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IRS Confirms PPP Loan Forgiveness Not Taxable

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by D. Robert Morris

Under general income tax principles, when a borrower has its indebtedness forgiven, the borrower recognizes income in the forgiven amount. Under the CARES Act, however, Congress made clear that forgiveness of a Paycheck Protection Program loan would not give rise to cancellation of indebtedness income. Section 1106(i) provides that “any amount which (but for this subsection) would be includible in gross income of the eligible recipient by reason of forgiveness ...shall be excluded from gross income.”

Notwithstanding the clarity of Section 1106(i), for the first six months after the enactment of the CARES Act, the Internal Revenue Service provided no comfort to taxpayers that this cancellation of indebtedness exemption was as straightforward as it appeared. Then, on September 22, 2020, the IRS did so when it released Announcement 2020-12, advising lenders not to issue Form 1099-C which, would be issued to borrowers with cancellation of indebtedness that could be taxable.

PPP loan borrowers are beginning just now to apply for forgiveness of all or part of their PPP loans. They can now rest assured that this forgiveness will not result in cancellation of indebtedness income to them.

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