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## Congress of the United States

JOINT COMMITTEE ON TAXATION  
502 FORD HOUSE OFFICE BUILDING  
WASHINGTON, DC 20515-6453  
(202) 225-3621  
<http://www.jct.gov>

July 27, 2020

Honorable John Cornyn  
United States Senate  
517 Hart Senate Office Bldg.  
Washington, DC 20510

Dear Senator Cornyn:

This letter discusses the staff of the Joint Committee on Taxation's revenue estimate of your proposed legislation, S. 3612, the "Small Business Expense Protection Act of 2020" (the "proposal").

As background, the Coronavirus Aid, Relief, and Economic Security ("CARES") Act (Public Law 116-136)<sup>1</sup> established an emergency loan program to be administered by the Small Business Administration (the "Paycheck Protection Program").<sup>2</sup> A recipient of a covered loan (*i.e.*, a loan pursuant to the Paycheck Protection Program) is eligible for forgiveness of indebtedness on the loan in an amount generally equal to the sum of certain costs incurred and payments made during the eight-week period beginning on the date of the origination of the covered loan, including certain payroll costs, certain mortgage interest payments, certain rent payments, and certain utility payments.<sup>3</sup> For Federal tax purposes, any amount which (but for the provision providing such forgiveness) would be includible in gross income of the recipient of a covered loan by reason of such forgiveness is excluded from gross income.<sup>4</sup>

In March 2020 the Congressional Budget Office ("CBO") and the staff of the Joint Committee on Taxation ("Joint Committee staff") provided estimated budget effects of CARES. As newly proposed policy, the Paycheck Protection Program loans were not part of the baseline of projected Federal outlays. The forgiveness of the loans under qualifying circumstances did not "score" because these loans were not part of the baseline. The Joint Committee staff's understanding of the CBO's estimate of the Paycheck Protection Program is that it included the payments made to lenders for forgiveness of qualifying debt but made no adjustment to estimates of business net income or loss, as might arise from expenses business owners incurred to qualify for loan forgiveness.

<sup>1</sup> March 27, 2020.

<sup>2</sup> Sec. 1102 of the CARES Act.

<sup>3</sup> Sec. 1106(b) of the CARES Act.

<sup>4</sup> Sec. 1106(i) of the CARES Act.

**Congress of the United States**  
JOINT COMMITTEE ON TAXATION  
Washington, DC 20515-6453

Honorable John Cornyn  
United States Senate

Page 2

The Joint Committee staff understood the intent of the legislation was not to deny deductions for qualifying expenses. Therefore, the Joint Committee staff did not assume that the baseline of allowable expenses was modified by the policy of CARES. If a qualifying taxpayer received payment from the Paycheck Protection Program that was excludable under section 1106 of CARES, the CBO estimate measured that forgiveness as part of its outlay projections and the Joint Committee staff counted expenses as allowable to the taxpayer.

After the enactment of the CARES Act, the IRS issued Notice 2020-32<sup>5</sup> (the “Notice”), stating that no deduction is allowed under the Internal Revenue Code of 1986 (the “Code”) for an expense that is otherwise deductible if the payment of the expense results in forgiveness of a covered loan pursuant to section 1106(b) of CARES Act and the income associated with the forgiveness is excluded from gross income for purposes of the Code pursuant to section 1106(i) of the CARES Act. The Notice relies on section 265(a) of the Code, which denies a deduction to a taxpayer for any amount otherwise allowable as a deduction that is allocable to one or more classes of income other than interest (whether or not any amount of income of that class or classes is received or accrued) wholly exempt from Federal income tax. The Notice describes this treatment as necessary to prevent “a double benefit.”

The proposal would provide that no deduction would be denied or reduced, no tax attribute would be reduced, and no basis increase would be denied, by reason of the exclusion from gross income described above. In effect, the proposal would reverse the result provided in the Notice.

In the absence of the exclusion from gross income provided in section 1106(i) of the CARES Act, the amounts forgiven pursuant to section 1106(b) of the CARES Act would be includible in gross income of the taxpayer and a deduction generally would be allowed to the taxpayer for any ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business. In other words, in the absence of such exclusion, there would be an inclusion in gross income and an offsetting deduction. The combined effect of section 1106(i) of the CARES Act and the Notice is similar; that is, there is an exclusion from gross income and an associated denial of deductions.

The combined Federal income tax effect of the Notice and section 1106(i) of the CARES Act is similar to the Federal income tax effect of the forgiveness provided in section 1106(b) of the CARES without the exclusion in section 1106(i) of the CARES Act. Our staff understands (1) the exclusion in section 1106(i) of the CARES Act to be changing the baseline Federal

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<sup>5</sup> Published May 2, 2020.

**Congress of the United States**  
JOINT COMMITTEE ON TAXATION  
Washington, DC 20515-6453

Honorable John Cornyn  
United States Senate

Page 3

income tax result, and thus (2) that the intent of that provision was not to deny deductions with respect to otherwise qualifying expenses. In other words, we understand the proposal to be consistent with the original Congressional intent of section 1106(i) of the CARES Act.

The amendments made by the proposal would apply as if included in the enactment of section 1106 of the CARES Act. For the reasons stated above, the proposal would have no effect on Federal fiscal year budget receipts.

I hope this information is helpful to you. If we can be of further assistance in this matter, please let me know.

Sincerely,



Thomas A. Barthold

cc: Andrew Siracuse