

810-3-35.1-.03 Carryforward of Net Operating Losses for Corporations Filing Alabama Consolidated Returns.

(1) Corporations filing Alabama Consolidated Income Tax Returns will compute the net operating loss attributed to Alabama in the manner provided in Rules 810-3-31-.01 and 810-3-31-.02.

(2)(a) The deductibility of net operating losses incurred in a tax year before a corporation becomes a member of an Alabama affiliated group and elects to file an Alabama consolidated return is limited in accordance with the separate return limitation year (SRLY) rules contained in 26 U.S.C. §1502.

1. The term “separate return year” means a taxable year of a corporation for which it files a separate return or for which it joins in the filing of a consolidated return by another group.

2. The term separate return limitation year (or SRLY) means any separate return year of a member or of a predecessor of a member.

3. The term separate return limitation year (or SRLY) does not include:

(i) A separate return year of the corporation, which is the common parent for the consolidated return year to which the tax attribute is to be carried,

(ii) A separate return year of any corporation which was a member of the group for each day of such year, or

(iii) A separate return year of a predecessor of any member if such predecessor was a member of the group for each day of such year.

4. The term “group” means an affiliated group of corporations as defined in 26 USC §1504.

5. The term “member” means a corporation (including the common parent) that is included in the group, or as the context may require, a corporation that is included in a subgroup.

6. The term “predecessor” means a transferor or distributor of assets to a member (the successor) in a transaction -

(i) To which section 381(a) applies; or

(ii) That occurs on or after January 1, 1997, in which the successor’s basis for the assets is determined, directly or indirectly, in whole or in part, by reference to the basis of the assets of the transferor or distributor, but in the case

of a transaction that occurs before June 25, 1999, only one member may be considered a predecessor to or a successor of one other member.

(b) The aggregate of the net operating loss carryovers of a member arising in SRLYs that are included in the consolidated net operating loss deductions for all consolidated return years of the group under paragraph (1) of this section may not exceed the aggregate consolidated taxable income for all consolidated return years of the group. For this purpose:

1. Consolidated taxable income is computed without regard to consolidated net operating loss deductions;
2. Consolidated taxable income takes into account the member's losses and deductions actually absorbed by the group in consolidated return years;
3. In computing consolidated taxable income, the consolidated return years of the group include only those years, including the year to which the loss is carried, that the member has been continuously included in the group's consolidated return, but exclude any years ending after the year to which the loss is carried.

(c) EXAMPLE: 1. In Year 1, corporation P sustains a \$40 net operating loss that is carried forward. P has no income in Year 2. Unrelated corporation T sustains a net operating loss of \$50 in year 2 that is carried forward. P buys the stock of T during Year 3, but T is not a member of the P group for each day of the year. P and T file separate returns and sustain net operating losses of \$120 and \$60, respectively, for Year 3. The P group files consolidated returns beginning in Year 4. During Year 4, the P group has \$160 of consolidated taxable income (computed without regard to the consolidated net operating loss deduction). The consolidated taxable income would be \$70 if determined by reference to only T's items. These results are summarized as follows:

	Separate Year 1	Separate/ Affiliated Year 2	Consolidated Year 3	Year 4
P	\$(40)	\$ 0	\$(120)	\$ 90
T	\$ 0	\$(50)	\$(60)	\$ 70
CAI				\$160

2. P's Year 1, Year 2, and Year 3 are not SRLYs with respect to the P group. P's \$40 net operating loss arising in Year 1 and \$120 net operating loss arising in Year 3 are not subject to the SRLY limitation. The loss arising in Year 1 is the first loss that the P group must absorb in Year 4. Absorption of this loss

leaves \$120 of the group's consolidated taxable income available for offset by other loss carryovers.

3. T's Year 2 and 3 are SRLYs with respect to the P group. T's \$50 net operating loss arising in year 2 and \$60 net operating loss arising in Year 3 are subject to the SRLY limitation. Under paragraph (2)(b) of this section, the SRLY limitation for Year 4 is \$70. T's \$50 loss from year 2 must be included in the P group's consolidated net operating loss deduction for year 4. The absorption of this loss leaves \$70 of the group's consolidated taxable income available for offset by other loss carryovers.

4. P and T each carry over net operating losses to Year 4 from a taxable year ending on the same date (Year 3). The losses carried over from Year 3 total \$180. Under paragraph (b) of this section, the losses carried over from Year 3 are absorbed on a pro rata basis, even though one arises in a SRLY and the other does not. However, the group cannot absorb more than \$20 of T's \$60 net operating loss arising in Year 3 because its \$70 SRLY limitation for Year 4 is reduced by T's \$50 Year 2 SRLY loss already included in the consolidated net operating loss deduction for Year 4. Thus, the absorption of Year 3 losses is as follows:

Amount of P's Year 3 losses absorbed = $\$120/(\$120 + \$20) \times \$70 = \$60$

Amount of T's Year 3 losses absorbed = $\$20/(\$120 + \$20) \times \$70 = \$10$.

5. The absorption of \$10 of T's Year 3 loss further reduces T's SRLY limitation to \$10 (\$70 of initial SRLY limitation, reduced by the \$60 net operating loss already included in the consolidated net operating loss deductions for Year 4 under paragraph (a) of this section).

6. P carries its remaining \$60 Year 3 net operating loss and T carries its remaining \$50 Year 3 net operating loss over to Year 5. Assume that, in Year 5, the P group has \$90 of consolidated taxable income (computed without regard to the consolidated net operating loss deduction). The group's consolidated taxable income determined by reference to only T's items is a consolidated net operating loss of \$4. For Year 5, the consolidated net operating loss deduction includes \$60 of P's Year 3 loss but only \$6 of T's Year 3 loss (the aggregate consolidated taxable income for Years 4 and 5 determined by reference to T's items, or \$66, reduced by T's SRLY losses actually absorbed by the group in Year 4, or \$60).

(d) If any consolidated net operating loss that is attributable to a member may be carried to a separate return year of the member, the amount of the consolidated net operating loss that is attributable to the member is apportioned to the member (apportioned loss) and carried to the separate return

year. If carried over to a separate return year, the apportioned loss may not be carried over to an equivalent, or later, consolidated return year of the group.

1. The amount of a consolidated net operating loss that is attributable to a member is determined by a fraction the numerator of which is the separate net operating loss of the member for the year of the loss and the denominator of which is the sum of the separate net operating losses for that year of all members having such losses.

(e) If a corporation ceases to be a member during a consolidated return year, net operating loss carryovers attributable to the corporation are first carried to the consolidated return year, and only the amount so attributable that is not absorbed by the group in that year is carried to the corporation's first separate return year.

(f) In determining net operating loss carryovers for SRLY subgroups where an existing Alabama affiliated group acquires another affiliated group, the limitations on net operating loss carryovers from a SRLY apply to the SRLY subgroup and not to its members. In determining the members of a SRLY subgroup with respect to the carryover of a net operating loss, the SRLY subgroup is composed of the member carrying over the loss (the loss member) and each other member that was a member of the former group that becomes a member of the new group at the same time as the loss member.

(3) The limitation provided in paragraph (2) of this section does not apply to net operating loss carryovers when the application of paragraph 2 of this section results in an overlap with the application of 26 U.S.C. §382.

(a) An overlap of §382 with respect to a net operating loss occurs if a corporation becomes a member of a consolidated group (the SRLY event) within six months of the change date of an ownership change giving rise to a §382 limitation with respect to that carryover (the §382 event).

(b) If an overlap of this section occurs with respect to net operating loss carryovers of a corporation whose SRLY event occurs within the six month period beginning on the date of a §382 event then an overlap is treated as also occurring with respect to that corporation's net operating loss carryover that arises within the period beginning with the §382 event and ending with the SRLY event.

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