

New York State Department of Taxation and Finance
Office of Tax Policy Analysis
Technical Services Division

TSB-A-07(2)C
Corporation Tax
March 19, 2007

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C060824B

On August 24, 2006, a Petition for Advisory Opinion was received from Deloitte Tax LLP, Two World Financial Center, New York, NY 10281.

The issues raised by Petitioner, Deloitte Tax LLP, are:

1. Whether, in determining the New York State net operating loss deduction for a group of corporations filing a combined franchise tax report under Article 9-A of the Tax Law, the provisions of Internal Revenue Code (IRC) section 382 and the separate return limitation year (SRLY) overlap provisions of U.S. Treasury Regulation section 1.1502-21(g) are to be applied.
2. Whether, in computing the limitation on the use of net operating losses under Article 9-A of the Tax Law, the SRLY limitation applies to Corporation A's acquisition of Corporation B or Corporation A's acquisitions of Corporation C, Corporation D, and Corporation E as described below.
3. Whether, in computing the limitation on the use of net operating losses under Article 9-A of the Tax Law, the IRC section 382 limitation applies to Corporation A's use of the net operating losses of Corporation B, Corporation C, Corporation D, and Corporation E as described below.

Petitioner submits the following facts as the basis for this Advisory Opinion.

On October 24, 2001, Corporation A acquired all of the outstanding stock of Corporation B in a transaction covered by IRC section 382.

For the taxable year 2002, Corporation B and its subsidiaries were included in Corporation A's federal consolidated return and its combined franchise tax report under Article 9-A of the Tax Law.

At the time of the acquisition of Corporation B by Corporation A, Corporation B and its subsidiaries had a total federal and New York State net operating loss (NOL) carry forward of \$469 million and \$316 million, respectively.

The IRC section 382 NOL deduction limitation applicable to the Corporation B NOL for the taxable year 2002 was \$134 million. For federal income tax purposes pursuant to Treasury Regulation section 1.1502-21(g)(1), the SRLY rule pursuant to Treasury Regulation section 1.1502-21(c)(1)(i) did not apply since the provisions of IRC section 382 applied.

For the taxable year 2002, Corporation A deducted \$90 million of Corporation B's NOLs on its combined franchise tax report under Article 9-A of the Tax Law.

On November 17, 1999, Corporation A acquired 57% of all outstanding shares of Corporation E (including its subsidiaries, Corporation C and Corporation D) to supplement the 43% of Corporation E that was already owned by Corporation A. This transaction was covered by IRC section 382. As a result of this transaction, Corporation E, Corporation C, and Corporation D were included in Corporation A's federal consolidated returns and New York State combined franchise tax reports for the taxable years 2000, 2001, and 2002.

As of November 17, 1999, Corporation E and its subsidiaries, Corporation C and Corporation D, had federal and New York NOLs of \$219 million and \$184 million ("Corporation E NOLs"), respectively. For the taxable year 2000, the IRC section 382 limitation on this NOL was \$433 million.

As of November 17, 1999, in addition to the Corporation E NOLs, Corporation C and Corporation D had a federal and New York NOL carry forward of \$55 million and \$39 million ("Corporation C and D NOLs"), respectively. These NOLs were from taxable years prior to the year when Corporation E acquired ownership of Corporation C and its subsidiary Corporation D. (Corporation E acquired all of the stock of Corporation C on November 17, 1998.) For the taxable years 2000, 2001, and 2002, the IRC section 382 limitations relative to the Corporation C and Corporation D NOLs were \$29 million, \$16 million, and \$16 million, respectively.

For taxable year 2000, since the IRC section 382 limitation amount on the Corporation E NOLs was in excess of the available New York NOLs, the entire New York NOL was deducted in computing combined entire net income for purposes of Article 9-A of the Tax Law. For federal income tax purposes pursuant to Treasury Regulation section 1.1502-21(g)(1), the SRLY rule pursuant to Treasury Regulation section 1.1502-21(c)(1)(i) did not apply since the provisions of IRC section 382 applied.

With respect to the Corporation C and Corporation D NOLs for the taxable year 2000, since the IRC section 382 limitation amount of \$29 million was less than the available New York NOLs, the amount of NOL deducted in computing combined entire net income for purposes of Article 9-A of the Tax Law was limited to \$29 million. For taxable year 2001, the IRC section 382 limitation was in excess of the available New York NOLs, and therefore, the remaining New York NOLs were deducted in computing combined entire net income for purposes of Article 9-A of the Tax Law. For federal income tax purposes pursuant to Treasury Regulation section 1.1502-21(g)(1), the SRLY rule pursuant to Treasury Regulation section 1.1502-21(c)(1)(i) did not apply since the provisions of IRC section 382 applied.

Applicable law and regulations

IRC section 172(a) allows a NOL deduction and provides:

Deduction allowed. — There shall be allowed as a deduction for the taxable year an amount equal to the aggregate of (1) the net operating loss carryovers to such year, plus (2) the net operating loss carrybacks to such year. For purposes of this subtitle, the term "net operating loss deduction" means the deduction allowed by this subsection.

IRC section 382 contains rules for a limitation on NOL carryforwards and provides, in part

(a) General rule. — The amount of the taxable income of any new loss corporation for any post-change year which may be offset by pre-change losses shall not exceed the section 382 limitation for such year.

(b) Section 382 limitation. — For purposes of this section —

(1) In general. — Except as otherwise provided in this section, the section 382 limitation for any post-change year is an amount equal to —

(A) the value of the old loss corporation, multiplied by

(B) the long-term tax-exempt rate.

Treasury Regulation section 1.1502-21 contains rules for the computation of consolidated NOL deduction and provides, in part:

(a) *Consolidated net operating loss deduction.* The consolidated net operating loss deduction (or CNOL deduction) for any consolidated return year is the aggregate of the net operating loss carryovers and carrybacks to the year. The net operating loss carryovers and carrybacks consist of—

(1) Any CNOLs (as defined in paragraph (e) of this section) of the consolidated group; and

(2) Any net operating losses of the members arising in separate return years.

(b) *Net operating loss carryovers and carrybacks to consolidated return and separate return years.* Net operating losses of members arising during a consolidated return year are taken into account in determining the group's CNOL under paragraph (e) of this section for that year. Losses taken into account in determining the CNOL may be

carried to other taxable years (whether consolidated or separate) only under this paragraph (b).

(1) *Carryovers and carrybacks generally.* The net operating loss carryovers and carrybacks to a taxable year are determined under the principles of section 172 and this section....

* * *

(c) *Limitations on net operating loss carryovers and carrybacks from separate return limitation years — (1) SRLY limitation — (i) General rule.* Except as provided in paragraph (g) of this section (relating to an overlap with section 382), the aggregate of the net operating loss carryovers and carrybacks of a member arising (or treated as arising) in SRLYs that are included in the CNOL deductions for all consolidated return years of the group under paragraph (a) of this section may not exceed the aggregate consolidated taxable income for all consolidated return years of the group determined by reference to only the member's items of income, gain, deduction, and loss....

* * *

(g) *Overlap with section 382 — (1) General rule.* The limitation provided in paragraph (c) of this section does not apply to net operating loss carryovers ... when the application of paragraph (c) of this section results in an overlap with the application of section 382....

Section 208.9(f) of the Tax Law provides, in part:

A net operating loss deduction shall be allowed which shall be presumably the same as the net operating loss deduction allowed under section one hundred seventy-two of the internal revenue code... except that in every instance where such deduction is allowed under this article:

(1) any net operating loss included in determining such deduction shall be adjusted to reflect the inclusions and exclusions from entire net income required by paragraphs (a), (b) and (g) hereof,

* * *

(3) such deduction shall not exceed the deduction for the taxable year allowed under section one hundred seventy-two of the internal revenue code, ...

Section 211.4(a) of the Tax Law provides, in part:

Combined reports permitted or required. In the discretion of the commissioner, any taxpayer, which owns or controls either directly or indirectly substantially all the capital stock of one or more other corporations, or substantially all the capital stock of which is owned or controlled either directly or indirectly by one or more other corporations or by interests which own or control either directly or indirectly substantially all the capital stock of one or more other corporations, may be required or permitted to make a report on a combined basis covering any such other corporations and setting forth such information as the commissioner may require, subject to the provisions of paragraphs one through five of this subdivision.

Section 3-8.7(a) of the Business Corporation Tax Regulations (“Article 9-A Regulations”) provides for the computation of the net operating loss deduction on combined reports, in part, as follows:

In the case of a corporation which reports for purposes of article 9-A on a combined basis with one or more related corporations, either in the taxable year in which a net operating loss is sustained or in the taxable year in which a deduction is claimed on account of such loss, the deduction is subject to the same limitations which apply for purposes of the Federal income tax as if such corporation had filed for such taxable year a consolidated Federal income tax return with the same related corporations....

Opinion

In this case, it is assumed that Corporation A and its subsidiaries are permitted or required to file a combined report pursuant to section 211.4 of the Tax Law.

Petitioner states that for federal income tax purposes for taxable year 2002, pursuant to Treasury Regulation section 1.1502-21(g)(1), the SRLY rule pursuant to Treasury Regulation section 1.1502-21(c)(1)(i) did not apply and the Corporation B NOL deducted by Corporation A in computing combined entire net income for purposes of Article 9-A of the Tax Law was limited due to the provisions of IRC section 382. In addition, for federal income tax purposes for taxable years 2000 and 2001, the Corporation E NOLs and the Corporation C and Corporation D NOLs were also subject to the IRC section 382 limitation on NOL carryforwards.

With respect to Issue 1, section 208.9(f) of the Tax Law provides that the NOL deduction allowed is presumably the same as the NOL deduction allowed under IRC section 172, except that such deduction shall not exceed the deduction for the taxable year allowed under IRC section 172 (and such deduction shall be subject to the New York modifications pursuant to section 208.9(f)(1)]. Section 3-8.7(a) of the Article 9-A Regulations provides that in the case of a corporation reporting on a combined basis, either in the taxable year in which an NOL is sustained or in the taxable year in which an NOL deduction is claimed, the deduction is subject to the same limitations that apply for purposes of the federal income tax as if such corporation had filed for such taxable year a consolidated federal income tax return.

Treasury Regulation section 1.1502-21(b)(1) provides that the consolidated NOL carryovers and carrybacks are determined under the principles of such section and IRC section 172. Treasury Regulation section 1.1502-21(g)(1) provides that the SRLY limitation provided in Treasury Regulation section 1.1502-21(c) does not apply to NOL carryovers when the application of such section 1.1502-21(c) results in an overlap with the application of IRC section 382.

Accordingly, with respect to Issue 1, pursuant to section 208.9(f) of the Tax Law and section 3-8.7 of the Article 9-A Regulations, in determining the New York State NOL deduction for a group of corporations filing a combined franchise tax report under Article 9-A of the Tax Law, the provisions of IRC section 382 and the SRLY overlap provisions of Treasury Regulation section 1.1502-21(g) are to be applied.

With respect to Issues 2 and 3, in light of the conclusions reached in Issue 1, in computing the limitation on the use of net operating losses under Article 9-A of the Tax Law, the provisions of IRC section 382 and the SRLY overlap provisions of Treasury Regulation section 1.1502-21(g) are to be applied. Therefore, if, for federal income tax purposes, the SRLY rule pursuant to Treasury Regulation section 1.1502-21(c)(1)(i) does not apply to the New York NOL for a taxable year since the provisions of IRC section 382 apply, the provisions of IRC section 382 will apply under Article 9-A for such taxable year.

It should be noted that it is not within the scope of an advisory opinion to verify the accuracy of the NOL dollar amounts for Corporation A and its subsidiaries. An advisory opinion merely sets forth the applicability of pertinent statutory and regulatory provisions to “a specified set of facts.” (Tax Law, §171. Twenty-fourth; 20 NYCRR 2376.1(a).)

DATED: March 19, 2007

/s/
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NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth therein.