November 11, 2009

Special New Tax Election to Carry Back Net Operating Losses for up to 5 Years

On November 6, 2009, the Worker, Homeownership, and Business Assistance Act of 2009 (H.R. 3548) (the "Act") was signed into law. The Act provides taxpayers (including corporate and non-corporate taxpayers) with a special election to carry back net operating loss ("NOL") deductions for up to 5 years, rather than 2 years, as generally is permitted.

Mechanics of the New Election

The Act provides taxpayers with a special, irrevocable election to extend the 2-year NOL carryback period to as many as 5 years with respect to an "applicable net operating loss." However, specific rules and limitations apply to this election.

- An "applicable net operating loss" includes only those NOLs that are incurred in 2008 and 2009.
- A taxpayer generally may only make this election for one taxable year, either 2008 or 2009. Thus, if a taxpayer elects to carry back an NOL incurred in 2008, the regular 2-year carryback period will apply to an NOL incurred in 2009.
- The amount of any NOL that is carried back to the fifth prior taxable year may not exceed 50% of the taxpayer's taxable income for such prior year. No such limitation applies to NOLs carried back to any other prior taxable years. For example, if a corporation makes an election for the 2008 taxable year to carry back an NOL for 5 years, the NOL may only be used to offset 50% of the corporation's income for 2003, but no such limitation applies to any amount carried back to 2004 through 2007.
- This special election is not available to any taxpayer that received, or is a member of an affiliated group with a member that received, funds from the federal government (*i.e.*, TARP funds) pursuant to the Emergency Economic Stabilization Act of 2008 prior to the enactment of the Act.

Earlier this year, as part of the American Recovery and Reinvestment Act of 2009 (the "Stimulus Bill"), certain small businesses were provided a limited election to carry back an NOL for up to 5 years to the extent that the NOL was incurred in any taxable year generally ending in 2008. With respect to any small business that previously made the election provided in the Stimulus Bill, such business may also make a new election for the 2009 taxable year (*i.e.*, the taxpayer is not limited to making the election only for one taxable year). Additionally, the 50% income limitation described above does not apply to the election made under the Stimulus Bill, but would apply to an election made under the Act.

Suspension of Alternative Minimum Tax Deduction Limitation

For taxpayers that are subject to the alternative minimum tax (AMT), this new election can be particularly significant. For purposes of calculating the AMT, a taxpayer generally may deduct its NOLs from its alternative minimum taxable income (AMTI). However, a taxpayer is disallowed a deduction for NOLs to the extent such deduction reduces the taxpayer's AMTI by more than 90%. Pursuant to the Act, if the taxpayer makes an election with respect to an NOL incurred in 2008 or 2009, this 90% AMT limitation is not applicable to the years in which the NOL is carried back.

Given the irrevocable nature of the election, taxpayers are urged to consult with their tax advisers prior to making an election under the Act. The IRS will be releasing guidance regarding this election in the near future.

If you have any questions or would like additional information about this new election, please contact the Haynes and Boone, LLP **Tax** practice group or one of the attorneys identified below.

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