Larry's Tax Law

News From the Washington Department of Revenue to Taxpayers Subject to Its Business and Occupations Tax – Whether It Is Welcome News Is Yet to Be Determined

By Larry Brant and Peter Evalds on 5.18.20 | Posted in Legislation, State and Local Tax, Tax Laws

As we recently reported, the Oregon Department of Revenue ("ODOR") issued written guidance concluding that the receipt of funds pursuant to PPP loans (whether or not forgiven), EIDLP advances and SBA debt relief for certain business loans do not constitute commercial activity under Oregon's new gross receipts tax, the Corporate Activity Tax (the "CAT"). Accordingly, taxpayers subject to the CAT do <u>not</u> include these items in their computation of commercial activity.

Washington state enacted its Business and Occupations Tax ("B&O Tax") almost 90 years ago. The B&O Tax, like the CAT, is a gross receipts tax. Unlike the CAT, however, taxpayers subject to the B&O Tax are generally not allowed to deduct any of their costs, including materials and labor, from gross revenues.

The Washington Department of Revenue ("WDOR") issued written guidance last week, possibly joining the ranks with the ODOR. **Better late than never!**

The WDOR concludes that taxpayers subject to the B&O Tax <u>should not</u> include the receipt of funds pursuant to COVID-19 relief programs for purposes of computing their tax liability under the B&O Tax regime.

NOT SO FAST!

Practice Alert: The WDOR uses the phrase "should not" in its guidance. It was not as empathetic about excluding the proceeds from these COVID-19 assistance programs as the ODOR. The WDOR merely states that it believes the legislature may be interested in "clarifying" the B&O Tax statute with respect to these federal programs, particularly after it has "identified and analyzed" the programs. Consequently, the WDOR is kicking the can down the road! It is simply delaying a decision regarding the taxability of these items, deferring to the Washington State Legislature.

SOME GOOD NEWS!

The WDOR did clearly state that, until the legislature has had time to act, neither penalties nor interest will accrue with respect to any B&O tax that may ultimately be due upon the receipt of funds from these federal programs.

Additionally, the WDOR invites taxpayers with questions relating to specific COVID-19 assistance programs to submit a letter ruling request.

Practice Alert: Taxpayers and tax practitioners need to be aware that the WDOR pronouncement is <u>not</u> very clear relative to its scope. Unlike the ODOR in its recent announcement, the WDOR did not elaborate on what federal COVID-19 programs are included within the scope of its limited guidance. It merely states that:

The department has determined that businesses receiving assistance [financial assistance to cope with the impacts of the COVID-19 pandemic] under these federal programs (including the federal Paycheck Protection Program (PPP) program) should <u>not</u> report assistance as gross receipts for B&O tax purposes and should <u>not</u> pay B&O tax on that assistance at the present time.

Based upon the language of the WDOR's announcement, PPP loans are clearly included within the scope of its guidance. Hopefully, the other federal COVID-19 relief programs such as EIDLP loans and advances, and the employee retention credit programs, are covered by its announcement. Maybe the Washington State Legislature will offer declarative guidance soon.

CONCLUSION

Taxpayers receiving federal assistance to combat economic devastation in the wake of the COVID-19 pandemic are also faced with the question of taxability of these benefits under federal, state and local tax regimes. To date, we do not have clear and complete guidance!

As previously reported, the IRS issued Notice 2020-32, wherein (relying primarily on Code Section 265) it emphatically pronounced that taxpayers receiving PPP loan forgiveness (in accordance with the CARES Act) have no cancellation of debt income, but they do not get to deduct the business expenses for which the forgiven loan proceeds are used. Fortunately, legislation was introduced in the U.S. Senate on May 5, 2020, which would nullify Notice 2020-32. Senate Bill 3612 provides that business expenses otherwise deductible under Code Section 162 funded by forgiven PPP loan proceeds are deductible. Unfortunately, this bill, labeled the Small Business Expenses Protection Act of 2020, remains in the Senate. As of this date, it has not advanced in the legislative process. Additionally, the proposed legislation does not address the taxability of benefits from the other federal COVID-19 relief programs.

As stated above, the ODOR has announced that the receipt of funds pursuant to PPP loans (whether or not forgiven), EIDLP advances and SBA debt relief do not constitute commercial activity under the CAT. It has not commented on the taxation of these benefits under its income tax regime. Presumably, the ODOR is waiting for the IRS or Congress to act relative to the income tax implications.

For B&O Tax purposes, we know that the Washington State Legislature has been asked to review the matter. For now, the WDOR has promised that it will not assess penalties or interest if the legislature determines that the receipt of benefits under the federal COVID-19 relief programs are subject to the tax regime. It is, however, unclear what federal programs (other than the PPP loan program) are included within the WDOR's guidance.

State and local taxation cannot be ignored. The receipt of federal COVID-19 relief benefits need to be analyzed under the lenses of all state and local taxation regimes to which a taxpayer is subject. It would be terrible to get through this pandemic only to be surprised by an unwanted and unexpected state and/or local tax liability.