

Net Operating Loss Carryback Period Extended for Certain Small Businesses

March 20, 2009

The recently enacted American Recovery and Reinvestment Act of 2009 (the stimulus bill) extended the carryback period over which certain 2008 and 2009 net operating losses (NOLs) can be applied against prior years' taxable income. For certain small businesses, this carryback period has been extended from two years to up to five years. The use of the additional carryback period is wholly elective at the option of the small business, but may require action as soon as April 17, 2009 for those small businesses wishing to take advantage of the extended carryback period. On March 16, 2009, the Internal Revenue Service (IRS) published guidance on how to make the extended carryback election and on other administrative aspects of the extended carryback period.

Section 1211 of the stimulus bill allows an "eligible small business" to elect to apply its NOL for its tax year ending in 2008 (or, at the election of a business with a noncalendar tax year, beginning in 2008) against taxable income earned in its prior five tax years. Absent this extension, losses could only be carried back to the prior two tax years. To qualify as an "eligible small business" for purposes of Section 1211, the business cannot have average annual gross revenues over a three-year period (ending with the tax year of the NOL to be carried back, as interpreted by the IRS) in excess of \$15,000,000.

If a small business previously elected to waive the carryback of its 2008 net operating losses, it can still take advantage of this provision, but to do so it must revoke its prior election on or before April 17, 2009. If the small business operates on a fiscal-year basis, the election can be made for either the tax year that ends in 2008 or that begins in 2008, but not for both years. The election under Section 1211 of the stimulus bill is irrevocable. In addition, the small business can accelerate the refund created by the loss carryback by using either Form 1045 (Application for Tentative Refund) for small businesses that are not corporations or Form 1139 (Application for Tentative Refund) for small businesses that are corporations.

The IRS is providing additional staff to ensure that these refund applications are processed as quickly as possible and hopes to be able to issue refunds within 45 days of receipt of the applicable Form 1045 or 1139. The IRS's News Release can be accessed at <http://op.bna.com/dt.nsf/r?Open=csaz-7q7n5v>. The IRS's Revenue Procedure on the loss carryback can be accessed at <http://op.bna.com/dt.nsf/r?Open=csaz-7q7n68>. In addition, the IRS has issued helpful Questions and Answers on Section 1211 that can be accessed at <http://op.bna.com/dt.nsf/r?Open=csaz-7q7n62>. However, there are still some unresolved questions concerning the application of Section 1211 to eligible small businesses that are classified as partnerships for federal income tax purposes.

If you have any questions on any of the issues discussed in this LawFlash, please contact any of the Morgan Lewis attorneys listed below:

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