

June 26, 2020

## Federal Coronavirus Aid, Relief, and Economic Security (CARES) Act – Net Operating Losses (NOLs) guidance

**As businesses accept grants and loans to support their business recovery, this serves as a reminder that Philadelphia policies are sometimes independent from federal policies.**

The CARES Act provides for the following amendments to the provisions of IRC Section 172:

- *Elimination of the 80% of Taxable Income Limitation:* The CARES Act repeals the 80% NOL limitation for taxable years beginning before January 1, 2021. Companies are now permitted to fully offset their taxable income in such taxable years with NOL carryforwards without regard to the year in which such NOL arose.
- *Reinstatement of NOL Carrybacks:* The CARES Act reinstates loss carrybacks for NOLs arising in 2018, 2019, and 2020 (taxable years beginning after December 31, 2017 and before January 1, 2021), to the five taxable years preceding the taxable year in which the loss arose. NOLs arising in a fiscal tax year beginning in 2017 and ending in 2018 may be carried back two years.

**Philadelphia does *not* conform to the federal treatment of NOLs for the Business Income & Receipts Tax (BIRT) on Net Income (Method II filers).** Our NOL is computed independently from the federal NOL. The enabling legislation does not expressly reference IRC Section 172. The BIRT Net Income Tax calculation for Method II filers begins with federal taxable income, prior to the exclusions for dividends received and NOLs – effectively Line 28 of Federal Form 1120.

For both Method I and Method II BIRT filers, a NOL may be *carried forward for three (3) tax years* following the tax year for which it was first reported. The earliest NOL must be carried over to the earliest taxable year in which the taxpayer reports taxable net income before deducting a NOL carried forward. The amount of any NOL in excess of the net income for any tax year to which it is carried forward may be carried forward to subsequent tax years but may not be carried forward past the third tax year following the tax year for which it was first reported (Section 411 of BIRT Regulations).

If no return is filed for a year in which there is an overall loss and documentation supporting such loss has not been retained, the NOL cannot be carried forward to future years for BIRT purposes.

It is also important to know that for Net Profits Tax purposes, unlike the BIRT, NOLs of any tax year are *not* allowed to be carried forward to subsequent tax years.