TIDWELL
CERTIFIED PUBLIC ACCOUNTANTS

Summary Analysis of California AB 80

California Partial Conformity to Federal Tax Treatment of PPP Loan Forgiveness

On April 26th, 2021, the California General Assembly passed AB 80, which brings California into partial conformity with federal tax treatment of Paycheck Protection Program (PPP) Loans.

Current federal tax law excludes the debt forgiveness from PPP Loans as being included in Gross Income for tax purposes, meaning that PPP Loan proceeds and forgiven amounts are not considered to be taxable income at the federal level. Further, at the federal level, businesses are still allowed to deduct expenses paid for with this tax-exempt income; meaning that there are no negative tax implications of receiving a PPP Loan for federal income tax purposes.

California has previously conformed to the federal tax law excluding forgiven PPP Loan proceeds from gross income; however, California previously did not conform to the federal law allowing the deductibility of expenses paid with the class of tax-exempt income. This means that prior to the passage of AB 80, forgiven PPP Loans were effectively still taxable at the state level in California.

AB 80 changes the current California law which disallows the deduction of expenses paid with PPP Loan proceeds and allows for both tax-free forgiveness and fully deductible expenses for all businesses in California that are not an “ineligible entity”. AB 80 defines an ineligible entity as any business that:

1. Is a publicly-traded company
2. Did not experience a 25% or greater gross receipts reduction in calendar year 2020 when compared to the same calendar quarter for 2019.

Clearly, the second requirement stating that to qualify to deduct expenses paid with PPP loan forgiven amounts a business must have a 25% reduction in gross receipts in any 2020 calendar quarter as compared to that same 2019 calendar quarter is more applicable to many businesses that received PPP Loans in California. This means that if a business did not see their revenues for any given quarter in 2020 be reduced by 25% or more when comparing to the same quarter in 2019, then they will not be allowed to deduct expenses paid for with their forgiven PPP Loan proceeds, effectively making their PPP Loans taxable.

AB 80 specifically utilizes the same rules for calculating the 25% gross receipts reduction threshold as the SBA uses for determining eligibility for a business to receive a second draw of a PPP Loan. The SBA Guidance on this gross receipts test is available on The Department of Treasury’s website, or by following this link:

> https://home.treasury.gov/system/files/136/Second-Draw-PPP-Loans--How-Calculate-Revenue-Reduction-Maximum-Loan-Amounts-Including-Documentation-Provide1192021.pdf

To illustrate the required gross receipts reduction requirement for tax-free treatment of , consider the following examples of 3 different businesses that received PPP Loans in California in 2020:

TIDWELL
CERTIFIED PUBLIC ACCOUNTANTS

Business 1 - Quarterly Revenues			
	2019	2020	% Change
Q1	$ 1,000,000	$ 975,000	-2.50%
Q2	$ 1,100,000	$ 800,000	-27.27%
Q3	$ 1,150,000	$ 1,050,000	-8.70%
Q4	$ 1,080,000	$ 1,095,000	1.39%
Total	$ 4,330,000	$ 3,920,000	-9.47%

Qualified for CA Tax-Free Treatment (PPP Expenses Deductible): Yes

Analysis: Business 1 will qualify for tax-free treatment of PPP Loans, because their 2nd quarter 2020 revenue was declined by more than 25% compared to that same quarter in 2019.

Business 2 - Quarterly Revenues			
	2019	2020	% Change
Q1	$ 575,000	$ 625,000	8.70%
Q2	$ 600,000	$ 605,000	0.83%
Q3	$ 615,000	$ 425,000	-30.89%
Q4	$ 425,000	$ 575,000	35.29%
Total	$ 2,215,000	$ 2,230,000	0.68%

Qualified for CA Tax-Free Treatment (PPP Expenses Deductible): Yes

Analysis: Even though Business 2's total revenue was higher in 2020 than it was in 2019; Business 2 will qualify for tax-free treatment of PPP Loans because their 3rd quarter 2020 revenue declined by more than 25% compared to that same quarter in 2019.

Business 3 - Quarterly Revenues			
	2019	2020	% Change
Q1	$ 1,000,000	$ 975,000	-2.50%
Q2	$ 1,100,000	$ 900,000	-18.18%
Q3	$ 1,150,000	$ 955,000	-16.96%
Q4	$ 1,080,000	$ 980,000	-9.26%
Total	$ 4,330,000	$ 3,810,000	-12.01%

Qualified for CA Tax-Free Treatment (PPP Expenses Deductible): No

2209 Plaza Drive, Suite 200, Rocklin, CA 95765 • Phone: 916.784.1818 • Fax: 916.784.2818 • www.tidwellcpa.com

Analysis: Business 3 will not qualify for California tax-free treatment of PPP Loans, because even though they experienced declines in revenue for all quarters in 2020 when compared to 2019, they did not have any quarter in which revenue was at least 25% less than it was for that same quarter in 2019.

In summary, with the passage of AB 80 businesses that received PPP Loans and had significant revenue reductions in 2020 (more than 25% in any quarter) will see no negative tax consequences from receiving PPP Loan forgiveness at the state level. If a business does not have the required 25% quarterly revenue decline, then the business will effectively owe California Income Tax on their forgiven PPP Loans. The rules about “reasonable expectance” of forgiveness still also apply, meaning that even if a business does not actually have PPP Loan forgiveness in 2020, but reasonable expects that it will be forgiven in the future (or already has in 2021) then the disallowance of deductible expenses could still apply, subject to the 25% gross receipts reduction test.

AB 80 also brings California into full conformity with federal law concerning the EIDL Advance Grants, making them completely non-taxable at the state level.

AB 80 does not, however, conform California’s tax treatment of SBA subsidies or payments on SBA loans, Shuttered Venue Operator Grants, or Restaurant Revitalization Grants. These types of financial assistance remain taxable in California, pending any further legislation to the contrary.

The full text of AB 80 is available at:

https://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=202120220AB80

Please feel free to reach out to our office with any questions about how AB 80, PPP Loans or any other issue impacts your specific business or personal income tax situation.

2209 Plaza Drive, Suite 200, Rocklin, CA 95765 • Phone: 916.784.1818 • Fax: 916.784.2818 • www.tidwellcpa.com