

Current Federal Tax Developments

Week of August 31, 2020

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ACCOUNTING
CONTINUING EDUCATION

CURRENT FEDERAL TAX DEVELOPMENTS
WEEK OF AUGUST 31, 2020
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Published in 2020 by Kaplan Financial Education.

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SECTION: 61

INCOME WILL BE REALIZED BY PARTICIPANTS PAID IN CONVERTIBLE VIRTUAL CURRENCIES FOR COMPLETING MICROTASKS VIA A CROWDSOURCING PLATFORM

Citation: CCA 202035011, 8/28/2020

The IRS has returned to the virtual currency taxation subject area, this time in a Chief Counsel Advice ruling on the tax consequences for individuals that receive convertible virtual currency in exchange for performing microtasks through a crowdsourcing or similar platform.¹

The IRS in this memorandum looks at the tax consequences for individuals using a crowdsourcing platform to provide services. A crowdsourcing arrangement is described in the memorandum as follows:

A variety of digital platforms now enable individuals or entities to “crowdsource” jobs by using the Internet to outsource assignments to an undefined and often large group of other individuals or entities. A crowdsourcing arrangement may involve three parties referred to in this memorandum as vendors, firms, and workers. Vendors develop a platform upon which firms can broadcast their tasks and workers can accept, perform and/or submit the work.²

The memorandum then goes on to describe microtasking and microtasks:

Certain crowdsourcing platforms specifically facilitate the practice of microtasking, which may involve subdividing larger tasks into smaller tasks and distributing the tasks via online crowdwork platforms. In general, microtasks are simple, menial activities that still require some degree of human interaction beyond the current ability of artificial intelligence.³

In the case the IRS is looking at, those performing microtasks are paid in a convertible virtual currency, such as Bitcoin:

Certain microtasking platforms allow those who perform microtasks to receive payments in consideration for completing each microtask in the form of convertible virtual currency. For example, a firm may offer to pay workers in units of Bitcoin or other convertible virtual currency if the worker processes data or reviews images. Other examples include an offer of convertible virtual currency in exchange for downloading a particular app from an app store and leaving a positive review including a comment, downloading games and reaching certain

¹ CCA 202035011, August 28, 2020 <https://www.irs.gov/pub/irs-wd/202035011.pdf> (retrieved August 28, 2020)

² CCA 202035011, pp. 1-2

³ CCA 202035011, p. 2

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milestones, completing online quizzes and surveys, or registering accounts with various online services. These types of microtasks may provide individuals with “rewards” in the form of convertible virtual currency. The value of convertible virtual currency paid in exchange for a single microtask often is a small amount that may be less than \$1.⁴

The IRS had previously ruled that general tax principles apply to the taxation of transactions involving convertible virtual currencies.⁵ So, normally, if a taxpayer receives a convertible virtual currency, such as Bitcoin, in exchange for performing services, the taxpayer would have taxable income equal to the value of the convertible virtual currency received. But does the answer change when the payment for the service is very small, including below \$1?

The IRS concludes that the fact that the payment is small and is paid out in a convertible virtual currency does not change the result. Compensation received for services is taxable under IRC §61(a)(1) and performing a microtask is a service.

Because the term “service,” for purposes of § 61, is not defined in the Code, the term should be construed “in accord with its ordinary or natural meaning.” *Smith v. United States*, 508 U.S. 223, 228 (1993). A taxpayer who performs a task through a crowdsourcing platform, including a microtask, has performed a service for the party that requested the task with the expectation that he or she will receive compensation. If the taxpayer receives convertible virtual currency for performing the task, regardless of the value and the manner in which it is received, then the taxpayer has been compensated with property. See Notice 2014-21. The convertible virtual currency received must be reported on the taxpayer’s income tax return as ordinary income and may be subject to self-employment tax. See §§ 61, 83, and 1401.⁶

SECTION: 3101 MAJOR FEDERAL PAYROLL PROCESSING DEPARTMENT ULTIMATELY DECIDES TO WAIT ON TREASURY GUIDANCE BEFORE CEASING TO WITHHOLD EMPLOYEE OASDI

**Citation: National Finance Center Customer Notification,
“Update - Deferral of the Old Age, Survivors and Disability**

⁴ CCA 202035011, p. 2

⁵ See Notice 2014-21 and Revenue Ruling 2019-24

⁶ CCA 202035011, p. 3

Insurance (OASDI) Deductions,” Reference Number: NFC-1597683008, 8/28/20

The payroll tax holiday beginning date of September 1 is rapidly approaching but, as I write this on Friday, August 28, 2020 at just after 2:00 pm Mountain Standard Time⁷ no guidance has been issued by the Treasury Department. The memorandum issued on August 8 directed the Treasury Department to issue such guidance which then would provide for the deferral of the employee portion of old age, survivors and disability insurance (OASDI), more commonly referred to as FICA.

Without such Treasury guidance, most observers concluded that there was no authority for employers to stop withholding the tax, especially in light of IRC §3201(a) which provides, in part, that the OASDI tax “shall be collected by the employer of the taxpayer, by deducting the amount of the tax from the wages *as and when paid*.” The memorandum itself notes that “[t]his memorandum shall be implemented consistent with applicable law and subject to the availability of appropriations...” which strongly suggests that employers need to wait for Treasury guidance on exactly how it will interact with §3201(a), or face the potential of becoming liable for the tax not withheld.

But a bit of a furor developed as the National Finance Center (NFC) of the USDA which, surprisingly enough to many (including this author), processes much of the payroll for the federal government, originally announced in an August 21 letter that it would “eliminate the OASDI employee deductions for all employees whose gross social security wages that are less than \$3999.99. We will continue to calculate and remit the employer portion of OASDI. With that being said, the elimination of the withholding will vary by employee by PP⁸, based upon any changes in their gross social security wages.”⁹ This would be effective for the first payroll paid after September 1, 2020.

That notification also provided, in the final paragraph, a note that the *employee* would be liable if Congress failed to act to forgive the amounts not collected:

The executive order refers to the fact that this is a deferral of the deductions, and Treasury should look to have legislation put in place so that employees do not have to pay back these deferred amounts. NFC will provide additional information as it becomes available.¹⁰

On August 28, *Tax Notes Today Federal* published both a copy of the letter and an article where various commentators were quoted about issues with the letter.¹¹

⁷ That is not a typo—I’m in Phoenix and we are on standard time year round, not daylight saving time.

⁸ Payroll period

⁹ National Finance Center Customer Notification, “Deferral of the Old Age, Survivors and Disability Insurance (OASDI) Deductions,” Reference Number: NFC-1597683008, August 21, 2020 https://nfc.usda.gov/ClientServices/HR_Payroll/Client_Notifications/2020/General/082120-OASDI.pdf (retrieved August 28, 2020), p.1

¹⁰ National Finance Center Customer Notification, “Deferral of the Old Age, Survivors and Disability Insurance (OASDI) Deductions,” Reference Number: NFC-1597683008, August 21, 2020, p.2

¹¹ Johnathan Curry, “Payroll Tax Deferral for Federal Employees Prompts Criticism,” *Tax Notes Today Federal*, August 28, 2020, 2020 TNTF 167-1 <https://www.taxnotes.com/tax-notes-today-federal/employment-taxes/payroll-tax-deferral-federal-employees-prompts-criticism/2020/08/28/2cwvv>

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The publication of the letter caused confusion among payroll departments and raised concern that employees may point to the letter and wonder why their employer isn't following the same policy. Many employers are taking a wait and see attitude until Treasury clarifies the interaction of §3201(a) cited earlier with any deferral, as well as whether it will be the employee or the employer that is ultimately responsible for repaying the taxes if Congress does not act to forgive the balance due.

The NFC reversed course later in the afternoon on August 28, publishing a second notification.¹² The new guidance provides:

Upon receiving final guidance from OPM and Treasury, NFC may eliminate the OASDI employee deductions for employees whose gross social security wages that are less than \$3999.99. We will continue to calculate and remit the employer portion of OASDI. With that being said, the elimination of the withholding will vary by employee by PP, based upon any changes in their gross social security wages.¹³

Now the NFC seems to be endorsing the “wait and see” approach that most other employers appear to be taking in dealing with the question of whether to withhold employee OASDI once September 1 arrives.

SECTION: 3101 GUIDANCE ISSUED ON DEFERRAL OF EMPLOYEE OASDI WITHHOLDING SET TO BEGIN ON SEPTEMBER 1

Citation: Notice 2020-65, 8/28/20

After 5:00pm EDT on Friday, August 28, 2020, the IRS and the Treasury Department released their initial guidance on the payroll tax holiday scheduled to begin on September 1, 2020 in Notice 2020-65.¹⁴

Basic Deferral Rule

As with earlier relief granted related to COVID-19, this delay in the withholding and payment of employee OASDI is provided under the provisions of IRC §7508A. Such relief only applies to “Affected Taxpayers” which for purposes of this notice is defined as follows:

Accordingly, the Secretary has determined that employers that are required to withhold and pay the employee share of social security tax under section 3102(a) or the railroad retirement tax equivalent under

¹² National Finance Center Customer Notification, “Update - Deferral of the Old Age, Survivors and Disability Insurance (OASDI) Deductions,” Reference Number: NFC-1597683008, August 28, 2020 https://www.nfc.usda.gov/ClientServices/HR_Payroll/Client_Notifications/2020/General/082820-COVID_Update.pdf (retrieved August 28, 2020)

¹³ National Finance Center Customer Notification, “Update - Deferral of the Old Age, Survivors and Disability Insurance (OASDI) Deductions,” Reference Number: NFC-1597683008, August 28, 2020, p. 1

¹⁴ Notice 2020-65, August 28, 2020 <https://www.irs.gov/pub/irs-drop/n-20-65.pdf> (retrieved August 28, 2020)

section 3202(a) are affected by the COVID-19 emergency for purposes of the relief described in the Presidential Memorandum and this notice (Affected Taxpayers).¹⁵:

Put more simply, the “Affected Taxpayer” will be the *employer* not the employee.

The Notice describes the relief in general terms as follows:

For Affected Taxpayers, the due date for the withholding and payment of the tax imposed by section 3101(a), and so much of the tax imposed by section 3201 as is attributable to the rate in effect under section 3101(a), on Applicable Wages, as defined herein, (collectively Applicable Taxes) is postponed until the period beginning on January 1, 2021, and ending on April 30, 2021.¹⁶

Time to Deposit the Taxes

In a footnote, the Notice provides that it is the delay in the withholding that delays the time for the deposit of the taxes by the employer:

The deposit obligation for employee social security tax does not arise until the tax is withheld. Accordingly, by postponing the time for withholding the employee social security tax, the deposit obligation is delayed by operation of the regulations. Thus, this notice does not separately postpone the deposit obligation.¹⁷

Nothing in the notice appears to *require* the employer to cease withholding employee OASDI from an employee’s wages. But the above footnote would indicate that if an employer does withhold employee OASDI from an employee’s wages, the employer will need to deposit those taxes at the same time as the other taxes withheld at that time are required to be deposited.

Applicable Wages

Under the memorandum issued by the President, only those receiving the equivalent of a biweekly payroll of less than \$4,000 are eligible to have withholding deferred. “Applicable Wages” is used in the Notice to refer to wages from which the OASDI employee withholdings are eligible for deferral. The Notice provides:

For purposes of this notice, Applicable Wages means wages as defined in section 3121(a) or compensation as defined in section 3231(e) paid to an employee on a pay date during the period beginning on September 1, 2020, and ending on December 31, 2020, but only if the amount of such wages or compensation paid for a bi-weekly pay

¹⁵ Notice 2020-65, p. 1

¹⁶ Notice 2020-65, p. 1

¹⁷ Notice 2020-65, p. 1 Footnote 1

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period is less than the threshold amount of \$4,000, or the equivalent threshold amount with respect to other pay periods.¹⁸

A footnote to the above section indicates that since the definition refers to compensation as defined in §3121(a) (FICA/Medicare wages) or §3231(e) (RRTA/Medicare wages), any items excluded from those wages will be excluded from Applicable Wages.¹⁹ So, for instance, amounts removed from wages to pay for health care under a cafeteria plan will serve to reduce the amount of Applicable Wages, potentially allowing an employee who is just over the limit without a cafeteria plan deferral to qualify for a payroll tax deferral by making such a deferral to the cafeteria plan (assuming the plan allows for such a deferral to be elected at this point).

The guidance provides that the limitation applies on a pay period-by-pay period basis—thus, it is possible an employee with wages over \$104,000 for the year could qualify for deferral in any bi-weekly pay period where his/her wages are below \$4,000.²⁰

If the amount of wages or compensation payable to an employee for a pay period is less than the corresponding pay period threshold amount, then that amount is considered Applicable Wages for the pay period, and the relief provided in this notice applies to those wages or that compensation paid to that employee for that pay period, irrespective of the amount of wages or compensation paid to the employee for other pay periods.²¹

Eventual Payment of Deferred OASDI Taxes

The key question that had to be answered by the guidance was how the taxes would eventually be paid and by whom should Congress not act to forgive the balance due. Under the notice, the ultimate liability falls on the “Affected Taxpayer” which is defined as the *employer*, though the employer is directed to withhold the tax from the employees from whom withholding was deferred.

The Notice provides:

An Affected Taxpayer must withhold and pay the total Applicable Taxes that the Affected Taxpayer deferred under this notice ratably from wages and compensation paid between January 1, 2021 and April 30, 2021...²²

If the employer fails to pay over those taxes during that period, the Notice provides that “interest, penalties, and additions to tax will begin to accrue on May 1, 2021, with respect to any unpaid Applicable Taxes.”²³

¹⁸ Notice 2020-65, p. 2

¹⁹ Notice 2020-65, p. 2 Footnote 3

²⁰ Notice 2020-65, p. 2

²¹ Notice 2020-65, p. 2

²² Notice 2020-65, pp. 2-3

²³ Notice 2020-65, p. 3

Of course, that assumes both that the employee will remain an employee during the period from January 1, 2021 to April 30, 2021 and that the employee's paychecks will be large enough to absorb the additional withholding. If the employer is unable to recover the entire deferred balance through the ratable withholding the ruling provides the following:

If necessary, the Affected Taxpayer may make arrangements to otherwise collect the total Applicable Taxes from the employee.²⁴

Do I Have To Defer the Withholding? And Can I Force My Employer to Do This?

The Notice does not explicitly answer these questions. Presumably since nowhere does it require the employer to defer withholding, an employer could elect to just continue withholding OASDI for all of its employees.

As well, it would appear that if an employer wanted to allow employees to make an election to defer or not defer the OASDI taxes, that is not explicitly prohibited. In fact, the Notice appears to give the employer full discretion to simply force all employees to defer, or decide that, for instance, only the shareholders will participate in any deferral.

As well, since it is the employer rather than the employee that is the Affected Taxpayer, it does not appear that an employee would be able to force his/her employer to defer withholding. If an employer is concerned about being forced to repay amounts deferred by employees who leave service (perhaps specifically to avoid having that extra FICA withholding), it appears the employer could simply refuse to participate in the deferral program.

What About Forgiveness?

Treasury does not address forgiveness, presumably because Congress will have to take action for such a forgiveness of the deferred amount to take place. There is no assurance that Congress will take such action, or even will care to try to pass such a forgiveness provision.

But there's also a risk for employees who do not defer, or are not allowed to defer by their employer, that Congress might only address actually deferred amounts in a forgiveness bill—so any employees that do not have the OASDI deferred would not be able to obtain a refund of such taxes under a forgiveness program.

SECTION: 6011 IRS TEMPORARILY EXPANDS THE USE OF ELECTRONIC SIGNATURES FOR A LIMITED SET OF FORMS

Citation: Sunita Lough, Deputy Commissioner for Services and Enforcement, IRS, "Memorandum for All Services and

²⁴ Notice 2020-65, p. 4

Enforcement Employees: Temporary Deviation from Handwritten Signature Requirement for Limited List of Tax Forms,” 8/27/20

The IRS announced a limited, temporary relaxation of rules regarding the use of electronic or digital signatures for certain tax forms in lieu of handwritten signatures.²⁵ The relief will apply to forms signed and postmarked on or after August 28, 2020 through December 31, 2020.

The relief is limited only to the forms specifically listed in the memorandum. Those listed are:

- Form 3115, Application for Change in Accounting Method;
- Form 8832, Entity Classification Election;
- Form 8802, Application for U.S. Residency Certification;
- Form 1066, U.S. Income Tax Return for Real Estate Mortgage Investment Conduit;
- Form 1120-RIC, U.S. Income Tax Return for Regulated Investment Companies;
- Form 1120-C, U.S. Income Tax Return for Cooperative Associations;
- Form 1120-REIT, U.S. Income Tax Return for Real Estate Investment Trusts;
- Form 1120-L, U.S. Life Insurance Company Income Tax Return;
- Form 1120-PC, U.S. Property and Casualty Insurance Company Income Tax Return; and
- Form 8453 series, Form 8878 series, and Form 8879 series regarding IRS e-file Signature Authorization Forms.²⁶

The memorandum seems to allow virtually any e-signature system to be used for the purposes of this specific relief:

Electronic and digital signatures appear in many forms when printed and may be created by many different technologies. No specific

²⁵ Sunita Lough, Deputy Commissioner for Services and Enforcement, IRS, “Memorandum for All Services and Enforcement Employees: Temporary Deviation from Handwritten Signature Requirement for Limited List of Tax Forms,” August 27, 2020 https://www.irs.gov/pub/irs-utl/osee_e_wet_signature-deviation_8_27_2020.pdf (retrieved August 28, 2020)

²⁶ Sunita Lough, Deputy Commissioner for Services and Enforcement, IRS, “Memorandum for All Services and Enforcement Employees: Temporary Deviation from Handwritten Signature Requirement for Limited List of Tax Forms,” August 27, 2020, pp. 1-2

technology is required for this purpose during this temporary deviation.²⁷

Since the individual electronic filing authorization Form 8879 is in the list, this presumably means that, until December 31, 2020, the requirement to use an e-signature system with knowledge based authentication (KBA) has been suspended. Previously issued guidance allowed the use of e-signature systems by taxpayers electronically signing this authorization form only when the taxpayers' identity could be confirmed, normally by use of KBA.

The IRS explains the reason this relief was provided as follows:

As part of our response to the COVID-19 situation, we have taken steps to protect employees, taxpayers and their representatives by minimizing the need for in-person contact. Taxpayer representatives have expressed concerns with securing handwritten signatures during these times for forms that are required to be filed or maintained on paper. To alleviate these concerns while promoting timely filing, we are implementing a temporary deviation with this memorandum that allows taxpayers and representatives to use electronic or digital signatures when signing the following forms that currently require a handwritten signature...²⁸

The list of forms allowed to be signed in this manner is far from a complete list. The IRS explains why it is only allowing this option for this list of forms:

We recognize that this list of forms does not represent the full universe of forms filed or retained on paper that taxpayers and their representatives would like to see covered by this deviation guidance. However, while we seek to maximize remote capabilities for taxpayers and their representatives during this time, we know that the acceptance of electronic/digital signatures presents elements of risk. Therefore, this temporary deviation is limited to the list of forms set forth above. These forms cannot be filed electronically and the IRS can accept the associated risks with these forms at this time in a limited duration under these circumstances.²⁹

²⁷ Sunita Lough, Deputy Commissioner for Services and Enforcement, IRS, "Memorandum for All Services and Enforcement Employees: Temporary Deviation from Handwritten Signature Requirement for Limited List of Tax Forms," August 27, 2020, p. 1 Footnote 1

²⁸ Sunita Lough, Deputy Commissioner for Services and Enforcement, IRS, "Memorandum for All Services and Enforcement Employees: Temporary Deviation from Handwritten Signature Requirement for Limited List of Tax Forms," August 27, 2020, p. 1

²⁹ Sunita Lough, Deputy Commissioner for Services and Enforcement, IRS, "Memorandum for All Services and Enforcement Employees: Temporary Deviation from Handwritten Signature Requirement for Limited List of Tax Forms," August 27, 2020, p. 2

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The memorandum closes with a reminder that this current relief is limited, but the agency does indicate it will consider the status of e-signatures based on the experience the agency has with this program:

This memorandum is effective for the forms listed above, that are signed and postmarked beginning on or after August 28, 2020, through December 31, 2020. After the expiration of this temporary deviation, we will evaluate the full impact of this change to inform the future path for handwritten signatures, balancing flexibility for taxpayers and their representatives with ensuring that we do not introduce downstream risks for tax administration.³⁰

SECTION: PPP LOAN SBA DEFINES OWNER-EMPLOYEES AS THOSE HOLDING A 5% OR MORE INTEREST, CLARIFIES CERTAIN LEASE NONPAYROLL COST ISSUES IN NEW PPP FORGIVENESS IFR

Citation: RIN 3245-AH56, “Business Loan Program Temporary Changes; Paycheck Protection Program – Treatment of Owners and Forgiveness of Certain Nonpayroll Costs,” Small Business Administration, 8/24/20

After months of silence on the topic, the SBA has issued guidance on the percentage of ownership of a borrower that triggers the treatment of an employee as an owner in an August 24, 2020 Interim Final Rule.³¹ The IFR also provides for limitations on some rental and mortgage interest expenses a borrower might otherwise seek to treat as nonpayroll costs for forgiveness. But the guidance also gives the go-ahead for the use of certain office in home expenses for this purpose, so long as they are allowed as a deduction on the taxpayer’s tax filings for the years in question.

Ownership Percentage for Employee to Be Subject to Owner PPP Limitations

A number of times in the prior IFRs and FAQs the SBA had imposed special limitations that applied to employees who were owners in the computation of payroll costs that counted towards forgiveness, as well as providing that a person who was an owner of multiple businesses was subject to a single overall limitation on cash

³⁰ Sunita Lough, Deputy Commissioner for Services and Enforcement, IRS, “Memorandum for All Services and Enforcement Employees: Temporary Deviation from Handwritten Signature Requirement for Limited List of Tax Forms,” August 27, 2020, p. 2

³¹ RIN 3245-AH56, “Business Loan Program Temporary Changes; Paycheck Protection Program – Treatment of Owners and Forgiveness of Certain Nonpayroll Costs,” Small Business Administration, August 24, 2020 <https://www.sba.gov/sites/default/files/2020-08/PPP%20IFR%20-%20Ownership.pdf> (retrieved August 24, 2020)

compensation. Due to the lack of guidance, some advisers had latched onto a reference on page 3 of the PPP loan application form that provided, in instructions that:

All parties listed below are considered owners of the Applicant as defined in 13 CFR § 120.10, as well as “principals”:

...

- *For a partnership, all general partners, and all limited partners owning 20% or more of the equity of the firm;*
- *For a corporation, all owners of 20% or more of the corporation;*
- *For limited liability companies, all members owning 20% or more of the company; ...³²*

On the application form, this primarily impacted qualification for the loans, since owners with, for instance, certain felony convictions would render the borrower ineligible for the loan. And, certainly, the SBA never stated that this test applied outside the context of the questions on the application. But it was the one place the SBA had provided for an amount of ownership interest necessary to be treated as an owner, even if not in the context of the debt forgiveness rules.

The August 24, 2020 IFR does not use the 20% ownership test, rather using a 5% ownership trigger. The IFR provides:

1. Owners

Are any individuals with an ownership stake in a PPP borrower exempt from application of the PPP owner-employee compensation rule when determining the amount of their compensation that is eligible for loan forgiveness?

Yes, owner-employees with less than a 5 percent ownership stake in a C- or S-Corporation are not subject to the owner-employee compensation rule. The First Loan Forgiveness Rule, as revised by the Revisions to Loan Forgiveness and Loan Review Procedures Interim Final Rules, 85 FR 38304, 38307 (June 26, 2020), caps the amount of loan forgiveness for payroll compensation attributable to an owner-employee.³³

³² Paycheck Protection Program Borrower Application Form Revised June 24, 2020, Small Business Administration, June 24, 2020, p. 3 <https://www.sba.gov/sites/default/files/2020-07/PPP-Borrower-Application-Form-508.pdf> (retrieved August 24, 2020)

³³ RIN 3245-AH56, “Business Loan Program Temporary Changes; Paycheck Protection Program – Treatment of Owners and Forgiveness of Certain Nonpayroll Costs,” Small Business Administration, August 24, 2020, Section 1

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The SBA does not see this as lowering the limit—rather, the agency believes the prior ruling applies to any ownership, no matter how miniscule. So, in the view of the agency, the new rule is a significant relaxing of the original rule.

There is no exception in the rule based on the owner-employee's percentage of ownership. The Administrator, in consultation with the Secretary, has now determined that an owner-employee in a C- or S-Corporation who has less than a 5 percent ownership stake will not be subject to the owner-employee compensation rule. This exemption is intended to cover owner-employees who have no meaningful ability to influence decisions over how loan proceeds are allocated.³⁴

Note that the question and answer makes no reference to partners in this context, meaning a general partner with any interest in a partnership appears to be an owner under these rules.

Additional Clarification on Rental and Mortgage Interest Costs

The August 24 IFR also provides guidance on certain rent and mortgage interest payments. The first clarification denies treatment as eligible nonpayroll costs to certain rental and mortgage interest expenses.

A key bit of information found in the fourth example, though, clarifies that office in home expenses deducted on a home-based business' 2019 or expected 2020 tax filings will qualify as such expenses.

The IFR provides:

2. Eligibility of Certain Nonpayroll Costs for Loan Forgiveness

a. Are amounts attributable to the business operation of a tenant or sub-tenant of the PPP borrower or, in the context of home-based businesses, household expenses, eligible for forgiveness?

No, the amount of loan forgiveness requested for nonpayroll costs may not include any amount attributable to the business operation of a tenant or sub-tenant of the PPP borrower or, for home-based businesses, household expenses.³⁵

34 RIN 3245-AH56, "Business Loan Program Temporary Changes; Paycheck Protection Program – Treatment of Owners and Forgiveness of Certain Nonpayroll Costs," Small Business Administration, August 24, 2020, Section 1

35 RIN 3245-AH56, "Business Loan Program Temporary Changes; Paycheck Protection Program – Treatment of Owners and Forgiveness of Certain Nonpayroll Costs," Small Business Administration, August 24, 2020, Section 2.a

The IFR provides the following four examples:

EXAMPLE 1, AUGUST 24 IFR, 2.A

Lease of a Portion of Rented Office Building to Other Businesses

A borrower rents an office building for \$10,000 per month and subleases out a portion of the space to other businesses for \$2,500 per month. Only \$7,500 per month is eligible for loan forgiveness.

EXAMPLE 2, AUGUST 24 IFR, 2.A

Lease of a Portion of Owned Office Building to Other Businesses

A borrower has a mortgage on an office building it operates out of, and it leases out a portion of the space to other businesses. The portion of mortgage interest that is eligible for loan forgiveness is limited to the percent share of the fair market value of the space that is not leased out to other businesses. As an illustration, if the leased space represents 25% of the fair market value of the office building, then the borrower may only claim forgiveness on 75% of the mortgage interest.

EXAMPLE 3, AUGUST 24 IFR, 2.A

Borrower Shares Rented Space with Another Business

A borrower shares a rented space with another business. When determining the amount that is eligible for loan forgiveness, the borrower must prorate rent and utility payments in the same manner as on the borrower's 2019 tax filings, or if a new business, the borrower's expected 2020 tax filings.

EXAMPLE 4, AUGUST 24 IFR, 2.A

Office in the Home Expenses

A borrower works out of his or her home. When determining the amount of nonpayroll costs that are eligible for loan forgiveness, the borrower may include only the share of covered expenses that were deductible on the borrower's 2019 tax filings, or if a new business, the borrower's expected 2020 tax filings.

Another issue that arises quite often, but which the SBA had been silent on prior to the August 24, 2020 IFR, involved items leased from a related party. The SBA introduces a look through rule to deal with this case, capping eligible expenses based on only the mortgage interest owed on the property during the covered period. As well, in this case, *any* common ownership between the lessor and the lessee is enough to trigger this limit.

The IFR provides in Section 2b:

b. Are rent payments to a related party eligible for loan forgiveness?

Yes, as long as (1) the amount of loan forgiveness requested for rent or lease payments to a related party is no more than the amount of mortgage interest owed on the property during the Covered Period that is attributable to the space being rented by the business, and (2)

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the lease and the mortgage were entered into prior to February 15, 2020. Any ownership in common between the business and the property owner is a related party for these purposes. The borrower must provide its lender with mortgage interest documentation to substantiate these payments. While rent or lease payments to a related party may be eligible for forgiveness, mortgage interest payments to a related party are not eligible for forgiveness. PPP loans are intended to help businesses cover certain nonpayroll obligations that are owed to third parties, not payments to a business's owner that occur because of how the business is structured. This will maintain equitable treatment between a business owner that holds property in a separate entity and one that holds the property in the same entity as its business operations.³⁶

In a footnote to answer 2.b the SBA provides for a rule to prevent counting the same expense twice, once by the tenant and once by the landlord:

In this context, the related party itself would not also be eligible to request forgiveness for this amount.³⁷

36 RIN 3245-AH56, "Business Loan Program Temporary Changes; Paycheck Protection Program – Treatment of Owners and Forgiveness of Certain Nonpayroll Costs," Small Business Administration, August 24, 2020, Section 2.b

37 RIN 3245-AH56, "Business Loan Program Temporary Changes; Paycheck Protection Program – Treatment of Owners and Forgiveness of Certain Nonpayroll Costs," Small Business Administration, August 24, 2020, Section 2.b, Footnote 1