

## POINTS TO REMEMBER

# Temporary Regulations on NOL Carrybacks for Taxpayers Filing Consolidated Returns

By Andrew Reiter\* and Michael G. Lapidus\*\*

On June 22, 2010, the Service issued temporary and final regulations (T.D. 9490; REG-151605-09) which provide guidance to consolidated groups and implement the extended net operating loss (NOL) carryback rules of section 172(b)(1)(H).

## Background

The Worker, Homeownership and Business Assistance Act of 2009 (the Act), signed into law on November 6, 2009, amended section 172(b)(1)(H) by allowing taxpayers to extend their NOL carryback up to three additional years (Extended Carryback Period) for an NOL arising in a single taxable year ending after December 31, 2007, and beginning before January 1, 2010 (Applicable NOL). The Service subsequently issued Revenue Procedure 2009-52, which establishes procedures for when and how to make the extended NOL election. Revenue Procedure 2009-52 does not apply to consolidated groups; the temporary regulations outline the procedures for when and how to make the extended election for a consolidated group and invoke application of Revenue Procedure 2009-52 to consolidated groups.

Section 172(b)(1) provides, in part, that an NOL for any taxable year must generally be carried back to each of the two years preceding the year of the loss. Section 172(b)(3) provides that any taxpayer entitled to a carryback period pursuant to section 172(b)(1) may elect to relinquish the carryback period with respect to a loss for any taxable year. The election to relinquish the carryback period, which is normally irrevocable, must be made by the due date (including extensions) of the taxpayer's return. A consolidated group may make this election for its entire consolidated net operating loss (CNOL). A consolidated

group may make a separate election, which is irrevocable, to waive, for all taxable years of the acquiring group, and solely for all CNOLs attributable to certain acquired members, the portion of the carryback period for which the acquired corporations were members of another group. This separate election must be made by the return due date (including extensions) of the acquiring group for the tax year of the acquisition.

## The Temporary Regulations

### Application of section 172(b)(1)(H) to a Consolidated Group

The temporary regulations provide that a consolidated group may elect to carry back a CNOL arising in a consolidated return year ending after December 31, 2007, or beginning before January 1, 2010, to the Extended Carryback Period. The temporary regulations provide that a group may revoke a prior election in order to make an election pursuant to section 172(b)(1)(H). If a member of the consolidated group makes a 172(b)(1)(H) election for an NOL arising in a separate return year, the election will not disqualify the group from making an election for a consolidated return year. Treas. Reg. § 1.1502-21T(b)(3)(v)(A)(1)-(3).

### Procedures for Electing the Extended Carryback Period

Revenue Procedure 2009-52 describes how any taxpayer that previously elected to forgo the carryback period for a loss arising in a taxable year ending before the enactment of the Act may revoke that

election in order to take advantage of the Extended Carryback Period. Revenue Procedure 2009-52 also permits a taxpayer that filed an election for a tentative carryback period using the two-year carryback for an Applicable NOL to claim the Extended Carryback Period. The taxpayer's disclosure statement must affirm that the taxpayer is a member in an affiliated group filing and that they file a consolidated return, an Applicable NOL includes a CNOL, and the section 172(b)(1)(H) election is made by the common parent of the group. Specifically, to make an election for the Extended Carryback Period for a consolidated group, the consolidated group must follow the procedures from section 4.01(3) of Revenue Procedure 2009-52. Accordingly, the taxpayer must:

1. Attach a statement to the tax return for the taxable year in which the NOL arose;
2. Include in the statement that the taxpayer is electing to apply the NOL rules under Revenue Procedure 2009-52;
3. Affirm that the taxpayer did not receive money under The Troubled Asset Relief Program (TARP) and was not an affiliate of a TARP recipient in 2008 or 2009; and
4. Specify the length of the carryback period that the taxpayer elects.

Limitations Imposed on an NOL Section 172(b)(1)(H)(iv) limits the NOL that can be used in the fifth taxable year preceding the year in which the NOL arose to 50% of the fifth year's taxable

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income. For consolidated groups, the 50% limitation is calculated based on the consolidated taxable income.

The temporary regulations also impose a limitation when a consolidated group absorbs an NOL extended to the fifth year of the Extended Carryback Period, even if the consolidated group has not made a section 172(b)(1)(H)(iv) election. The temporary regulations use the example of a loss where the Separate Return Limitation Year (SRLY) limitation of Regulation section 1.1502-21(c) would apply.

#### Election to Waive a Pre-Consolidation Prior NOL Election

The temporary regulations permit a consolidated group to revoke a prior election for NOLs that can be attributed to an acquired member. This allows a taxpayer to waive an election made under the previous carryback rules. The

carryback may be waived only for the years prior to the acquisition and only if the Regulation section 1.1502-21(b)(3)(ii)(B) election was filed.

Temporary Regulation section 1.1502-21T(b)(3)(ii)(C) allows a consolidated group two waiver options. Each option requires that (1) the acquiring group makes a section 172(b)(1)(H)(iv) election; and (2) a portion of the CNOL can be attributed to a member acquired from outside the group.

The first waiver allows a group to waive a portion of the Extended Carryback Period for the time which the acquired member was a member of another group. This waiver is available only if none of the Extended Carryback Period was used by the previous group. If part of the Extended Carryback Period was used by the previous group during the first or second carryback years, the

taxpayer may make an election using the second waiver. This election applies only to the third, fourth, and fifth carryback years. These elections to waive apply only to the NOLs for which the taxpayer makes a 172(b)(1)(H) election.

#### Conclusion

Consolidated groups must continue to be careful in analyzing and applying the extended NOL carryback rules. Among the issues that must be considered are the application of the SRLY limitation in Regulation section 1.1502-21(c), the Corporate Equity Reduction Transaction rule, and whether the NOL carryback is subject to a section 382 limitation (and if so, if the company was in a net unrealized built-in loss position at the time of the limitation). ■

## Limitation by Regulation: Heads the Service Wins, Tails the Taxpayer Loses?

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When an Internal Revenue Code section does not contain an express deadline, or contains a limitation period that is at least arguably ambiguous in scope, the Treasury Department may promulgate regulations to fill the gap. A couple of recent cases, *Lantz v. Commissioner*, 132 T.C. 131 (2009) (reviewed by the court), *rev'd and remanded*, 607 F.3d 479 (7th Cir. 2010), and *Intermountain Ins. Serv. of Vail, LLC v. Commissioner*, 134 T.C. No. 11 (2010), 2010 WL 1838297, provide an interesting contrast because, in one, the Treasury imposed a deadline on a taxpayer benefit, where none existed in the statute, and, in the other, the Treasury tried to expand the scope of an extended statute of limitations on assessment.

*Lantz* involved an ultimately successful attempt by the Treasury to impose a deadline. The plaintiff in *Lantz*, whose husband had been convicted of Medicare fraud, sought equitable innocent spouse relief under section 6015(f). The Service denied relief on the ground that she failed to satisfy Regulation section 1.6015-5(b)(1), which mandates that a spouse request relief within two years of the Service's first collection action. *Lantz*, 132 T.C. at 133.

A majority of the Tax Court judges sided with the taxpayer and invalidated the time limitation in the Treasury regulations. Unlike the two other forms of relief from joint and several liability in

sections 6015(b) and (c), section 6015(f) does not include a deadline. Relying on this statutory difference, the majority found that Congress did not intend for a limitation period to apply to section 6015(f): "We find that by explicitly creating a 2-year limitation in subsections (b) and (c) but not subsection (f), Congress has 'spoken' by its audible silence." *Id.* at 139. It concluded that the regulation was not entitled to deference. *Id.* The Service disagreed. It appealed to the Seventh Circuit, and also advised its attorneys to continue to argue that relief under section 6015(f) is unavailable if the taxpayer files outside

the two-year period. Notice CC-2009-012 (Apr. 17, 2009).

The Seventh Circuit agreed with the Service's position and upheld the regulations' provision of a two-year limitations period. *Lantz*, 607 F.3d 479 (7th Cir. 2010) (reversing and remanding to the Tax Court). Judge Posner wrote for the court, "[P]robably because [section 6015(f) is] a safety-valve provision for innocent spouses who fall through cracks in (b) or (c)," Congress left the details, including the deadline, up to the Treasury Department. *Id.* at 484. Judge Posner also took issue with the Tax Court's "audible silence" argument:

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