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## Corporate Tax Losses

Turning lemons into lemonade.

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2008 has proven to be a very challenging year for many companies. In addition to consumers slowing their spending, and valuations of investments and inventories plummeting, corporations in many industries are seeing their bankers increase fees and rates, while reducing their access to term lines of credits and term loans.

These combined pressures will result in large numbers of companies experiencing operating losses for their current fiscal years. While losses are never a good thing, there are a number of significant benefits to be derived from a tax perspective. With proper planning, these tax benefits can be rapidly turned into cash flow for these cash-strapped businesses.

### Accelerating Refunds of Estimated Tax Payments

Corporate taxpayers who have made estimated tax payments earlier in the year when they were projecting current-year profits, do not need to wait until they file their fiscal 2008 tax return to obtain their refund of overpaid estimated taxes. By simply filing IRS Form 4466 (Corporate Application for Quick Refund of Overpayment of Estimated Taxes) with the Feds immediately following the tax year-end (e.g. January 2009 for calendar year C Corps), the overpaid estimated payments will generally be refunded early in 2009.

The taxpayer is not required to have a net operating loss (NOL) in the current year, they simply need to show that they have sufficiently overpaid their estimates. The IRS is required to act on the refund request within 45 days of filing and the taxpayer can still extend their time for filing, their actual corporate tax return, up to eight and one-half months year-end.

In order to qualify for this expedited refund process, the corporation must:

- File Form 4466 no later than the 15th day of the third month following the fiscal year end, and
- Have overpaid their current estimated tax by 10 percent or more of their currently estimated tax liability for the year (minimum refund must exceed \$500).

The determination of whether the taxpayer is overpaid by at least 10 percent is made by the taxpayer based on the facts known at the time the Form 4466 is filed. If the final tax return shows a net liability

in excess of the amount projected when filing Form 4466, penalties may apply. Therefore a detailed tax projection should be determined as soon as possible after year-end.

If a taxpayer files on a consolidated basis with other affiliates, the Form 4466 must be filed by the common parent if the parent company deposited the estimated tax payments during the year. However, if the affiliated members paid their estimates separately, Form 4466 must be filed by one or more of the entities that made the overpayments. Regardless of how the consolidated group made their overpayments, the determination of whether a 10 percent or more overpayment was made, is made on a consolidated basis.

### **Refund of Prior Year Taxes Via NOL Carryback**

In addition to the quick refund procedure for monetizing your overpaid estimated tax payments, C Corps (or an S Corp with Built-in-Gains Tax Liabilities) that expect to incur a current year loss can start planning for carrying back any current year NOL or capital loss to the two prior years — assuming the taxpayer had taxable income in the prior years.

Unlike the refund procedure for estimated tax payments, the taxpayer must wait until they actually file their fiscal 2008 return before they can file Form 1139 (Corporation Application for Tentative Refund).

Form 1139 can be used to:

- carryback an NOL (generally up to two years),
- carryback a net capital loss (generally three years),
- carryback an unused general business credit (generally one year) or
- secure an overpayment of tax, due to a claim of right adjustment under section 1341(b)(1).

The Form 1139 must be filed within 12 months of the end of the tax year in which the NOL is reported. Therefore, a loss incurred in calendar 2008, must be carried back on Form 1139 no later than December 31, 2009. If a taxpayer misses this window to file Form 1139, they can still file a refund claim via Form 1120X. However, the refund will generally take much longer and will not require the IRS to pay interest on the delayed refund.

The significant benefit of filing the refund claims via Form 1139 is that the form allows the taxpayer to easily file for multiple year refunds on one form — versus separate 1120Xs for each year, if that procedure is used. In addition, Form 1139 requires the IRS to act on the refund claim within 90 days of filing and interest accrues on the refund if the IRS does not act in a timely manner.

Taxpayers can elect to forego carrying back their NOLs and instead carry them forward. This may make sense when the taxpayer is confident that they will have taxable income in the subsequent period and the prior years had minimal refund potential. The NOL carryforward can minimize future years' estimated tax payments.

### **Other Refund Strategies**

Taxpayers with carryback potential for NOLs for the two prior years, or three years in the case of capital loss carrybacks or one year in the case of General Business Credits, should evaluate the various methods for maximizing refunds from prior years carefully.

For example, taxpayers can claim the current 50 percent bonus depreciation (*Note: IRC Section 179 expensing is not allowed in a loss year*), claim inventory write-downs, specific bad debt write-offs and write-off accrued expenses in the case of accrual basis taxpayers in order to maximize current-year NOLs and maximize the NOL carryback and refund of prior year taxes.

Cash basis taxpayers can also claim accelerated depreciation deductions, maximize deferred qualified retirement plan funding, sell-off certain devalued assets and pre-pay certain deductible expenses before year-end, in order to maximize their NOLs and refunds.

The impact of the Alternative Minimum Tax (AMT) in a loss carryback period needs to be considered given that the AMT will often apply since generally only 90 percent of the NOL carryback or carryforward is allowed to offset Alternative Minimum Taxable Income (AMTI) and the remaining 10 percent, plus various AMT adjustments, are still subject to the AMT tax.

The state impact of various federal elections and the ability to carryback and/or carryover NOLs for state purposes, must also be factored into the overall tax plan.

The Housing Assistance Tax Act of 2008 also added provisions which allow taxpayers to temporarily claim a credit for prior year AMT or Research & Development credits in lieu of taking the 50 percent bonus depreciation. These credits can be claimed as an immediate tax refund — even if the taxpayer is in a current loss position and cannot carryback their current year NOL.

S Corp shareholders can employ similar strategies to maximize loss flow-throughs and tax refunds for their shareholders. However, the tax basis of the shareholders must be evaluated before year-end, to ensure that any allocable losses will be eligible for shareholder-level deduction under the various tax basis, active vs. passive and at-risk rules.

A careful review of current and prior year tax activity, before and after year-end, can ensure that a corporate taxpayer can maximize the cash flow for both the corporation and their shareholders via expedited tax refunds.

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