

MEMORANDUM

Date: July 31, 2017

To: Lennie Collins, Chair, Nexus Committee

From: Richard Cram

Re: Draft Q & A to address NOL issue

At the March 9, 2017 meeting, the Committee moved to amend the Standard Agreement to add a provision stating that in determining income tax liability during the lookback period, carrying forward of net operation losses (NOLs) cannot be allowed unless a return is filed for the tax year in which the NOL accrued (meaning no NOL can be claimed if it accrued prior to the lookback period). Draft language amending the Standard Agreement (adding Paragraph 5.5 shown in red type) is submitted for the Committee's review, but the question arises: could this issue be covered more effectively in a Q&A published on the Nexus Program website?

Getting into the specifics of determining tax liability may be outside the scope of a voluntary disclosure agreement, which is limited to stating: the taxpayer represents facts showing its contacts with the state, agrees to register and file returns for the lookback period and pay tax due plus interest, and in return, the state grants penalty and liability relief for time periods prior to the lookback period. If the voluntary disclosure agreement contains provisions that get into issues that involve how to calculate actual tax liability during the lookback period—particularly when NOLs are involved (which would be limited to income tax)—this will likely raise questions and may cause confusion with taxpayers. As an alternative to amending the Standard Agreement, it is suggested that a Q&A could be used to address the NOL topic. A suggested Q&A is shown below:

Question: May a net operating loss that has accrued prior to the lookback period be carried forward in determining income/franchise tax liability for tax years included in the lookback period?

Answer: No. The filing of an income/franchise tax return for the tax year in which a net operating loss accrues establishes the net operating loss. If the taxpayer does not file an income/franchise tax return for the tax year in which the net operating loss accrued because that tax year is prior to the lookback period, then no net operating

loss has been established, and therefore no such net operating loss can be carried forward to a future tax year.