

## 103 KAR 16:250. Net operating loss computation and deduction for corporations.

RELATES TO: KRS 141.011, 141.200, 141.201, 141.202

STATUTORY AUTHORITY: KRS 131.130, ~~141.018~~

NECESSITY, FUNCTION AND CONFORMITY: KRS 131.130(1) authorizes the Department of Revenue to promulgate administrative regulations necessary to administer and enforce Kentucky's tax laws. This administrative regulation establishes methods of computing a corporation's net operating loss deduction and application of the deduction to subsequent taxable years on taxable net income as authorized by KRS 141.011, 141.200(11)(b), and KRS 141.202(5).

### Section 1. Definitions.

- (1) "Combined group" is defined by KRS 141.202(2)(a).
- (2) "Combined group filer" means a group of corporations filing in accordance with KRS 141.202.
- (3) "Combined group return" means a return filed under KRS 141.202(3).
- (4) "Corporation" is defined by:
  - (a) KRS 141.202(2)(b) for a combined group return; or
  - (b) KRS 141.010(4) for a separate return for periods beginning on or after January 1, 2018;or
  - (c) KRS 141.201(2)(d) for an elective consolidated return.
- (5) "Doing business in this state" is defined by KRS 141.010(7).
- (6) "Elective consolidated filer" means a corporation as defined in Section 7701(a)(3) of the Internal Revenue Code, 26 U.S.C. 7701(a)(3), filing in accordance with KRS 141.201.
- (7) "Elective consolidated return" means a return defined under KRS 141.201(2)(b).
- (8) "Net operating loss" or "NOL" means net operating loss defined under the Internal Revenue Code as adjusted for differences between KRS Chapter 141 and the Internal Revenue Code.
- (9) "Nexus consolidated filer" means a corporation as defined under KRS 141.010(4) or 141.900(24), filing in accordance with KRS 141.200(8), (9), (10) and (11).
- (10) "Nexus consolidated return" means a return defined under KRS 141.200(9)(g).
- (11) "Separate return" is defined by KRS 141.201(2)(c).
- (12) "Separate return filer" means a corporation filing in accordance with KRS 141.201(3).

### Section 2. Computation and Application of Net Operating Loss.

- (1) Combined group filers, elective consolidated filers, and separate return filers shall compute net operating loss for Kentucky purposes in the following manner:
  - (a) For combined group returns and elective consolidated returns, the net operating loss shall be multiplied by the group's apportionment factor provided by KRS 141.120 or 141.121;
  - (b) For separate returns, the net operating loss shall be multiplied by the apportionment factor provided by KRS 141.120 or KRS 141.121; and
  - (c) The apportioned net operating loss shall be available for carryforward.(2) Elective consolidated filer net operating loss carryforward to a combined group return or separate returns. This subsection shall apply if an elective consolidated filer who has incurred net operating losses as a consolidated group will now be filing combined group returns or separate entity returns, and establishes how those elective consolidated net operating losses shall be treated for purposes of the combined group returns or separate entity returns.
    - (a) An elective consolidated filer having a net operating loss carryforward on the last elective consolidated return may carry that loss forward to combined group returns or separate returns.

The following requirements shall apply to this situation:-

1. Determine the post-apportioned elective consolidated group net operating loss carryforward. The elective consolidated group's apportionment factor provided by KRS 141.120, KRS 141.121, or KRS 141.901 shall be used to determine the post-apportioned net operating loss.

2. Determine the years that are in the post-apportioned elective consolidated group net operating loss carryforward. All post-apportioned net operating loss carryforwards shall be used on a first-in-first-out basis (i.e., most recent losses remain).

3. Determine each loss corporation's share of the net operating loss for each year in the following manner:

a. Allocate the post-apportioned elective consolidated group net operating loss carryforward by year to each loss corporation in each year. For a year in which the total loss generated exceeds the carryforward allocated to that year, the post-apportioned net operating loss shall be prorated for that year proportionally based on the loss generated by each member;

b. Add together each loss corporation's allocated share of the losses for each year it was a member of an elective consolidated group; and

c. Carry the separate entity net operating loss carryforward computed in clauses a. and b. of this subparagraph to the first combined group return or separate return due after the elective consolidated return.

4. No prior year net operating loss carryforward shall be available to separate entities that were not doing business in this state prior to becoming part of an elective consolidated return.

(3) Nexus consolidated net operating loss carryforward to a combined group return, an elective consolidated return, or a separate return period. This subsection shall apply if a nexus consolidated filer ceases to exist who had incurred net operating losses as a consolidated group and establishes how those nexus consolidated net operating losses shall be treated.

(a) If a nexus consolidated filer ceases to exist or a member leaves the group and a consolidated net operating loss carryforward exists, that net operating loss carryforward may be carried forward to the combined group return, the elective consolidated return, or the separate returns. The following requirements shall apply to this situation:

1. Determine the pre-apportioned nexus consolidated group net operating loss carryforward.

2. Determine the years that are in the pre-apportioned nexus consolidated group net operating loss carryforward. All pre-apportioned net operating loss carryforwards shall be used on a first-in-first-out basis (i.e., most recent losses remain).

3. Determine each loss corporation's share of the net operating loss for each year in the following manner:

a. Allocate the pre-apportioned nexus consolidated group net operating loss carryforward by year to each loss corporation in each year. For a year in which the total loss generated exceeds the carryforward allocated to that year, the pre-apportioned net operating loss shall be prorated for that year proportionally based on the loss generated by each member in that year;

b. Multiply the pre-apportioned net operating loss carryforward amounts as assigned to the members by the nexus consolidated group's apportionment factor for each year a net operating loss exists to determine the post-apportioned net operating loss carryforward that member may carryforward in the future. The apportionment factor calculation is provided by KRS 141.120, 141.121, or 141.901;

c. Add together the post-apportioned losses generated for each loss corporation during the time in which it was included in a nexus consolidated return; and

d. Carry the separate entity net operating loss carryforward computed in clauses a. to c. of this subparagraph to the first combined group return, elective consolidated return, or separate return due after the nexus consolidated group ceases to exist.

4. No prior year net operating loss carryforward shall be available to separate entities that

were not doing business in this state prior to becoming part of a nexus consolidated return. To generate a net operating loss in this state, a taxpayer shall be doing business in this state in the year in which the loss is generated.

Section 3. Net Operating Loss Limitation. (1) Corporations that generated net operating losses may carryforward those losses to deduct against taxable net income. The deduction for losses generated for tax years beginning on or after January 1, 2018, shall be limited to eighty (80) percent of the taxable net income as allowed by Section 172 of the Internal Revenue Code.

(2) Nexus consolidated returns shall be subject to the fifty (50) percent limitation as required in KRS 141.200(11)(c).

Section 4. Net Operating Losses by Corporations Included in a Combined Group Return. This section shall apply if a net operating loss is generated by a corporation included in a combined group return.

(1) Net operating losses generated by corporations included in a combined group shall not be used to offset income of other corporations included in the combined group.

(2) Net operating losses may be carried forward to subsequent years.

(3) Net operating losses may only be used if the corporation that generated the loss has taxable net income in subsequent years.

(4) All net operating loss carryforwards shall be used on a first-in-first-out basis (i.e., most recent losses remain).

(5) No prior year net operating loss carryforward shall be available to separate entities that were not doing business in this state prior to becoming part of a combined group return.

Section 5. This administrative regulation shall apply to the computation of the net operating loss deduction of corporations for taxable years beginning on or after January 1, 2018, except where otherwise noted in this administrative regulation.

Section 6. Examples for the computation and application of net operating losses. The following examples relate to the net operating loss computations found in Section 2 of this administrative regulation:

(1) Example 1 – Member Leaves Nexus Consolidated Group

Parent Corporation and its three subsidiaries, Sub A, Sub B, and Sub C, have nexus in Kentucky. Parent Corporation files nexus consolidated group returns for Year 1 through Year 4, but Sub A will not be included in the group in Year 4. Parent Corporation has a pre-apportioned nexus group NOL carryforward of \$85,000 at the end of Year 3 (see Figure 1-1). Apportionment factors for each member are given below (see Figure 1-2).

Figure 1-1

	Year 1	Year 2	Year 3
Sub A In- come/(Loss)	(\$25,000)	(\$25,000)	(\$15,000)
Sub B In- come/(Loss)	(10,000)	(10,000)	(10,000)
Sub C In- come/(Loss)	(5,000)	30,000	50,000
Parent Corpo- ration In-	(5,000)	(5,000)	(15,000)

come/(Loss)			
Group In- come/(Loss)	(\$45,000)	(\$10,000)	\$10,000
Nexus Group NOL Adjust- ment	45,000	25,000	15,000
Group Taxable Income	0	15,000	25,000
Accumulating Group NOL Carryforward	\$45,000	\$70,000	\$85,000

Figure 1-2

	Year 1 Ap- por- tion- ment Fac- tor	Year 2 Appor- tion- ment Factor	Year 3 Appor- tion- ment Factor	Year 4 Appor- tion- ment Factor
Nex us Gro up	23%	28%	32%	17%

The following steps determine the post-apportioned net operating loss ("NOL") assigned to Sub A when it departs the group as well as the pre-apportioned NOL that will be carried forward by the group to Year 4.

(a) Determine the pre-apportioned group NOL carryforward: \$85,000 (see Figure 1-1).

(b) Determine what years are in the pre-apportioned group NOL carryforward assuming all pre-apportioned NOL carryforward amounts are used on a first-in-first-out basis (i.e., most recent losses remain).

1. Year 3 Losses Remaining: \$40,000
2. Year 2 Losses Remaining: \$40,000
3. Year 1 Losses Remaining: \$5,000

(c) Allocate the pre-apportioned group NOL carryforward by year to each loss corporation in each year. For a year in which the total loss generated exceeds the carryforward allocated to that year, prorate the pre-apportioned NOL carryforward for that year proportionally based on the loss generated by each member (see Figure 1-3).

Figure 1-3

	Year 1*	Year 2	Year 3
Sub A Loss	\$2,777	\$25,000	\$15,000
Sub B Loss **	1,111	10,000	10,000
Sub C Loss **	556	-	-
Parent Corpora- tion Loss **	556	5,000	15,000

Group NOL	\$5,000	\$40,000	\$40,000
** Remaining Members' NOL	\$2,223	\$15,000	\$25,000

\* Sub A:  $\$25,000/\$45,000 \times \$5,000 = \$2,777$

Sub B:  $\$10,000/\$45,000 \times \$5,000 = \$1,111$

Sub C:  $\$5,000/\$45,000 \times \$5,000 = \$556$

Parent Corporation:  $\$5,000/\$45,000 \times \$5,000 = \$556$

(d) Multiply the pre-apportioned NOL carryforward amounts assigned to the member that is leaving the group by the nexus consolidated group's apportionment factors in each year an NOL carryforward exists to determine the post-apportioned NOL that member may carryforward in the future (see Figure 1-4).

Figure 1-4

	Year 1	Year 2	Year 3
Sub A NOL Carryforward	\$2,777	\$25,000	\$15,000
Nexus Group Apportionment Factor	23%	28%	32%
Post-Appportioned NOL Carryforward	\$638	\$7,000	\$4,800

The nexus consolidated group will carryforward a pre-apportioned NOL of \$42,223 ( $\$2,223 + \$15,000 + \$25,000$ ) to Year 4 (see Figure 1-3), and Sub A will carryforward a post-apportioned NOL of \$12,438 ( $\$638 + \$7,000 + \$4,800$ ) to Year 4 (see Figure 1-4).

## (2) Example 2 – Remaining Nexus Consolidated Group Dissolves

This example is a continuation of Example 1.

Parent Corporation and its two (2) remaining subsidiaries, Sub B and Sub C, have nexus in Kentucky. Parent Corporation files nexus consolidated group returns for Year 1 through Year 4, but each group member will file separately in Year 5. Parent Corporation has a pre-apportioned nexus group NOL carryforward of \$42,223 at the end of Year 3 (see Figure 1-3 from Example 1). Apportionment factors for each member are given below (see Figure 2-2).

Figure 2-1

	Year 1	Year 2	Year 3	Year 4
Sub B Income/(Loss)	(\$10,000)	(\$10,000)	(\$10,000)	(\$10,000)
Sub C Income/(Loss)	(5,000)	30,000	50,000	60,000
Parent Corporation Income/(Loss)	(5,000)	(5,000)	(15,000)	(30,000)
Group Income (loss)				\$20,000
Nexus Group NOL Adjust-				10,000

ment				
Group Taxable Income				30,000
Group NOL Generated	\$2,223*	\$15,000*	\$25,000*	\$10,000
Cumulative Carryforward				\$52, 223

\* See Figure 1-3 from Example 1

Figure 2-2

	Year 1 Apportionment Factor	Year 2 Apportionment Factor	Year 3 Apportionment Factor	Year 4 Apportionment Factor
Nexus Group	23%	28%	32%	17%

The following steps determine the post-apportioned NOL that will be carried forward separately by each group member to Year 5 when the nexus consolidated group dissolves.

(a) Determine the pre-apportioned group NOL carryforward: \$52,223 (see Figure 2-1).

(b) Determine what years are in the pre-apportioned group NOL carryforward assuming all NOL carryforward amounts are used on the first-in-first-out basis (i.e., most recent losses remain).

1. Year 4 Losses Remaining: \$40,000

2. Year 3 Losses Remaining: \$12,223

(c) Allocate the pre-apportioned group NOL carryforward by year to each loss corporation in each year. For a year in which the total loss generated exceeds the carryforward allocated to that year, prorate the pre-apportioned NOL carryforward for that year proportionally based on the loss generated by each member (see Figure 2-3).

Figure 2-3

	Year 3	Year 4
Sub B Loss	\$4,890	\$10,000
Parent Corporation Loss	\$7,333	30,000
Group NOL	\$12,223	\$40,000

\* Sub B:  $\$10,000/\$25,000 \times \$12,223 = \$4,890$

Parent Corporation:  $\$15,000/\$25,000 \times \$12,223 = \$7,333$

(d) Multiply the pre-apportioned NOL carryforward amounts assigned to each member that is leaving the group by the nexus consolidated group's apportionment factors in each year an NOL exists to determine the post-apportioned NOL that member may carryforward in the future (see Figure 2-4).

Figure 2-4

	Year 3	Year 4
Sub B NOL Carryforward	\$4,890	\$10,000
Nexus Group Apportionment Factor	32%	17%
Sub B Post-Appportioned NOL Carryforward	\$1,564	\$1,700
Parent Corporation NOL Carryforward	\$7,333	\$30,000
Nexus Group Apportionment Factor	32%	17%
Parent Corp Post-Appportioned NOL Carryforward	\$2,346	\$5,100

Sub B will carryforward a post-apportioned NOL of \$3,264 (\$1,564+\$1,700) to Year 5, and Parent Corporation will carryforward a post-apportioned NOL of \$7,446 (\$2,346+\$5,100) to Year 5 (see Figure 2-4). The total post-apportioned NOLs carried forward to Year 5 is \$10,710 (see Figure 2-4).

(3) Example 3 – Member Leaves Elective Consolidated Group

Parent Corporation and its three subsidiaries, Sub A, Sub B, and Sub C, file elective consolidated group returns for Year 1 through Year 4, but Sub A will not be included in the group in Year 4. Parent Corporation has a post-apportioned elective consolidated group NOL carryforward of \$23,500 at the end of Year 3 (see Figure 3-1).

Figure 3-1

	Year 1	Year 2	Year 3
Sub A Income/(Loss)	(\$25,000)	(\$25,000)	(\$15,000)
Sub B Income/(Loss)	(10,000)	(10,000)	(10,000)
Sub C Income/(Loss)	(5,000)	30,000	50,000
Parent Corporation Income/(Loss)	(5,000)	(5,000)	(15,000)
Group Income/(Loss)	(\$45,000)	(\$10,000)	\$10,000
Group Apportionment Factor	50%	40%	30%
NOL Generated/(Used)	22,500	4,000	(3,000)
Accumulating Group NOL Carryforward	\$22,500	\$26,500	\$23,500

The following steps determine the post-apportioned NOL assigned to Sub A when it departs

the group as well as the post-apportioned NOL that will be carried forward by the group to Year 4.

(a) Determine the post-apportioned group NOL carryforward: \$23,500 (see Figure 3-1).

(b) Determine what years are in the post-apportioned group NOL carryforward assuming all post-apportioned NOL carryforward amounts are used on a first-in-first-out basis (i.e., most recent losses remain).

1. Year 3 No NOL Generated
2. Year 2 Losses Remaining: \$4,000
3. Year 1 Losses Remaining: \$19,500

(c) Prorate the post-apportioned group NOL carryforward by year to each loss corporation in each year proportionally based on the loss generated by each member (see Figure 3-2).

Figure 3-2

	Year 1*	Year 2**
Sub A Loss	\$10,833	\$2,500
Sub B Loss ***	4,333	1,000
Sub C Loss ***	2,167	-
Parent Corporation Loss ***	2,167	500
Group NOL	\$19,500	\$4,000
*** Remaining Members' Loss (per year)	\$8,667	\$1,500

\* Sub A:  $\$25,000/\$45,000 \times \$19,500 = \$10,833$   
 Sub B:  $\$10,000/\$45,000 \times \$19,500 = \$4,333$   
 Sub C:  $\$5,000/\$45,000 \times \$19,500 = \$2,167$   
 Parent Corporation:  $\$5,000/\$45,000 \times \$19,500 = \$2,167$

\*\* Sub A:  $\$25,000/\$40,000 \times \$4,000 = \$2,500$   
 Sub B:  $\$10,000/\$40,000 \times \$4,000 = \$1,000$   
 Parent Corporation:  $\$5,000/\$40,000 \times \$4,000 = \$500$

The elective consolidated group will carryforward a total post-apportioned NOL of \$10,167 to Year 4, and Sub A will carryforward a total post-apportioned NOL of \$13,333 to Year 4 (see Figure 3-2).

(4) Example 4 – Remaining Elective Consolidated Group Dissolves

This example is a continuation of Example 3.

Parent Corporation and its two remaining subsidiaries, Sub B, and Sub C, file elective consolidated group returns for Year 1 through Year 4, but each group member will file separately in Year 5. Parent Corporation has a post-apportioned elective consolidated group NOL carryforward of \$10,167 at the end of Year 3 (see Figure 4-1).

Figure 4-1

	Year 1	Year 2	Year 3	Year 4
Sub B Income/(Loss)	(10,000)	(10,000)	(10,000)	(15,000)
Sub C Income/(Loss)	(5,000)	30,000	50,000	25,000



Parent Corporation Income/(Loss)	(5,000)	(5,000)	(15,000)	(20,000)
Group Income/(Loss)				(\$10,000)
Group Apportionment Factor				30%
NOL Generated/(Used) per year	\$8,667*	\$1,500*	\$ -	3,000
Accumulating Group NOL Carryforward	\$8,667	\$10,167	\$10,167	\$13,167

\* See Figure 3-2 from Example 3

The following steps determine the post-apportioned NOL that will be carried forward separately by each group member to Year 5 when the elective consolidated group dissolves.

(a) Determine the post-apportioned group NOL carryforward: \$13,167 (see Figure 4-1).

(b) Determine what years are in the post-apportioned group NOL carryforward assuming all post-apportioned NOL carryforward amounts are used on a first-in-first-out basis (i.e., most recent losses remain).

1. Year 4 Losses Remaining: \$3,000
2. Year 3 No NOL Generated
3. Year 2 Losses Remaining: \$1,500
4. Year 1 Losses Remaining: \$8,667

(c) Prorate the post-apportioned group NOL carryforward by year to each loss corporation in each year proportionally based on the loss generated by each member (see Figure 4-2).

Figure 4-2

	Year 1**	Year 2**	Year 4*
Sub B Loss	4,333	1,000	1,286
Sub C Loss	2,167	-	-
Parent Corporation Loss	2,167	500	1,714
Group NOL	\$8,667	\$1,500	\$3,000

\* Sub B:  $\$15,000/\$35,000 \times \$3,000 = \$1,286$

Parent Corporation:  $\$20,000/\$35,000 \times \$3,000 = \$1,714$

\*\* See Figure 3-2 from Example 3

Sub B will carryforward a post-apportioned NOL of \$6,619 ( $\$4,333 + \$1,000 + \$1,286$ ) to Year 5, Sub C will carryforward a post-apportioned NOL of \$2,167 to Year 5, and Parent Corporation will carryforward a post-apportioned NOL of \$4,381 ( $\$2,167 + \$500 + \$1,714$ ) to Year 5 (see Figure 4-2). The total post-apportioned NOLs carried forward to Year 5 is \$13,167 (see Figure 4-2). (32 Ky.R. 1827; 33 Ky.R. 70; eff. 8-7-2006; 45 Ky.R. 2153, 2571; eff. 4-5-2019.)