

## OBSERVATIONS

### New Hampshire Taxation of COVID-19 Relief Funds

January 21, 2021

The New Hampshire Department of Revenue has today issued a Technical Information Release (TIR 2021-001) relative to the New Hampshire Taxation of Federal and State Covid-19 Financial Relief Funds. The TIR can be found online at <https://www.revenue.nh.gov/documents/2021-001.pdf>

Simply stated, the release addresses these main issues:

1. Federal relief funds like Paycheck Protection Program (PPP) Funds:
  - a. will be taxable for Business Profits Tax purposes
  - b. will be taxed in the year the loan is actually forgiven.
2. State relief funds like the Main Street Relief Funds (MSRF) will be taxable for State purposes unless there is a reason to believe they will be deemed to be loans that must be repaid.

The TIR references “For taxable periods beginning on or after January 1, 2020 taxpayers should utilize the IRC in effect on December 31, 2018”. Under current NH law, this is the applicable federal tax code for applicable for NH 2020 Business Profits Tax (BPT) and Business Enterprise Tax (BET) Returns. This means the current federal provisions that exempt these funds from taxation do not apply. As such, the State is applying applicable IRC sections including 61(a)(11) and 108 relative to discharge of indebtedness, meaning taxable when actually discharged unless exceptions apply like bankruptcy or insolvency.

The TIR indicates Main Street Relief Funds will be taxable unless they take the form of a loan. Presumably this means if there is an indication that some or all of the funds must be repaid. In such a case, the funds would not be subject to taxation until it is confirmed what amount, if any, has to be repaid. The TIR does not reference the timing of the inclusion of the Main Street Relief Funds for fiscal year taxpayers. Despite the reference above to “taxable periods beginning on or after January 1, 2020”, the taxation of the Main Street relief funds would potentially be taxable for a fiscal year ending in 2020 that started before January 1, 2020. We believe the State will require fiscal year taxpayers to apply a reasonable basis method to determine which year the Main Street Relief funds are includable in taxable income, including consideration of when the funds are included in federal taxable income. Calendar year taxpayers who do not believe any MSRFs will be required to be returned would need to include these funds in both the federal and state income tax returns for 2020.

Although it is not specifically identified in the TIR, our interpretation is that the BPT taxation of the PPP funds will NOT provide an additional amount for the BPT personal compensation deduction allowed to sole proprietors and partnerships. That deduction is based on income subject to Self-Employment Tax. Since PPP funds are not federally taxable, those funds will not be deductible from Business Profits as reasonable compensation. As such, a taxpayer may find they are unable to fully offset the BPT taxable income with a reasonable compensation deduction.

Other provisions of the TIR indicate.

- “Taxpayers may continue to take deductions for deductible expenses of operating their business” even if paid for with PPP or MSRF funds even when those expenses are paid for with state-level relief.
- “any federal-level” [or state level] “relief received by taxpayers required to file a BET return that is utilized to pay wages or other compensation to employees, interest, or dividends shall be included in the enterprise value tax base of the business and subject to the BET.”

As a result of the TIR, New Hampshire businesses will include in BPT returns the PPP funds in the year the related loan is forgiven. This may be contradictory to the timing of the non-taxable inclusion in the federal return or financial statements.

We encourage business owners to read the TIR issued and to contact us with any questions.