BUSINESS PRIVILEGE TAX: Net Operating Loss Carry Forward Provisions

Q: The City of Philadelphia Business Privilege Tax allows for a three year carry forward of net operating losses. Can the survivor of the merger carry forward net operating losses generated by a taxpayer prior to a merger? If so, are there any limitations on the net operating losses? Please distinguish between Method I and Method II taxpayers, if applicable.

A. *For Federal tax- planning purposes, corporations with accumulated net operating losses have long been in demand for tax saving purposes. A corporation that acquires another by purchase or reorganization also gets the acquired corporation's tax position for many items, one of which is net operating loss carryovers. A profitable corporation will acquire and merge with a loss corporation or vice versa, with the idea of offsetting the income of the profitable corporation with the losses of the loss corporation. If a corporation that has sustained a loss is acquired by purchase or reorganization, there is a question of how the loss carryover is affected. The deductibility of the net operating loss is governed by a specific provision of the Federal tax code (i.e. IRC § 382 limitations).*

The Philadelphia Code prohibits the filing of a consolidated or combined tax return. The Code provides no authority for the use by one taxpayer of an operating loss generated by another taxpayer under any circumstances. Moreover, the rules for net operating losses under the Code expressly do not incorporate the provisions of the Federal Internal Revenue Code for either Method I or Method II taxpayers. Accordingly, it has been the Department's consistent position since the inception of the BPT that the survivor of a merger cannot report the net operating loss of the non-survivor.