

Current Federal Tax Developments

Week of January 24, 2022

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CURRENT FEDERAL TAX DEVELOPMENTS
WEEK OF JANUARY 24, 2022
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Published in 2022 by Kaplan Financial Education.

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SECTION: 71

UPDATED NOTICE ON SUBSTANTIALLY EQUAL PAYMENTS ISSUED BY IRS

Notice 2022-6, 1/18/22

When the IRS released the final regulations updating the required minimum distribution and other life expectancy tables, the agency noted that it would be releasing additional guidance to deal with the impact on substantially equal payments. In Notice 2022-06¹ the IRS has now released that guidance.

Effective Date

One of the more interesting items in the notice is found at the very end where the effective dates for this notice are listed.

The guidance provides first a choice of options for a series of payments commencing in 2022:

The guidance in this notice replaces the guidance in Rev. Rul. 2002-62 and Notice 2004-15 for any series of payments commencing on or after January 1, 2023, and it may be used for a series of payments commencing in 2022.²

As well, the ruling provides that, for taxpayers using the required minimum distribution method to compute their substantially equal payment amounts, using the updated tables will not be treated as an impermissible modification of the payment stream.

In the case of a series of payments commencing in a year prior to 2023 using the required minimum distribution method, if the payments in the series are calculated by substituting the Single Life Table, the Joint and Last Survivor Table, or the Uniform Lifetime Table described in section 3.02(a) of this notice for the corresponding table that was used under Rev. Rul. 2002-62, then the substitution will not be treated as a modification within the meaning of section 72(t)(4) or section 72(q)(3).³

¹ Notice 2022-6, January 18, 2022, <https://www.irs.gov/pub/irs-drop/n-22-06.pdf> (retrieved January 18, 2022)

² Notice 2022-6, January 18, 2022, Section 4

³ Notice 2022-6, January 18, 2022, Section 4

Rules Apply to IRAs as Well as Employer Retirement Accounts

Although the notice consistently refers to the employee when talking about the primary beneficiary of the retirement account, the IRS notes that:

In the case of distributions from an IRA, the IRA owner is treated as an employee for purposes of applying this notice.⁴

Methods of Taking Substantially Equal Periodic Payments

As with prior rulings, this ruling provides that taxpayers are considered to have taken substantially equal periodic payments if they take payments using one of the following three methods as described in this ruling:

- The required minimum distribution method
- The fixed amortization method
- The fixed annuitization method.⁵

Required Minimum Distribution Method

Under the *required minimum distribution method* the annual payment is determined by dividing

- The account balance for that distribution year by
- The number of years from the chosen life expectancy table (described later) for that distribution year.⁶

The guidance provides:

Under this method, the account balance, the number of years from the chosen life expectancy table, and the resulting annual payments are redetermined for each distribution year. This redetermination of the annual payment is not considered a modification of the series of substantially equal periodic payments, provided that the required minimum distribution method continues to be used and the same life expectancy tables continue to be used, except to the extent required in section 3.02(b) of this notice.⁷

⁴ Notice 2022-6, January 18, 2022, Section 3.02(f)

⁵ Notice 2022-6, January 18, 2022, Section 3.01

⁶ Notice 2022-6, January 18, 2022, Section 3.01(a)

⁷ Notice 2022-6, January 18, 2022, Section 3.01(a)

Section 3.02(b) of the notice deals with the use of the Joint and Last Survivor table for determining the appropriate life expectancy.

Fixed Amortization Method

Under the *fixed amortization method* the annual payment is determined as the amount that will result in the level amortization of the account balance:

- Over a specified number of years using one of the life expectancy methods provided for in this Notice and
- Using an interest rate that is permitted under this notice.⁸

The Notice points out the following:

Under this method, once the account balance, the number of years from the chosen life expectancy table, and the resulting annual payment are determined for the first distribution year, the annual payment is the same amount in each succeeding distribution year.⁹

Fixed Annuitization Method

Under the fixed annuitization method the annual payment for each year is determined by dividing the account balance by an annuity factor that is the present value of an annuity of \$1 per year beginning at the employee's age and continuing for the life of the employee (or the joint lives of the employee and designated beneficiary).¹⁰

The annuity factor is derived using:

- The mortality tables found in Reg. §1.409(a)(9)-9(e) and
- An interest rate that is permitted under this notice.¹¹

Again, the notice points out the following effect of using this method:

Under this method, once the account balance, the annuity factor, and the resulting annual payment are determined for the first distribution year, the annual payment is the same amount in each succeeding distribution year.¹²

⁸ Notice 2022-6, January 18, 2022, Section 3.01(b)

⁹ Notice 2022-6, January 18, 2022, Section 3.01(b)

¹⁰ Notice 2022-6, January 18, 2022, Section 3.01(c)

¹¹ Notice 2022-6, January 18, 2022, Section 3.01(c)

¹² Notice 2022-6, January 18, 2022, Section 3.01(c)

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Life Expectancy Tables

The life expectancy tables that can be used to determine distribution periods under the required minimum distribution method and fixed amortization method are:

- The Uniform Lifetime Table found in Appendix A of this notice;
- The Single Life Table in § 1.401(a)(9)-9(b); or
- The Joint and Last Survivor Table in § 1.401(a)(9)-9(d) (which can be used even if the designated beneficiary is not the spouse).¹³

The notice provides the following method for determining the employee/IRA account holder's age and, if applicable, the designated beneficiary's age:

The number of years that is used for the required minimum distribution method for a distribution year is the entry from the table for the employee's age on the employee's birthday in that distribution year. If the Joint and Last Survivor Table is used, the age of the designated beneficiary on the designated beneficiary's birthday in the distribution year is also used.¹⁴

The following rules apply when the required minimum distribution method is used:

In the case of the required minimum distribution method, except as provided section 3.02(b)¹⁵ or section 4¹⁶ of this notice, the same life expectancy table that is used for the first distribution year must be used in each following distribution year. Thus, if the employee uses the Single Life Table to apply the required minimum distribution method in the first distribution year, the Single Life Table must be used in subsequent distribution years.¹⁷

The following rule applies to those using the fixed amortization method:

The number of years that is used to apply the fixed amortization method is the entry from the table for the employee's age on the employee's birthday in the first distribution year (and, if applicable, the designated beneficiary's age on the designated beneficiary's birthday in that year).¹⁸

¹³ Notice 2022-6, January 18, 2022, Section 3.02(a)

¹⁴ Notice 2022-6, January 18, 2022, Section 3.02(a)

¹⁵ Related to the designated beneficiary under the Joint and Last Survivor table

¹⁶ The effective date and transition rules discussed earlier

¹⁷ Notice 2022-6, January 18, 2022, Section 3.02(a)

¹⁸ Notice 2022-6, January 18, 2022, Section 3.02(a)

Designated Beneficiary When Using the Joint and Survivor Annuity Table

The notice first provides rules for identifying the proper beneficiary when the Joint and Survivor Annuity method is used.

If the Joint and Last Survivor Table in § 1.401(a)(9)-9(d) is used to apply the required minimum distribution method or the fixed amortization method (or if the fixed annuitization method is applied using an annuity factor determined for the joint lives of the employee and designated beneficiary), then the beneficiary whose life expectancy or expected mortality is used must be the actual designated beneficiary of the employee with respect to the account for the year of the determination.¹⁹

The designated beneficiary rules refer to the rules that apply for required minimum distributions from retirement plans. The notice references those provisions for determining the proper beneficiary when more than one beneficiary is designated.

If the employee has more than one beneficiary, the identity and age of the designated beneficiary used for purposes of each of the methods described in section 3.01 of this notice are determined under the rules for determining the designated beneficiary for purposes of section 401(a)(9).²⁰

The notice also provides that the beneficiary is determined as of January 1 of the distribution year in question:

The designated beneficiary is determined for a distribution year as of January 1 of the distribution year, without regard to changes in the designated beneficiary later in that distribution year or designated beneficiary determinations in prior distribution years.²¹

The notice provides the following example to illustrate this rule.

EXAMPLE

For example, if an IRA owner starts distributions from an IRA in 2023 at age 50, and applies either the required minimum distribution method or fixed amortization method using the Joint and Last Survivor Table for the IRA owner and the designated beneficiary, and the beneficiaries on January 1, 2023 are 25 and 55 years old, the number of years used to calculate the payment for 2023 would be 40.2 (the entry from the Joint and Last Survivor

¹⁹ Notice 2022-6, January 18, 2022, Section 3.02(b)

²⁰ Notice 2022-6, January 18, 2022, Section 3.02(b)

²¹ Notice 2022-6, January 18, 2022, Section 3.02(b)

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Table for ages 50 and 55), even if later in 2023 the 55-year-old is eliminated as a designated beneficiary.

However, under the required minimum distribution method, if the 55-year-old beneficiary is eliminated or dies in 2023, that individual would not be taken into account in future distribution years (and if there is no designated beneficiary in a future year, the Single Life Table in § 1.401(a)(9)-9(b) is used for that distribution year).²²

Interest Rates

The interest rate used for the fixed amortization method or the fixed annuitization method can be no more than the greater of:

- 5% or
- 120% of the federal mid-term rate (determined in accordance with section 1274(d) for either of the two months immediately preceding the month in which the distribution begins).²³

Analysis

The 5% rate option is added by this Notice. Previously Revenue Ruling 2002-62, which governed this calculation, only allowed a maximum rate of 120% of the federal mid-term rate.

Links to the Revenue Rulings that include the mid-term rates are found at:

<https://apps.irs.gov/app/picklist/list/federalRates.html>.

Account Balance

The notice provides the following rules for determining the account balance:

For purposes of applying the required minimum distribution method, the account balance for a distribution year is determined under § 1.401(a)(9)-5. For the fixed amortization and fixed annuitization methods, the account balance must be determined in a reasonable manner based on the facts and circumstances. The account balance will be treated as determined in a reasonable manner if it is the account balance on any date within the period that begins on December 31 of the year prior to the date of the first distribution and ends on the date of the first distribution.²⁴

²² Notice 2022-6, January 18, 2022, Section 3.02(b)

²³ Notice 2022-6, January 18, 2022, Section 3.02(c)

²⁴ Notice 2022-6, January 18, 2022, Section 3.02(d)

The notice provides that a taxpayer will be treated as making a modification to a series of periodic payments if there is a modification to the account balance after the valuation date chosen above. The modification will occur if, after that date, there is

- Any addition to the account balance other than by reason of investment experience,
- Any transfer of a portion of the account balance to another retirement plan, or
- A rollover of the amount received by the employee.²⁵

If such a modification is made it will trigger the recapture tax under IRC §72(t)(4)(A), which will result in all previously avoided early distribution penalties being due.

Exception from Modification When Account Exhausted Solely By Following Allowable Distribution Method

If things go wrong for the taxpayer, it may turn out that taking the required distributions under the method selected may exhaust the entire account prematurely. The Notice provides the following relief from the recapture tax in this case:

If, as a result of following a method of determining substantially equal periodic payments that qualifies for the exception of section 72(t)(2)(A)(iv), an individual's assets in an individual account plan or an IRA are exhausted, any resulting reduction in the amount of the final payment (and the subsequent cessation of payments) is not a modification within the meaning of section 72(t)(4). Accordingly, the recapture tax described in section 72(t)(4)(A) will not apply in this case.²⁶

Permitted One Time Switch to Required Minimum Distribution Method

The Notice allows a taxpayer to make a one-time switch to the required minimum distribution method if that method was not selected initially:

An individual who begins distributions using either the fixed amortization method or the fixed annuitization method is permitted in any subsequent distribution year to switch to the required minimum distribution method to determine the payment for the distribution year of the switch and all subsequent distribution years, and this change in method will not be treated as a modification within the meaning of section 72(t)(4). Once a change is made under this paragraph, any subsequent change from the required minimum

²⁵ Notice 2022-6, January 18, 2022, Section 3.02(d)

²⁶ Notice 2022-6, January 18, 2022, Section 3.03(a)

distribution method will be a modification for purposes of section 72(t)(4).²⁷

Application to Distributions from Non-Qualified Annuities

The Notice also provides that these rules can be used for non-qualified annuity substantially equal distribution payments as well:

Taxpayers may use one of the methods set forth in section 3.01 of this notice (applying the rules in section 3.02 of this notice) to determine whether a distribution from a non-qualified annuity contract is part of a series of substantially equal periodic payments under section 72(q)(2)(D). Taxpayers may use the principles of section 3.03 of this notice to determine whether a change in substantially equal periodic payments will be treated as a modification under section 72(q)(3).²⁸

SECTION: 1366 FINAL VERSION OF FORM 7203 TO REPORT S CORPORATION STOCK AND DEBT BASIS ON FORM 1040 RELEASED

Form 7203, 1/19/22

The IRS has released the final version of the proposed Form 7203, *S Corporation Shareholder Stock and Debt Basis Limitations*,²⁹ to be used to report S corporation stock basis, debt basis, and allowed/disallowed losses on Forms 1040. The form is virtually identical to the one we discussed in July of 2021 when the IRS published information about the form in the Federal Register³⁰ and later released in draft form.

When the Form Must Be Filed with Form 1040

The instructions for the form provide that it must be filed in the following situation with the shareholder's Form 1040 when the shareholders:

- Are claiming a deduction for their share of an aggregate loss from an S corporation (including an aggregate loss not allowed last year because of basis limitations),

²⁷ Notice 2022-6, January 18, 2022, Section 3.03(b)

²⁸ Notice 2022-6, January 18, 2022, Section 3.04

²⁹ Form 7203, *S Corporation Shareholder Stock and Debt Basis Limitations*, January 19, 2022, <https://www.irs.gov/pub/irs-pdf/f7203.pdf> (retrieved January 19, 2022)

³⁰ Edward K. Zollars, CPA, "IRS Proposes New Form 7203 for S Corporation Shareholders to Report Basis Computations with Form 1040," *Current Federal Tax Developments* website, July 21, 2021, <https://www.currentfederaltaxdevelopments.com/blog/2021/7/19/irs-proposes-new-form-7203-for-s-corporation-shareholders-to-report-basis-computations-with-form-1040> (retrieved October 23, 2021)

- Received a non-dividend distribution from an S corporation,
- Disposed of stock in an S corporation (whether or not gain is recognized), or
- Received a loan repayment from an S corporation.³¹

The instructions also suggest the form be completed even in years where it is not required to be filed with the return, noting:

It may be beneficial for shareholders to complete and retain Form 7203 even for years it is not required to be filed, as this will ensure their bases are consistently maintained year after year.³²

Shareholder’s Basis in Stock

Part I details the computation of the stock basis of the shareholder.

Stock block (see instructions) ▶			
Part I	Shareholder Stock Basis		
1	Stock basis at the beginning of the corporation’s tax year	1	
2	Basis from any capital contributions made or additional stock acquired during the tax year	2	
3a	Ordinary business income (enter losses in Part III)	3a	
b	Net rental real estate income (enter losses in Part III)	3b	
c	Other net rental income (enter losses in Part III)	3c	
d	Interest income	3d	
e	Ordinary dividends	3e	
f	Royalties	3f	
g	Net capital gains (enter losses in Part III)	3g	
h	Net section 1231 gain (enter losses in Part III)	3h	
i	Other income (enter losses in Part III)	3i	
j	Excess depletion adjustment	3j	
k	Tax-exempt income	3k	
l	Recapture of business credits	3l	
m	Other items that increase stock basis	3m	
4	Add lines 3a through 3m	4	
5	Stock basis before distributions. Add lines 1, 2, and 4	5	
6	Distributions (excluding dividend distributions)	6	
Note: If line 6 is larger than line 5, subtract line 5 from line 6 and report the result as a capital gain on Form 8949 and Schedule D. See instructions.			
7	Stock basis after distributions. Subtract line 6 from line 5. If the result is zero or less, enter -0-, skip lines 8 through 14, and enter -0- on line 15	7	
8a	Nondeductible expenses	8a	
b	Depletion for oil and gas	8b	
c	Business credits (sections 50(c)(1) and (5))	8c	
9	Add lines 8a through 8c	9	
10	Stock basis before loss and deduction items. Subtract line 9 from line 7. If the result is zero or less, enter -0-, skip lines 11 through 14, and enter -0- on line 15	10	
11	Allowable loss and deduction items. Enter the amount from line 47, column (c)	11	
12	Debt basis restoration (see net increase in instructions for line 23)	12	
13	Other items that decrease stock basis	13	
14	Add lines 11, 12, and 13	14	
15	Stock basis at the end of the corporation’s tax year. Subtract line 14 from line 10. If the result is zero or less, enter -0-	15	

³¹ Instructions for Form 7203 (December 2021), January 19, 2022, p. 1, <https://www.irs.gov/pub/irs-pdf/i7203.pdf> (retrieved January 19, 2022)

³² Instructions for Form 7203 (December 2021), January 19, 2022

Basis in Debt Owed to the Shareholder by the Corporation

Part II handles the calculation of debt basis, with Part A providing information on the amount of each debt owed to the shareholder and whether the debt is a formal note or an open account debt.

Part II Shareholder Debt Basis				
Section A—Amount of Debt (If more than three debts, see instructions.)				
Description	Debt 1	Debt 2	Debt 3	Total
	<input type="checkbox"/> Formal note <input type="checkbox"/> Open account debt	<input type="checkbox"/> Formal note <input type="checkbox"/> Open account debt	<input type="checkbox"/> Formal note <input type="checkbox"/> Open account debt	
16 Loan balance at the beginning of the corporation's tax year				
17 Additional loans (see instructions)				
18 Loan balance before repayment. Combine lines 16 and 17				
19 Principal portion of debt repayment (this line doesn't include interest)	()	()	()	()
20 Loan balance at the end of the corporation's tax year. Combine lines 18 and 19				

Part B computes the actual debt basis as well as any gain that would be reportable due to repayments of the various debts.

Part II Shareholder Debt Basis (continued)				
Section B—Adjustments to Debt Basis				
Description	Debt 1	Debt 2	Debt 3	Total
21 Debt basis at the beginning of the corporation's tax year				
22 Enter the amount, if any, from line 17				
23 Debt basis restoration (see instructions)				
24 Debt basis before repayment. Combine lines 21, 22, and 23				
25 Divide line 24 by line 18				
26 Nontaxable debt repayment. Multiply line 25 by line 19				
27 Debt basis before nondeductible expenses and losses. Subtract line 26 from line 24				
28 Nondeductible expenses and oil and gas depletion deductions in excess of stock basis				
29 Debt basis before losses and deductions. Subtract line 28 from line 27. If the result is zero or less, enter -0-				
30 Allowable losses in excess of stock basis. Enter the amount from line 47, column (d)				
31 Debt basis at the end of the corporation's tax year. Subtract line 30 from line 29. If the result is zero or less, enter -0-				
Section C—Gain on Loan Repayment				
32 Repayment. Enter the amount from line 19				
33 Nontaxable repayments. Enter the amount from line 26				
34 Reportable gain. Subtract line 33 from line 32				

Allowable Losses and Carryover Amounts

Finally, Part III calculates the allowable loss and the amounts of any carryovers to the following year:

Part III Shareholder Allowable Loss and Deduction Items					
Description	(a) Current year losses and deductions	(b) Carryover amounts (column (e)) from the previous year	(c) Allowable loss from stock basis	(d) Allowable loss from debt basis	(e) Carryover amounts
35 Ordinary business loss					
36 Net rental real estate loss					
37 Other net rental loss					
38 Net capital loss					
39 Net section 1231 loss					
40 Other loss					
41 Section 179 deductions					
42 Charitable contributions					
43 Investment interest expense					
44 Section 59(e)(2) expenditures					
45 Other deductions					
46 Foreign taxes paid or accrued					
47 Total loss. Combine lines 35 through 46 for each column. Enter the total loss in column (c) on line 11 and enter the total loss in column (d) on line 30					

SECTION: 1368 IRS EXPANDS ON REPORTING EXPENSES USED TO OBTAIN PPP LOAN FORGIVENESS ON FORM 1120S, SCHEDULE M-2

“2021 Instructions for Form 1120-S,” 1/20/22

The IRS has added more clarification in the final Form 1120S instructions³³ about how expenses paid with PPP loan funds that lead to debt forgiveness should be treated in the computation of the accumulated adjustments account (AAA) and the other adjustments account (OAA).

On January 3, 2022, the [IRS released draft instructions](#) that first indicated that expenses paid with PPP loan proceeds should be treated as expenses related to tax exempt income under IRC §1368(e)(1)(A) and excluded from the calculation of AAA.

³³ 2021 Instructions for Form 1120S, January 20, 2022, <https://www.irs.gov/pub/irs-pdf/i1120s.pdf> (retrieved January 22, 2022)

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However, some advisers weren't sure how exactly this should be reported on Schedule M-2.

Schedule M-2 Analysis of Accumulated Adjustments Account, Shareholders' Undistributed Taxable Income Previously Taxed, Accumulated Earnings and Profits, and Other Adjustments Account (see instructions)				
	(a) Accumulated adjustments account	(b) Shareholders' undistributed taxable income previously taxed	(c) Accumulated earnings and profits	(d) Other adjustments account
1	Balance at beginning of tax year			
2	Ordinary income from page 1, line 21			
3	Other additions			
4	Loss from page 1, line 21	()		
5	Other reductions	()		()
6	Combine lines 1 through 5			
7	Distributions			
8	Balance at end of tax year. Subtract line 7 from line 6			

Line 2 of Schedule M-2 places the net ordinary income from line 1, page 21 into the AAA column and that will generally already be reduced by the expenses used for forgiveness which, though related to tax exempt income, were made deductible by the Comprehensive Appropriations Act, 2021 (CAA) in December 2020.

While some (including this author) argued that the “other additions” line should be used to add the expenses back in computing AAA, not all were comfortable making that entry without explicit IRS instructions. However, there was no other way to make the worksheet come to the result specified by the IRS while still following the implied instructions to put the net ordinary income on line 2, column (a).

The IRS has now explained that, yes, that is what the agency meant should be done, expanding the “Tip” by adding additional paragraphs not found in the original draft instructions:

PPP loans. An S corporation should include tax-exempt income from the forgiveness of PPP loans in column (d) on line 3 of the Schedule M-2.

An S corporation should report expenses paid this year with proceeds from PPP loans that were forgiven this year in column (d) on line 5 of the Schedule M-2.

If column (a) on line 2 or line 4 of the Schedule M-2 includes expenses paid with proceeds from forgiven PPP loans, an S corporation should report that amount in column (a) on line 3 and in column (d) on line 5 of the Schedule M-2.

If column (a) on line 1 of the Schedule M-2 includes expenses that were paid in a prior year with proceeds from PPP loans that were forgiven this year, an S corporation should report that amount in column (a) on line 3 and in column (d) on line 5 of the Schedule M-2.

Note that the last paragraph contains guidance for how to correct AAA if the amount reported on the return for the previous year erroneously had been reduced by such expenses paid in a prior year.

What the instructions do not say, but which an adviser should recognize, is that this “fix” only completely resolves the issue if the misclassified AAA did not have an impact on the prior year’s tax reporting. As there was no underlying law change, this treatment should have been followed on 2020 returns as this author argued immediately following the passage of the CAA.

IRC §1368(d)(1)(A)’s wording has not been changed for many years and the IRS had consistently taken the position these expenses related to the tax-exempt income from PPP loan forgiveness during 2020. When Congress made such expenses deductible, it did not do so by making these expenses not related to tax-exempt income—the law just made that point irrelevant to claiming the deduction.

If the S corporation made distributions in 2020 and those distributions *appeared* to have exceeded AAA prematurely due to these expenses erroneously reducing AAA and the corporation had accumulated earnings and profits, amounts would have been reported as taxable dividends on Forms 1099-DIV by the S corporation and shareholders would have included these dividends in income and not used those amounts as distributions that reduced their basis in the S corporation stock.

If the Forms 1099-DIV are not reissued reporting the reduced dividends and the shareholders do not revise their returns, the IRS would still be able to reduce the shareholders’ basis in their S corporation shares by those distributions, as they were distributions that reduced the shareholders’ basis. The fact the shareholder paid tax on the distribution is simply a mistake made by the shareholder and would not justify adjusting the shareholder’s basis upward to make up for the error.

As well, the shareholder would have likely paid additional tax on their 2020 individual income tax return he/she did not owe. So only if there were no erroneous Forms 1099-DIV issued by the S corporation for 2020 should making the adjustments as noted in the last paragraph of the IRS tip be the only step taken to adjust for the reporting issue for 2020.

SECTION: 6011

IRS PROVIDES DETAILS FOR REPORTING PPP FORGIVENESS OPTIONS UNDER REVENUE PROCEDURE 2021-48

Form 1120S 2022 Instructions, 1/20/22

In final versions of instructions to Forms 1120S³⁴ and Form 1065,³⁵ the IRS has provided additional guidance on reporting PPP loan forgiveness on those forms using the methods outlined in Revenue Procedure 2021-48.

In Section 3.04 of Revenue Procedure 2021-48 the IRS noted that further instructions would be issued on how this should be reported, though taxpayers did not have to wait to use the procedure until that guidance was released:

04 Reporting consistent with this revenue procedure. The IRS will publish form instructions for the 2021 filing season that will detail how taxpayers can report consistently with sections 3.01 through 3.03 of this revenue procedure. However, taxpayers do not need to wait until the instructions are published to apply this revenue procedure.³⁶

The instructions for Form 1120S provide that the tax-exempt income from the forgiveness of PPP loans should be reported on Line 16b of Schedule K, Form 1120S and Schedule K-1 of Form 1120S.³⁷ The instructions also provide the following requirements for the attachment:

Attach a statement to the S corporation return for each tax year in which the S corporation is applying Rev. Proc. 2021-48, sections 3.01(1), (2), or (3). The statement should also include the following information for each PPP loan.

1. The S corporation's name, address, and EIN;
2. A statement that the S corporation is applying section 3.01(1), (2), or (3) of Rev. Proc. 2021-48, as applicable;

³⁴ Form 1120S Instructions, January 20, 2022, <https://www.irs.gov/pub/irs-pdf/i1120s.pdf> (retrieved January 14, 2022)

³⁵ Form 1065 Instructions, January 14, 2022, <https://www.irs.gov/pub/irs-pdf/i1065.pdf> (retrieved January 21, 2022)

³⁶ Revenue Procedure 2022-48, Section 3.04, November 18, 2021

³⁷ Form 1120S Instructions, January 20, 2022, p. 34

3. The amount of tax-exempt income from forgiveness of the PPP loan that the S corporation is treating as received or accrued during the tax year; and

4. Whether forgiveness of the PPP loan has been granted as of the date the return is filed.³⁸

The instructions confirm that taxpayers who reported PPP loan forgiveness on their 2020 Form 1120S in accordance with one of the methods found in the Revenue Procedure do not need to file an amended return to add the statement:

An S corporation that reported tax-exempt income from a PPP loan on its 2020 return, the timing of which corresponds to one of the options presented in Rev. Proc. 2021-48, need not file an amended return solely to attach the statement that is described in the instructions for Schedule K, line 16(b).³⁹

If the S Corporation reported forgiveness income on a tax return prior to receiving formal forgiveness and later discovers that a lesser amount was forgiven, Section 3.03 of Revenue Procedure 2022-48 provides that an amended return should be filed.⁴⁰ The 2022 Instructions to Form 1120S provide the following guidance in that case:

The S corporation should attach a statement to such amended return that includes the following information.

1. The S corporation's name, address, and EIN;
2. A statement that the S corporation is making adjustments in accordance with section 3.03 of Rev. Proc. 2021-48; and
3. The tax year in which tax-exempt income was originally reported, the amount of tax-exempt income that was originally reported in such tax year, and the amount of tax-exempt income being adjusted on the amended return.⁴¹

The Form 1065 instructions contain similar instructions, though noting an Administrative Adjustment Request would be necessary rather than an amended return when reporting a change in the amount of PPP forgiveness exempt income if the partnership had not been eligible to or had not opted out of the BBA partnership audit regime for the year in question.⁴²

³⁸ Form 1120S Instructions, January 20, 2022, p. 34

³⁹ Form 1120S Instructions, January 20, 2022, p. 34

⁴⁰ Form 1120S Instructions, January 20, 2022, p. 34, Revenue Procedure 2022-48, Section 3.03

⁴¹ Form 1120S Instructions, January 20, 2022, pp. 34-35

⁴² Form 1065 Instructions, January 14, 2022, p. 43

16 Current Federal Tax Developments

The same requirement is found in the Form 1040 2021 instructions,⁴³ though it's not totally clear what impact this has for most issues—the timing of the recognition of the tax-exempt income would generally not have an impact in the Form 1040 context.

As well, the Revenue Procedure allows taxpayers to report exempt income in three ways that the IRS has approved—but does not indicate these are the exclusive ways to report such income (just ways that will not be challenged by the IRS on an exam). However, since failing to follow the instructions in theory opens up a theoretical finding that the taxpayer had not filed a proper return, it will be best to comply with these requirements, even in the context of a Form 1040.

⁴³ Form 1040 Instructions, p. 23, December 22, 2021, <https://www.irs.gov/pub/irs-pdf/i1040gi.pdf> (retrieved January 21, 2022)