LEGISLATIVE FISCAL ESTIMATE

SENATE, No. 3234

STATE OF NEW JERSEY
219th LEGISLATURE

DATED: JANUARY 22, 2021

SUMMARY

Synopsis:	Allows deduction from tax of certain expenses when taxpayer's federal paycheck protection program loan is forgiven and excludes those forgiven loans from gross income tax.
Type of Impact:	State revenue loss to the General Fund and Property Tax Relief Fund.
Agencies Affected:	Department of the Treasury.

Office of Legislative Services Estimate

Fiscal Impact	**Fiscal Years 2021 & 2022**
State Revenue Loss	Indeterminate

- The Office of Legislative Services (OLS) concludes that the bill will result an indeterminate loss of State revenues in Fiscal Years 2021 and 2022. There is no information available regarding the purposes for which Paycheck Protection Program (PPP) loans were used and the total amount of loans forgiven.

- According to the Small Business Administration (SBA), New Jersey businesses and non-profit organizations received $17.3 billion through the PPP as of January 2021. After adjusting the Statewide total to exclude amounts awarded to corporations and non-profit organizations, the OLS estimates that $6.4 billion in loans awarded through the first round of PPP funding may be excluded from gross income. Applying current New Jersey tax rates to the $6.4 billion that may be excluded yields a maximum State revenue of $688.0 million from the first round of PPP loans.

- The OLS notes that the federal government recently appropriated an additional $284.4 billion for PPP loans. If this bill becomes law, eligible second round PPP loan funds may be excluded and deducted from calendar year 2021 gross income. Calendar year 2021 tax returns will be filed in April 2022, or in Fiscal Year 2022.

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BILL DESCRIPTION

The bill ensures that forgiven PPP loans will not be subject to the State's gross income tax. This bill also allows the deduction of expenses paid for by a paycheck protection program loan even if the loan is forgiven.

The PPP was established by the "Coronavirus Aid, Relief, and Economic Security Act" or "CARES Act," a federal law enacted in response to the economic impact of the COVID-19 pandemic, and reauthorized by a separate federal law, the "Consolidated Appropriations Act, 2021". The PPP offers loans to small businesses as an incentive to keep employees on their payroll during the pandemic. Some or all of the loan may be forgiven if certain conditions are met.

Federal law generally considers forgiven loans to be taxable income. However, the "Consolidated Appropriations Act, 2021," clarified that the amount of a PPP loan which is forgiven may be excluded from income for federal tax purposes and that expenses covered by PPP loans may be deducted from income for federal tax purposes. New Jersey generally follows the federal treatment of income when determining income of C Corporations and S Corporations, so C Corporations and taxpayers with S corporation income have already been granted the same benefit given by this bill through the operation of federal and preexisting State law. C Corporations and taxpayers with S corporation income will therefore not be affected by this bill.

In the case of pass-through entities, other than S corporations, a forgiven federal loan maybe subject to the State's gross income tax. These pass-through entities do not generally pay income tax because the income of the business is passed along to businesses owners who then pay tax on the income under the State's gross income tax. However, PPP loans awarded to pass-through entities that are forgiven may be subject to New Jersey gross income tax when the business's income is passed-through to the business owners. To prevent such forgiven loans from being taxable, this bill excludes them from the gross income tax. To match the federal treatment, the bill also allows the deduction of expenses paid for by a forgiven PPP loan.

FISCAL ANALYSIS

EXECUTIVE BRANCH

None received.

OFFICE OF LEGISLATIVE SERVICES

The OLS concludes that the bill will result in an indeterminate loss of State revenues in Fiscal Years 2021 and 2022. The bill excludes from gross income the amount of a PPP loan that is forgiven by the federal government and allows a deduction from gross income for the amount of business expenses paid for with proceeds of a PPP loan. The exclusion and deduction of these amounts from gross income will reduce the amount of income subject to taxation, thereby reducing State tax collections. This bill would affect revenues generated by the gross income tax (deposited in the Property Tax Relief Fund) and the pass-through business alternative income tax (deposited in the General Fund). The bill will affect PPP loan recipients that have a New Jersey gross income tax liability and are not impacted by the changes to federal law regarding the taxability of PPP loans.

The OLS cannot provide a specific estimate of the revenue loss resulting from the bill. However, based on currently available PPP data, the OLS concludes that the changes to State tax law proposed by the bill could have a significant impact on State tax collections. According to the

SBA, New Jersey businesses received $17.3 billion in assistance through the first round of PPP funding. Deducting the amount of PPP loans awarded to corporations and non-profit organizations reduces this amount by approximately $10.9 billion to $6.4 billion. This amount represents the maximum that may be *excluded* from gross income. The bill also allows expenses covered by a PPP loan to be *deducted* from gross income. The OLS anticipates that the amount deducted from gross income will be much lower because these expenditures may already deductible under current law as normal business expenses.

The maximum amount of first round PPP loan funding that may be excluded from gross income is $6.4 billion. Taxpayers will see varying tax benefits from the exclusion under the bill, as State marginal tax rates range between 1.4 percent and 10.75 percent. Applying these rates to the $6.4 billion that may be excluded yields a potential State revenue loss up to $688.0 million.

Loan recipients were permitted to use first round funding (supported by the CARES Act) to support the following expenses: payroll costs; costs related to the continuation of health benefits and medical insurance, employee salaries and compensation, payment of mortgage interest, rent, utilities, and interest on any other debt obligations incurred February 15, 2020 and June 30, 2020. Loan funding used to pay four categories of costs (payroll, interest on mortgage obligations, rent, and utilities) incurred eight weeks after loan origination may be forgiven.

Recently enacted federal legislation made additional changes to the PPP that will impact the revenue losses resulting from the bill. PPP loans may now be used to pay operating costs, property damage costs, supplier costs and worker protection expenditures and loan funds used to these purposes are eligible for loan forgiveness. The covered period (the period during which loan proceeds may be applied) for all PPP loans has been extended to March 31, 2021. The forgiveness period for all loans has been lengthened to from eight weeks after loan origination to between eight weeks and 24 weeks after loan origination, as chosen by recipient. This additional flexibility regarding the use of loan funds and the forgiveness period will allow for additional exclusions and deductions from income and contribute to the State revenue loss.

The CARES Act appropriated $349 billion to support loans to eligible businesses. The Consolidated Appropriations Act, 2021 provided an additional $284.4 billion for the PPP, thereby increasing total program funding to $633.4 billion. The SBA began accepting applications for PPP loans through the second round of funding on January 13, 2021. There is no information available on the amount of additional loan funding awarded to date.

Section: *Revenue, Finance and Appropriations*

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This legislative fiscal estimate has been produced by the Office of Legislative Services due to the failure of the Executive Branch to respond to our request for a fiscal note.

This fiscal estimate has been prepared pursuant to P.L.1980, c.67 (C.52:13B-6 et seq.).