DEPARTMENT OF REVENUE

Federal Update
Paycheck Protection Program and Unemployment Subtraction

May 14, 2021

	Yes	No
DOR Administrative Costs/Savings	X	

Department of Revenue
Analysis of S.F.2300 (Nelson) as Proposed to be Amended (sc2300a-1)

	Fund Impact			
	F.Y. 2022	**F.Y. 2023**	**F.Y. 2024**	**F.Y. 2025**
	(000's)			
PPP Loan Exclusion				
Individual Income Tax	($191,500)	($18,200)	($14,400)	($9,900)
Corporate Franchise Tax	($183,500)	($15,900)	($12,200)	($9,200)
Unemployment Benefit Subtraction	($234,800)	$0	$0	$0
General Fund Total	($609,800)	($34,100)	($26,600)	($19,100)

The PPP loan exclusion is effective for tax years 2020 and 2021. The unemployment insurance subtraction is effective for tax year 2020 only.

EXPLANATION OF THE BILL

The bill updates reference to the Internal Revenue Code to include the paycheck protection program exclusion and the unemployment insurance subtraction only.

Paycheck Protection Program

The Paycheck Protection Program (PPP) provides low-interest loans to small businesses with less than 500 employees to assist with payroll, mortgage interest, rent, and utilities. The loans are to be spent over an 8-week to 24-week period for qualified business expenses. The total loan covers up to 2.25 times the business's average monthly costs up to $10 million. After the covered period, business can contact the loan provider to seek possible loan forgiveness. Loans are eligible for forgiveness if they meet certain requirements.

The amount of the loan that is forgiven is not included in gross income. The Consolidated Appropriations Act of 2021 (CAA 2021) clarified that expenses paid with forgiven loans may be deducted from income.

The bill conforms to federal law by excluding the amount of the loan that is forgiven from gross income.

- The first and second round of PPP loans ended on August 8, 2020. At that time, about 5,212,100 loans totaling $525.0 billion had been approved by the Small Business Administration (SBA), as reported in the Paycheck Protection Program Report. Of this total, about 102,400 loans totaling $11.3 billion were approved in Minnesota.
- The CAA 2021 appropriated an additional $284 billion for PPP loans. Based on the loans issued so far, Minnesota businesses are expected to receive an additional $6.1 billion in loans in tax year 2021.

EXPLANATION AND ANALYSIS OF THE BILL (Cont.)

- Based on the distribution and magnitude of the loans, it is assumed 80% of the loans will be forgiven.
- C corporations account for 39.5% of PPP loans in Minnesota, according to information obtained from the Small Business Administration. Pass-through entities, estates, trusts, and individuals account for 51.9%. Nonprofit organizations account for 8.6%.
- Nonprofits are not included in the estimate because their operating income is already excluded from tax.
- The estimate was reduced by 68% to exclude businesses without taxable income in tax year 2020, based on taxable income in 2018, adjusted for expected losses in 2020.
- The SBA data for Minnesota loan recipients does not include out-of-state businesses with sales into Minnesota. The size of that impact is unknown but is assumed to be offset by out-of-state sales of businesses located in Minnesota.
- Amounts that cannot be deducted immediately may be carried forward as net operating losses (NOLs) to offset income in future years. Between 2.7% and 6.3% of NOLs are assumed to be claimed each year over the forecast period.
- The CARES Act removed the 80% limitation on NOLs and allowed losses to be carried back for up to five years. Adopting those provisions when combined with the PPP loan exclusion would result in an additional immediate impact in FY 2022. This estimate assumes the current limitations on NOLs will remain in place.
- A marginal rate of 8.0% was assumed for individuals and pass-through entities. A marginal rate of 9.8% was applied to corporations.
- Corporate tax impacts are allocated 30% / 70% to fiscal years. Income tax impacts were allocated to the following fiscal year.

Unemployment Insurance Subtraction
Effective for tax year 2020 only.

The bill creates a temporary subtraction for taxable unemployment insurance compensation. For tax year 2020 only, an individual taxpayer with adjusted gross income less than $150,000 is allowed a subtraction equal to the taxpayer's regular and supplemental unemployment compensation up to $10,200. For a joint return, the subtraction is limited to $10,200 in unemployment compensation received by each spouse.

- About 821,300 individuals received $9.68 billion in unemployment insurance payments in 2020, according to information provided by the Department of Employment and Economic Development.
- It was assumed that around 65% of claims would result in taxable income on individual returns, based on the average percentage of claims that were reported as taxable income.
- Subtractions in tax year 2020 are expected to total $3.612 billion with the $10,200 maximum and the $150,000 income limit, based on unemployment insurance reported on 2018 returns, adjusted to reflect payments in 2020.
- A marginal rate of 6.5% was assumed.
- Retroactive impacts were allocated to fiscal year 2022.

EXPLANATION AND ANALYSIS OF THE BILL (Cont.)

- Subtractions in tax year 2020 are expected to total $3.612 billion with the $10,200 maximum and the $150,000 income limit, based on unemployment insurance reported on 2018 returns, adjusted to reflect payments in 2020.
- A marginal rate of 6.5% was assumed.
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Minnesota Department of Revenue
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