Office of Chief Counsel
Internal Revenue Service
Memorandum

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to:

(LB&I Team 1544)

from: Paul Colleran
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subject: Extended Five-Year Carryback of Net Operating Losses from Operations

This memorandum responds to your request for assistance. This advice may not be used or cited as precedent.

LEGEND

ISSUES

Whether the taxpayer is eligible to claim an extended five year net operating loss carryback from its taxable year ended under the provisions of I.R.C. § 172(b)(1)(H).

CONCLUSIONS

The taxpayer is not eligible to claim an extended five year net operating loss carryback from its taxable year ended , under the provisions of I.R.C. § 172(b)(1)(H) since it is the successor under § 381 of the Internal Revenue Code to a taxpayer that received monies from the US Treasury for its preferred stock and warrants under the Troubled Asset Relief Program.

FACTS[1]

The following facts are those found by the examination team. Any additions to or changes in these facts could affect the conclusions set forth below under "Law and Analysis"

(Taxpayer) is the common parent of an affiliated group of corporations which files a consolidated return. Taxpayer is

. . Taxpayer is wholly owned by which in turn is wholly owned by .

On , acquired all the outstanding common shares of , a for $. was a in the and the parent of an affiliated group of corporations filing a consolidated return. At , had approximately $ in total assets and . operated , which conducted in .

formed a wholly owned corporation, for the purpose of the acquisition. merged with and into , with as the survivor. At the conclusion of the merger, owned all the shares of and all of businesses and obligations.

Each outstanding share of common stock was converted into and became exchangeable for shares of (with cash in lieu of any fractional shares) or $ in cash. After the closing of the merger, the shares of common stock, which had traded under the symbol " " on the , ceased trading and were delisted.

had received $ for its preferred stock with warrants from the US Treasury on under the Troubled Asset Relief Program (TARP), which was established under the Emergency Economic Stabilization Act of 2008 (EESA), Pub. L. No. 110-343, 122 Stat. 3765 (2008), codified at 12 U.S.C. §§ 5201 *et*

[1] Our understanding of the facts of this case is limited to the information that you have provided us unless otherwise stated. We have not undertaken any independent investigation of the facts of this case. If the facts known to us are incorrect or incomplete in any material respect, you should not rely on this advice, but instead you should contact our office immediately.

seq. As part of the acquisition, acquired the US Treasury's preferred stock and the associated warrants in for $.

acquisition of is a reverse subsidiary cash merger treated as a stock purchase. did not make a § 338 election for . Section 338 provides generally that a purchasing corporation may make an election to treat a stock acquisition as an asset purchase.

On , immediately following the acquisition of by , merged with and into the Taxpayer. The shares of were cancelled and its subsidiaries became affiliates of the consolidated group.

The plan of merger of and provides that was merged with and into . The separate corporate existence of ceased and was the surviving entity and continued its existence as a corporation under the laws of the . The merger of with and into is a statutory merger pursuant to § 368(a)(1)(A).

filed Articles of Merger on with the , Secretary of State. The articles of merger provide that is the surviving corporation in the merger with .

On , filed a Form 8-K, Current Report with the United States Securities and Exchange Commission on behalf of . The report notified the SEC of the merger. filed this report as "

"

On or about , Taxpayer filed a Form 1120 consolidated income tax return for the tax year ended , reporting a net operating loss (NOL) of $. This consolidated income tax return included the former and its subsidiaries. The Taxpayer did not attach a statement to its income tax return for the tax year ended , stating that it was electing the extended carryback under § 172(b)(1)(H).

On or about , Taxpayer filed Form 1139, Corporation Application for Tentative Refund applying for a quick refund of taxes from the tentative carryback adjustment of taxes from prior taxable years from the NOL carryback from the tax year ended . On the Form 1139, Taxpayer tentatively carried back $ of the NOL to its 5th preceding tax year ended reporting a decrease in tax of $ and $ of the NOL to its 4th preceding tax year ended reporting a decrease in tax of $

. The following statement is attached to the Form 1139 that the Taxpayer filed on or about :

> The net operating loss incurred in year ended is carried back five taxable years to year ended and four taxable years to year ended per IRC §172(b)(1)(H).

On or about , Taxpayer filed a second Form 1139, Corporation Application for Tentative Refund applying for a quick refund of taxes from the tentative carryback adjustment of taxes from prior taxable years from the NOL carryback from the tax year ended . On this Form 1139, Taxpayer tentatively carried back $ of the NOL to its 5th preceding tax year ended reporting a decrease in tax of $ and $ of the NOL to its 4th preceding tax year ended reporting a decrease in tax of $. The second Form 1139 made a correction to the 50 percent limitation under § 172(b)(1)(H)(iv). The following statement is attached to the Form 1139 that the Taxpayer filed on or about :

> The net operating loss incurred in year ended is carried back five taxable years to year ended and four taxable years to year ended per IRC § 172(b)(1)(H).
>
> The taxpayer is not a TARP recipient. The taxpayer acquired on . issued preferred stock to the Treasury in exchange for TARP money. Prior to acquisition of , purchased preferred stock in its entirety from the Treasury.

On or about the Internal Revenue Service issued the Taxpayer a tentative refund and credits against other tax liabilities of $ pursuant to the Forms 1139 tentatively carrying back the NOL from its taxable year ended to its taxable years ended and .

On or about , the Taxpayer filed Form 1120X, Amended US Corporation Income Tax Return for the year ended to include additional dividend income of $.

On or about , the Taxpayer filed a third Form 1139 to adjust for the dividend income, to account for an adjustment from an Internal Revenue Service Exam which reduced the taxable income for the year ended , and to make a correction for . On this Form 1139, Taxpayer tentatively carried back $ of the NOL to its 5th preceding tax year ended reporting a decrease in tax of $, compared to the refund already received, and $ of the NOL to its 4th preceding tax year ended

reporting a decrease in tax of $. The Taxpayer attached the exact same IRC § 172(b)(1)(H) statement as was included with the second Form 1139.

On or about , the Internal Revenue Service issued the Taxpayer an additional tentative refund of $ pursuant to the Form 1139 tentatively carrying back the NOL from its taxable year ended to its taxable years ended and .

LAW AND ANALYSIS

Section 172(c) provides that a taxpayer's net operating loss (NOL) is the excess of its deductions allowed by Chapter 1 of the Internal Revenue Code over its gross income.

Once a taxpayer determines the amount of its NOL, the NOL may be carried back or carried over in accordance with the rules of § 172(b). The amount carried back or carried over to a taxable year results in an NOL deduction in the year of the carryback or carryover.

Sections 172(b)(1) and (2) require, generally that an NOL for any taxable year be carried back to each of the 2 previous taxable years, and to the extent still available, carried forward to each of the 20 taxable years following the taxable year of the loss.

Section 13 of the Worker, Homeownership, and Business Assistance Act of 2009, Pub. L. No. 111-92, 123 Stat. 2984 (November 6, 2009) (WHBAA) amends §§ 172(b)(1)(H) and 810(b) to allow taxpayers to elect to carry back an applicable net operating loss for a period of 3, 4, or 5 years, in lieu of the 2-year period provided by § 172(b)(1)(A)(i).

Section 172(b)(1)(H)(ii) provides that the term "applicable net operating loss" (applicable NOL) means the taxpayer's net operating loss for a taxable year ending after December 31, 2007, and beginning before January 1, 2010.

Section 172(b)(1)(H)(iii) provides in general that the extended 5-Year carryback of applicable NOLs may be made only with respect to 1 taxable year.

Section 172(b)(1)(H)(iii)(II) provides that an election[2] for the extended 5-Year carryback shall be made in such manner as may be prescribed by the Secretary and shall be made by the due date (including extensions of time) for filing the return for the taxpayer's last taxable year beginning in 2009. The election, once made is irrevocable and, in general, may be made only with respect to one taxable year.

[2] The common parent of an affiliated group of corporations filing a consolidated return makes the election which is binding on all members of the group.

Section 172(b)(1)(H)(iv)(I) provides that an election to carry a 2008 or 2009 applicable NOL back to the fifth prior year is limited to 50% of the taxpayer's income (computed without regard to the NOL for the loss year or any taxable year thereafter) in that earlier year. Any unused portion of the NOL carryback in excess of the 50% limitation applicable to the fifth preceding year is then carried without limitation to the fourth preceding taxable year. See Notice 2010-58, 2010-37 I.R.B. 326 (discussing extended carryback of NOLs) and Revenue Procedure 2009-52 (providing guidance on the procedures for making the extended carryback of NOLs).

Section 1502 provides that the Secretary shall prescribe such regulations as he may deem necessary in order that the tax liability of any affiliated group of corporations making a consolidated return and of each corporation in the group, both during and after the period of affiliation, may be returned, determined, computed, assessed, collected, and adjusted, in such manner as clearly to reflect the income tax liability and the various factors necessary for the determination of such liability, and in order to prevent avoidance of such tax liability. In carrying out the preceding sentence, the Secretary may prescribe rules that are different from the provisions of Chapter 1 that would apply if such corporations filed separate returns.

Treas. Reg. § 1.1502-21(b) provides that losses taken into account in determining a consolidated NOL (CNOL) may be carried to other taxable years (whether consolidated or separate) only under paragraph (b) of Treas. Reg. § 1.1502-21.

A CNOL represents the aggregate of each member of the affiliated group's activities. Treas. Reg. § 1.1502-21(a). When a group carries back a CNOL, it must determine whether portions of the CNOL are attributable to members that are required to carry their portion of the CNOL back to a period before joining the group which may be subject to separate return limitation year (SRLY) provisions of Treas. Reg. § 1.15021(c), as modified by Treas. Reg. § 1.1503(d)-4 and § 382 restrictions.

Treas. Reg. § 1.1502-21(b)(1) provides that net operating loss carryovers and carrybacks to a taxable year are determined under the principles of § 172 and Treas. Reg. § 1.1502-21.

Treas. Reg. § 1.1502-21T(b)(3)(v)(A)(1) provides that a consolidated group can elect an extended carryback period pursuant to § 172(b)(1)(H) with regard to a CNOL arising in a taxable year ending after December 31, 2007, and beginning before January 1, 2010.

Rev. Proc. 2009-52, 2009-49 I.R.B. 744, provides when and how a taxpayer may make an election under § 172(b)(1)(H). Section 4.01(2) of Rev. Proc. 2009-52 provides that the common parent of a consolidated group makes the election for the group. Sections 4.01(3) and 4.01(4) of Rev. Proc. 2009-52 permit the election to be made for consolidated taxpayers by attaching a statement to the original or amended consolidated return for the taxable year of the applicable CNOL, by attaching a statement to the taxpayer's amended consolidated return applying the applicable CNOL

to the carryback year, or by attaching a statement to a claim for a tentative carryback adjustment on Form 1139. Sections 4.01(3)(b) and 4.01(4)(b) of Rev. Proc. 2009-52 require the election, regardless of the manner in which made, to be filed no later than the due date (including extensions) for filing the return for the taxpayer's last taxable year beginning in 2009.

Section 6411 provides a special procedure for prompt refund of tax relating to NOLs. The procedure allows a taxpayer to apply for a quick refund based on a tentative carryback adjustment. An application for a tentative carryback adjustment does not constitute a claim for credit or refund within the meaning of § 6511. Section 6411(a); Treas. Reg. § 1.6411-1(b)(2). Where the tentative carryback adjustment results in a tax refund, such tax refund is a “rebate” under section 6211(b)(2). Pesch v. Commissioner, 78 T.C. 100, 109-112 (1982).

Section 6501(k) provides that when an NOL is carried back on Form 1139, Corporation Application for Tentative Refund, the limitation period for assessment is determined by reference to the limitation period for the year of the loss. See also Treas. Reg. § 301.6501(m)-1. The deficiency to be assessed may be attributed to general adjustments to the carryback year as well as the carryback itself. See IRM 4.11.11.5. The amount of the deficiency that may be assessed is limited to the amount of the tentative allowance received by the taxpayer. The portion of the deficiency attributable to the carryback is assessed first.

Section 13(f) of the WHBAA provides an exception for the extended carryback for certain taxpayers, including TARP recipients. The extended carryback provision under § 172(b)(1)(H) does not apply to:

> (1) any taxpayer if (a) the Federal government acquired or acquires at any time an equity interest in the taxpayer pursuant to the Emergency Economic Stabilization Act of 2008, Pub. L. No. 110-43, or (b) the Federal government acquired or acquires, at any time, any warrant (or other right) to acquire any equity interest with respect to the taxpayer pursuant to such act (TARP recipients);
>
> (2) the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation; and
>
> (3) any taxpayer which at any time in 2008 or 2009 was or is a member of the same affiliated group (as defined in § 1504 without regard to subsection (b) thereof) as a taxpayer described in paragraphs (1) or (2).

WHBAA § 13(f).

The Explanation of the Staff of the Joint Committee on Taxation (Blue Book) contains an example of a taxpayer with an NOL in 2008 that in 2009 joins an affiliated group with

a member in which the Federal government acquired an equity interest pursuant to the Emergency Economic Stabilization Act of 2008. The Blue Book concludes that the taxpayer may not utilize the extended carryback rules under § 172(b)(1)(H) with regard to the 2008 NOL. Further, the taxpayer is required to amend prior filings to reflect the amended carryback period. Staff of the Joint Committee on Taxation, Technical Explanation of Certain Revenue Provisions of the Worker, Homeownership, and Business Assistance Act of 2009, JCX-44-09. See also, 155 Cong. Rec. S 11197, Comment of Senate Finance Committee Chairman Baucus that the Joint Committee on Taxation technical explanation of the WHBAA expresses the Senate Finance Committee's understanding and legislation intent behind the legislation.

In 1954 Congress enacted § 381 which provides a set of rules for the carryover of tax attributes in certain corporate acquisitions. Section 381(a) list the types of acquisitions governed by the section, while § 381(c) contains a list of non-exclusive items of the transferor corporation that the acquiring corporation succeeds to and takes into account.

Section § 381(a) describes the acquisitions to which § 381(c) applies and includes statutory mergers under § 368(a)(1)(A) such as the merger of with and into the Taxpayer. Under § 381(b)(3) any loss of the acquiring corporation may be carried back to its prior years, but not to a taxable year of the transferor corporation.

Treas. Reg. § 1.1502–1(f)(4)(i) defines "successor" as the transferee or distributee of assets in a transaction to which § 381(a) applies.

acquisition of is a reverse subsidiary cash merger. See, Rev. Rul. 90-95, 1990-2 C.B. 67. did not make a § 338 election for . Consequently, the second merger of into Taxpayer is a tax free merger. Treas. Reg. § 1.338-3(d).

Tax attributes carry over to the successor corporation in situations where the reorganization is in the form of a statutory merger. Helvering v. Metropolitan Edison Co., 306 U.S. 522 (1939). In Metropolitan Edison, the court noted that in a statutory merger the corporate personality of the transferor is drowned in that of the transferee. Id. at 529. See also, Dover v Commissioner, 122 T.C. 324, 349 (2004) ("The crucial finding in all of the rulings discussed [above] is that, in any corporate amalgamation involving the attribute carryover rules of section 381, the surviving or recipient corporation is viewed as if it had always conducted the business of the formerly separate corporation(s) whose assets are acquired by the surviving corporation.") Here, is the successor corporation in the statutory merger with and succeeds to the tax attributes of .

is a TARP recipient by reason of it receiving $ million for its preferred stock with warrants from the US Treasury on under TARP. As a TARP recipient, is not eligible for the extended NOL carryback under §172(b)(1)(H).

§ 13(f) of the WHBAA. As a result of the statutory merger of with and into the Taxpayer, the Taxpayer is a successor to . As the successor to , Taxpayer steps into the shoes of and assumes its tax attributes. One of these inherited tax attributes is status as a TARP recipient.

As the successor to a TARP recipient, succeeds to the characterization as a TARP recipient and is therefore not eligible for the extended NOL carryback under § 172(b)(1)(H).

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call (617) 788-0804 if you have any further questions.

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