



December 15, 2020

VIA ELECTRONIC SUBMISSION

The Honorable Marco Rubio
Chairman
Committee on Small Business &
Entrepreneurship
United States Senate
428A Russell Senate Office Building
Washington, D.C. 20510

The Honorable Nydia Velázquez
Chairwoman
Committee on Small Business
United States House of Representatives
2361 Rayburn House Office Building
Washington, DC 20515

The Honorable Ben Cardin
Ranking Member
Committee on Small Business &
Entrepreneurship
United States Senate
428A Russell Senate Office Building
Washington, D.C. 20510

The Honorable Steve Chabot
Ranking Member
Committee on Small Business
United States House of Representatives
2069 Rayburn House Office Building
Washington, D.C. 20515

Re: Deductibility of Business Expenses Paid with Forgiven PPP Loans

Dear Chairman Rubio, Chairwoman Velázquez, Ranking Member Cardin, and Ranking Member Chabot:

The Coronavirus Aid, Relief, and Economic Security (CARES) Act provided much needed economic relief for small businesses suffering from the economic conditions created by the current pandemic. The legislation created the Paycheck Protection Program (PPP), which allowed millions of small businesses to keep employees on the payroll and physical business locations intact even when their doors had to be closed because of state and local stay-at-home and business closure orders. The PPP premise is relatively straightforward: use the funds to pay for payroll and other qualifying non-payroll expenses and the loan will be forgiven. Section 1106(i) of the CARES Act specifically states that forgiven PPP loans are not taxable income. The PPP seemed to be the lifeline small businesses needed. Approximately one month later those same small businesses were handed a surprise when the Internal Revenue Service (IRS) published [Notice 2020-32](#), which announced the agency's position that otherwise deductible business expenses paid with forgiven PPP loans are not deductible. Small business taxpayers could now be faced with unplanned and unbudgeted increases in federal income tax liabilities of up to 37 percent for 2020. The Office of Advocacy urges Congress to pass legislation to amend

the CARES Act to state that otherwise deductible business expenses paid with a forgiven PPP loan are still deductible business expenses.

Congress established Advocacy under Pub. L. 94-305 to represent the views of small entities before federal agencies and Congress. Advocacy is an independent office within the U.S. Small Business Administration (SBA); as such the views expressed by Advocacy do not necessarily reflect the views of the SBA or the Administration. The Office of Advocacy held a roundtable on December 4, 2020, to discuss the federal and state tax issues surrounding the PPP. There were approximately 150 people in attendance, including small business stakeholders, representatives from Treasury, the IRS, and the SBA, and congressional staff. Representatives of KPMG and the Tax Foundation were presenters at the roundtable; they and a majority of the small business stakeholders in attendance agreed that Treasury and the IRS's position on the deductibility of expenses paid with forgiven PPP loans is contrary to congressional intent and that legislation is needed to address the issue.

Generally, taxpayers can deduct ordinary and necessary business expenses paid or incurred during a taxable year. The business expenses paid with PPP loans would ordinarily be included in such expenses. The IRS published Notice 2020-32 on April 30, 2020, almost one month after the CARES Act was signed into law and millions of dollars of PPP funding was already distributed. The notice provides guidance on the agency's position that business expenses paid with forgiven PPP loans are not deductible under § 265 of the Internal Revenue Code (Code) because the expenses flow from a class of tax-exempt income – the forgiven PPP loan. Therefore, the taxpayer would be receiving a double tax benefit – a forgiven loan not included in taxable income and a deduction for the expenses paid with the forgiven loan. Secretary Mnuchin has stated publicly that such “double dipping” is not allowed under the Code.¹ On May 5, 2020, Senate Finance Committee Chairman Chuck Grassley and Ranking Member Ron Wyden and House Ways and Means Committee Chairman Richard Neal sent a letter to Secretary Mnuchin stating that Treasury and the IRS's position is contrary to the intent of the PPP.²

In November, however, Treasury and the IRS published Revenue Procedure 2020-51 and Revenue Ruling 2020-27. Not only does the IRS reaffirm its position that otherwise deductible ordinary and necessary business expenses paid with forgiven PPP loans are not deductible – despite Congress' direct statements to Treasury that such a position was in conflict with the intent of the PPP– it increases the universe of loans to which Notice 2020-32 applies to include

¹ Naomi Jagoda, *Mnuchin Defends IRS Guidance on PPP Loans*, The Hill, (May 4, 2020, 2:13 PM EDT), [Mnuchin defends IRS guidance on PPP loans | TheHill](#).

² Letter from Senator Chuck Grassley, Senator Ron Wyden, and Representative Richard Neal to Treasury Secretary Steven T. Mnuchin (May 5, 2020), [2020-05-05 CEG, RW, RN to Treasury \(PPP Business Deductions\).pdf \(senate.gov\)](#).

all PPP loans that have “a reasonable expectation of forgiveness.”³ According to the IRS, this reasonable expectation of forgiveness requirement applies even if the taxpayer has not yet applied for forgiveness of a PPP loan.

The intent of the PPP is for businesses to keep employees on the payroll even though those businesses are or have been either completely closed by or experiencing greatly reduced revenues because of the pandemic. Treasury and the IRS are misinterpreting this intended benefit of the PPP, and, thus, small businesses will have to shoulder a large portion of the economic weight of the pandemic through increased tax liabilities for 2020. Legislation correcting the tax treatment of PPP loans and explicitly stating that ordinary and necessary business expenses paid with forgiven PPP loans are deductible business expenses is necessary to save millions of taxpayers from increases in tax liabilities that will cause lasting damage to small businesses.

If you have any questions or require additional information please contact me, Assistant Chief Counsel for Tax and Employee Benefits Policy Charles Jeane at (202) 205-7168 or Charles.Jeane@sba.gov, or Assistant Chief Counsel for Congressional and Legislative Affairs Stephanie Fekete at (202) 205-6888 or Stephanie.Fekete@sba.gov.

Sincerely,



Major L. Clark, III
Acting Chief Counsel
Office of Advocacy
U.S. Small Business Administration

/s/ Charles G. Jeane
Assistant Chief Counsel
Office of Advocacy
U.S. Small Business Administration

Copy to: Paul Ray, Acting Administrator
Office of Information and Regulatory Affairs
Office of Management and Budget

³ After publication of the Revenue Procedure and Revenue Ruling, Congress again stated that Treasury’s position was contrary to the intent of the PPP. *See* Press Release, Senator Chuck Grassley, Grassley, Widen: Treasury Misses the Mark on PPP Loan Expense Deductibility Guidance (Nov. 19, 2020) ([Grassley, Wyden: Treasury Misses the Mark on PPP Loan Expense Deductibility Guidance | Chuck Grassley \(senate.gov\)](https://www.senate.gov/legislative/record/2020/press_releases/20201119-grassley-widen-treasury-misses-the-mark-on-ppp-loan-expense-deductibility-guidance)). *See also* Press Release, Representative Nydia Velázquez, Velázquez Calls on Trump Administration to Reverse Stance on Deductibility for PPP Borrowers (Nov. 23, 2020) ([Velázquez Calls on Trump Administration to Reverse Stance on Deductibility for PPP Borrowers | Small Business Committee \(house.gov\)](https://www.house.gov/representatives/nydia-velazquez/velazquez-calls-on-trump-administration-to-reverse-stance-on-deductibility-for-ppp-borrowers)).