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PPP Loan State Tax Implications

One of the greatest concerns for small business owners following COVID-19 stimulus legislation last year was whether loans forgiven under the Paycheck Protection Program (PPP) would be taxable. While Congress never intended the loans to be taxed, the IRS determined that the loans indeed would be subject to federal taxation. To the collective relief of taxpayers, the Consolidated Appropriations Act signed into law last December clearly states that loans forgiven under the PPP will not be subject to federal taxation.

Now that the federal controversy is settled, where do the states stand on this issue? Like many state and local tax issues, it depends on where the business is located. Some states are following the federal example, while others have indicated they will tax all or a portion of PPP loan income.

Jurisdictions Conforming to Federal Standards

The following states have ruled they will follow the federal treatment of the non-taxability of PPP loan forgiveness:

- Alabama
- California
- Connecticut
- Hawaii
- Indiana
- Kentucky
- Mississippi
- Montana
- New York
- North Carolina
- Oregon
- Pennsylvania
- South Carolina
- Tennessee

Jurisdictions Not Conforming to Federal Standards

The following states have released guidance and do not conform to the federal treatment:

- Massachusetts
- Minnesota
- New Hampshire
- Wisconsin

It is still to be determined whether these states will tax all or a portion of the PPP loan amounts.

Jurisdictions Not Releasing Guidance

When jurisdictions do not release guidance, adherence to federal standards typically depends on how the state conforms to the Internal Revenue Code (IRC). The methods that they apply when conforming to the IRC are Fixed/Static, Rolling or Selective as defined below:

- Fixed/Static Conformity: The state conforms to the IRC to a specific date.
- Rolling Conformity: The state conforms to the most recent version of the IRC.
- Selective Conformity: The state conforms to certain provisions of the IRC.

To date, 22 jurisdictions have rolling conformity. Based on this type of conformity, we can expect that federally forgiven loans will not be subject to state taxation, unless they release guidance stating otherwise.

Business owners should work with their tax advisors to carefully assess how their state(s) will treat the taxation of PPP loans. There may be additional risks and opportunities to consider regarding the state taxation of loan forgiveness. Finally, be aware that jurisdictions that issued initial guidance could change their guidance in the future.

If you have questions about this topic, please contact Frankel Zacharia at 402. 496.9100.