

## **Congress Kiboshes Liberal Loss Utilization** *TCJA Limits Business Losses for Everyone*

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The tax code already had several limitations on who and how losses could be used. Profitable Corporations who acquired loss corporations are subject to the complex calculations in Section 382. Passive investors can only use losses to offset passive income. Active pass-through business owners' losses are limited to both their At-Risk basis and their Tax basis. Sole proprietors must avoid the hobby 3 out of 5 year rule. And let's not forget that ugly 90% Alternative Minimum Tax limitation on Net Operating Losses carried forward.

Well Congress decided that they needed to add a couple more hoops for taxpayers to jump through.

First, the easy one. **NEW** (aka Post 2017) Net Operating Losses (NOLs) can no longer be carried back (with a few special exceptions). So, no more going back to obtain a refund of past taxes paid. This rule applies to all tax paying entities.

And going forward? The NOLs are only allowed to offset up to 80% of taxable income. This means those with new loss carry forwards will have to pay tax on part of their future income regardless of how much in NOLs they have being carried forward. Old NOLs can still be used as they have in the past. And unlike the Old NOLs which expire after 20 years, the new ones only expire upon termination or death.

The second one, Section 461(l), affects any taxpayer that is not a corporation. From 2018 through 2025, any business losses in excess of \$250,000 ("Excess Business Losses" or EBL) are disallowed. Yup, not allowed! And no this isn't per business, but rather per taxpayer. The amount does double for those filing a joint return to \$500,000.

The EBL is calculated after applying all other limitation rules – hobby loss, at-risk, tax basis, and passive activity limitations. On the good side, the loss is limited after all business income and losses have been netted together, and any amount that is disallowed is converted to an NOL for the following year. On the bad side, Congress (and the IRS) have yet to define what counts as "aggregate deductions" over "aggregate gross income or gain" for EBL – consider Guaranteed Payments, SEP contributions, §1231 gains - and those losses converted to NOLs will be subject to those new limitations. And on the ugly side, an EBL which gets converted to an NOL for a Charitable Remainder Trust (CRT) or an NOL for an Estate in the year of an owners' death – POOF! - it evaporates as there is no carryover to the income tax return of an estate and there are no such things as NOLs for a CRT.

Why is all this important? Sheltering income with prior year losses or carryovers will have a new layer of limitations and complexity when planning for anticipated taxes. Translation – you’re going to owe taxes while trying to get your business back on track.

**For more information, please contact:**



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Victoria has over 25 years of experience in providing tax consulting, compliance and tax audit representation to closely held businesses and the owners of closely held businesses. She delivers a full range of tax services in covering federal and multi-state laws and regulations for partnerships, S and C corporations, and individuals.