

News

I.1, PPP Deduction Safe Harbor Provided if Loan Is Not Forgiven (Rev. Proc. 2020-51; Rev. Rul. 2020-27)

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The IRS has released rulings concerning deductions for eligible Paycheck Protection Program (PPP) loan expenses. The rulings:

- (1) deny a deduction if the taxpayer has not yet applied for PPP loan forgiveness, but expects the loan to be forgiven; and
- (2) provide a safe harbor for deducting expenses if PPP loan forgiveness is denied or the taxpayer does not apply for forgiveness.

Business Expenses Paid for by Forgiven PPP Loans Not Deductible

In response to the COVID-19 (coronavirus) crisis, the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) expanded Section 7(a) of the Small Business Act for certain loans made from February 15, 2020, through August 8, 2020 (PPP loans). An eligible PPP loan recipient may have the debt on a covered loan forgiven. The cancelled debt will be excluded from gross income. Under Reg. §1.265-1, taxpayers cannot deduct expenses that are allocable to income that is either wholly excluded from gross income or wholly exempt from the taxes. This rule exists in order to prevent double tax benefits.

The IRS previously determined that businesses whose PPP loans are forgiven cannot deduct business expenses paid for by the loan. The new guidance expands on the previous guidance, but provides a safe harbor for taxpayers whose loans are not forgiven.

No Deduction if Loan Is Expected to Be Forgiven

In Rev. Rul. 2020-27, the IRS amplifies guidance in Notice 2020-32, I.R.B. 2020-21, 837, that businesses whose PPP loans are forgiven cannot deduct business expenses paid for by the loan. A taxpayer that received a covered PPP loan and paid or incurred certain otherwise deductible expenses may not deduct those expenses in the tax year in which the expenses were paid or incurred if, at the end of the tax year, the taxpayer reasonably expects to receive forgiveness of the covered loan on the basis of the expenses it paid or accrued during the covered period. This is the case even if the taxpayer has not applied for forgiveness by the end of the tax year.

Deduction Safe Harbor for Loans not Forgiven

In Rev. Proc. 2020-51, the IRS provides a safe harbor allowing taxpayers to claim a deduction in the tax year beginning or ending in 2020 for certain otherwise deductible eligible expenses if:

- (1) the eligible expenses are paid or incurred during the taxpayer's 2020 tax year;
- (2) the taxpayer receives a PPP covered loan that, at the end of the taxpayer's 2020 tax year, the taxpayer expects to be forgiven in a subsequent tax year; and
- (3) in a subsequent tax year, the taxpayer's request for forgiveness of the covered loan is denied, in whole or in part, or the taxpayer decides never to request forgiveness of the covered loan.

A taxpayer may be able to deduct some or all of the eligible expenses on:

- (1) the taxpayer's timely, including extensions, original income tax return or information return, as applicable, for the 2020 tax year;
- (2) an amended return or an administrative adjustment request (AAR) under Code Sec. 6227 for the 2020 tax year, as applicable; or
- (3) the taxpayer's timely, including extensions, original income tax return or information return, as applicable, for the subsequent tax year.

Applying the Safe Harbor

To apply the safe harbor, a taxpayer attaches a statement to the return on which the taxpayer deducts the expenses. The statement must be titled "Revenue Procedure 2020-51 Statement," and must include:

- (1) the taxpayer's name, address, and social security number or employer identification number;
- (2) a statement specifying whether the taxpayer is an eligible taxpayer under either section 3.01 or section 3.02 of Revenue Procedure 2020-51;
- (3) a statement that the taxpayer is applying section 4.01 or section 4.02 of Revenue Procedure 2020-51;
- (4) the amount and date of disbursement of the taxpayer's covered PPP loan;
- (5) the total amount of covered loan forgiveness that the taxpayer was denied or decided to no longer seek;
- (6) the date the taxpayer was denied or decided to no longer seek covered loan forgiveness; and
- (7) the total amount of eligible expenses and non-deducted eligible expenses that are reported on the return.

Rev. Proc. 2020-51

Rev. Rul. 2020-27