



IRS Provides Guidance on NOL Carryback and Section 163(J) Elections

By: Anna K. Derewenda

04.13.2020

In a flurry of guidance, the Internal Revenue Service (IRS) has issued Revenue Procedure 2020-22, Revenue Procedure 2020-24, and Notice 2020-26 providing guidance to taxpayers wanting to elect out of new net operating loss (NOL) carryback rules, to file tentative carryback adjustment applications and to make elections pursuant to Section 163(j).

Waiver of NOL Carryback Rules

Waiver of Five Year Carryback Period

The Coronavirus Aid, Relief, and Economic Security Act (CARES Act) provides that NOLs arising in 2018, 2019 and 2020 must be carried back to the five taxable years preceding the year of the NOL. Taxpayers are permitted to make an irrevocable election to waive the entire carryback period for an NOL for any taxable year. Revenue Procedure 2020-24 provides guidance on how to make the election.

A taxpayer that wants to elect to waive the carryback period for an NOL arising in 2018 or 2019 must make the election no later than the due date, including extensions, of the taxpayer's Federal income tax return for the first taxable year ending after March 27, 2020. For calendar year taxpayers, this will generally be the return for the 2020 year. The election is made by attaching to the return a separate statement for each year (2018 or 2019) that the taxpayer intends to make the election.

Exclusion of Section 965 Inclusion Years

For taxpayers with foreign operations that were impacted by the one-time transition tax under Section 965 of the Internal Revenue Code, the CARES Act provides that such taxpayers may irrevocably elect to exclude all Section 965 years from an NOL carryback period in lieu of waiving the entire period. The taxpayer would then look to the remaining years in the carryback period to determine whether it can receive a refund or credit. To the extent that the election is not made and an NOL is carried back to a year in which a taxpayer has a Section 965 inclusion, the taxpayer will be treated as if it made an election under Section 965(n) not to apply the NOL to the Section 965 amount. This deemed Section

965(n) election may not be waived.

A taxpayer that wants to elect to exclude all Section 965 years from a carryback period for an NOL arising in 2018 or 2019 must also make this election no later than the due date, including extensions, for filing the taxpayer's Federal income tax return for the first taxable year ending after March 27, 2020. For an NOL arising in the 2020 tax year, the election must be made no later than the due date, including extensions for filing the taxpayer's 2020 Federal income tax return. Taxpayers make the election by attaching a statement to whichever of the following is filed earliest after April 9, 2020:

- The Federal income tax return for the taxable year in which the NOL arises;
- The taxpayer's claim for a tentative carryback adjustment applying the NOL to a taxable year in the carryback period; or
- The amended Federal income tax return applying the NOL to the earliest taxable year in the carryback period that is not a Section 965 year.

A taxpayer who files an amended return to claim a refund or credit as a result of the NOL must attach a statement to each amended return stating that the taxpayer is making the election, the taxable year in which the NOL arose and the Section 965 years.

Applications for Tentative Carryback Adjustments under Section 6411(a)

General Provisions

Instead of filing an amended return, a taxpayer may file an application for a tentative carryback adjustment of tax for a prior year affected by an NOL carryback on an expedited basis under Section 6411(a). The application is completed by filing Form 1139, *Corporation Application for Tentative Refund*, or Form 1045, *Application for Tentative Refund*, for other taxpayers. Generally, the application must be filed on or after the filing date for the return for the year in which the NOL carryback results, but within a period of 12 months after that year. The Code provides 90 days for the IRS to review the application.

The CARES Act does not provide additional time to file tentative carryback adjustment applications for NOLs arising in a year beginning on or after January 1, 2018 and ending before March 27, 2019. Therefore, although taxpayers with NOLs arising in those years may file amended tax returns, they would not be able to file tentative carryback adjustment applications because the time for doing so has expired as of the date of enactment of the CARES Act.

To provide relief on this issue, Notice 2020-26 grants a **six-month extension** to file a tentative carryback adjustment application to taxpayers with an NOL arising in a tax year beginning in 2018 and ending on or before June 30, 2019. The applicable form must include "Notice 2020-26, Extension of Time to File Application for Tentative Carryback Adjustment." Therefore, a taxpayer with an NOL arising in 2018 will have until June 30, 2020 to file a tentative carryback adjustment application instead of December 31, 2019.

The CARES Act also provided for the acceleration of remaining corporate minimum tax credits, stating

that a corporation may apply for the accelerated tax credits under Section 6411. Notice 2020-26 provides that, if the taxpayer is a corporation with a claim for minimum tax credits, its deadline would be December 30, 2020. If a taxpayer wishes to file a single application for both the NOL carryback and the minimum tax credit, the Notice provides that that taxpayer must do so by the earlier of the two deadlines, June 30, 2020.

Special Rules for 2017 Straddle Periods

The CARES Act does provide a special rule for applications for NOLs arising in straddle years that begin before January 1, 2018 and end after December 31, 2017. Tentative carryback adjustment applications with respect to NOLs arising in such years will be treated as timely if filed no later than 120 days after March 27, 2020. Elections to forgo or reduce the carryback of such NOLs, or elections to revoke any such prior elections, shall be treated as timely made if done within 120 days after March 27, 2020.

Revenue Procedure 2020-24 confirms the 120 day extension, treating elections and applications related to NOLs arising in such years as being timely filed if filed no later than **July 27, 2020**.

The IRS has provided a **FAQ website** with respect to filing claims for refunds and adjustments.

Elections Pursuant to Section 163(j)

Revenue Procedure 2020-22 provides guidance on how to make or revoke elections under Section 163(j).

Elections for Real Property and Farming Businesses

The Tax Cuts and Jobs Act (TCJA) amended Section 163(j) providing new rules limiting the amount of business interest expense that can be deducted for tax years after 2017. Real property trade or businesses and farming businesses can elect out of the application of Section 163(j). In exchange, such electing businesses are required to use the alternative depreciation system, generally resulting in longer depreciation periods.

The CARES Act includes at least two provisions that may affect a taxpayer's decision to make the election under Section 163(j)(7). First, the increase of the Section 163(j) limitation from 30 percent to 50 percent of taxable income for 2019 and 2020. Second, the corrected treatment of qualified improvement property as property eligible for 100 percent bonus depreciation retroactive to the date of the TCJA.

Given these changes, taxpayers may be reassessing the benefit of an election under Section 163(j)(7). Revenue Procedure 2020-22 provides welcome guidance and flexibility for taxpayers who may want to make or revoke an election under Section 163(j)(7).

Real property and farming businesses that want to elect out of Section 163(j) Such taxpayers will be considered to have properly made the election if they did do so under the Section 163(j) proposed regulations issued in 2018 or make a late election under the Revenue Procedure. In order to make a late election, a taxpayer may make an election for the 2018, 2019, or 2020 tax year by filing an

amended Federal income tax return, amended Form 1065 or Administrative Adjustment Request (AAR), as applicable.

- If the taxpayer is a partnership subject to the centralized partnership audit regime (BBA partnership) that chooses to make the election by filing an amended return for 2018 or 2019 under Revenue Procedure 2020-23, it must do so under the timeline provided by that Revenue Procedure. i.e., by September 30, 2020.
- If the taxpayer is a BBA partnership that chooses not to file an amended return under Revenue Procedure 2020-23, the partnership may make a late election under Section 163(j) by filing an AAR on or before October 15, 2021, but before the period of limitations on making adjustments for the reviewed year.
- For other taxpayers, the amended Federal income tax return or amended Form 1065 must be filed on or before October 15, 2021, but before the period of limitations for the reviewed year.

The taxpayer must include a statement making the election as outlined by the Revenue Procedure. The return or AAR must include the adjustment for the late Section 163(j) election and any collateral adjustments. The collateral adjustments must also be made on amended returns or AARs for affected succeeding taxable years (e.g., adjustments to depreciation methods).

The Revenue Procedure specifically indicates that the Treasury and IRS will provide additional guidance in forthcoming final and proposed regulations under Section 163(j), which will address issues arising under the CARES Act.

Real property and farming business that want to withdraw an election under Section 163(j) Taxpayers that made an election under Section 163(j)(7) may withdraw the election and will be treated as if the election were never made. Taxpayers do so by filing a withdrawal statement with an amended Federal income tax return, amended Form 1065 or AAR under generally the same time frame and process as outlined above.

Elections for Taxpayers not to Apply the 50 Percent Limitation

The CARES Act provides that a taxpayer may elect not to apply the 50 percent limitation for a 2019 or 2020 taxable year. A partnership can only elect out of the 50 percent limitation for a 2020 year since it can only apply the 50 percent limitation for a 2020 year.

Revenue Procedure 2020-22 provides that taxpayers make the election by timely filing a Federal income tax return or Form 1065, including extensions, an amended Federal income tax return, amended Form 1065 or AAR, as applicable, and using the 30 percent limitation. A formal statement is not required. The election must be made on a yearly basis. In the case of a taxpayer that is a partnership, the election is made by the partnership. In the case of a controlled foreign corporation (CFC), the election is made by each controlling domestic shareholder.

A taxpayer may revoke the election by timely filing an amended Federal income tax return, amended Form 1065 or AAR using the 50 percent limitation.

Elections for Taxpayers to use 2019 Adjusted Taxable Income in 2020 Taxable Year

The CARES Act provides that a taxpayer may elect to use its 2019 adjusted taxable income (ATI) as the ATI for its 2020 tax year. The taxpayer does so by timely filing a Federal income tax return or Form 1065, including extensions, an amended Federal income tax return, an amended Form 1065 or an AAR using the taxpayer's 2019 ATI. An election may be revoked by timely filing an amended Federal income tax return, an amended Form 1065 or an AAR not using the 2019 ATI. A formal statement is not required to revoke or make the election.

For a taxpayer that is a partnership, the election is made by a partnership. For a CFC, the election is made by each controlling domestic shareholder. In the case of a CFC group, as defined under the proposed Section 163(j) regulations, the election must be made for every available tax year and for every CFC group member.

Elections for Partners who Wish to Elect out of the 50 Percent EBIE Rule

The CARES Act provides that a partner treats 50 percent of its allocable share of a partnership's excess business interest expense (EBIE) for 2019 as an interest deduction in the partner's 2020 tax year without limitation. The remaining EBIE remains subject to the applicable 163(j) limitation. A partner may elect out of the 50 percent EBIE rule.

A partner makes the election by timely filing a federal income tax return or a Form 1065, including extensions, an amended Federal income tax return, an amended Form 1065, or an AAR for the 2020 year by not applying the 50 percent EBIE rule. An election is revoked by timely filing an amended Federal income tax return, an amended Form 1065, or an AAR for the 2020 year by applying the 50 percent EBIE rule.

Those wishing to read the full guidance may do so here:

<https://www.irs.gov/pub/irs-drop/rp-20-24.pdf>

<https://www.irs.gov/pub/irs-drop/n-20-26.pdf>

<https://www.irs.gov/pub/irs-drop/rp-20-22.pdf>

For a link to Williams Mullen's previous alert describing Revenue Procedure 2020-23 and BBA Partnerships, **click here**.

Please note: This alert contains general, condensed summaries of actual legal matters, statutes and opinions for information purposes. It is not meant to be and should not be construed as legal advice. Readers with particular needs on specific issues should retain the services of competent counsel.

Please click here for additional legal updates from Williams Mullen regarding COVID-19.

Related People

- Anna K. Derewenda ? 804.420.6094 ? aderewenda@williamsmullen.com

Related Services

- Tax Law