Everything You Want to Know about Loss Carrybacks

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Speaking with you today

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Overview

Refresher of Basic Rules

• Carryback periods
• Exceptions to basic rules
• Procedural matters
• Considerations

Hypotheticals
**Carryback period – general rule**

**NOL** incurred by a corporate taxpayer can be **carried back 2 years and carried forward 20 years**. §172(b)

NOL incurred in 2015 can be carried back to 2014 and 2013 and/or carried forward to 2035. The 2015 NOL will **not** be available to offset taxable income in 2036.

**Capital losses** incurred by corporate taxpayer can be **carried back 3 years and carried forward 5 years**. §1212(a)

Need to consider short-period tax years. §1.172-4(a)(2)
**Carryback period – exceptions**

Specified liability loss (10 years) §172(b)(1)(C)
Federally declared disaster loss (5 years) §172(b)(1)(J)
Bad debt of commercial bank (10 years) §172(b)(1)(D)
§382 RBILs (not carryback) §382(h)(4)
CERT interest loss §172(b)(1)(E)
REITs and regulated investment companies (various)
Small business loss or farming loss (various)
Capital loss carryback cannot create an NOL §1212(a)(1)(A)(ii)
Foreign expropriation loss (no carryback allowed) §1212(a)(1)(A)(i)
Other special rules
NOL carryback – waiver election

NOL carryback is **automatic unless an election is made** to forego the carryback §172(b)(3)

- Annual election
- Irrevocable
- Applicable losses

How to make the election

- Question on Form 1120, Schedule Schedule K
- Whitepaper statement for consolidated returns
- §301.9100-2 statement within 6 months of filing return
**Carryback claim – Procedural matters**

Forms to file

- **Form 1139** Corporation Application for Tentative Refund Claim (within 12 months, but after tax return filed)
- **Form 1120X** Amended U.S. Corporate Income Tax Return (after 12 months)

Ordering rule – carryback to most recent tax year first

State tax filings may also be impacted by carryback
Recalculate taxable income and tax due (including AMT)

- New taxable income now includes the tax loss carryback deduction
- Re-calculate income and deduction items that are impacted by taxable income
- Tax credits allowed to be claimed are recalculated
- US versus foreign sourcing of some items may change also

Complications often arise when recalculating taxable income!
Statute of Limitation Considerations

General rule – if statute remains open for year of loss, able to file a carryback claim.

- Generally 3 year statute of limitation, unless extended
- Certain losses have a longer statute of limitation (e.g., bad debt losses, worthless stock losses)

§6511 contains detailed rules (lots of nuances)

Filing a refund claim near the close of statute does not extend the statute.
**IRS Exam and Joint Committee Considerations**

Tentative refund claims

- IRS must **process within 90 days**
- **Interest accrues** on refund amount **after 45 days**

**IRS review and approval of all refund claims** – tentative refund claims and amended returns

- May occur after refund processed for tentative refund claim
- Will always occur before refund processed for amended return

**JCT review required for any refunds in excess of $5 million** for C-corporations (in excess of $2 million for all other taxpayers)

Can litigate if refund claim on amended return denied and statute is expired
Interest and Penalty Considerations

No interest accruable for tax loss carryback claims.

Underpayments – if you have a carryback that eliminates a previous deficiency, but interest was accruing on that previous year, when does the interest stop accruing? Do you still owe the interest?

See Saltzman 6.02[1][d]. et.seq.

Interest on Overpayments Created by Carrybacks – see Saltzman 6.03[1][b]

Special Negligence Penalty Rules – Treas. Reg. §1.6662-3(d)

Erroneous Claim for Refund or Credit - §6676
Issues to Consider

Considerations for each carryback claim should include the following:

- Form to use
- Timing issues
- JCT involvement in refund
- Statute of limitations implications
- IRS exam implications
- Prior year transactions that could impact carryback claim
- Impact on total cash tax liability
- Others?
Hypothetical #1

Taxpayer incurs an NOL in 2015 but has not yet filed its tax return. Taxpayer would like to carryback the NOL to 2014 and 2013.

What procedural and IRS considerations come to mind?
Any other factors to consider?
**Hypothetical #2**

Taxpayer incurs a capital loss in 2015. Taxpayer incurred a capital gain in 2014 that is available to offset the capital loss incurred in 2015. Tax year 2013 was not audited. Taxpayer filed its 2015 tax return in April 2016. The 3 year statute of limitation for filing an amended return is about to expire.

What procedural and IRS considerations come to mind?  
Any other factors to consider?
**Hypothetical #3**

Same facts as Hypothetical #2 except that 2013 was audited and the statute was extended 12 months. The exam is complete. In preparing the carryback claim, Taxpayer discovers an error in 2013 that reduces taxable income in 2013.

**What procedural and IRS considerations come to mind?**

**Any other factors to consider?**
**Hypothetical #4**

Taxpayer incurs an NOL in 2015. In 2014, Taxpayer was spun-off and became a stand-alone consolidated return filing group. Taxable income from 2014 is not sufficient to absorb the NOL carryback. Taxpayer benefited from FTCs, General Business Credits, and an AMT credit in 2014.

**What procedural and IRS considerations come to mind?**

**Any other factors to consider?**

What if taxpayer were bought rather than spun-off?
Hypothetical #5

Taxpayer incurs an NOL in 2015, carries a portion of it back to 2014 and 2013 and is carrying the remainder forward. In 2017, Taxpayer determines that a portion of the NOL carryforward includes a specified liability loss.

What procedural and IRS considerations come to mind?
Any other factors to consider?
Hypothetical #6

Taxpayer carried back a capital loss generated in 2014 to the 2011 tax year by filing a Form 1120X. During the IRS examination of the carryback claim, the IRS determines that the Taxpayer did not have reasonable cause to claim the capital loss and assesses an erroneous refund claim penalty under §6676.

How should you handle?
Questions?
Shawn O'Brien is a Tax partner who represents clients in all types of tax disputes with taxing authorities on international, federal and state levels. He routinely advises clients on various tax issues during tax examinations, in administrative appeals and as an advocate in trial and appellate litigation before the US Tax Court, US District Courts and US Court of Federal Claims. Shawn's tax controversy and litigation experience spans a broad range of areas, including transfer pricing controversies, debt v. equity issues, international withholdings, advance pricing agreements, "tax shelter" disallowances, research and development tax credits, excise taxes, and changes in accounting methods.

Shawn advises foreign and domestic corporations, partnerships, MLPs, and LLCs seeking corporate and tax advice in connection with various types of foreign and domestic transactions, including 1031 exchanges, mergers and acquisitions, restructurings, divestitures, leveraged buyouts, structured financings, and oil and gas transactions. Shawn is a Certified Public Accountant (CPA) licensed in Louisiana.

Shawn is particularly focused on a variety of tax issues facing the energy industry including tax controversy, joint ventures, restructuring, acquisition and disposition of energy assets. He was recently selected to join the US Internal Revenue Service Advisory Council (IRSAC) and currently serves on its Large Business & International (LB&I) subcommittee. Shawn served as Chair of the Energy and Natural Resources Committee of the State Bar of Texas Tax Section from 2011 to 2013.

According to International Tax Review's "World Tax" 2014, Mayer Brown's Houston tax practice is "known for its sophisticated transactional tax and tax controversy work. Clients recognize the quality of its lawyers, many of whom have extensive backgrounds in the energy sector. The practice is strong in international tax, and advises both US and non-US multinationals on their energy investments. The practice is also strong in transfer pricing and controversy, and has represented clients in some of the biggest transfer pricing disputes filed in US courts. The Houston practice is led by Shawn O'Brien, who focuses on tax controversy."
Maria has 16 years of experience serving clients in the energy industry with domestic and international tax matters. She is a Tax Partner in the Houston office and a member of PwC’s Energy Practice. Maria is also a member of PwC’s Tax Accounting Services group.

Maria provides domestic and international tax advice and has experience working with a variety of companies in the energy industry: independent upstream companies, refiners, offshore drillers, oilfield service companies, integrated oil and gas companies, foreign-based companies investing in the U.S. energy market, MLPs, royalty trusts, private-equity funds with investments in oil and gas ventures, and utilities. Maria has also experience working with alternative energy companies (wind, geothermal, and biofuels). Maria’s technical experience includes managing federal, state and international compliance; foreign income tax creditability analyses; oil and gas partnership structuring and compliance; tax accounting methods; IRS audit defense and protest writing; international reorganizations; tax credit studies; capital cost recovery studies; and tax opinion drafting.

Throughout her career, Maria has also worked extensively with multinational companies on income tax accounting reviews and issues such as: deferred tax reconciliations and tax basis balance sheet preparation; assessment of income tax process function effectiveness; valuation allowance assessment methodologies; business combinations and carve-outs; and uncertain tax position tracking and assessment.

Maria serves on the Federal Tax Policy Committee and International Tax Policy Committee for the Texas Society of CPAs. Maria is a frequent contributor for the Recent Cases, Regulations and Rulings section of the Oil, Gas and Energy Quarterly. She has spoken to the Tax Executives Institute, the Texas Society of CPAs, the American Petroleum Institute, and other organizations on energy industry tax topics and income tax accounting topics.