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## **IRS ISSUES NEW GUIDANCE REGARDING DEDUCTIBILITY OF EXPENSES WHICH ARE FORGIVEN UNDER THE PAYROLL PROTECTION PROGRAM**

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On April 30, 2020, the IRS published Notice 2020-32 (the “Notice”) regarding the deductibility of expenses, which would otherwise be properly deductible, if the payment of such expenses results in forgiveness of a Payroll Protection Program (“PPP”) loan. Specifically, the Notice states that “...no deduction is allowed under the Internal Revenue Code (Code) for an expense that is otherwise deductible if the payment of the expense results in forgiveness of a covered loan pursuant to Section 1106(b) of the [CARES Act] and the income associated with the forgiveness is excluded from gross income for purposes of the Code pursuant to Section 1106(i) of the CARES Act.”

### **What does this mean to recipients of a PPP loan?**

First, let’s lay some groundwork. Debt forgiveness is typically re-characterized as income. However, the CARES Act specifically excluded the amount of PPP loan forgiveness from gross income. Therefore, PPP loans could be received and used tax-free. In this regard, a PPP loan may be used to pay the following expenses: (1) payroll costs, which expressly excludes independent contractors; (2) certain employee healthcare benefits; (3) interest on mortgage obligations incurred before February 15, 2020; (4) rent under lease agreements in force before February 15, 2020; and (5) utilities for which service began before February 15, 2020. In order to achieve PPP loan forgiveness, a recipient must utilize at least 75% of the funds toward payroll costs and 25% toward permitted non-payroll costs.

Thus, prior to the Notice being issued, some had questioned whether recipients of a PPP loan were entitled to deduct the permitted PPP expenses (as they otherwise would be) if forgiveness was obtained. The IRS, with this Notice, answered that question with a resounding NO. The Notice refers to Internal Revenue Code 265(a)(1) which provides that a deduction that is otherwise allowable is not permitted if that deduction is allocable to a class of income exempt from taxes – here, that income being the portion of the PPP loan which was forgiven.

Conceptually, this makes sense as PPP loan forgiveness is expressly not to be counted as income; therefore, there is no income to offset the expenses. If the expenses were permitted to be deducted, it would result in a double tax benefit to taxpayers (i.e. receiving the benefit of no tax on the forgiveness and being permitted to deduct the expenses associated with the forgiveness).

**About the Author:**



**About Christopher M. Leddy:** Chris is a partner in the firm's Corporate and Transportation Departments. Chris has experience handling and litigating complex employment law issues as well as counseling all aspects of the employment/contractor relationship. Chris provides counsel with the goal of maintaining essential trust relationships and protracting costly legal disputes.

**About Becker LLC:** Becker LLC is a premiere mid-market firm recognized as a leader in the staffing industry. With offices in New York, New Jersey, Philadelphia and California, the firm provides forward thinking, mission-critical advice to staffing industry entrepreneurs and management on high stakes, complex legal matters as well as day-to-day matters and long-term plans. The firm are proud to be members of the following Staffing Associations: SIA, ASA, ASG, TempNet, CSP, MSA, NJSA, NYSA and serves as general counsel to the Mid Atlantic Staffing Association.