

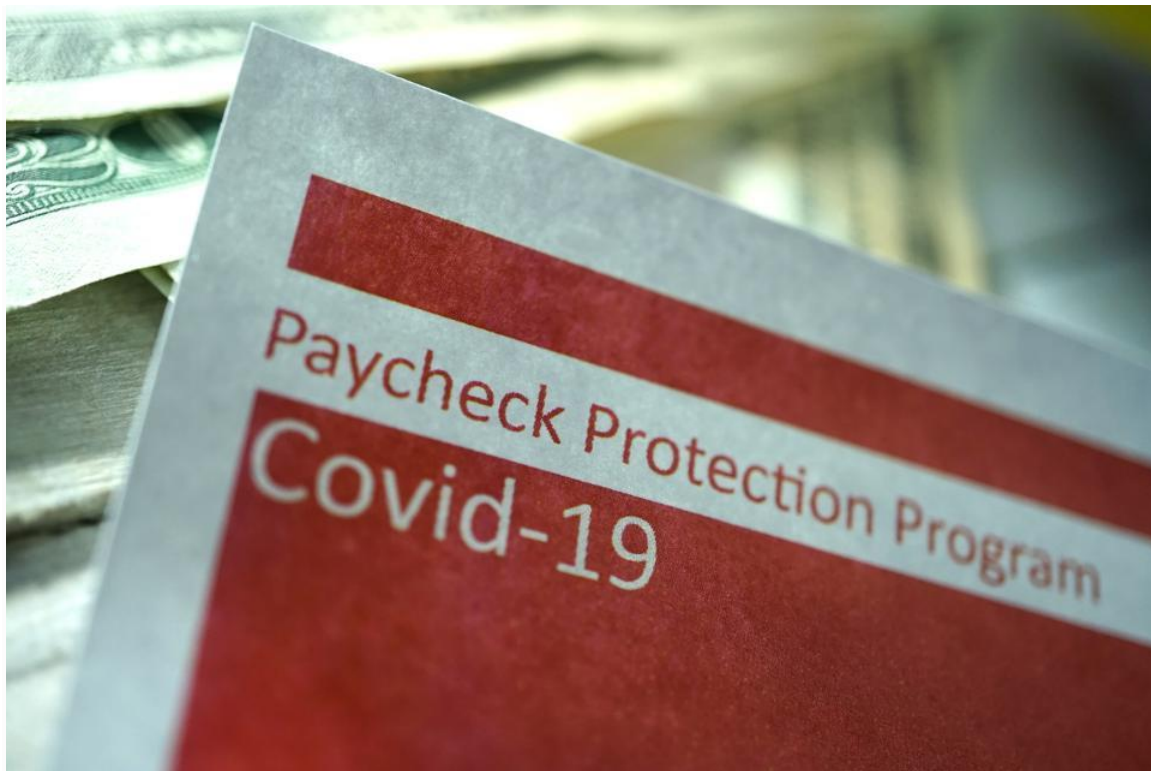


Robert W. Wood
THE TAX LAWYER

TAXES 11/19/20

IRS Denies PPP Tax Deductions Even If Loan Might Be Forgiven In Future

The Paycheck Protection Program was the centerpiece of the CARES Act, providing loans to businesses of up to \$10M. If you comply, you don't even have to pay your loan back. What's more, there is not even any forgiveness of debt income when your loan is forgiven, something that normally is a standard tax result from a forgiven loan. So far, so good, but can businesses claim tax *deductions* for business expenses? It sounds like a silly question, but when it comes to the Paycheck Protection Program (PPP), it has been a thorny question from the start. Rent and wages are deductible expenses, so surely you can write off the wages, rent and other expenses you pay with PPP money, right? Not so fast, said the IRS. In [Notice 2020-32](#), the IRS [denied tax deductions](#) even for expenses that are *normally* fully deductible. The IRS says allowing a deduction would be a double dip. Congress quickly moved to reverse the IRS in the Small Business Expense Protection Act, [S.3612 - 116th Congress \(2019-2020\)](#). That bill languished and has still not passed, although [Congress could still reverse IRS denial of tax deductions](#).



But what if you pay and write off the wages and rent, and *later* apply for loan forgiveness? The IRS hasn't been kind to PPP loans, and here is another example. Now, here's the latest from the IRS. To stop people from claiming deductions and then *later* getting forgiveness, the IRS has said no again. The IRS released [Revenue Ruling 2020-27](#) to address situations where a loan is not yet forgiven but might be in the future. In the ruling, the IRS described two situations. In the first, a borrower pays payroll and mortgage interest that are valid PPP expenditures. The borrower applies for forgiveness in November 2020 and satisfied all the requirements under the CARES Act to have it forgiven, but it doesn't yet have an answer as to whether it will be forgiven.

In the second case, the borrower paid the same type of expenses with its PPP loan, but expects to apply for forgiveness in 2021. In both cases, the IRS says the business cannot deduct these business expenses. The businesses both have a "reasonable expectation" that the loans will be forgiven. The IRS also released [Rev. Proc. 2020-51](#), which provides a safe harbor for PPP borrowers

whose loan forgiveness has been partially or fully denied and who wish to claim deductions for otherwise eligible payments on a return, amended return, or administrative adjustment request.

The debate about allowing or not allowing deductions harkens back to some traditional tax principles. The IRS says that if income is tax exempt, you usually cannot *also* claim deductions relating to it. Applying the rules consistently, the IRS says, you shouldn't be able to get the free money, not pay discharge of debt income, *and still* deduct the payments of wages and rent made with the free money. Still, there are good arguments for deductions, and maybe Congress needs to step in.

Check out my [website](#).