Frequently Asked Questions and Defenses of Taxing Forgiven PPP Loans

Wasn't the federal decision to make these non-taxable a "last-minute" decision made by Congress in December?

- No, CARES Act Section 1106(i) explicitly made forgiven PPP loans non-taxable. The Trump Administration's Treasury Secretary misinterpreted the act and its intent, making them taxable. This was met by bipartisan pushback as well as bipartisan intent to correct the mistake in the next package after a report by the Congressional Research Service clarified, without doubt, the intent of Congress was not to tax these forgiven loans. Congress then took the extraordinary step of reaffirming their CARES Act decision in the Consolidated Appropriations Act in December.
- Why didn't they do it sooner? There was not much opportunity to pass coronavirus relief after the CARES Act; the Democrats tried multiple times with two iterations of the HEROES Act, which the GOP stonewalled.
- Additionally, Senator Patrick Leahy's spokesperson took the unique step of weighing in on a state legislative situation in an interview with VTDigger, saying, "congress wanted businesses and individuals to both receive the full benefit of federal support during the pandemic by not taxing PPP loans."

Doesn't the state need this money?

- No, the consensus revenue forecast for the Tax Year 2022 or Tax Year 2023, which the budget is based on, did not account for PPP loans being taxable (backed up by the legislature's joint fiscal office). In fact, the state's budget is based on a revenue *surplus* of over $200 million above forecast.

But doesn't an employer get a double benefit because they can deduct payroll and expenses paid with a PPP loan?

- No! First, this is a "red herring" argument designed to drag you into a weedy conversation that is outdated and already been settled definitively at the federal level by Congressional Democrats and Republicans. It is irrelevant, as the CARES Act explicitly allowed this, and it was the program's intent to provide this benefit.
- Second, if you play out a situation where an employer could not deduct these expenses, the benefit would be minimal to the employer. For example, if an employer has $100,000 of a PPP loan forgiven, they can and should deduct those expenses. Taxing what otherwise would have been deductible means that the employer is in a worse place than if they had laid off employees and sent them to the UI system. Furthermore, the state already collected revenue from PPP loans in the form of payroll taxes.

Vermont Economic Recovery Grants were taxable income, so why shouldn't PPP be taxable income?

- It is true that VT's ERGs were taxable income, however, that was always the intention of the legislature, and the business always knew that when they received them. More importantly, these programs are dramatically different in their goal, allowable uses, rules, and virtually every other criterion. The ERG program was a revenue replacement program, while the PPP program provided loans that could be converted to grants if you preserved payroll. This required every dollar to be spent on payroll and eligible expenses, leaving nothing if you followed the rules.

The state doesn't always conform with national tax law and can decide to link up to the federal tax code where they see fit…

- They can, this is true; however, why would you? The state does not need the revenue, and everyone who created the program has conveyed that the program only fully works if forgiven PPP loan is not taxable. The federal government created this lifeline and extended it to vulnerable employers to retain their employees at the most turbulent time in most of our lives.

Didn't some businesses that got a PPP loan not need it?

- First, this is a favorite unsubstantiated claim of many. Early in the pandemic, there were high-profile businesses that applied for PPP loans and were subjected to public backlash, which resulted in loans being returned. These were few and far between and not what we are discussing now.
- Second, if this was true, these employers were likely in the program's early stages and would not be eligible for later iterations of the program, which required proof of a 25% loss. Those hypothetical businesses would also certainly have had forgiveness processed in 2020, which is the year the Vermont legislature *has already signed off on as non-taxable*. In short, if they wanted to target those *highly hypothetical* businesses with this decision, they did the opposite.
- Additionally, employers receiving forgiveness in 2021 will, by definition, be the most vulnerable businesses. Earlier iterations of the program did not serve small businesses well until changes in the Consolidated Appropriations Act. When he entered office, President Biden signed an Executive Memorandum pausing all PPP applications except for those historically underserved; sole proprietors, women, and minority-owned businesses. These are not large businesses, with the most recent numbers on the program pointing to 90% of these loans being under $150,000 and the average loan being $53,000.
- Finally, no employer had a crystal ball. Let's all remember how scary and uncertain the early days, weeks, and months of the pandemic were and how a person never knew what would happen one day to the next. People were encouraged to reach for this lifeline so they didn't end up in a position where they may need to put their employees on the heavily strained unemployment insurance system. This program was a *parallel unemployment insurance program* at a time in which the state systems were inundated with record levels of claims and the system was strained to the breaking point.

Nonprofit organizations will not have to pay tax, right?

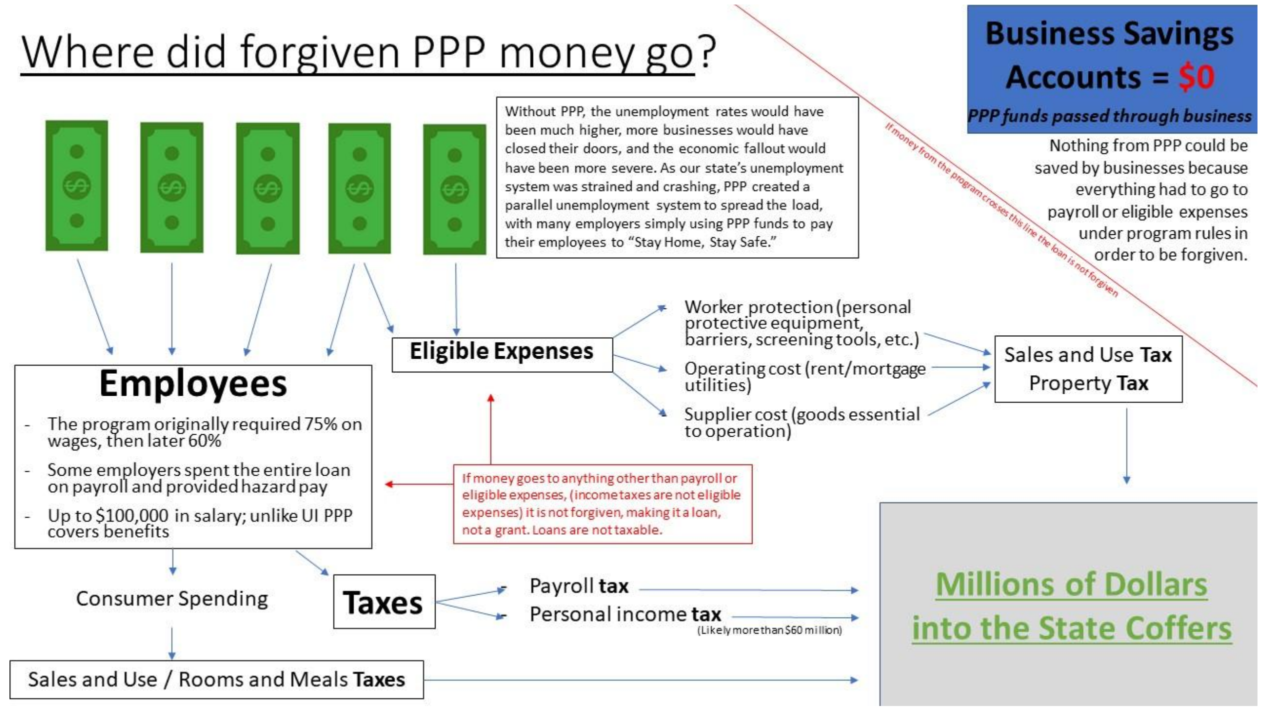
- This is not entirely clear. Nonprofits are generally exempt from paying state corporate income tax, however, some organizations pay state tax on unrelated business income (UBI). The analysis of this issue is still ongoing, and the general supposition is that the forgivable portion of PPP loans should generally not be taxable for nonprofits; however, reversing the decision made in H.315 would provide greater certainty to nonprofits that received PPP loans.

Other states are taxing PPP loans, right?

- Not many states are applying the same outdated interpretations of the CARES Act that was originally advanced by the IRS under the Trump Administration and others who chose to tax forgiven PPP loans have since reversed their decision. Many proponents of the tax will cite a report by the Tax Foundation which incorrectly listed states, such as Vermont, that link up to federal tax code via static conformity and had not made a decision on the matter yet. The report also doesn't accommodate states in the process of reversing their decisions to conform with federal tax code. Since February, about eight states have changed from taxing to not taxing Taxing PPP loans.
- New Hampshire, Minnesota, Massachusetts, Florida have passed bills in one chamber to make PPP nontaxable.
- Vermont would be an extreme outlier if the legislature decided to tax these forgiven loans.

PPP was a program for businesses

- This is an overly simplistic view of this program. Without PPP, the unemployment rates would have been much higher, more businesses would have closed their doors, and the economic fallout would have been more severe. As our state's unemployment system was strained and crashing, PPP created a parallel unemployment system to spread the load, with many employers simply using PPP funds to pay their employees to "stay home, stay safe." There is a trauma associated with losing one's job, even with UI, PPP kept this trauma from occurring by keeping employees on the employer's payroll.
- Furthermore, personal income tax, sales tax, and rooms and meals tax revenue to the state was not decreased due to these loans.



This factsheet was created by the Lake Champlain Chamber. If you have any questions, please contact Austin Davis at austin@vermont.org.