



Tax Practitioner Seminar

January 27, 2017

Taxable Income Changes – Business Net Profit Filers



Adjusted Federal Taxable Income (AFTI)

- When **calculating AFTI**, a net profit taxpayer will now **strip off all pass-through income (and add back pass-through losses)** – not just the pass-through income that is subject to municipal tax elsewhere.
- Beginning with **net operating losses (“NOLs”) incurred in tax year 2017**, NOLs will be used **pre-apportionment** and will not be tracked by municipality.
 - ❖ Pre-2017 NOLs will still have to be tracked and used post-apportionment, by municipality.
 - ❖ Until all pre-2017 NOLs are exhausted, net profit filers will have to track and use NOLs differently, depending on when the NOL was incurred.

NOL CF - Pre HB 5 vs. Post HB 5

Pre-HB5 (Post-Appportionment Basis)

Post-HB5 (Pre-Appportionment Basis)

NOL CF Requirements

- HB 5 provides for a state-wide five-year carryforward for NOLs incurred in taxable years beginning **after** 2016.
 - ❖ Applies to losses incurred in taxable years beginning on or after January 1, 2017, and then carried forward to future taxable years.
- NOL CFs apply to:
 - ❖ Business Net Profits;
 - ❖ Schedule C, E, & F income of non-residents earned in taxing municipalities; and
 - ❖ All Schedule income of residents of taxing municipalities.

NOL CF Requirements

- NOL CFs do not include unutilized losses resulting from basis limitations, at-risk limitations or passive activity loss limitations.
 - ❖ Losses that are ***not reportable*** on Federal Schedule E Part II ***are not included*** in current year taxable income or ***allowed*** to be carried forward.
 - ❖ Applies to partners and S Corporation shareholders.
- NOL CFs may not be used to offset qualifying wages.

NOL CF Requirements

- NOL CF Provision is phased in:
 - ❖ Taxpayers may only claim 50% of the available NOL carryforward during years 2018 through 2022.
 - ❖ 100% utilization of NOL CFs is delayed until tax year 2023.

NOL CF Requirements

- NOL CF Provision is phased in:

- ❖ TPs may carry forward any “unutilized” NOLs for 5 years.
 - From technical clarification in State Budget Bill (HB 64) on how unutilized NOL CFs are handled in regards to the bill’s NOL CF phase-in provisions.
- ❖ Phase-in provisions also apply to NOL CF related to Schedule income of residents and non-residents.

NOL CF Requirements

- Pre-2017 NOLs are permitted to be carried forward to the extent already allowed by municipalities.
- The 50% phase-in limitation **does not apply** to pre-2017 NOLs.
- Pre-2017 NOLs must be utilized **before** utilizing new NOLs generated after tax year 2016.
- Post-2016 NOL carry-forwards are calculated and applied on a **pre-apportionment basis**.

Consolidated Net Profit Returns

- Municipalities **must accept** a consolidated municipal net profit return **if the federal return is filed consolidated.**
- New with HB 5 is a **five-year opt-in and opt-out** provision.
 - ❖ Consolidated net profit filers can discontinue filing consolidated, without the tax administrator's permission, after five years.
 - ❖ A decision to deconsolidate remains in place for five years.
- Those **already filing** on a consolidated basis, pre-HB 5, **may continue to do so.**

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Alternative Apportionment Method

- Taxpayers may use an alternative method for apportioning net profits on an annual return (other than the 3-factor property, payroll and sales formula) by submitting a written request with the return.
- Taxpayers may use the requested alternative method unless the tax administrator denies the use.
- The tax administrator's denial of an alternative method request must be issued in the form of an appealable Assessment.
 - ❖ Tax administrators may also impose alternative methods by issuing appealable Assessments.

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