



## **Important Notice: Impact of Session Law 2021-180 on North Carolina Individual and Corporate Income Tax Returns**

The following important information is addressed in this notice:

- An explanation of how specific provisions of Session Law 2021-180, the recently enacted State budget, affects the 2020 North Carolina individual and corporate income tax returns.
- Instructions on how to file a 2020 amended return if the provisions of Session Law 2021-180 affect North Carolina individual and corporate income tax returns.

### **Background**

On November 18, 2021, Governor Cooper signed into law [Session Law 2021-180](#) (Senate Bill 105). This legislation updated North Carolina's reference to the Internal Revenue Code (the "Code") from May 1, 2020 to April 1, 2021. As enacted, any changes made to the Code as of April 1, 2021, including any changes made by the [Consolidated Appropriations Act, 2021](#) ("CAA") and the [American Rescue Plan Act of 2021](#) ("ARPA") (collectively, "federal tax provisions"), apply to North Carolina income tax to the extent North Carolina follows the federal tax provisions.

The purpose of this notice is to explain how specific federal provisions included in the CAA and the ARPA affect North Carolina individual and corporate income tax returns, (collectively, "NC Tax Returns"), for tax year 2020. This notice also provides instructions on how a taxpayer can amend a NC Tax Return for tax year 2020. Any impact of the CAA and the ARPA on NC Tax Returns for tax year 2021 will be addressed in the instructions for the 2021 NC Tax Returns, which should be released in early 2022.

### **Paycheck Protection Program ("PPP") Expenses**

Generally, federal income tax law treats the proceeds from a forgiven loan as taxable income. Nevertheless, the [Coronavirus Aid, Relief, and Economic Security Act](#) (the "CARES Act") created the Paycheck Protection Program ("PPP") that permits eligible small businesses to treat a forgivable loan in a way that does not follow the general rule.

Notably, section 1106 of the CARES Act provides "any amount that would be includible in the gross income of the recipient by reason of forgiveness of a PPP loan [is] excluded from gross income." Thus, for federal tax purposes, the proceeds from a forgiven PPP loan are not includable in federal taxable income. The 2020 General Assembly conformed to the federal tax treatment

of excluding the proceeds of a forgiven loan in the computation of State taxable income by updating the State's reference to the Code as of May 1, 2020.<sup>1</sup>

In addition, in most cases, federal income tax law does not allow taxpayers a deduction for expenses paid with tax-exempt income.<sup>2</sup> However, the CAA made eligible expenses paid with the proceeds of a forgiven PPP loan (i.e. income that is completely tax-exempt) deductible for federal income tax purposes. Notwithstanding federal law, the 2020 General Assembly enacted [legislation](#) that added G.S. 105-153.5(c2)(20) (for individuals) and G.S. 105-130.5(a)(32) (for corporations) requiring North Carolina taxpayers to addback the amount of expenses deducted under the Code to the extent that expenses were paid with forgiven PPP loan proceeds.<sup>3</sup>

Importantly, the 2021 General Assembly retroactively amended G.S. 105-130.5(a)(32) and G.S. 105-153.5(c2)(20), **delaying the State's decoupling adjustment**.<sup>4</sup> As amended, a taxpayer is not required to add to federal income the amount of otherwise deductible expenses paid with forgiven PPP loan proceeds until tax years beginning on or after January 1, 2023. Because the General Assembly chose to suspend the State-level PPP addback until 2023, North Carolina conforms to the federal treatment of expenses paid by PPP loans for tax year 2020.

Taxpayers who have already filed a NC Tax Return for tax year 2020 that included a State addition for otherwise deductible expenses paid with forgiven PPP loan proceeds should file a State amended return removing this addition. **The Department will not automatically adjust a taxpayer's NC Tax Return, nor will the Department automatically refund any overpayment resulting from the delayed PPP decoupling adjustment.**

### **Other Items of Income Excluded from 2020 Federal Taxable Income**

As noted previously, North Carolina income tax law incorporates many of the provisions of the Code as of a specific date. [Session Law 2021-180](#) updated North Carolina's reference to the Code to April 1, 2021. This Code update incorporated by reference many of the provisions of the CAA, including the provision to exclude from federal income certain items of income, including Economic Injury Disaster Loans ("EIDL") grants, targeted EIDL advances, and certain Small Business Association ("SBA") loan payments.

Taxpayers who have already filed a NC Tax Return for tax year 2020 that included a State addition for EIDL grants, targeted EIDL advances, SBA loan payments, or other types of income specifically excluded from federal income should file an amended return removing this income.

### **2020 Unemployment Benefits**

Section 9042 of the ARPA excluded certain unemployment compensation from gross income for tax year 2020. In general, the first \$10,200 of 2020 unemployment benefits was not subject to federal individual income tax. While [Session Law 2021-180](#) updated the Code reference to include the provisions of the ARPA, [Session Law 2021-180](#) specifically decoupled from the federal treatment of unemployment benefits for tax year 2020. Thus, for North Carolina income tax purposes, unemployment compensation excluded from federal gross income under section 85(c)

<sup>1</sup> See HB 1080, s. 1.(a,b), [S.L. 2020-58](#).

<sup>2</sup> See [Code § 265](#).

<sup>3</sup> See HB 1080, s. 1.(c.f.), [S.L. 2020-58](#).

<sup>4</sup> See SB 105, s. 42.4.(c.d), [S.L. 2021-180](#).

of the Code is included in North Carolina taxable income for tax year 2020. As enacted, G.S. 105-153.5(c2)(23) requires an individual to add to adjusted gross income the amount excluded from the individual's gross income for unemployment compensation received by the taxpayer under section 85(c) of the Code.

Taxpayers who have already filed a NC Individual Income Tax Return ("Form D-400") for tax year 2020 who **did not include** a State addition for the portion of unemployment benefits not included in federal gross income should file an amended return adding this income. For more information, see the [Department's Important Notice dated October 8, 2021](#). Taxpayers who already filed a Form D-400 for tax year 2020 that **did include** a State addition for unemployment benefits not included in federal gross income as outlined in the Department's important notice do not need to take any further action.

### **How to Amend a NC Tax Return**

If you have already filed a NC Tax Return for tax year 2020, and the provisions of [Session Law 2021-180](#) affect your State taxable income for tax year 2020, you should file an amended North Carolina income tax return. If the amended return reflects an overpayment, the amended return must be filed within the [general statute of limitations for obtaining a refund](#).

If the amended return reflects additional tax due, you can avoid a late payment penalty if you pay the additional tax due when the amended return is filed. If the amended return reflects additional tax due but some or all of the additional tax is not paid when the amended return is filed, the unpaid tax is subject to [applicable penalties](#). In addition, [statutory interest](#) accrues on tax not paid by the original due date of the tax return. Taxpayers that owe additional North Carolina income tax may request a waiver of penalties within the provisions of the Department's [Penalty Waiver Policy](#).

When you file an amended NC Tax Return, it is important to remember the following:

- You must fill out the amended NC Tax Return completely. *(For more information on how to amend your NC Tax Return, see the instructions for filing the applicable NC Tax Return available on the [Department's website](#).)*
- You must submit all documents that support the change you made to the original return. *(For purposes of the delayed PPP decoupling adjustment, you are not required to submit an amended Schedule K-1 if the original NC Tax Return clearly reflects an addition to federal income for expenses deducted under a forgiven PPP loan.)*

### **Assistance**

If you have any questions about this notice, you may call the North Carolina Department of Revenue Customer Interaction Center at 1-877-252-3052 (8:00 am until 4:30 pm EST, Monday through Friday), or write the Department at PO Box 1168, Raleigh, NC 27602. Additional information on new legislation affecting North Carolina taxes may be obtained from the Department's annual law change document. When published, the 2021 law change document will be available on the Department's website, [www.ncdor.gov](http://www.ncdor.gov).

*To the extent there is any change to a statute or regulation, or new case law subsequent to the date of this notice, the provisions in this notice may be superseded or voided. To the extent that any provisions in any other notice, directive, technical bulletin, or published guidance regarding the subject of this notice and issued prior to this notice conflict with this notice, the provisions contained in this important notice supersede the previous guidance.*