheduled to expire in 2020 have been extended through 2021: (1) the charitable deduction for nonitemizers; (2) increases in the income limits for deducting charitable contributions (for itemizers); and (3) the ability to roll over amounts in flexible spending accounts to the next year.

Other provisions are scheduled to expire in 2025.² One is the exclusion for canceled mortgage debt, which has been extended as part of past tax extenders legislation. The exclusion for certain employer payments for student loans, enacted in the CARES Act for 2020, was also extended through 2025.

Other temporary provisions were made permanent in P.L. 116-260: (1) the medical expense deduction adjusted gross income (AGI) floor of 7.5%; and (2) the exclusion for income of certain state and local tax rebates and reimbursement for volunteer firefighters and emergency medical responders. The above-the-line deduction for qualified tuition and related expenses, a provision that was extended in the past as a tax extender, was repealed in concert with an increase in the income limits for phasing out the Lifetime Learning credit (LLC) for higher education.

The estimated cost of the extensions, conversion to permanent provisions, or repeal and revisions in related provisions enacted in the Taxpayer Certainty and Disaster Tax Relief Act of 2020 (P.L. 116-260) is provided in **Table 1**.

¹ For an overview of tax extenders, see CRS Report R46627, *Tax Provisions Expiring in 2020 (“Tax Extenders”)*, by Molly F. Sherlock.

² This report discusses provisions that were part of previous tax extenders legislation, as well temporary provisions that were included in the CARES Act and subsequently extended. The report does not include the many temporary modifications to the individual income tax system, made as part of the 2017 tax revision (the “Tax Cuts and Jobs Act;” P.L. 115-97), that are scheduled to expire in 2025. For additional information, see CRS Report R45092, *The 2017 Tax Revision (P.L. 115-97): Comparison to 2017 Tax Law*, coordinated by Molly F. Sherlock and Donald J. Marples.

Table I. Estimated Cost of Temporary Individual Provisions in P.L. 116-260
(billions of dollars)

Provision	Length of Extension	Cost of Extension in P.L. 116-260
Mortgage Insurance Premium Deductibility	1 year expires 12/31/2021	\$0.2
Health Coverage Tax Credit	1 year expires 12/31/2021	(*)
Certain Charitable Contributions Deductible for Nonitemizers	1 year expires 12/31/2021	\$2.9
Increase in Limits on Charitable Contributions	1 year expires 12/31/2021	\$0.6
Flexible Spending Accounts Rollover	effective for 2020 and 2021 amounts	\$0.1
Exclusion for Employer Payments for Student Loans	5 years expires 12/31/2025	\$3.4
Tax Exclusion for Canceled Mortgage Debt	5 years expires 12/31/2025	\$2.8
Medical Expense Deduction Adjusted Gross Income Floor of 7.5%	permanent	\$32.9
Benefits for Volunteer Firefighters and Emergency Medical Responders	permanent	\$0.7
Repeal of Above-the-Line Deduction for Qualified Tuition and Related Expenses and increases in Credit Income Phaseouts	substantial modification; permanent	\$5.9

Source: Joint Committee on Taxation, *Estimated Budget Effects of the Revenue Provisions Contained in Rules Committee Print 116-68, The "Consolidated Appropriations Act, 2021,"* December 21, 2020, JCX-24-20.

Notes: (*) is less than \$50 million. The cost estimates are estimated reductions in revenue over a 10-year budget period (FY2021-FY2030).

Individual "Tax Extender" Provisions Expiring in 2021

Mortgage Insurance Premium Deductibility³

Traditionally, homeowners who itemize their tax deductions have been able to deduct the interest paid on their mortgages, as well as any property taxes they pay. Beginning in 2007, homeowners could also deduct qualifying mortgage insurance premiums as a result of changes made to the provision included in the Tax Relief and Health Care Act of 2006 (P.L. 109-432). Specifically, homeowners could effectively treat qualifying mortgage insurance premiums as mortgage interest, thus making the premiums deductible if the homeowner itemized, and if the homeowner's adjusted gross income was below a certain threshold (\$55,000 for single, and \$110,000 for married filing jointly). Originally, the deduction was only to be available for 2007,

³ Section 163(h)(3)(E) of the Internal Revenue Code.

but it was extended several times. The deduction was extended through December 31, 2021, in the Taxpayer Certainty and Disaster Tax Relief Act of 2020, enacted as Division EE of the Consolidated Appropriations Act, 2021 (P.L. 116-260).

Taxpayers of all ages may be less likely to claim the mortgage insurance premium deduction compared to prior periods because of other provisions of the 2017 tax revision, popularly known as the Tax Cuts and Jobs Act (TCJA; P.L. 115-97). Specifically the law included a higher standard deduction (in part as a trade-off for the elimination of personal exemptions) and a cap on the deduction of state and local taxes. These changes contributed to an expected reduction in the number of itemizers from about one-third of individual income tax returns to one-eighth (12%).⁴

A justification for the deduction of mortgage insurance premiums is that it helps to promote homeownership and, relatedly, the recovery of the housing market following the December 2007-June 2009 Great Recession. Homeownership is often argued to bestow certain benefits to society, such as higher property values, lower crime, and higher civic participation. Homeownership may also promote a more even distribution of income and wealth, as well as establish greater individual financial security. Furthermore, homeownership may have a positive effect on living conditions, which can lead to a healthier population.

With regard to the first justification, it is not clear that the deduction for mortgage insurance premiums affects the homeownership rate. Economists have identified the high transaction costs associated with a home purchase—mostly resulting from the down payment requirement, but also from closing costs—as the primary barrier to homeownership.⁵ The ability to deduct insurance premiums does not lower this barrier—most lenders will require mortgage insurance if the borrower's down payment is less than 20% regardless of whether the premiums are deductible. The deduction may allow buyers to borrow more, however, because they can deduct the higher associated premiums and therefore afford a higher housing payment.

Concerning the second justification, it is also not clear that the deduction for mortgage insurance premiums is still needed to assist in the housing market's recovery. Based on the S&P CoreLogic Case-Shiller U.S. National Composite Index, home prices have generally increased since the bottom of the market following the Great Recession.⁶ In addition, the available housing inventory is now slightly below its historical level.⁷ Both of these indicators suggest that the market is stronger than when the provision was enacted.

Economists have noted that owner-occupied housing is already heavily subsidized via tax and nontax programs. To the degree that owner-occupied housing is oversubsidized, it could be

⁴ The 12% estimate for 2021 is from Joint Committee on Taxation, *Overview of the Federal Tax system as In Effect for 2021*, JCX-18-21, April 15, 2021, <https://www.jct.gov/publications/2021/jcx-18-21/>.

⁵ See for example, Peter D. Linneman and Susan M. Wachter, "The Impacts of Borrowing Constraints," *Journal of the American Real Estate and Urban Economics Association*, vol. 17, no. 4 (Winter 1989), pp. 389-402; Donald R. Haurin, Patrick H. Hendershott, and Susan M. Wachter, "Borrowing Constraints and the Tenure Choice of Young Households," *Journal of Housing Research*, vol. 8, no. 2 (1997), pp. 137-154; and Mathew Chambers, Carlos Garriga, and Donald Schlagenhauf, "Accounting for Changes in the Homeownership Rate," *International Economic Review*, vol. 50, no. 3 (August 2009), pp. 677-726.

⁶ S&P Dow Jones Indices, S&P CoreLogic Case-Shiller U.S. National Home Price NSA Index, retrieved from FRED, Federal Reserve Bank of St. Louis, <https://fred.stlouisfed.org/series/CSUSHPINSA>, February 25, 2020.

⁷ U.S. Bureau of the Census and U.S. Department of Housing and Urban Development, "Monthly Supply of Houses in the United States," retrieved from FRED, Federal Reserve Bank of St. Louis, <https://fred.stlouisfed.org/series/MSACSR>.

argued that extending the deduction for mortgage insurance premiums would lead to a greater misallocation of resources that are directed toward the housing industry.

Credit for Health Insurance Costs of Eligible Individuals⁸

The credit for health insurance costs of eligible individuals, commonly known as the health coverage tax credit (HCTC), reduces the cost of qualified health insurance for eligible individuals.⁹ To be eligible to claim the HCTC, taxpayers must be (1) an eligible trade adjustment assistance (TAA) recipient,¹⁰ or (2) an eligible Pension Benefit Guaranty Corporation (PBGC) pension recipient.¹¹ Additionally, an individual is not eligible for the HCTC if they have access to "other specified coverage," which includes coverage for which an employer (or former employer) incurs 50% of the cost, as well as Medicare, Medicaid, the Children's Health Insurance Program, and other federal and military health or medical benefit plans.

Under this provision, eligible taxpayers are allowed a refundable tax credit for 72.5% of the premiums they pay for qualified health insurance for themselves and their family members. Eligible taxpayers with qualified health insurance may claim the tax credit (1) when tax returns are filed; or (2) as advance payments, on a monthly basis, throughout the year. This latter option helps taxpayers pay for health plan premiums as they become due. The credit is not available for months beginning on or after January 1, 2021.

The HCTC was originally authorized by the Trade Act of 2002 (P.L. 107-210). The credit has been extended and modified several times. Extensions or modifications have been made in trade adjustment assistance legislation as well as tax extenders legislation. The Trade Preferences Extension Act of 2015 (P.L. 114-27) extended the HCTC through December 31, 2019, and also made changes to address the interaction between the HCTC and the premium tax credit established under the Patient Protection and Affordable Care Act (P.L. 111-148, as amended).¹² The credit was extended through December 31, 2020, in the Taxpayer Certainty and Disaster Tax Relief Act of 2019, enacted as Division Q of the Further Consolidated Appropriations Act, 2020 (P.L. 116-94). It was extended through December 31, 2021, by the Taxpayer Certainty and Disaster Tax Relief Act of 2020, enacted as Division EE of the Consolidated Appropriations Act, 2021 (P.L. 116-260).

Some evidence suggests that the credit has not reached many of the individuals it was designed to help. The credit also provides the same benefit regardless of the eligible individual's income status, therefore providing benefits regardless of ability to pay, but not benefitting others who have experienced economic dislocations beyond their control. The credit's refundability, however, makes it available to the lowest-income individuals.¹³

⁸ Section 35 of the Internal Revenue Code.

⁹ For additional information on this provision, see CRS Report R44392, *The Health Coverage Tax Credit (HCTC): In Brief*, by Bernadette Fernandez.

¹⁰ For more information, see CRS Report R44153, *Trade Adjustment Assistance for Workers and the TAA Reauthorization Act of 2015*, by Benjamin Collins.

¹¹ For more information, see CRS Report 95-118, *Pension Benefit Guaranty Corporation (PBGC): A Primer*, by John J. Topoleski.

¹² For more information, see CRS Report R44425, *Health Insurance Premium Tax Credit and Cost-Sharing Reductions*, by Bernadette Fernandez.

¹³ For more information, see United States Senate, Committee on the Budget, *Tax Expenditures: Compendium of Background Material on Individual Provisions*, 116th Congress, 2nd Session, S.Prt. 116-53, December 2020, pp. 863-869, at <https://www.congress.gov/committee-print/116th-congress/senate-committee-print/42597?s=1&r=42>.

CARES Act and COVID-Related Provisions Expiring in 2021

Charitable Contributions Deductible by Nonitemizers¹⁴

The deduction for charitable contributions is one of an array of tax benefits for charitable giving and tax-exempt organizations.¹⁵ Individuals may take a charitable deduction if they itemize deductions on their tax returns. The Coronavirus Aid, Relief, and Economic Security (CARES) Act (P.L. 116-136) provided for a deduction for cash donations for nonitemizers of up to \$300 through December 31, 2020. That is, taxpayers can deduct these amounts even if they elect the standard deduction. This provision was extended through December 31, 2021, by the Taxpayer Certainty and Disaster Tax Relief Act of 2020, enacted as Division EE of the Consolidated Appropriations Act, 2021 (P.L. 116-260).

The \$300 nonitemizer deduction is likely to have a limited effect on charitable contributions because of its relatively small cap. One study estimated that the induced charitable giving from the nonitemizer deduction would be \$100 million, a relatively negligible effect, because most taxpayers who donate are already contributing amounts in excess of \$300.¹⁶

Increased Limits to Charitable Contributions¹⁷

Prior to the TCJA (P.L. 115-97), the limit on charitable deductions for individuals was 50% of adjusted gross income for gifts (other than gifts of appreciated property) to public charities.¹⁸ (The limit was 30% for gifts of appreciated property, 30% for ordinary gifts to private foundations, and 20% for gifts of appreciated property to private foundations.) The TCJA increased the 50% limit to 60% through 2025 for cash contributions. The TCJA also made unrelated changes through 2025 (i.e., an increased standard deduction and limits on other itemized deductions) that made itemized deductions less attractive and reduced the share of taxpayers with a deduction for charitable contributions from an estimated 25% to 10%.¹⁹ (Note that not all itemizers report charitable deductions, so the share of taxpayers itemizing charitable contributions is smaller than the share of itemizers in general.)

The corporate charitable deduction is limited to 10% of taxable income. Corporations (and individuals, in some instances) are also allowed special deductions for contributions of inventory. Normally, charitable inventory contributions are limited to the lesser of basis (cost) or fair market value, with inventory reduced by the contributions (as a result of this limitation, any inventory cost that is in excess of fair market value can still be deducted in calculating taxable income as the cost of goods sold). For C corporations contributing inventory to 501(c)(3) organizations for

¹⁴ Section 170(p) of the Internal Revenue Code.

¹⁵ See CRS Report R45922, *Tax Issues Relating to Charitable Contributions and Organizations*, by Jane G. Gravelle, Donald J. Marples, and Molly F. Sherlock for further discussion.

¹⁶ "New Charitable Deduction in the CARES Act, Budgetary and Distributional Analysis," blog post, Tax Policy Center, Penn-Wharton Budget Model, March 27, 2020, <https://budgetmodel.wharton.upenn.edu/issues/2020/3/27/charitable-deduction-the-cares-act>.

¹⁷ Section 170(b)(c) and (d) of the Internal Revenue Code.

¹⁸ See CRS Report R45922, *Tax Issues Relating to Charitable Contributions and Organizations*, by Jane G. Gravelle, Donald J. Marples, and Molly F. Sherlock for further discussion.

¹⁹ The 10% estimate for 2021 is from Joint Committee on Taxation, *Overview of the Federal Tax system as In Effect for 2021*, JCX-18-21, April 15, 2021, <https://www.jct.gov/publications/2021/jcx-18-21/>.

the care of the ill, the needy, or infants, special rules provide an enhanced deduction equal to the basis plus half the difference between the fair market value and basis, not to exceed twice the basis. A similar enhanced deduction exists for businesses (both corporate and noncorporate) for food inventory contributions for the care of the ill, needy, and infants. Cash basis taxpayers who do not keep inventories (including many farmers and some other small businesses) are allowed to deduct half the fair market value under the enhanced food inventory deduction, even though they already deduct these costs as a business expense. This enhanced deduction for food inventory is limited to 15% of taxable income from the business for both individuals and corporations.

Unused charitable deductions that exceed the income limits can be carried forward and deducted in the following five years.

The Coronavirus Aid, Relief, and Economic Security (CARES) Act (P.L. 116-136) eliminated the limit on cash gifts of individuals to public charities (but not to donor advised funds, supporting organizations, or private foundations). It increased the limit on charitable contributions from corporations to 25% of taxable income (including donations of qualified food inventory). The deduction for contributions of qualified food inventory for individuals was also increased to 25%. This provision was extended through December 31, 2021, by the Taxpayer Certainty and Disaster Tax Relief Act of 2020, enacted as Division EE of the Consolidated Appropriations Act, 2021 (P.L. 116-260).

Lifting caps on the deductions for both individuals and businesses can provide an incentive for additional charitable giving. Evidence on the response of charitable giving by individuals has been widely studied with mixed results. A review of this evidence suggests that an enhanced charitable deduction is likely to increase charitable giving by less than the associated revenue loss.²⁰ Lifting the limits affects a relatively small share of charitable giving, and the revenue pattern suggests that much of the initial revenue loss (77%) can be attributed to an accelerated realization of carryovers.²¹ With charitable giving estimated at \$427.4 billion in 2018, if all of the permanent revenue loss led to an increase in charitable giving by the same amount (i.e., approximately \$1 billion), additional giving would be 0.3% of expected giving prior to the current economic slowdown.²²

Flexible Spending Accounts Rollover²³

Flexible spending accounts (FSAs) allow employees whose employers offer these benefits to pay for certain health and dependent care using pretax dollars (i.e., not subject to income or payroll taxes).²⁴ Contributions to FSAs are limited to \$2,750 for health care FSAs and \$5,000 for

²⁰ See the review of the empirical evidence in CRS Report R45922, *Tax Issues Relating to Charitable Contributions and Organizations*, by Jane G. Gravelle, Donald J. Marples, and Molly F. Sherlock.

²¹ According to the revenue estimates for the CARES Act, the initial revenue loss in the first two years was \$4,828 million, followed by a gain of \$3,535 million, indicating that 77% (\$3,535 divided by \$4,828) of the revenue loss was temporary and likely due to carryovers of prior unused deductions. See Joint Committee on Taxation, *Estimated Revenue Effects Of The Revenue Provisions Contained In An Amendment In The Nature Of A Substitute To H.R. 748, The "Coronavirus Aid, Relief, And Economic Security ('CARES') Act," As Passed By The Senate On March 25, 2020, And Scheduled For Consideration By The House Of Representatives On March 27, 2020*, JCX-11R-20, April 23, 2020, at <https://www.jct.gov/publications/2020/jcx-11r-20/>.

²² \$1.1 billion divided by \$427.4 billion = 0.3%.

²³ Sections 125 and 129 of the Internal Revenue Code.

²⁴ See CRS In Focus IF11576, *Potential COVID-19 Impacts on Health Flexible Spending Arrangements (FSAs) and Recent Health FSA Changes*, by Ryan J. Rosso; CRS In Focus IF11597, *Potential Impact of COVID-19 on Dependent Care Flexible Spending Arrangements (FSAs)*, by Conor F. Boyle and Margot L. Crandall-Hollick; and CRS Report

dependent care FSAs for 2020. For 2021, this amount is raised to \$10,500. Individuals may have both types of accounts.

Employees’ contributions are generally forfeited if not used during the plan year (or, where applicable, an allowed grace period of 2.5 months). Employers may allow \$500 of health FSAs to be rolled over to subsequent plan years as an alternative to the grace period. These accounts are allowed as part of a cafeteria plan. The “use-or-lose” rule ensures that a cafeteria plan is not used to defer compensation (and the taxes paid on that compensation) to a future date, which is generally prohibited under IRC Section 125.

The Internal Revenue Service (IRS) allowed employers to provide employees with the ability to make midyear changes to the amounts contributed to FSAs during 2020. Because some plans do not follow a calendar year, the IRS also allowed employers to extend the availability of FSA funds through the end of 2020 for plans that were scheduled to end before December 31. This extension reflected the difficulty in using funds due to COVID-19 shutdowns and social distancing, which made use of child and dependent care and health services difficult.

The Taxpayer Certainty and Disaster Tax Relief Act of 2020, enacted as Division EE of the Consolidated Appropriations Act, 2021 (P.L. 116-260), allows employers to extend the availability of FSA contribution amounts from 2020 to 2021, and from 2021 to 2022. It also allows employers to increase the coverage of dependent care expenses from children under age 13 to children under age 14. Additionally, it allows employers to make health FSA funds available to employees who made contributions to their health FSA and were terminated in 2020 or 2021. Finally, it allows employers to provide employees with the opportunity to make midyear, prospective FSA contribution changes for plans ending in 2021.

In general, health FSA funds can be used to pay for an employee’s share of health insurance premiums, including cases where the employee pays the entire premium. However, insurance bought through the individual exchanges established under the Affordable Care Act (ACA; P.L. 111-148, as amended) is not eligible for tax benefits under cafeteria plans.

Individual CARES Act and “Tax Extender” Provisions Expiring in 2025

Exclusion for Employer Payments of Student Loans²⁵

An individual may not have to pay income or payroll taxes on up to \$5,250 of educational assistance provided by their employer. Specifically, an individual may be able to exclude from their gross income up to \$5,250 annually of educational assistance for both graduate and undergraduate education provided by their employer under an education assistance program. The temporary provision provides that educational assistance includes certain student loan payments.

There are three main requirements that must be satisfied in order for employer-provided educational assistance to be excludable from gross income and hence tax-free. First, the educational assistance must be provided pursuant to a written qualified educational assistance program. Second, the plan may not discriminate in favor of highly compensated employees. Third, no more than 5% of the total amount paid out during the year may be paid to or for

R44993, *Child and Dependent Care Tax Benefits: How They Work and Who Receives Them*, by Margot L. Crandall-Hollick and Conor F. Boyle for further discussion.

²⁵ Section 127 of the Internal Revenue Code.

employees who are shareholders or owners of at least 5% or more of the business. (The employer must maintain records and file a plan return.)

The employer may make qualified assistance payments directly, by reimbursement to the employee, or may directly provide the education. (The exclusion only applies to the employee and not their spouses or dependents.)

Qualifying assistance payments generally include, but are not limited to, tuition, fees, and similar payments; books; supplies; and equipment. Courses do not have to be job related. Qualifying assistance payments do not include amounts for tools or supplies that can be kept by the employee or amounts for meals, lodging, or transportation. Qualified education assistance does not include payment for any course or other education involving sports, games, or hobbies.

The Coronavirus Aid, Relief, and Economic Security (CARES) Act (P.L. 116-136) temporarily expanded the definition of employer-sponsored educational assistance to include qualified student loan payments made to employees in 2020. Payments can cover both the principal and interest of a qualified student loan. Qualified student loans are those eligible for the student loan interest deduction²⁶ that are incurred by the employer for the employee's education. This provision applies to any student loan payment made by an employer on an employee's behalf after the date of enactment of the CARES Act (March 27, 2020) and before January 1, 2021. The Taxpayer Certainty and Disaster Tax Relief Act of 2020, enacted as Division EE of the Consolidated Appropriations Act, 2021 (P.L. 116-260), allows these payments to be excluded if made before January 1, 2026.

This provision provides benefits to those who are working and receiving employer assistance with their student loans. These individuals may have experienced wage reductions, slower wage growth, and reduced hours during the pandemic. They may also be more likely to spend additional income, resulting in economic stimulus. In the longer run, advocates have proposed allowing tax benefits for employer repayment of student loans as an employee retention or recruitment incentive.

Tax Exclusion for Canceled Mortgage Debt²⁷

Historically, when all or part of a taxpayer's mortgage debt has been forgiven, the amount canceled has been included in the taxpayer's gross income.²⁸ This income is typically referred to as canceled mortgage debt income. Canceled (or forgiven) mortgage debt is common with a short sale, in which a homeowner agrees to sell a house and transfer the proceeds to the lender in exchange for the lender relieving the homeowner from repaying any debt in excess of the sale proceeds. For example, in a short sale, a homeowner with a \$300,000 mortgage may be able to sell the house for \$250,000. The lender would receive the \$250,000 from the home sale and forgive the remaining \$50,000 in mortgage debt.²⁹ Lenders report the canceled debt to the Internal Revenue Service (IRS) using Form 1099-C. A copy of the 1099-C is also sent to the borrower, who in general must include the amount listed in his or her gross income in the year of discharge.

²⁶ Section 221(d)(1) of the Internal Revenue Code.

²⁷ Section 108(a)(1)(E) of the Internal Revenue Code.

²⁸ Generally, any type of debt that has been canceled is to be included in a taxpayer's gross income. Several permanent exceptions to this general tax treatment of canceled debt exist. They are discussed in CRS Report RL34212, *Analysis of the Tax Exclusion for Canceled Mortgage Debt Income*, by Mark P. Keightley and Erika K. Lunder.

²⁹ A lender must agree to a short sale prior to a borrower selling a house, or the borrower will still be obligated to repay the balance remaining on the mortgage.

To understand why forgiven debt has historically been taxable, it may be helpful to explain why it is viewed as income from an economic perspective. Income is a measure of the increase in an individual's purchasing power over a designated period of time. When individuals experience a reduction in their debts, their purchasing power has increased (because they no longer have to make debt payments). Effectively, their disposable income has increased. From an economic standpoint, it is irrelevant whether a person's debt was reduced via a direct transfer of money to the borrower (e.g., wage income) that was then used to pay down the debt, or whether it was reduced because the lender forgave a portion of the outstanding balance. Both have the same effect, and thus both are subject to taxation.

The Mortgage Forgiveness Debt Relief Act of 2007 (P.L. 110-142), signed into law on December 20, 2007, temporarily excluded qualified canceled mortgage debt income that is associated with a primary residence from taxation. Thus, the act allowed taxpayers who did not qualify for one of several existing exceptions to exclude canceled mortgage debt from gross income. The provision was originally effective for debt discharged before January 1, 2010. Since then, the provision has regularly been extended as part of the tax extenders. The exclusion was extended through December 31, 2020, in the Taxpayer Certainty and Disaster Tax Relief Act of 2019, enacted as Division Q of the Further Consolidated Appropriations Act, 2020 (P.L. 116-94). It was further extended through December 31, 2025, in the Taxpayer Certainty and Disaster Tax Relief Act of 2020, enacted as Division EE of the Consolidated Appropriations Act, 2021 (P.L. 116-260).

The rationales for extending the exclusion are to minimize hardship for households in distress and lessen the risk that nontax homeowner retention efforts are thwarted by tax policy. The exclusion's supporters may also argue that extending the exclusion would continue to assist the recoveries of the housing market and overall economy. The exclusion's opponents may argue that extending the provision would make debt forgiveness more attractive for homeowners, which could encourage homeowners to be less responsible about fulfilling debt obligations. Some may also view the exclusion as unfair because its benefits depend on whether a homeowner is able to negotiate a debt cancellation, the taxpayer's income tax bracket, and whether the taxpayer retains ownership of the house following the debt cancellation.

Individual "Tax Extender" Provisions Made Permanent in P.L. 116-230

Medical Expense Deduction Adjusted Gross Income (AGI) Floor of 7.5%³⁰

Individuals are allowed to deduct unreimbursed medical expenses above a specific income threshold if they itemize their deductions. Prior to 2013, these deductions were allowed only for amounts in excess of 7.5% of income. Expenses reimbursed by an employer or insurance company are not eligible for deduction.

The Affordable Care Act (P.L. 111-148, as amended) increased the floor for individuals claiming the itemized deduction for medical expenses from 7.5% to 10% of adjusted gross income (AGI).³¹

³⁰ Section 213(f) of the Internal Revenue Code.

³¹ Taxpayers first were allowed to deduct health care expenses above a specific income threshold in 1942. The deduction was a provision of the Revenue Act of 1942 (P.L. 77-753). In adopting such a rule, Congress was trying to encourage improved public health standards and ease the burden of high tax rates during World War II. Congress has

The higher floor went into effect for taxpayers under age 65 beginning for the 2013 tax year. Individuals 65 or older, however, were still able to claim the deduction under the lower, 7.5% floor for tax years 2013 through 2016. The 2017 tax revision (TCJA; P.L. 115-97) temporarily allowed all taxpayers (not just those aged 65 or older) to claim the deduction subject to the 7.5% floor for the 2017-2018 tax years. The Taxpayer Certainty and Disaster Tax Relief Act of 2019, enacted as Division Q of the Further Consolidated Appropriations Act, 2020 (P.L. 116-94), extended the 7.5% floor for all taxpayers through 2020. After 2020, under current law, the floor was scheduled to increase to 10% of AGI for all taxpayers. The lower 7.5% floor was made permanent in the Taxpayer Certainty and Disaster Tax Relief Act of 2020, enacted as Division EE of the Consolidated Appropriations Act, 2021 (P.L. 116-260).

A complicated set of rules governs the expenses eligible for the deduction.³² Generally, these expenses include amounts paid by the taxpayer on behalf of himself or herself, his or her spouse, and eligible dependents for the following purposes: (1) health insurance premiums (including employee payments for employer-sponsored health plans, Medicare Part B premiums, and other self-paid premiums); (2) diagnosis, treatment, mitigation, or prevention of disease, or for the purpose of affecting any structure or function of the body, including dental care; (3) prescription drugs and insulin (but not over-the-counter medicines); (4) transportation primarily for and essential to medical care; and (5) lodging away from home primarily for and essential to medical care, up to \$50 per night for each individual.³³

Taxpayers may be less likely to claim the medical expense deduction compared to prior periods because other provisions of the 2017 tax revision (TCJA; P.L. 115-97) reduced the tax benefits of itemizing deductions.³⁴ These provisions, while currently in effect, are slated to expire after 2025. The likelihood of itemizing generally increases with income. However, the AGI floor for the medical expenses deduction reduces the likelihood that very high-income individuals would claim the deduction.³⁵ For all taxpayers, medical expenses alone might not make it worthwhile to itemize unless they can also claim other itemized deductions (e.g., home mortgage interest or state and local taxes).

modified the deduction a number of times, typically by either raising or lowering the AGI floor, or establishing or adjusting additional floors for various subcategories of medical spending within the deduction. For more information, see pp. 887-884 in United States Senate, Committee on the Budget, *Tax Expenditures: Compendium of Background Material on Individual Provisions*, 116th Congress, 2nd Session, S.Prt. 116-53, December 2020, <https://www.congress.gov/committee-print/116th-congress/senate-committee-print/42597?s=1&r=42>.

³² United States Senate, Committee on the Budget, *Tax Expenditures: Compendium of Background Material on Individual Provisions*, 116th Congress, 2nd Session, S.Prt. 116-53, December 2020, <https://www.congress.gov/committee-print/116th-congress/senate-committee-print/42597?s=1&r=42>.

³³ For more information, see IRS Publication 502, "Medical and Dental Expenses," <https://www.irs.gov/publications/p502/index.html>.

³⁴ After the 2017 tax revision, the share of taxpayers who itemized was estimated to be 12%. The 12% estimate for 2021 is from Joint Committee on Taxation, *Overview of the Federal Tax system as In Effect for 2021*, JCX-18-21, April 15, 2021, <https://www.jct.gov/publications/2021/jcx-18-21/>.

³⁵ In general, a larger percentage of the tax returns from the medical expense deduction goes to taxpayers in the lower-to middle-income brackets, relative to other common itemized deductions. Lower-income taxpayers have relatively low rates of health insurance coverage because they cannot afford health insurance coverage or coverage is not offered by their employers. As a result, many of these taxpayers are forced to pay out-of-pocket for the health care they and their immediate families receive. In addition, medical spending constitutes a larger fraction of household budgets among low-income taxpayers than it does among high-income taxpayers, making it easier for low-income taxpayers to exceed the AGI threshold. See United States Senate, Committee on the Budget, *Tax Expenditures: Compendium of Background Material on Individual Provisions*, 116th Congress, 2nd Session, S.Prt. 116-53, December 2020, <https://www.congress.gov/committee-print/116th-congress/senate-committee-print/42597?s=1&r=42>.

Benefits for Volunteer Firefighters and Emergency Medical Responders³⁶

The Mortgage Forgiveness Debt Relief Act of 2007 (P.L. 110-142) provided an exclusion from gross income of certain benefits for members of qualified voluntary emergency response organizations. These payments include the forgiveness or rebate of state and local income and property taxes or payments by states or their political subdivisions to reimburse for expenses. The exclusion was limited to \$30 a month. The provision disallowed any itemized deductions for the state and local taxes otherwise excluded. The provision was temporary, effective from the date of enactment (December 20, 2007) through 2010. The provision was allowed to expire as scheduled.

This provision was enacted after a 2002 IRS decision that a reduction in property taxes for volunteers who are emergency responders was includible in gross income.³⁷

The SECURE Act of 2019, enacted as Division O of the Further Consolidated Appropriations Act, 2020 (P.L. 116-94), reinstated the provision for 2020 and increased the amount to \$50 a month. The provision was made permanent in the Taxpayer Certainty and Disaster Tax Relief Act of 2020, enacted as Division EE of the Consolidated Appropriations Act, 2021 (P.L. 116-260).

The reinstated provision is likely to have a wider scope than it previously did because of the reduction in the number of itemizers due to provisions in the TCJA (P.L. 115-97), which is expected to reduce the share of taxpayers who itemize deductions.

Provision Repealed and Replaced

Above-the-Line Deduction for Qualified Tuition and Related Expenses: Repealed and Replaced With Higher Phaseout for Credit³⁸

The above-the-line deduction for qualified tuition and related expenses was repealed and the income limits for the Lifetime Learning Credit (LLC) were increased to make that credit available to higher-income taxpayers who had benefited from the above-the-line deduction.

Above-the-Line Deduction

Before 2021, taxpayers could deduct up to \$4,000 of qualified tuition and related expenses for postsecondary education (both undergraduate and graduate) from their gross income. Expenses that qualified for this deduction included tuition payments and any fees required for enrollment at an eligible education institution.³⁹ Other expenses, including room and board expenses, were generally not qualifying expenses for this deduction. The deduction was "above-the-line," that is, it was not restricted to itemizers.

³⁶ Section 139B of the Internal Revenue Code.

³⁷ IRS Chief Counsel Advice 200302045, December 3, 2002, <https://www.irs.gov/pub/irs-wd/0302045.pdf>.

³⁸ Section 222 of the Internal Revenue Code for the above-the-line deduction and Section 25A for the Lifetime Learning Credit.

³⁹ Payments made with borrowed funds are eligible for the deduction: the year of eligibility is determined by the date payment is made to the institution and not when the loan is repaid.

Individuals who could be claimed as dependents, married persons filing separately, and nonresident aliens who do not elect to be treated as resident aliens did not qualify for the deduction, in part to avoid multiple claims on a single set of expenses.

The amount that could be claimed for the deduction was generally reduced by any tax-free assistance, if that assistance could be used to pay for expenses that qualify for the deduction. Tax-free assistance includes tax-free grants and scholarships (including Pell Grants), employer-provided educational assistance, and veterans' educational assistance.⁴⁰

The maximum deduction taxpayers could claim depended on their income level. Taxpayers could deduct up to

- \$4,000 if their income was \$65,000 or less (\$130,000 or less if married filing jointly); or
- \$2,000 if their income was between \$65,000 and \$80,000 (\$130,000 and \$160,000 if married filing jointly).

The deduction was phased out between \$65,000 and \$80,000 for single returns and between \$130,000 and \$180,000 for joint returns. These income limits were not adjusted for inflation.

The above-the-line deduction for qualified tuition and related expenses was enacted temporarily by the Economic Growth and Tax Relief Reconciliation Act of 2001 (P.L. 107-16). It was extended a number of times. Most recently, the deduction was extended through December 31, 2020, in the Taxpayer Certainty and Disaster Tax Relief Act of 2019, enacted as Division Q of the Further Consolidated Appropriations Act, 2020 (P.L. 116-94). The Taxpayer Certainty and Disaster Tax Relief Act of 2020, enacted as Division EE of the Consolidated Appropriations Act, 2021 (P.L. 116-260), repeals the tuition and fees deduction and increases the phaseout for another higher education tax benefit, the Lifetime Learning Credit (LLC), discussed below.

The deduction benefited taxpayers according to their marginal tax rate. Students usually have relatively low incomes, but they may be part of families in higher tax brackets. The maximum amount of deductible expenses limited the tax benefit's impact on individuals attending schools with comparatively high tuitions and fees. Because the income limits were not adjusted for inflation, the deduction became available to fewer taxpayers over time.

The Lifetime Learning Credit

Taxpayers could claim the tuition and fees deduction instead of education tax credits for the same student. These credits include permanent tax credits: the American Opportunity Tax Credit (AOTC) and Lifetime Learning Credit (LLC). The AOTC is directed at undergraduate education and is limited to the first four years of postsecondary education.⁴¹ The credit is phased out between \$80,000 and \$90,000 for single returns and between \$160,000 to \$180,000 for joint returns. The LLC is not limited in years of coverage and equals up to \$2,000 per taxpayer.⁴² It was phased out between \$59,000 and \$69,000 for single returns and from \$118,000 to \$138,000 for joint returns, for 2020, with these limits adjusted annually for inflation. These credits generally were more advantageous than the deduction, except for higher-income taxpayers, in

⁴⁰ Qualified expenses being deducted also must be reduced if paid with tax-free interest from Education Savings Bonds, tax-free distributions from Coverdell Education Savings Accounts, and tax-free earnings withdrawn from Qualified Tuition Plans (i.e., 529 Plans).

⁴¹ See CRS Report R41967, *Higher Education Tax Benefits: Brief Overview and Budgetary Effects*, by Margot L. Crandall-Hollick.

⁴² 20% of up to \$10,000 of qualifying expenses.

part because the credits are phased out at lower levels of income than the deduction. The legislation permanently increases the phaseout for the LLC to the same levels as the AOTC.

One criticism of education tax benefits is that the taxpayer is faced with a confusing choice of deductions and credits and tax-favored education savings plans, and that these benefits should be consolidated. The deduction's distribution indicated that some of the benefit was concentrated in the income range where the LLC has phased out, but also that significant deductions were claimed at lower income levels. Because the LLC was preferable to the deduction at lower income levels, it seems likely that confusion about the education benefits may have caused taxpayers not to choose the optimal education benefit.⁴³ By repealing the deduction and increasing the credit's income limits, a single set of tax benefits will be more available to higher-income individuals, and lower-income individuals will no longer use the deduction instead of the credit.

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⁴³ The Government Accountability Office (GAO) has also discussed the lack of optimal choices with education preferences. See GAO, *Improved Tax Information Could Help Families Pay for College*, GAO-12-560, May 18, 2012, <http://www.gao.gov/products/GAO-12-560>; and GAO, *Multiple Higher Education Tax Incentives Create Opportunities for Taxpayers to Make Costly Mistakes*, GAO-08-717T, May 1, 2008, <http://www.gao.gov/products/GAO-08-717T>.