WMC
WISCONSIN MANUFACTURERS & COMMERCE

To: Wisconsin Legislature

From: Corydon Fish, Director of Tax

Date: January 26, 2021

Re: **Protect Small Businesses, Do Not Let DOR Sleep Walk into Tax Hike**

During the opening days of the COVID-19 pandemic, state governments across the nation took drastic responses shutting down whole economic sectors in a bid to slow the spread of the virus. These shutdowns helped push Wisconsin, and the nation, into its worst economic crisis since the Great Depression.

Congress reacted to these twin public health and economic crises by passing the Coronavirus Aid, Relief, and Economic Security (CARES) Act, which prevented the business community from suffering the very worst of the economic damage that could have been caused by the pandemic. One of the most effective portions of the CARES Act was the Paycheck Protection Program (PPP), which helped employers keep people employed in the early months of the pandemic. This program included a promise to small business owners that if they used the loans for appropriate payroll and non-payroll expenses, the loans would be forgiven *and that the aid was tax free*. However, because of disagreements between the elected officials who wrote the law and the unelected agency employees who enforce it, small businesses may be saddled with almost half a billion dollars of surprise tax liability.

The Internal Revenue Service (IRS) contradicted Congress by issuing Revenue Ruling 2020-27 stating that expenses funded through a PPP loan are not deductible for 2020 if "the taxpayer reasonably expects to receive forgiveness of the covered loan on the basis of the expenses it paid or accrued during the covered period, even if the taxpayer has not submitted an application for forgiveness of the covered loan by the end of such taxable year." The effect of this ruling transformed tax free loan forgiveness into taxable income.

U.S. Senator Chuck Grassley (R-IA), Chair of the Senate Finance Committee, and Representative Richard Neal (D-MA), chair of the House Ways & Means Committee—primary authors of the PPP provision—had this to say about the intent and language of the bill:

"The CARES Act provides that a PPP loan recipient will not recognize taxable income if the loan is forgiven, in effect making the loan a tax-free grant. Additionally, as was expressed to Treasury during the development of the PPP, we did not intend to deny the deductibility of ordinary and necessary business expenses…"[1]

[1] https://www.grassley.senate.gov/news/news-releases/grassley-wyden-neal-push-treasury-allow-small-businesses-deduct-ppp-expenses

Congressional intent is clear, this aid was meant to be tax free. WMC understands that this is not ordinary tax policy, but these are not ordinary times. While supporters of DOR's interpretation argue this is how Wisconsin ordinarily collects tax revenue, Congress intended to enact extraordinary tax policy essentially making these loans a tax-free grant once forgiven. Every indication is that the Wisconsin legislature originally wanted to follow this intent.

The CARES Act was signed into law in late March 2020, and Wisconsin conformed to many of its tax provisions, including the treatment of PPP loans, on April 15th. At the time of passage, the Wisconsin Department of Revenue (DOR) published a fiscal estimate where they did *not* include anything about collecting $450 million in additional taxes by conforming to the PPP loan provisions.[2] To WMC's knowledge, no legislator indicated support for or believed they were voting to tax these loans. Further, the IRS had yet to raise any issues at the federal level either. *In other words, at the time Wisconsin Act 185 was enacted, policymakers at the federal and state level thought forgivable PPP loans would be tax free aid.*

Now, almost a year later, DOR is reversing course by issuing a guidance document stating the forgivable loans are actually taxable[3] to help fund bigger government expenditures by imposing unplanned for—and unintended—surprise tax liability on Wisconsin small businesses[4] who are struggling to weather a pandemic and economic crisis.

Congress never intended to these loans to be taxable. There is no evidence the state legislature did either. If there is going to be a tax increase, there should be an open and honest debate about it. Policymakers should not allow DOR to "sleep walk" into a tax increase that no one ever intended to be enacted.

WMC calls on the legislature to quickly clarify the law, as Congress did, to reflect the intent of the CARES Act—that forgivable PPP loans were meant to be tax free aid. Wisconsin Small businesses should not be saddled with almost half a billion dollars of unplanned tax liability because of sloppy drafting and questionable legal interpretation at the federal level.

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[2] https://docs.legis.wisconsin.gov/2019/related/fe/ab1038/ab1038_dor.pdf

[3] https://www.revenue.wi.gov/Pages/TaxPro/2021/news-2021-CAA-Impact.aspx

[4] At least 89,615 Wisconsin businesses received PPP loans. At least 65,534 of those businesses received loans below $150,000. https://www.sba.gov/sites/default/files/2020-08/PPP_Report%20-%202020-08-10-508.pdf; https://home.treasury.gov/policy-issues/cares-act/assistance-for-small-businesses/sba-paycheck-protection-program-loan-level-data.