Vermont Department of Taxes
TECHNICAL BULLETIN

TAX: INCOME | TB- 35

SUBJECT: Net Operating Losses | ISSUED: March 13, 2007
REVISED: October 7, 2008

REFERENCE: 32 V.S.A. §§ 5811(25), 5832 and 5888

The purpose of this bulletin is to explain the treatment of net operating losses under 2005, Act 207 (Adj. Sess.) §§ 15, 16, 17 and 18, which created a Vermont net operating loss that can be carried forward.

Prior Law. Previous to the enactment of Act 207, the federal net operating loss was passed through to the Vermont return because the calculation of Vermont tax starts with federal taxable income (Form 1120, Line 30), which is net of any net operating loss. However, no refunds were available on carrybacks. This is still the law for losses incurred in tax years beginning before January 1, 2007.[1]

New Law. For losses occurring in tax years beginning January 1, 2007[2] and after, the new law is effective. The new law does two things:

1) Creates a Vermont Net Operating Loss (VNOL), defined as "any negative income after allocation and apportionment of Vermont net income pursuant to 32 V.S.A. § 5833," which is available as a carryforward in the ten years following the loss year. A VNOL may not be carried back.

2) Establishes a transition rule for loss years 2007, 2008 and 2009 when a portion of the taxpayer's federal net operating loss is carried back. Under the transition rule the carryforward is approximately what would have been available under the old rule plus an additional amount that is a percentage of the federal NOL carryback. For loss year 2007, it is ten percent; for loss year 2008, it is 30 percent; and for loss year 2009, it is 40 percent.

Transition Rule. Transition to the new rule will be phased in over three years. For 2007, 2008 and 2009 losses, a VNOL is calculated under the new rule. The percentage of the current year actual Vermont operating loss that is available to be carried forward as a VNOL on the Vermont return is the same percentage as the federal loss that is carried forward plus an additional specified percentage of the federal carryback. The remaining percentage of the federal NOL carryback is not available.

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[1] Tax years are defined by the first day of the tax year so that any year that begins in 2008 is the 2008 tax year, regardless of the fact that it may end in 2009.
[2] The first full-year tax returns affected by the new NOL law will be due March 15, 2008.

The following formula can be used to calculate the portion of the current year Vermont operating loss that is available as a carryforward on a taxpayer's 2007 Vermont return when a portion of the federal net operating loss was carried back:

Portion of 2007 current year Vermont operating loss available for carryforward = VNOL=

$$\text{total federal NOL} \times \left[\frac{\text{federal NOL carryforward} + 10\% \times \text{federal NOL carryback}}{\text{total federal NOL}}\right]$$

For 2008, the percentage increases to 30 and in 2009, to 40 percent. For losses occurring in taxable years 2010[3] and after, the full amount of the Vermont net operating loss may be carried forward.

If the entire federal NOL is carried forward, then taxpayer simply calculates the VNOL under the new law. The VNOL available to carry forward equals the actual current year Vermont operating loss.

Converting Federal NOLs. The law is silent on the treatment of NOLs created prior to 2007. Based on the assumption that the Legislature did not intend that prior NOLs would be lost and to facilitate the change to the new NOL scheme, the Department will allow taxpayers to "convert" their pre-2007 Federal NOLs to an initial VNOL that may be carried forward ten years. Converted NOLs must be used before a post-2007 VNOL. Once elected, the decision to convert will be binding. Conversion will require the taxpayer to calculate the portion of unused Federal NOL that is attributable to Vermont. The VNOL for any year would be the actual (not pro forma) unused Federal NOL generated that year multiplied by the VT apportionment percentage for that year, adjusted to account for state adjustments and allocated income. The Department will promulgate a rule with respect to conversion of NOLs generated prior to 2007.

Treatment of NOLs Under Unitary Combined Reporting. Federal NOLs generated prior to the enactment of the unitary law and carried forward to 2006 are available to taxable corporations. The NOL is limited to the loss available on the individual returns of the corporations taxable in Vermont. *See Vermont Department of Taxes Reg. §1.5862(d) – 9.*[4] If two or more corporations elect a consolidated return pursuant to 32 V.S.A. § 5662(c) the available net operating loss carryover is the net operating loss available to the consolidated group.

Examples:

1) A Corp, B Corp and C Corp are affiliated corporations operating a unitary business. A and B operate in Vermont. C has no nexus with Vermont. A, B and C file a federal consolidated return for 2006 which carries forward an NOL from the

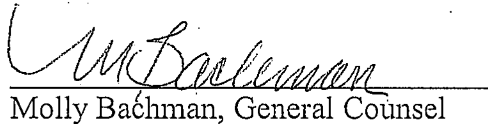
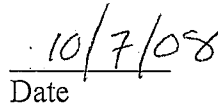
[3] The session law contains an error in that it repeats "2009" in the last paragraph; it should be "2010".
[4] Note, however, that this regulation was promulgated prior to the enactment of the new VNOL rule and therefore applies with respect to 2006 tax returns only. For 2006, NOL usage on the Vermont return remains piggy-backed to the amount used on the federal return, which is included in taxable income on Line 30 of federal Form 1120 .

consolidated 2005 return. A and B file a Vermont consolidated return for 2005 and elect to continue filing consolidated for 2006.

The federal NOL that would be available from a 2005 consolidated return including only A and B is available to reduce the Vermont net income of A and B. C's NOL may not be used to reduce Vermont net income.

2) A Corp, B Corp, C Corp and D Corp are affiliated corporations operating a unitary business. A, B and D operate in Vermont. A, B and C file a consolidated federal return with a net operating loss for 2005 that is carried forward to its 2006 return. A and B file consolidated in Vermont. D is not eligible to be included in the Vermont consolidated return because it has only 52 percent common owners with the other corporations and is not included in the federal consolidated group.

   The federal NOL that is available from a consolidated return including only A and B is available to reduce the Vermont net income of A and B. It may not be used to reduce the income of D. D may have its own separate loss, however.

Molly Bachman, General Counsel   Date

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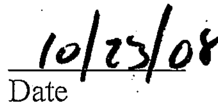

Tom Pelham, Commissioner   Date