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- PPP expenses are deductible thanks to the new round of stimulus allowing business expenses paid for with PPP funds to be deducted on your tax return
- A second round of PPP Loans have opened up with new eligibility requirements, including a revenue decrease of 25% or more in any 2020 quarter as compared to the same 2019 quarter
- PPP Loan forgiveness applications will be simplified as the SBA will release a one-page certification form for borrowers with a PPP Loan (new or old) less than \$150,000

## PPP Deductions, Forgiveness, and Applying for Round 2

By Mary Lundstedt, Esq. and Justin Liberatore.

### PPP Expenses are Deductible

In November, the Internal Revenue Service (IRS) issued Notice 2020-32 declaring that business expenses paid with Paycheck Protection Program (PPP) funds were not tax deductible to the extent they resulted in forgiveness of PPP funds. Shortly thereafter, the IRS clarified that business expenses would not be deductible if the borrower reasonably expects forgiveness. However, a new round of stimulus allows business expenses paid for with PPP funds to be deducted on your tax return—whether or not they are ultimately forgiven (or reasonably expected to be forgiven).

### Congress Clarifies Treatment of PPP Loan (and EIDL) Expense Deductions

Under the new Emergency Coronavirus Relief Act of 2020 (Act), Congress clarified that (1) expenses paid for with PPP Loan proceeds are deductible, (2) PPP Loan forgiveness is not taxable, and (3) tax basis remains unaffected despite the resulting exclusion from gross income. Note that, similarly, the Act provides that Eco-

nomic Injury Disaster Loans (EIDL) do not result in taxable income, and EIDL-paid expenses are deductible.

Under IRS guidance issued before the passage of the Act, contrary to what many believed to be Congress's actual intent behind the CARES Act, businesses would not be able to deduct expenses that were paid with PPP funds if: (1) the loaned proceeds were forgiven, or (2) reasonably expected to be forgiven. That IRS position left many businesses and tax professionals displeased that otherwise deductible expenses would no longer be deductible. We have covered this issue with an in-depth review here.

Congress's new Act directly addresses these concerns, stating that "no deduction shall be denied, no tax attribute shall be reduced, and no basis increase shall be denied, by reason of the exclusion from gross income" resulting from the forgiveness of indebtedness provided in the CARES Act. Emergency Coronavirus Relief Act of 2020, §276(a)(1)(i)(1).

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Further, the Act states that for pass through entities that are S corps or partnerships, any amount excluded from income by the Act shall be treated as tax-exempt income and will receive a basis increase equal to the partner's distributive share of deductions resulting from the costs giving rise to forgiveness in the CARES Act.

This is a massive overriding of IRS guidance and significantly amplifies PPP Loan benefits for borrowers! Forgiveness is a tax-free event. So, consider the business that received a \$100,000 PPP Loan, spent the entire amount on qualified expenses (like rent and payroll), and received forgiveness for the entire loan. There is \$0 income tax on the \$100,000, and the business can reduce its taxable income by deducting \$100,000 spent on qualified PPP expense.

Now, many borrowers will need to rethink their recent tax planning, which was based on the earlier, less helpful IRS guidance.

## What to Expect From the Second Round of PPP Loans

The first round of PPP Loans resulted in a great deal of confusion that has fortunately been made clearer through additional updates from Congress and the IRS.

Now, you have a second opportunity to secure additional relief funds with clearer expectations on how to receive the funds and how to have those funds forgiven. Additionally, borrowers may even find a way in the new Act to increase their original loan amounts.

### Securing PPP Loan Funds

The new Act, contains a new pool of roughly \$284 billion for a second draw of the PPP. These funds, which are intended to help struggling small businesses across America, are an extension of the program created under the CARES Act in March of 2020. There are several changes from the original program, including changing who and how to qualify for the loans, as well as the total loan amounts that are offered to businesses.

## A. The Second PPP Loan

### Eligibility for Second PPP Loan

The new Act provides that eligible business may apply for a second PPP Loan. To apply for a second PPP Loan, the business must:

- Have experienced a revenue decrease of 25% or more in any 2020 quarter as compared to the same 2019 quarter, and
- Have a total amount of employees not exceeding 300 (down from the original requirement of no more than 500 employees in order to qualify for the loan).

### Calculating the Second PPP Loan Amount

- The maximum amount of a second PPP Loan (not to exceed \$2 million in any case) is either 2.5 (3.5 for food service establishment and restaurants) times the average monthly payroll for the last twelve months through the application date, or the average 2019 monthly payroll.
- All affiliated borrowers' loans from the first and second rounds of PPP Loans may not exceed \$10 million.
- Limitations apply for businesses with multiple locations (aggregated total must be less than \$2 million)

The covered period for a second PPP Loan lasts through March 31, 2021; however, note that borrowers can now choose between a covered period ending at any point between 8-weeks and 24-weeks after the loan is disbursed (previously, borrowers could only either elect an 8-week or 24-week covered period.) The funds can be used for the same list of qualified expenses as the first draw loans, with the added benefit of being able to use the second draw funds for operating expenses, workplace protection costs for COVID prevention, and covered property damage.

As with Round One PPP Loans, in order for Second Round PPP Loans to qualify for forgiveness, 60% of the total amount of the loan must be used for the payment of payroll expenses.

## B. You May be Able to Increase Your Round One PPP Loan

Perhaps most significantly for partnerships and certain sole proprietors, the new Act provides the opportunity to in-

crease a Round One PPP Loan. Remember, initially, it was widely believed that those partnerships and sole proprietors could borrow based only on the wages paid to employees and were precluded from factoring in their partner compensation or self-employment income.

When guidance was finally released to resolve the confusion around this matter, many borrowers were past the point where they could return to their lender and request an increase in the loan.

Now, the Act allows borrowers who faced that predicament to go back to their lenders and try to increase their loans.

Additionally, note that some borrowers returned all, or part of their First Round PPP Loans based on early SBA guidance. The new Act provides that the SBA must release new guidance about this subject within 17 days of the new Act's passage.

### C. PPP Loan Forgiveness Changes

Certain borrowers will find that the new Act has simplified obtaining forgiveness of their PPP Loans. The new Act allows 24 days after enactment for the SBA to create a one-page certification form for borrowers with a PPP Loan (new or old) less than \$150,000. Using that form, borrowers certify their compliance with the loan requirements and provide certain required information. Thereafter, it is expected that the loan will be forgiven.

**If you or your business is unsure if you qualify for the new second draw PPP loans or have questions about applying, please feel free to contact our team by calling (410) 862-2834 or requesting a consult online.**

## Additional Resources



### FinCEN Notice Continues Deferral Trend for Certain Signatories Lacking Financial Interest in Foreign Accounts

Executive Summary ✓ Notice 2020-1 maintains deferral of FBAR filing deadline for certain individuals having signature authority ...



### The Unforgiving Nature of PPP Forgiveness and the IRS' New Guidance

Executive Summary ✓ The IRS issued guidance clarifying that a taxpayer (even one that has not applied for PPP loan forgiveness by ...

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