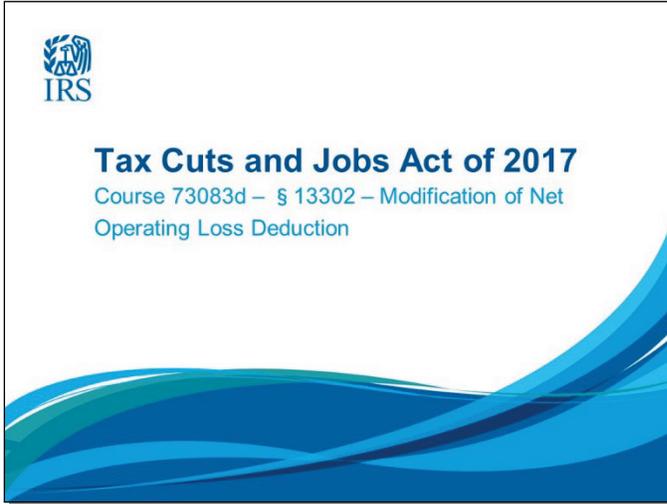


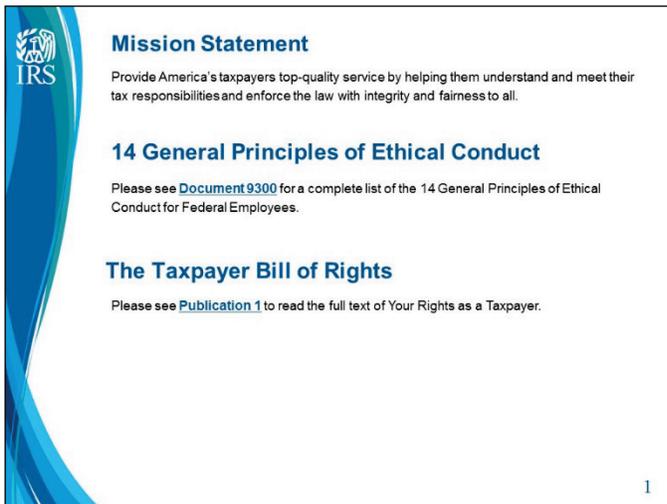
Tax Cuts and Jobs Act (TCJA)

Modification of Net Operating Loss Deduction

Slide 1 – Tax Cuts and Jobs Act of 2017



Slide 1 – Mission Statement, 14 General Principles of Ethical Conduct, The Taxpayer Bill of Rights



Slide 2 – Objectives



Objectives

At the end of this lesson you will be able to:

- Explain the Changes to the Net Operating Loss Deduction rules relating to TCJA
- Identify the Effective Dates
- Identify the Exceptions to the New Rules
- Compute a Net Operating Loss Deduction

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Slide 3 – Abbreviation Definitions



Abbreviation Definitions

- NOL – Net Operating Loss
- NOL year – Year of the Loss
- NOLD – Net Operating Loss Deduction
- NOL Carryback – The NOL that is carried to a prior year
- NOL Carryforward – The NOL that is carried to a subsequent year

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Slide 4 – Comparison of Old and New Law



Comparison of Old and New Law

Pre-TCJA (December 31, 2017)	TCJA
NOL is the amount by which a taxpayer's business deductions exceed its gross income [IRC § 172(c)]	No change
An NOL could be carried back two years and carried over 20 years to offset taxable income in those years [Former IRC § 172(b)(1)].	No carryback allowed for most taxpayers, most taxpayers must carry forward indefinitely.
NOLs offset taxable income in the order of the taxable years to which the NOL may be carried [IRC § 172(b)(2)].	No change

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Slide 5 – Comparison of Old and New Law Continued



Comparison of Old and New Law Continued

Pre-TCJA – December 31, 2017	TCJA
Different carryback periods applied with respect to NOLs arising in different circumstances. [Former IRC § 172(b)(1)(C)(E)].	Two exceptions – farming losses and nonlife insurance companies
Taxable income limitation - none	80% taxable income limitation

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Slide 6 – Section 13302 Modification of Net Operating Loss Deduction



**Section 13302
Modifications of Net Operating Loss Deduction**

IRC § 172 Changes:

- 80% Taxable income limitation (with only one exception)
- Carrybacks are eliminated, but carryforwards are allowed indefinitely - exceptions apply to:
 - Farming businesses – NOLs carried back 2 years/carried forward indefinitely
 - Non-life insurance companies – NOLs carried back 2 years/carried forward 20 years

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Slide 7 – Section 13302 Modifications of Net Operating Loss Deduction – Effective Dates



**Section 13302
Modifications of Net Operating Loss Deduction - Effective Dates**

- 80% Taxable income limitation
 - Taxable Years **beginning** after 12/31/2017
- Elimination of carrybacks for most taxpayers
 - Taxable years **ending** after 12/31/2017

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Slide 10 – Step 1 Determine if the Taxpayer has an NOL Corporations

Step 1 Determine if the Taxpayer has an NOL - Corporations
RGS Special Application

§ 172(d) MODIFICATIONS FOR TAXABLE LOSSES

- Net Operating Loss Deduction
- Deduction for income attributable to domestic production activities (§ 199)
- Adjustment to Dividend Received Deduction per IRC § 246(b)

TAXABLE INCOME (LOSS) BEFORE § 172(b)(2) MODIFICATIONS

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Slide 11 – Step 2 Determine whether the loss may be carried back or whether it must be carried forward. Determine the Carryover year.

Step 2 – Determine whether the loss may be carried back or whether it must be carried forward. Determine the Carryover year.

- For NOLs not affected by TCJA (NOLs for periods ending 12/31/2017 and prior – usually could carry back 2 years)
- If a Taxpayer does not want to carry back the loss, the Taxpayer must make a timely irrevocable election to forego the carryback.
- For NOLs affected by TCJA, most taxpayers can only carry forward, except farming and nonlife insurance losses.

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Slide 12 – Step 3 Compute taxable income for the Carryover year



Step 3 – Compute taxable income for the Carryover year

- If there is a carryback, the taxable income can be recomputed:
 - For Individuals: On Form 1045 or 1040X
 - For Corporations: On Form 1139 or 1120X
- If there is a carryforward from a prior year, the NOLD can be included in the “other income” line for the 1040. (Schedule 1 starting in 2018)
- Some forms such as the Form 1120 have a special line for the NOLD.

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Slide 13– Step 3 Compute taxable income for the Carryover year - Continued



Step 3 – Compute taxable income for the Carryover year - Continued

Example 1

Taxpayer A has an NOL for 2017 of \$100,000 and carries the NOL to 2015 where the taxable income is \$50,000.

The taxpayer might apply only \$50,000 to 2015, because it appears that would be the amount absorbed. It may be the case that \$50,000 is absorbed, and \$50,000 is carried over to the next year, but the proper way to carryback the loss is to carryback the entire loss and go through the process to determine how much of the loss is absorbed.

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Slide 14 – Step 3 Compute taxable income for the Carryover year - Continued



Step 3 – Compute taxable income for the Carryover year - Continued

Example 2

Taxpayer B has an NOL carryover from 2015 to 2016 of 60,000. The taxable income in 2016 computed without any NOLD is \$100,000. Computed with the 2015 NOLD, the taxable income is \$40,000. The taxpayer has a farming NOL carryback from 2018 to 2016 of \$200,000.

The farming loss is limited to 80% taxable income computed without any NOLD (80% \$100,000 is \$80,000). Assuming the taxpayer does not elect to waive the carryback, the NOL carryback is \$80,000, even though the taxable income in 2016 prior to the carryback is only \$40,000. The taxpayer should then go to step 4 to determine how much of that \$80,000 is absorbed.

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Slide 15 – Step 4 Determine the Amount of the NOL absorbed – the rest is carried to the next year



Step 4 – Determine the Amount of the NOL absorbed – the rest is carried to the next year

- The amount that is not absorbed is the NOL less MODIFIED taxable income.
- The amount of the NOL absorbed can be computed on Schedule B of Form 1045 for individuals.
- For corporations, the modifications are:
 - Net Operating Loss Deduction
 - Section 199 deduction
 - Deduction for foreign derived intangible income
 - Charitable contributions are refigured without considering any NOL Carryback

IRC § 172(b)(2)(C)

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**Slide 16 – New Provision for 2018
Taxable Income Limitation of 80%**



**New Provision for 2018
Taxable Income Limitation of 80%**

The new provision limits the NOL deduction for a tax year to 80% of taxable income. It provides that the NOLD is the **lesser of**:

- The aggregate of the net operating loss carryovers to such year, plus the net operating loss carrybacks to such year, or
- 80 % of taxable income computed without regard to the deduction allowable under this section (IRC § 172(a)).

Transition rule: This provision is for net operating losses **arising** in taxable years **beginning** after 12/31/2017, so prior year losses carried forward are not subject to this 80% limitation. This limitation also does not apply to a 12 month fiscal year ended before 12/31/2018.

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Slide 17 – New Provision for 2018 - Taxable Income Limitation of 80%



**New Provision for 2018 - Taxable Income
Limitation of 80%**

Example 3

Taxpayer C has a 2018 farming NOL carryback to 2016 of 150,000. There are no other NOLs for 2016. The taxable income for 2016 before the NOLD from 2018 is \$100,000. The NOLD carryback is limited to \$80,000.

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Slide 18 – New Provision for 2018 2018 - Taxable Income Limitation of 80%



New Provision for 2018 - Taxable Income Limitation of 80%

Example 4

Assume the same facts as Example 3, except that Taxpayer C's taxable income included an NOLD from 2015 of \$20,000. The 80% limitation has to be computed without the 2015 NOLD. So, the 2016 taxable income for the purposes of this computation is \$120,000, if there are no other items on the return that are affected by the increase in AGI or taxable income. If there are amounts such as medical or contributions, the computation can be more involved.

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Slide 19 – New Provision for 2018 2018 - Taxable Income Limitation of 80%



New Provision for 2018 -80% Taxable Income Limitation

Under TCJA, most taxpayers can only carry the NOL forward.

Example 5

Taxpayer D has a \$90,000 NOL in 2018 which must be carried forward to 2019. The taxpayer completes his 2019 tax return without the NOLD and arrives at a taxable income of \$100,000. So, the NOLD for 2019 is limited to 80% or \$80,000. Now the taxpayer includes the \$80,000 in the "other income" line of Schedule 1. This will result in a reduction in AGI, which can affect other amounts (such as medical, charitable contributions, and amounts that are limited by modified AGI such as IRA, credits, and the special \$25,000 allowance on a rental).

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Slide 20 – New Provision for 2018 – Introduction to Exceptions



New Provision for 2018 – Introduction to Exceptions

- The new provision provides that **generally**, NOLs can no longer be carried back but are allowed to be carried forward indefinitely.
- This provision applies to NOLs arising in years ended **after** 12/31/2017, so it could apply to some fiscal years ended before 12/31/2018 (IRC § 172(b)(1)(A)).

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Slide 21 – New Provision Exception #1 Farming Loss



New Provision – Exception #1 Farming Loss

The definition of a *farming loss* remains unchanged:

- For this purpose, "farming loss" is defined as the lesser of:
 - The amount that would be the NOL for the tax year if only income and deductions attributable to farming businesses (as defined in IRC § 263A(e)(4)) are taken into account, or
 - The amount of the NOL for the tax year.
 - IRC § 172(172(b)(1)(B)(ii) (former IRC § 172(h)(1))

For any portion of an NOL for a tax year that is a farming loss, the loss is allowed a two-year carryback.
(IRC § 172(b)(1)(B)(i) removing the five-year carryback rule)

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Slide 22 – Example 6 – Farming



Example 6 - Farming

Taxpayer E files a tax return for 2016 reflecting taxable income of \$20,000 shown as follows:

Income From Farming	75,429
NOL Carryover from prior years	(40,000)
Deductible portion of SE tax	<u>(5,329)</u>
AGI	30,100
Standard deductions/exemptions	<u>(10,100)</u>
Taxable Income	<u>20,000</u>

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Slide 23 – Example 6 – Farming Continued



Example 6 – Farming Continued

Taxpayer E incurs a \$50,000 net operating loss in 2018 all of which is attributable to farming.

The amount of the 2018 net operating loss deduction for 2016 is the lesser of the amount of the loss (\$50,000) or 80 percent of \$60,000 (\$48,000). Therefore, the amount of the 2018 net operating loss that is deductible for 2016 is \$48,000.

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Slide 24 – Example 6 – Farming Continued



Example 6 – Farming Continued

Since the taxable income before the carryback is \$20,000, and the only modification on Schedule B is exemptions, the carryforward to 2017 would be as follows:

NOLD from 2018	48,000
Less Modified 2016 taxable income (\$20,000 taxable income + \$4,050 exemptions)	(24,050)
NOLD not absorbed in 2016	23,950
NOLD not used due to 80% limitation (\$50,000 NOLD less \$48,000)	2,000
NOL carried to 2017	25,950

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Slide 25 – New Provision – Exception #2 Nonlife Insurance Companies



New Provision – Exception #2 Nonlife Insurance Companies

As defined by IRC § 816(a)

- Such as Casualty and Property Insurance Companies
 - Continue to be subject to 2-year carryback,
 - 20-year carryforward rules, and
 - The 80% limitation does not apply
 - IRC § 172(b)(1)(C) and 172(f).

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Slide 26 – Example 7



Example 7

A MFJ Calendar-Year Taxpayer with Taxable income (loss) of (computed without any NOL carryover) is as follows:

- \$400,000 in Year A,
- \$100,000 in Year B
- (\$500,000) in Year C
- \$100,000 in Year D

Prior Law:
If year C is the year ended 12/31/2017, the taxpayer would be able to carry the NOL back to Year A, and assuming it is not absorbed, carry the remainder to Year B.

Current Law:
If year C is the year ended 12/31/2018 and the loss is not from farming or a nonlife insurance company, the NOL can only be carried forward to year D. The NOLD would be limited to \$80,000 (80% of \$100,000).

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Slide 27 – Summary



Summary

A business may have a net operating loss if its deductions for the year are more than its business income. TCJA limits the NOL deduction to 80 percent of taxable income for the year rather than allowing the loss to offset 100 percent of taxable income.

Most businesses can no longer carry back their NOLs to the prior two tax years as was allowed under prior law. Now, a business may carry forward an NOL indefinitely, rather than expiring after 20 years as was the case under prior law.

Farms and non-life insurance companies still have the option to carry back NOLs. Non-life insurance companies are not subject to the 80% limit.

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Slide 28 – Objectives



Objectives

You are now able to:

- Explain the Changes to the Net Operating Loss Deduction rules relating to TCJA
- Identify the Effective Dates
- Identify the Exceptions to the New Rules
- Compute a Net Operating Loss Deduction

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