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Guidance addresses deductibility of expenses related to Paycheck Protection Program loans

The Internal Revenue Service and Treasury Department on April 30 announced in Notice 2020-32 that no deduction is allowed for an expense that is otherwise deductible if the payment of the expense (*i.e.*, rent, utility and payroll costs) results in forgiveness of a covered loan under the Paycheck Protection Program in the Coronavirus Aid, Relief, and Economic Security Act (CARES) Act (P.L. 116-136).
URL: https://www.irs.gov/pub/irs-drop/n-20-32.pdf

The Service further held that the income associated with the forgiveness is excluded from gross income – an outcome expressly contemplated by the text of the CARES Act – and is therefore a “class of exempt income.” Accordingly, Treasury would prevent a “double benefit” and deny deductions under section 265. Neither the statute nor the recently a released report from the Joint Committee on Taxation staff describing the CARES Act’s tax title provides that deductions associated with loan forgiveness should be denied.
URL: https://www.jct.gov/publications.html?func=startdown&id=5256

The Service’s holding is expected to attract attention on Capitol Hill, and Congress may attempt to include corrective language in the next coronavirus economic recovery package – or in a possible interim bill authorizing additional funds for the Paycheck Protection Program should lawmakers decide another infusion of cash is needed to meet the continuing demand for loans. (Alternatively, lawmakers could instead urge Treasury to reverse its decision.)

The government also released several additional guidance items this week that address other issues related to the Paycheck Protection Program.

- **Loan reviews, qualification issues:** An updated FAQ page published by the Small Business Administration (SBA) in consultation with the Treasury Department indicates that the SBA will review all loans in excess of $2 million, in addition to other loans as appropriate, following the lender's submission of the borrower's loan forgiveness application (Question 39). It also addresses whether businesses owned by private companies with adequate sources of liquidity to support the business's ongoing operations qualify for a loan under the program (Question 37).
  URL: https://home.treasury.gov/system/files/136/Paycheck-Protection-Program-Frequently-Asked-Questions.pdf
- **Promissory notes, authorizations, affiliation, and eligibility:** The Treasury Department released an interim final rule under the Paycheck Protection Program addressing requirements for promissory notes, authorizations, affiliation, and eligibility.
  URL: https://home.treasury.gov/system/files/136/Interim-Final-Rule-on-Requirements-for-Promissory-Notes-Authorizations-Affiliation-and-Eligibility.pdf
- **Loans to seasonal employers:** Treasury also issued an interim final rule authorizing all lenders eligible to originate loans under the Paycheck Protection Program to use an alternative criterion for calculating the maximum loan amount for loans issued to seasonal employers.
  URL: https://s3.amazonaws.com/public-inspection.federalregister.gov/2020-09239.pdf

Employee retention credit guidance

In other developments, the IRS updated its FAQ page on the CARES Act's employee retention tax credit enacted to address issues such as:
URL: https://www.irs.gov/newsroom/faqs-employee-retention-credit-under-the-cares-act

- How the credit interacts with other tax code provisions such as the Paycheck Protection Program and payroll tax deferral (both enacted in the CARES Act), as well as the Work Opportunity Tax Credit, and the credit under section 45S for employers that provide paid family and medical leave.
- When an employer's trade or business operations are considered to be fully or partially suspended due to a governmental order;
- When an employer is considered to have a significant decline in gross receipts;
- How to determine the maximum amount of an eligible employer's employee retention credit;
- How to determine qualified wages; and
- How to determine the amount of qualified health plan expenses that is treated as qualified wages under the credit – including whether an employer can treat health plan expenses as qualified wages if it continues the employees' health care coverage, but does not pay the employees' wages for the time for which the employees are not providing services.

Estate and gift tax guidance

The IRS also published a new FAQ page that discusses changes to filing and payment deadlines for estate and gift taxes as a result of the coronavirus pandemic.
URL: https://www.irs.gov/businesses/small-businesses-self-employed/covid-19-relief-for-estate-and-gift

Electronic submission of guidance requests

The IRS on April 30 issued Rev. Proc. 2020-29, which temporarily allows electronic submission of requests for letter rulings, closing agreements, determination letters, and information letters under the jurisdiction of the Office of Chief Counsel, and for determination letters issued by the Service's Large Business and International Division, and explains the specific procedures taxpayers will need to follow. Rev. Proc. 2020-29 is effective as of April 30, 2020, and will remain in effect until it is modified or superseded.
URL: https://www.irs.gov/pub/irs-drop/rp-20-29.pdf

Find out more

A running list of resources that address significant tax issues stemming from the pandemic is available from Deloitte Tax LLP.
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/Stimulus-Resource-Table.pdf

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No clear path for next economic recovery bill as House and Senate stagger their return to Capitol Hill

While the House this week reversed course on its schedule and decided to postpone its return to Washington, the Senate is still on course to be back in session beginning on May 4. However, Democrats and Republicans are still at loggerheads over the path forward on the next economic relief and recovery bill to address the coronavirus emergency, and the Senate is not expected to take up any measures on that front in the coming days.

House leaders said the decision to delay their return to session was based on advice from the Capitol physician, who noted that COVID-19 cases in the Washington region are still on the rise. (The District of Columbia's current stay-at-home order runs through May 15.) In addition, House Majority Leader Steny Hoyer, D-Md., said that his caucus is still developing their proposal for the next relief package and does not need to bring members in from across the country until that legislation is ready for House consideration. House Speaker Nancy Pelosi, D-Calif., told reporters April 30 that the current plan is for the House to return the week of May 11.

Senate Majority Leader Mitch McConnell, R-Ky., meanwhile, said in an April 29 radio interview that "if people on the front lines are willing to work during the pandemic, we should be as well. And so the Senate will…be in session next week." But McConnell has disagreed with Democrats' push for another bill in the near term, repeatedly saying that the relief measures that have been enacted to date – amounting to nearly $3 trillion in spending – should be allowed to work their way into the economy first. The Senate's full agenda for its first week back in session is unclear, but there are at least two nomination hearings teed up, including one in the Intelligence Committee to consider President Trump's nomination of Rep. John Ratcliffe, R-Texas, to become director of national intelligence.

House Democrats eyeing aid to states

House Democrats reportedly have been holding near-daily conference calls during the recess to discuss the implementation of earlier relief legislation and ideas for another package. One priority certain to be included in the Democrats' next proposal is additional funding for state and local governments, which they unsuccessfully sought to include in the most recent relief bill – the Paycheck Protection Program and Health Care Enhancement Act (P.L. 116-139) enacted late last month. (For prior coverage, see *Tax News & Views*, Vol. 21, No. 23, Apr. 24, 2020.)
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/200424_1.html

House Ways and Means Committee Chairman Richard Neal, D-Mass., told members of the United States Conference of Mayors during an April 29 video call that Democrats will insist "that this package include direct assistance to all of you."

"As Congress works on the next response legislation, we want to be sure we can help you shore up the economic health of your cities," Neal said. He also noted that details of the Democrats' plan are likely to be unveiled "in the next few days and certainly within the next week."

Brady demurs: But some congressional Republican leaders have countered in recent days that Congress already has allocated a significant amount to state and local governments in the economic relief measures it has approved to date.

"Congress has already funded over $700 billion to state and local governments, that's more than we funded our small businesses," said Ways and Means Committee ranking member Kevin Brady, R-Texas, in a press statement April 29. "And that's direct aid, state and local government, state unemployment funding, local hospitals, state and local disaster aid, local school funding, state college funding, local mass transit funding, plus we muscled up Medicaid 6 percent to help them through this crisis."

McConnell attaches conditions: For his part, Senate Majority Leader Mitch McConnell told Fox News April 28 that he and his Republican colleagues are open to considering further assistance in the next bill for state and local governments but that anything they support will be limited in scope to address economic losses specifically tied to the coronavirus.

McConnell also told Fox News Radio April 29 that in exchange for further funding for state and local governments, he wants Congress to include liability protections for health care workers, business owners, and employees as the country emerges from its lockdown over the coming weeks and months.

"I want to make sure we protect the people we've already sent assistance to who are going to be set up for an avalanche of lawsuits if we don't act," he said, noting that he wants to ensure businesses can't be sued by customers who contract the coronavirus.

Such liability protections have met with opposition from Democrats, with a spokesman for House Speaker Nancy Pelosi telling *The Washington Post*, that "[t]he House has no interest in diminishing protections for employees and customers."

White House wavers: President Trump recently expressed support for including federal aid to localities, among other priorities, in the next recovery bill. In an April 23 statement posted on Twitter ahead of the Senate vote on the Paycheck Protection Program and Health Care Enhancement Act, for example, the president said "After I sign this Bill, we will begin discussions on the next Legislative Initiative with fiscal relief […] to State/Local Governments for lost revenues from COVID 19, much needed Infrastructure Investments for Bridges, Tunnels, Broadband, Tax Incentives for Restaurants, Entertainment, Sports, and Payroll Tax Cuts to increase Economic Growth."

However, the president has since backed away some from that position, asking in an April 27 post on Twitter why taxpayers should "be bailing out poorly run states…and cities." He also told a reporter on April 30 after a meeting with Democratic New Jersey Gov. Phil Murphy that whether to provide federal aid to state and local governments is "a tough question."

Going big – or small – on infrastructure?

Ways and Means Chairman Neal said in his April 29 call with the United States Conference of Mayors that the House Democrats' plan will include a revival of the now-expired Build America Bonds – taxable municipal bonds enacted in the American Recovery and Reinvestment Act of 2009 to encourage investment in local areas, which featured federal tax credits or subsidies for bondholders or state and local government bond issuers – and the use of private activity bonds. He said he also favors revenue-sharing arrangements similar to those of the 1980s and he noted that he is working closely with Treasury Secretary Steven Mnuchin to include major infrastructure provisions.

Across the Capitol, however, Senate Majority Leader McConnell has been much more bearish on the idea of including infrastructure in the next recovery bill despite the president's stated enthusiasm. In an April 28 interview with Fox News, McConnell said he agrees with President Trump on the need for an infrastructure bill but is concerned about the rapidly increasing national debt.

"We have an equal interest in doing an infrastructure bill," he said. "We don't have an equal interest in borrowing money from future generations to pay for it. It's unrelated to the coronavirus pandemic."

McConnell added that the Senate will pass "a more modest infrastructure bill" in the near future. An aide later told reporters that McConnell was referring to several bipartisan bills drafted by Sen. John Barrasso, R-Wyo., that are focused on roads, bridges, and water infrastructure. At less than $300 billion combined, the funding in these bills would be far less than the $2 trillion President Trump has often called for, although the president also has endorsed Barrasso's highway bill.

Other potential contenders

Other ideas that have been widely floated among House Democrats for possible inclusion in the next recovery package include a second round of rebate checks to supplement the payments sent to many taxpayers under the Coronavirus Aid, Relief, and Economic Security Act (CARES) Act (P.L. 116-136), increased funding for nutrition assistance, and funding for the cash-strapped US Postal Service. Democrats also are mulling proposals such as direct assistance for housing, a further extension of expanded unemployment insurance, money for election security and vote-by-mail initiatives, hazard pay for front-line workers, child-care assistance, and more money for health providers and hospitals.

Some congressional Republicans, meanwhile, seem interested in pursuing a robust relief package, although other voices in the GOP, echoing Majority Leader McConnell, are urging their colleagues to better measure the effect of the relief that has already been enacted before pursuing additional measures that will further increase the deficit.

Democratic members named to House coronavirus subcommittee

Also this week, House Speaker Nancy Pelosi announced the names of the Democrats who will serve on the House Select Subcommittee on the Coronavirus Crisis, a newly formed panel charged with overseeing implementation of coronavirus relief legislation.

Democratic members of the subcommittee include Financial Services Committee Chairwoman Maxine Waters of California, Oversight and Reform Committee Chairwoman Carolyn Maloney of New York, and Small Business Committee Chairwoman Nydia Velázquez of New York, along with Reps. Bill Foster of Illinois, Jamie Raskin of Maryland, and Andy Kim of New Jersey.

The panel, which will operate as part of the House Oversight Committee, will be headed by Majority Whip Jim Clyburn of South Carolina.

Speaker Pelosi announced her intention to form the subcommittee in March. A resolution (H. Res. 935) formally establishing the panel cleared the House on April 23 by a party-line vote of 212-182. (For prior coverage, see *Tax News & Views*, Vol. 21, No. 23, Apr. 24, 2020.)
URL: https://www.govinfo.gov/content/pkg/BILLS-116hres935ih/pdf/BILLS-116hres935ih.pdf
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/200424_2.html

The resolution provides that the subcommittee will include up to 12 members – 7 Democrats and 5 Republicans. As of press time, House GOP leaders had not announced who they will name to serve on the subcommittee.

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CBO preliminary estimates show budget deficit reaching $3.7 trillion this year

Preliminary projections released by the nonpartisan Congressional Budget Office (CBO) on April 24 show the federal budget deficit reaching $3.7 trillion in fiscal year 2020 (which ends on September 30) – more than three times what the agency predicted in early March – a revenue-spending mismatch that could grow even more should lawmakers agree on additional unpaid-for fiscal relief related to the coronavirus pandemic.

The figures – published in a blog post by CBO Director Phill Swagel – are intended to give policymakers an initial view into the cumulative impact on near-term budget deficits of recently enacted coronavirus relief legislation, as well as insight into how the contracting economy has changed the agency's most recent "baseline" projections of revenues and spending that were released in March and which were keyed off of economic projections formulated in January.
URL: https://www.cbo.gov/publication/56335
URL: https://www.cbo.gov/publication/56268
URL: https://www.cbo.gov/publication/56073#_idTextAnchor003

"To develop a preliminary view of the deficit…CBO took into account the estimated effects on the deficit of pandemic-related legislation enacted on March 4, March 18, March 27, and April 24," Swagel wrote. "CBO made a rough assessment of the overall changes in federal spending and revenues resulting from the sharp deterioration in the economic outlook since January, when the agency issued its most recent complete economic forecast."

Deficits and debt to set new records

Although the numbers released April 24 do not constitute a full baseline – that is, the agency's usual "current law" analysis of projected federal revenue and spending, typically over the next 10 years – they do detail CBO's current best thinking as to how the coronavirus pandemic may affect the federal budget and economy this year and next. (Swagel pointed out that an update of the 10-year baseline will be released "later this year." Although he did not state it in his post, CBO often publishes an update each August.)

Altogether, CBO sees deficits reaching $3.7 trillion in the current fiscal year and $2.1 trillion in fiscal year 2021, up from the already-elevated $1 trillion annual deficits projected in the agency's March baseline.

By far, the largest contributor to the increase is the so-called "Phase 3" coronavirus relief bill – the Coronavirus Aid, Relief, and Economic Security (CARES) Act (P.L. 116-136) – which will add about $1.7 trillion to the deficit in fiscal 2020 alone. (For prior coverage of the CBO's revenue estimate for CARES Act, see *Tax News & Views*, Vol. 21, No. 22, Apr. 17, 2020.)
URL: https://www.cbo.gov/system/files/2020-04/hr748.pdf
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/200417_1.html

As a share of gross domestic product (GDP), CBO projects the fiscal 2020 deficit will amount to 17.9 percent of the economy, easily surpassing the post-World War II peak of 9.8 percent of GDP reached during the 2009 recession. Next year, the agency sees the deficit falling back to slightly less than 10 percent of the economy. For comparison, over the past five decades, deficits have averaged about 3.0 percent of GDP.

CBO also estimates that the publicly held debt – that is, debt not held in intragovernmental accounts such as the Social Security and Medicare trust funds – will exceed the size of the economy by the end of the current fiscal year. In previous projections, the agency did not expect that outcome would occur until about 2030.

And of course, if additional unoffset fiscal stimulus is enacted later this year as is presently expected, these deficit and debt projections would presumably get even larger.

Still, in an odd twist, due to recent Federal Reserve interest rate policy, CBO predicts that the government's debt service costs will actually decrease this year relative to its previous projections as rates fall both on newly issued and rolled-over Treasury debt.

Economic contraction

Setting aside the coronavirus relief legislation enacted so far, a significant portion of the increases in the budget deficit this year and next – relative to CBO's March baseline which, again, was formulated based on a stronger economic forecast developed in January – is attributable to the agency's updated prediction that the economy will contract, particularly during the second calendar quarter of 2020, and the reverberating effect that will have on federal revenues and spending.

According to the CBO, real GDP could fall by an annualized rate of 39.6 percent in the second quarter of this year as the unemployment rate reaches 14 percent – a figure that itself would be muted by the agency's prediction that roughly 8 million people will be counted as leaving the labor force in the second and third quarters of 2020, and thus not be counted in the denominator that determines the jobless rate.

On a positive note, however, the agency sees the economy recovering in the second half of the year such that GDP would contract by a comparatively smaller 5.6 percent over the course of calendar year 2020.

Even so, CBO cautions that its preliminary projections are "subject to enormous uncertainty" that rely in large part on hard-to-decipher predictions about the future course of the pandemic and the resulting social distancing mandates that could apply.

"CBO's projections incorporate an expectation that the current extent of social distancing across the country will continue…through June," Director Swagel notes in the blog post. "The agency's projections also include the possibility of a reemergence of the pandemic. To account for the possibility, social distancing is projected to continue, although to a lesser degree, through the first half of next year."

The post goes on: "To develop [its] projections, CBO examined an array of outside projections…by academic institutions, government agencies, and other research groups. Those efforts pointed to a wide range of possible outcomes. In CBO's assessment, the agency's projection of the extent of social distancing is consistent with a pandemic projection in the center of that range."

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