

IRS Provides Safe Harbor to Deduct Certain 2020 PPP Related Expenses in 2021

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Before enactment of the 2021 Consolidated Appropriations Act on December 27, 2020, the Internal Revenue Service took the position that [taxpayers could not deduct expenses](#) paid with proceeds of a forgiven PPP loan. By passage of the [Consolidated Appropriations Act](#), Congress [reversed this position](#). The Internal Revenue Service now has announced a safe harbor in [Revenue Procedure 2021-20](#) that will permit certain taxpayers an election to deduct in 2021 expenses paid with proceeds of a forgiven PPP loan that were not claimed as a deduction on their tax return or information return filed in 2020. Without this election, a taxpayer would need to file an amended return or administrative adjustment request for its 2020 taxable year to claim a deduction for expenses paid in 2020 with the proceeds of a forgiven PPP loan.

A taxpayer eligible to make the election (referred to as a “Covered Taxpayer”) is one who satisfies all of the following:

- The taxpayer received an original PPP covered loan;
- The taxpayer paid or incurred original eligible expenses during the taxpayer’s 2020 taxable year;
- On or before December 27, 2020, the taxpayer timely filed, including extensions, a Federal income tax return or information return, as applicable, for the taxpayer’s 2020 taxable year; and
- On the taxpayer’s Federal income tax return or information return, as applicable, the taxpayer did not deduct the original eligible expenses because:
 - The expenses resulted in forgiveness of the original PPP covered loan; or
 - The taxpayer reasonably expected at the end of the 2020 taxable year that the expenses would result in such forgiveness.

An important point to note is that a calendar year taxpayer with a taxable year ending December 31, 2020, is not eligible to make the election. This election only is applicable to certain taxpayers with a fiscal tax year other than the calendar year. Presumably, taxpayers filing returns after December 27, 2020, would have known that the Consolidated Appropriations Act changed the law to permit a deduction for expenses paid with proceeds of a forgiven PPP loan.

To make a valid election to apply the safe harbor, a Covered Taxpayer must satisfy the following conditions:

1. It must make the election by attaching an election statement to its timely filed, including extensions, Federal income tax return or information return, as applicable, for its first taxable year following its 2020 taxable year in which the original eligible expenses were paid or incurred; and
2. The election statement must be titled “Revenue Procedure 2021-20 Statement” (and named RevProc2021-20.pdf for e-file attachments) and include the following information:
 1. The Covered Taxpayer’s name, address, and social security number or taxpayer identification number;
A statement that the Covered Taxpayer is applying the safe harbor provided by section 3.01 of Revenue Procedure 2021-20;
 2. The amount and date of disbursement of the taxpayer’s original PPP covered loan; and
 3. A list, including descriptions and amounts, of the original eligible expenses paid or incurred by the Covered Taxpayer during the Covered Taxpayer’s 2020 taxable year that are reported on the Federal income tax return or information return, as applicable, for the Covered Taxpayer’s first taxable year following that 2020 taxable year.

The safe harbor will help those taxpayers whose 2020 fiscal taxable year ended on or before December 27, 2020. Taxpayers whose 2020 taxable year ends after December 27, 2020, which would include all calendar year taxpayers, will have to file an amended return or administrative adjustment request if they failed to claim a deduction for expenses paid in 2020 with proceeds of a forgiven PPP loan. A taxpayer eligible to make the election should review last year’s return to determine whether to file the election or an amended return. If the taxpayer had taxable income and paid taxes in the 2020 tax year, it may be better to file an amended return with a refund request than to file the election. Any unused loss which the expenses created could then be carried over to the next year’s tax return.

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