

THE NEW TAX LAW DOESN'T HELP LOSERS

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During economic downturns, the ability to carryback current year net operating losses (NOLs) and recoup income taxes paid in the prior two years has been crucial at times to the survival of a business taxed as a corporation. While the new tax law has lowered the tax rate for profitable businesses, it also imposed new restrictions on the use of net operating losses that will eliminate their use as a quick source of cash when times are tough.

Previously, corporate taxpayers were generally able to carryback NOLs 2 tax years and carry them forward for 20 tax years. Furthermore, in general, the carryovers and carrybacks could fully offset a tax year's regular taxable income (although taxpayers would potentially still be limited in using NOLs to offset only 90-percent of alternative minimum taxable income).

Under the new law, for NOLs arising in a taxable year ending after December 31, 2017, most corporate taxpayers can no longer carryback NOLs but can carry them forward indefinitely. Additionally, the new law generally limits the NOL a corporation may utilize in a single tax year to the lesser of the available NOL or 80% of taxable income computed without regard to the NOL deduction. The limitation is effective for losses arising in tax years beginning after December 31, 2017.

The effective dates for these two provisions has left many scratching their heads. For example, as the law is currently written, a company with a fiscal year ending March 31, 2018 would be subject to the carryback disallowance because the tax year ends after December 31, 2017. However, it would not be subject to the 80-percent limitation since the loss arose in a tax year that began before December 31, 2017. While it is possible Congress may issue a technical correction to address the difference in applicable tax years, at this point, the best advice is to follow the pure reading of the statute until further guidance is provided.



In an ideal world, the economy will continue to grow; businesses will be profitable; and net operating losses will be a rare occurrence... But we all know that our world is far from ideal. These rules might make it an even less forgiving place.



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¹ This change does not apply to insurance companies (see definition in Code Sec. 816(a)) other than life insurance companies for which 2-year carryback and 20-year carryforward rules remain in place. There is also an exception to the no-carryback rule for farming losses.