

## **New Legislation Reverses IRS Guidance on Deduction of Expenses Paid with PPP Loan Proceeds**

The COVID-related Tax Relief Act of 2020, adopted as part of “omnibus” legislation passed by Congress on December 21, 2020, reverses the guidance previously adopted by the Internal Revenue Service (“IRS”) with respect to business expenses paid from Paycheck Protection Program (“PPP”) loans that are forgiven or are reasonably expected to be forgiven.

Earlier in the year, the IRS issued guidance stating that expenses paid using PPP loan proceeds would not be deductible as business expenses. The IRS contended – since there is an expectation that PPP loans would be forgiven, and such forgiveness would not be taxable – that longstanding tax rulings required that expenses incurred in anticipation of tax-free gains are not deductible.

Further guidance stated that the expenses could not be deducted even if forgiveness had been obtained but merely “reasonably anticipated.” This raised the possibility of unexpected tax expense while the forgiveness of PPP loan remained uncertain.

Section 276 of the new COVID-related Tax Relief Act reverses the IRS guidance and states that no deduction shall be denied by reason of the fact that the PPP forgiveness is intended to be tax-free.

In addition, the section provides that “no tax attribute shall be reduced” and “no basis increase shall be denied” as a result of tax-free PPP forgiveness.

The revisions are retroactive to all tax years ending after the date of enactment of the Coronavirus Aid Relief and Economic Security Act (“CARES Act”), which created the PPP program.

Finally, the same standards will apply to the newly adopted second round of PPP loans created by the omnibus legislation.