COMMONWEALTH OF KENTUCKY FISCAL NOTE STATEMENT
LEGISLATIVE RESEARCH COMMISSION
2021 REGULAR SESSION

MEASURE

2021 BR NUMBER 1288 HOUSE BILL NUMBER 278/HCS 1

TITLE AN ACT relating to the expenses paid with Paycheck Protection Program loans.

SPONSOR Representative Patrick Flannery

FISCAL SUMMARY

STATE FISCAL IMPACT: ☒ YES ☐ NO ☐ UNCERTAIN

OTHER FISCAL STATEMENT(S) THAT MAY APPLY: ☐ ACTUARIAL ANALYSIS
☐ LOCAL MANDATE ☐ CORRECTIONS IMPACT ☐ HEALTH BENEFIT MANDATE

APPROPRIATION UNIT(S) IMPACTED: _____

FUND(S) IMPACTED: ☒ GENERAL ☐ ROAD ☐ FEDERAL ☐ RESTRICTED _____

FISCAL ESTIMATES	2020-2021	2021-2022	ANNUAL IMPACT AT FULL IMPLEMENTATION
REVENUES	(Indeterminable)	(Indeterminable)	(Indeterminable)
EXPENDITURES			
NET EFFECT	(Indeterminable)	(Indeterminable)	(Indeterminable)

( ) indicates a decrease/negative

PURPOSE OF MEASURE: HB 278 HCS1 would mirror federal law by allowing a deduction for expenses paid using Paycheck Protection Program (PPP) loan proceeds, against the taxes imposed by KRS Chapter 141. The provisions of HB 278 HCS1 are retroactive to taxable years beginning on or after January 1, 2020, and would end for taxable years beginning after December 31, 2021.

The Coronavirus Aid, Relief, and Economic Security Act (CARES), and subsequent legislation, authorized PPP loans and set out the terms for loan forgiveness. The first draw of loans ($342.3 billion) was granted between April 3 and April 16, 2020, and the second draw ($320 billion) was authorized on April 24, 2020. PPP loan proceeds must be spent within a 24-week period, or by December 31, 2020, whichever comes first. PPP loans granted before June 5, 2020, may opt to spend the loan proceeds in an 8-week period per the original CARES Act language. This is known as the covered period. PPP loans made before June 5, 2020, have a term of 2 years, and loans made after this date have a term of 5 years.

For a PPP loan to be forgiven, borrowers must 1) maintain employee and compensation levels during the covered period, 2) spend the loan proceeds on allowable expenses, and 3) spend at least 60 percent of the loan proceeds on payroll costs. Allowable expenses include business mortgage interest payments, business rent or lease payments, business utility payments, covered operations expenditures, covered property damage costs, covered supplier costs, and covered worker protection expenditures. In addition to normal wages, payroll costs include all forms of cash compensation paid to employees including tips, commissions, bonuses, hazard pay, and employer-paid health care expenses.

PPP borrowers can apply for loan forgiveness once the loan proceeds have been expended. Loan forgiveness can be applied for any time up to the loan date of maturity. If the borrower does not apply for loan forgiveness within 10 months after the covered period, PPP principal and interest payments are no longer deferred, and borrowers must begin making payments to their lender.

According to the Small Business Administration (SBA), approximately $5.3 billion in PPP loans have been dispersed to over 50,000 Kentucky businesses from the two initial loan draws. The vast majority of the loans, in terms of the number of loans granted, were for less than $150,000. Loans in excess of $150,000 represent the majority (72 percent) of total dollar amount of loans granted.

FISCAL EXPLANATION:

Developing a fiscal impact estimate of HB 278 HCS1 is difficult for several reasons. While the total amount of PPP loans granted to Kentucky businesses is known, when borrowers will apply for forgiveness and the dollar amount of loans forgiven cannot be determined at this time. Also, there is insufficient data to determine how much of each loan will be spent on forgivable expenses.

Borrowers have 2 to 5 years to apply for PPP loan forgiveness. The provisions of HB 278 HCS1 would encourage borrowers to apply for loan forgiveness by December 31, 2021. Given the uncertainty regarding when and how each borrower will file their tax return, staff are not able to estimate the timing and magnitude of the fiscal impact in the current biennium.

According to the SBA, as of the date of this fiscal note, borrowers have applied for forgiveness for $83 billion of the over $600 billion in PPP loans that have been granted. The timing and awarding of loan forgiveness dictates when those expenses can be deducted against Kentucky income taxes.

Another complicating factor is that tax filing season is already underway. Kentucky forms and instructions have already been published and do not reflect the deduction that would be allowed by HB 278 HCS1. Passage of HB 278 HCS1 will require modifications to instructions, software, and forms to accommodate the proposed changes. Returns filed before these changes are made will likely be amended to claim the deductions allowed under HB 278. These amended returns will lead to higher refunds after FY 21.

Staff could not develop a point estimate of the fiscal impact of HB 278 HCS1. The primary fiscal impact will be dependent on when loans are forgiven, the total amount forgiven, and whether the loan proceeds were used for deductible expenses.

While the estimated fiscal impact of HB 278 HCS1 is negative indeterminable, the provisions of this bill may have a substantial negative impact over the next two years. The potential exists for a substantial negative impact due to the number of PPP loans that have been approved and the incentive for businesses to spend the proceeds on deductible expenses. SBA data indicate $5.3 billion in loans have been granted to Kentucky business. In terms of an upper-bound, if all loans are forgiven and the proceeds are used on allowable expenses, the potential fiscal impact, which may be taken over a 2-3 year period would be ($250 million).

DATA SOURCE(S): **LRC Staff**
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