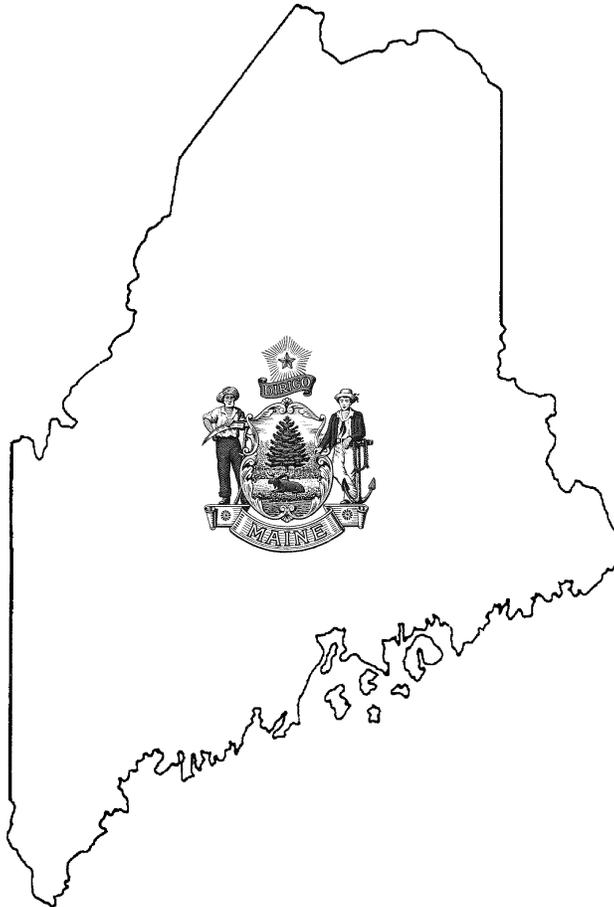


**MODIFICATIONS RELATED TO NET
OPERATING LOSSES –
EXAMPLES FOR C CORPORATIONS**



GUIDANCE DOCUMENT

Maine Revenue Services, Income/Estate Tax Division

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INTRODUCTION

If a business sustains a net operating loss (“NOL”) in a taxable year under the Internal Revenue Code (“IRC”), that loss may be applied against federal taxable income in years surrounding the loss. Generally, federal losses incurred in tax years beginning prior to 2018 may be carried back two years and carried forward up to twenty years. Federal losses incurred in tax years beginning after 2017 generally may be carried back up to five years and carried forward indefinitely. Federal losses incurred in tax years beginning after 2020 generally may not be carried back but may be carried forward indefinitely. However, there are exceptions that allow some NOLs incurred after 2020 to also be carried back. Deductions for the carryback and carryforward of NOLs incurred in tax years beginning prior to 2021 may offset taxable income up to the amount of the loss.

Prior to enactment of the federal Coronavirus Aid, Relief, and Economic Security (“CARES”) Act, deductions for NOLs incurred in tax years beginning after 2017 were limited to 80% of adjusted federal taxable income. However, the CARES Act suspended the 80% limitation for tax years beginning before January 1, 2021, thus reinstating full deductibility of NOLs for tax years beginning in 2018, 2019, and 2020. CARES Act, P.L. 116-136 § 2303. Under the provision, the 80% limitation now applies to tax years beginning after 2020 with respect to NOLs arising in tax years beginning after 2017.

Over the years, Maine has been in various stages of conformity with the federal loss carryback and carryforward rules. Currently, Maine law does not allow any federal loss carryback, but does permit income in future years (other than 2009, 2010 and 2011) to be offset by the amount of federal carryback not allowed on the Maine income tax return.

In addition, for tax years beginning on or after January 1, 2018, Maine law conforms to the federal tax treatment of NOL carryforward deductions allowed under IRC § 172. Under that provision, as previously mentioned, the NOL carryforward deduction for tax years beginning on or after January 1, 2021 with respect to NOLS arising in tax years beginning after December 31, 2017 is limited to 80% of adjusted federal taxable income. The 80% limitation does not apply to NOL deductions claimed for tax years beginning in 2018, 2019, and 2020, nor does it apply to NOL deductions that are claimed for tax years beginning after 2020 if the deduction is associated with an NOL arising in tax years beginning prior to January 1, 2018.

Nonconformity with federal law requires adjustments to federal taxable income through addition and subtraction modifications. This guidance document provides information about income modifications related to federal NOLs in more detail than is available in the filing instructions for the corporate income tax returns. The applicable statutory references are listed below.

| <u>Section</u> | <u>Applicable Years</u> |
|--------------------------|---|
| Addition Modifications | |
| 36 M.R.S. § 5200-A(1)(B) | 1982 through 2001 |
| 36 M.R.S. § 5200-A(1)(C) | 1982 and later |
| 36 M.R.S. § 5200-A(1)(H) | Losses in 1989 – 1992 and after 2001 carried back |
| 36 M.R.S. § 5200-A(1)(M) | Loss in 2001 carried back |
| 36 M.R.S. § 5200-A(1)(U) | Carryforwards to 2008 |
| 36 M.R.S. § 5200-A(1)(V) | Carryforwards to 2009 – 2011 |

Subtraction Modifications

| | |
|--------------------------|--------------------------------------|
| 36 M.R.S. § 5200-A(2)(H) | After 1989 (recapture of sub-§ 1(H)) |
| 36 M.R.S. § 5200-A(2)(L) | After 2001 (recapture of sub-§ 1(M)) |
| 36 M.R.S. § 5200-A(2)(S) | After 2008 (recapture of sub-§ 1(U)) |
| 36 M.R.S. § 5200-A(2)(T) | After 2011 (recapture of sub-§ 1(V)) |

Link to the statute: mainelegislature.org/legis/statutes/36/title36sec5200-A.html

Except for a four-year period from 1989 through 1992, Maine was in full conformity with federal law regarding NOLs until 2001. For tax years beginning in 2001, Maine decoupled from the special federal allowance for carrybacks of more than two years. Beginning with 2002 tax years, Maine law has decoupled from all federal carrybacks. Except for tax years 2009 through 2011, Maine does allow an income offset in years after the loss for the federal carrybacks that were disallowed.

For tax years beginning in 2008, Maine law also disallowed a portion of large NOL carryforwards. The disallowance was equal to 10% of any loss in excess of \$100,000 carried forward to 2008. The disallowed amount may be recaptured through a Maine subtraction modification in subsequent years remaining in the federal carryforward limitations period plus one year.

For tax years 2009 through 2011, all federal carryforwards and almost all Maine NOL subtractions were deferred. Starting with tax year 2012, these adjustments again become available. Amounts disallowed during the three-year deferral period may be recaptured through subtraction modifications beginning in 2012 during the remaining federal carryforward period, plus the number of years the NOL carryforwards or Maine modifications were denied.

Federal NOLs, including carrybacks and carryforwards, are reflected in the federal taxable income reported on the Maine corporate income tax return, Form 1120ME, line 1. If a Maine amended return is being filed due to a federal NOL carryback, you must attach a copy of federal Form 1139 or Form 1120X and a schedule that reflects, from year to year, the use of the federal NOL carryback or carryforward and related income modifications described in this document. A corporation included in a federal consolidated return that is filing a separate Maine return with a federal NOL carryback must complete and attach to Maine Form 1120X-ME a pro forma federal Form 1139 (or similar schedule containing all of the information required by federal Form 1139) to support that entity's portion of the federal NOL deduction. Clearly mark the form "Maine pro forma."

The following modifications related to net operating losses are reported on the Maine corporate income tax return:

- 1) For loss years from 1982 through 2001, an addition equal to the amount of any federal loss which is carried back in accordance with IRC § 172 (36 M.R.S. § 5200-A(1)(B));
- 2) For tax years 1982 and later, the amount of any federal NOL deduction which was used to offset Maine income in the loss year (36 M.R.S. § 5200-A(1)(C));
- 3) For tax years beginning in 2008, 10% of any federal NOL carryforward in excess of \$100,000 (36 M.R.S. § 5200-A(1)(U)). This addition modification is recaptured through a subtraction modification in years 2009 and later (36 M.R.S. § 5200-A(2)(S));

- 4) For tax years beginning in 2009, 2010 and 2011, the amount of any federal NOL carryforward (36 M.R.S. § 5200-A(1)(V)). This addition modification is recaptured through a subtraction modification in years 2012 and later (36 M.R.S. § 5200-A(2)(T));
- 5) In the year to which an NOL is carried back, the amount of a federal loss originating in tax years 1989, 1990, 1991 or 1992 that is applied to that carryback year (36 M.R.S. § 5200-A(1)(H)). Except for tax years beginning in 2009, 2010 and 2011, this addition modification is recaptured through a subtraction modification in years subsequent to the loss year (36 M.R.S. § 5200-A(2)(H));
- 6) In the year to which an NOL is carried back, the amount of a federal loss originating in tax years 2002 or later that is applied to that carryback year (36 M.R.S. § 5200-A(1)(H)). Except for tax years beginning in 2009, 2010 and 2011, this addition modification is recaptured through a subtraction modification in years subsequent to the loss year (36 M.R.S. § 5200-A(2)(H));
- 7) In the year to which an NOL is carried back, the amount of a federal loss originating in a tax year ending or beginning in 2001 that is carried back more than two years (36 M.R.S. § 5200-A(1)(M)). This addition modification does not apply to 2001 losses carried back to 1999 or 2000 and does not apply to certain small businesses and farmers. Except for tax years beginning in 2009, 2010 and 2011, this addition modification is recaptured through a subtraction modification in years 2002 and later (36 M.R.S. § 5200-A(2)(L));

PART 1 – TAX YEARS AFTER 2011

For all tax years after 2001, Maine has decoupled from federal carryback provisions. Any federal carryback must be offset by an addition modification of the same amount in the year of the carryback. 36 M.R.S. § 5200-A(1)(H). Similarly, Maine disallowed carryforwards in 2009, 2010, and 2011 and any federal carryforward in those years must have been offset with a corresponding Maine addition modification.

The addition modifications for a federal carryback or carryforward can be recaptured in years subsequent to the year of the loss, excluding tax years 2009, 2010, and 2011, through subtraction modifications. 36 M.R.S. §§ 5200-A(2)(H), 5200-A(2)(L) and 5200-A(2)(T). The recapture modifications must be reduced by any Maine income that is offset in the year of the loss. NOL recapture subtractions denied for tax years beginning in 2009, 2010, and 2011 can be claimed beginning with the 2012 tax year. The allowable carryover period for suspended losses and suspended recapture subtraction modifications is extended by the number of years the subtraction modification was suspended.

To maximize the benefit of an NOL recapture carryforward, a taxpayer may utilize only the recapture deduction amount needed to reduce taxable income so that there is no income tax liability after the application of other deductions and tax credits. Any remaining NOL recapture can be carried forward to additional future years within the allowable carryover period.

For tax years beginning on or after January 1, 2018, Maine law conforms to the federal tax treatment of NOL carryforward deductions allowed under IRC § 172. Under that provision, the NOL carryforward deduction for tax years beginning on or after January 1, 2021 with respect to NOLs arising in tax years beginning after December 31, 2017 is limited to 80% of adjusted federal taxable income. Below are the statutory paragraphs related to NOL modifications in effect for tax years after 2011.

§5200-A. Modifications

1. Additions. The taxable income of the taxpayer under the laws of the United States shall be increased by:

C. The amount of any deduction claimed for the taxable year under the Code, Section 172, which has previously been used to offset the modifications provided by this subsection;

H. The absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 1989 but before January 1, 1993 and the absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 2002 that, pursuant to the United States Internal Revenue Code, Section 172, are being carried back for federal income tax purposes to the taxable year by the taxpayer;

M. The absolute value of the amount of any net operating loss arising from a tax year beginning or ending in 2001 that the taxpayer, pursuant to Section 102 of the federal Job Creation and Worker Assistance Act of 2002, Public Law 107-147, carries back more than 2 years to the taxable year for federal income tax purposes;

U. For tax years beginning in 2008, 10% of the absolute value in excess of \$100,000 of any net operating loss that, pursuant to the Code, Section 172, is being carried over for federal income tax purposes to the taxable year by the taxpayer;

V. For any taxable year beginning in 2009, 2010 or 2011, an amount equal to the absolute value of any net operating loss carry-forward claimed for purposes of the federal income tax;

2. Subtractions. The taxable income of the taxpayer under the laws of the United States shall be decreased by:

H. For each taxable year subsequent to the year of the loss, an amount equal to the absolute value of the net operating loss arising from tax years beginning on or after January 1, 1989 but before January 1, 1993 and the absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 2002, for which federal taxable income was increased under subsection 1, paragraph H and that, pursuant to the Code, Section 172, was carried back for federal income tax purposes, less the absolute value of loss used in the taxable year of loss to offset any addition modification required by subsection 1, but only to the extent that:

(1) Maine taxable income is not reduced below zero;

(2) The taxable year is within the allowable federal period for carry-over;

(3) The amount has not been previously used as a modification pursuant to this subsection;

(4) For taxable years beginning in 2008, the amount does not exceed \$100,000. In the case of an affiliated group of corporations engaged in a unitary business, the \$100,000 threshold applies with respect to the entire affiliated group of corporations; and

(5) The modification under this paragraph is not claimed for any tax year beginning in 2009, 2010 or 2011. The amount not deducted as the result of the restriction with respect to tax years beginning in 2009, 2010 or 2011 may be deducted in any tax year beginning after December 31, 2011, but only to the extent that the requirements of subparagraphs (1) and (3) are met and the taxable year is within the allowable federal period for carry-over plus the number of years that the net operating loss carry-over adjustment was not deducted as a result of the restriction with respect to tax years beginning in 2009, 2010 or 2011;

L. An amount equal to the absolute value of any net operating loss arising from a tax year beginning or ending in 2001 for which federal taxable income was increased under subsection 1, paragraph M and that, pursuant to Section 102 of the federal Job Creation and Worker Assistance Act of 2002, Public Law 107-147, was carried back more than 2 years to the taxable year for federal income tax purposes, but only to the extent that:

(1) Maine taxable income is not reduced below zero;

(2) The taxable year is either within 2 years prior to the year in which the loss arose or within the allowable federal period for carry-over of net operating losses;

(3) The amount has not been previously used as a modification pursuant to this subsection;

(4) For taxable years beginning in 2008, the amount does not exceed \$100,000. In the case of an affiliated group of corporations engaged in a unitary business, the \$100,000 threshold applies with respect to the entire affiliated group of corporations; and

(5) The modification under this paragraph is not claimed for any tax year beginning in 2009, 2010 or 2011. The amount not deducted as the result of the restriction with respect to tax years beginning in 2009, 2010 or 2011 may be deducted in any tax year beginning after December 31, 2011, but only to the extent that the requirements of subparagraphs (1) and (3) are met and the taxable year is within the allowable federal period for carry-over plus the number of years that the net operating loss carry-over adjustment was not deducted as a result of the restriction with respect to tax years beginning in 2009, 2010 or 2011;

S. An amount equal to the value of any prior year addition modification under subsection 1, paragraph U, but only to the extent that:

(1) Maine taxable income is not reduced below zero;

(2) The taxable year is within the allowable federal period for carryover of the net operating loss plus one year; and

(3) The amount has not been previously used as a modification pursuant to this subsection;

T. An amount equal to the value of any prior year addition modification under subsection 1, paragraph V, but only to the extent that:

(1) Maine taxable income is not reduced below zero;

(2) The taxable year is within the allowable federal period for carry-over plus the number of years that the net operating loss carry-over adjustment was not deducted as a result of the restriction with respect to tax years beginning in 2009, 2010 and 2011;

- (3) The amount has not been previously used as a modification pursuant to this subsection; and
- (4) The modification under this paragraph is not claimed for any tax year beginning in 2009, 2010 or 2011;

Examples

Example #1.1 – NOL in 2018, all of the loss is carried forward

The taxpayer has a federal net operating loss of \$65,000 in tax year 2020. The 2020 loss is available to offset Maine addition modifications. In this example, \$5,000 of Maine income in 2020 is offset by the federal loss. In order to prevent that portion of the federal loss used to offset Maine income from also reducing income in a carryforward year, Maine requires an adjustment. The entire amount of the loss is carried forward; federally, \$20,000 is applied to 2021 and \$45,000 to 2022. An addition modification of \$5,000 is required to reflect the appropriate amount of carryforward remaining available for 2022.

| | <u>2018</u> | <u>2019</u> | <u>2020</u> | <u>2021</u> | <u>2022</u> |
|-----------------------------------|--------------------|--------------------|--------------------|--------------------|--------------------|
| Federal income prior to NOL | \$40,000 | \$50,000 | (\$65,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | <u> </u> | <u> </u> | <u> </u> | (\$20,000) | (\$45,000) |
| Federal taxable income | \$40,000 | \$50,000 | (\$65,000) | \$5,000 | \$25,000 |
| Maine unrelated modification | | | \$5,000 | | |
| NOL Modifications: § 5200-A(1)(C) | | | | | \$5,000 |
| Maine taxable income | <u>\$40,000</u> | <u>\$50,000</u> | <u>(\$60,000)</u> | <u>\$5,000</u> | <u>\$30,000</u> |

Example #1.2 – NOL in 2018, all of the loss is carried back

The taxpayer has a federal net operating loss of \$75,000 in tax year 2018. Federally, \$50,000 of the loss is carried back to 2017. To reverse the federal carryback, a \$50,000 Maine addition modification is entered in the column for tax year 2017. The addition modification is recaptured as subtraction modifications of \$40,000 for tax year 2020 and \$10,000 for 2021. Because the federal loss did not offset any Maine addition modifications in 2018, no addition modifications are required in tax years 2019 through 2021.

| | <u>2017</u> | <u>2018</u> | <u>2019</u> | <u>2020</u> | <u>2021</u> |
|-----------------------------------|--------------------|--------------------|--------------------|--------------------|--------------------|
| Federal income prior to NOL | \$50,000 | (\$75,000) | \$25,000 | \$40,000 | \$30,000 |
| NOL carryback/carryforward | (\$50,000) | <u> </u> | (\$25,000) | <u> </u> | <u> </u> |
| Federal taxable income | \$0 | (\$75,000) | \$0 | \$40,000 | \$30,000 |
| NOL Modifications: § 5200-A(1)(H) | \$50,000 | | | | |
| § 5200-A(2)(H) | | | (\$0) | (\$40,000) | (\$10,000) |
| Maine taxable income | <u>\$50,000</u> | <u>(\$75,000)</u> | <u>\$0</u> | <u>\$0</u> | <u>\$20,000</u> |

Example #1.3 – NOL in 2018, some of the loss is carried back, some is carried forward

The taxpayer has a federal net operating loss of \$80,000 in tax year 2018. Part of the loss (\$30,000) is carried back to 2017. The remaining loss (\$50,000) is carried forward; \$20,000 is applied to 2019 and \$30,000 to 2020. To reverse the federal carryback, a \$30,000 addition modification is entered in the column for tax year 2017. The addition modification in 2017 is recaptured as subtraction modifications of \$10,000 for 2020 and \$20,000 for 2021.

| | <u>2017</u> | <u>2018</u> | <u>2019</u> | <u>2020</u> | <u>2021</u> |
|-----------------------------------|-----------------|-------------------|-------------|-------------|----------------|
| Federal income prior to NOL | \$30,000 | (\$80,000) | \$20,000 | \$40,000 | \$20,000 |
| NOL carryback/carryforward | (\$30,000) | | (\$20,000) | (\$30,000) | |
| Federal taxable income | \$0 | (\$80,000) | \$0,000 | \$10,000 | \$20,000 |
| NOL Modifications: § 5200-A(1)(H) | \$30,000 | | | | |
| § 5200-A(2)(H) | | | | (\$10,000) | (\$20,000) |
| Maine taxable income | <u>\$30,000</u> | <u>(\$80,000)</u> | <u>\$0</u> | <u>\$0</u> | <u>\$0,000</u> |

Example #1.4 – NOL in 2018, some of the loss is carried back, some is carried forward

The taxpayer has a federal net operating loss of \$80,000 in tax year 2018. Part of the loss (\$55,000) is carried back; \$15,000 is applied to 2016 and \$40,000 to 2017. The remaining loss (\$25,000) is carried forward; \$20,000 to 2019 and \$5,000 to 2020. To reverse the federal carrybacks, a \$15,000 Maine addition modification is entered in the column for tax year 2016 and a \$40,000 addition modification is entered in the column for tax year 2017. The 2018 loss is available to offset Maine addition modifications. In this example, \$5,000 of Maine income in 2018 is offset by the federal loss. In order to prevent that portion of the federal loss used to offset Maine income from also reducing income in a carryforward year, Maine requires an adjustment. The recapture subtraction modification related to the carryback offsets in 2016 and 2017 must be reduced by the amount of addition modification offset in the loss year. In this example, the \$55,000 recapture modification must be reduced by \$5,000, resulting in subtraction modifications of \$0 in 2019, \$35,000 in 2020, and \$15,000 in 2021. In this example, the recapture reduction under section 5200-A(2)(H) prevents the taxpayer from avoiding tax on the \$5,000 unrelated modification in 2018 and also reducing income in the carryforward years by the full carryback recapture.

| | <u>2016</u> | <u>2017</u> | <u>2018</u> | <u>2019</u> | <u>2020</u> | <u>2021</u> |
|-----------------------------------|-----------------|-----------------|-------------------|-------------|-------------|-----------------|
| Federal income prior to NOL | \$15,000 | \$40,000 | (\$80,000) | \$20,000 | \$40,000 | \$30,000 |
| NOL carryback/carryforward | (\$15,000) | (\$40,000) | | (\$20,000) | (\$5,000) | |
| Federal taxable income | \$0 | \$0 | (\$80,000) | \$0 | \$35,000 | \$30,000 |
| Maine unrelated modification | | | \$5,000 | | | |
| NOL Modifications: § 5200-A(1)(H) | \$15,000 | \$40,000 | | | | |
| § 5200-A(2)(H) | | | | | (\$35,000) | (\$15,000) |
| Maine taxable income | <u>\$15,000</u> | <u>\$40,000</u> | <u>(\$75,000)</u> | <u>\$0</u> | <u>\$0</u> | <u>\$15,000</u> |

PART 2 – TAX YEARS 2009, 2010, AND 2011

For all tax years after 2001, Maine has decoupled from federal carryback provisions. Any federal carryback must be offset by an addition modification of the same amount in the year of the carryback. 36 M.R.S. § 5200-A(1)(H). Similarly, Maine disallows carryforwards in 2009, 2010, and 2011 and any federal carryforward in those years must also be offset by a corresponding addition modification. The addition modifications for a federal carryback or carryforward can be recaptured in years subsequent to the year of the loss, beginning with tax year 2012, through subtraction modifications. 36 M.R.S. §§ 5200-A(2)(H), 5200-A(2)(L) and 5200-A(2)(T). The recapture modifications must be reduced by any Maine income that is offset in the year of the loss. In addition, for tax years beginning in 2009, 2010, and 2011, most NOL recapture subtraction modifications are suspended until 2012. The one exception to the recapture suspensions is the modification for limitations of federal carryforwards in excess of \$100,000 for tax year 2008. These limitations may be recaptured beginning in tax year 2009. The allowable carryover period for suspended losses and suspended recapture subtraction modifications is extended by the number of years the subtraction modification is suspended. Below are the statutory paragraphs related to NOL modifications in effect for tax years beginning in 2009, 2010, and 2011.

§5200-A. Modifications

1. Additions. The taxable income of the taxpayer under the laws of the United States shall be increased by:

C. The amount of any deduction claimed for the taxable year under the Code, Section 172, which has previously been used to offset the modifications provided by this subsection;

H. The absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 1989 but before January 1, 1993 and the absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 2002 that, pursuant to the United States Internal Revenue Code, Section 172, are being carried back for federal income tax purposes to the taxable year by the taxpayer;

M. The absolute value of the amount of any net operating loss arising from a tax year beginning or ending in 2001 that the taxpayer, pursuant to Section 102 of the federal Job Creation and Worker Assistance Act of 2002, Public Law 107-147, carries back more than 2 years to the taxable year for federal income tax purposes;

U. For tax years beginning in 2008, 10% of the absolute value in excess of \$100,000 of any net operating loss that, pursuant to the Code, Section 172, is being carried over for federal income tax purposes to the taxable year by the taxpayer;

V. For any taxable year beginning in 2009, 2010 or 2011, an amount equal to the absolute value of any net operating loss carry-forward claimed for purposes of the federal income tax;

2. *Subtractions. The taxable income of the taxpayer under the laws of the United States shall be decreased by:*

H. For each taxable year subsequent to the year of the loss, an amount equal to the absolute value of the net operating loss arising from tax years beginning on or after January 1, 1989 but before January 1, 1993 and the absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 2002, for which federal taxable income was increased under subsection 1, paragraph H and that, pursuant to the Code, Section 172, was carried back for federal income tax purposes, less the absolute value of loss used in the taxable year of loss to offset any addition modification required by subsection 1, but only to the extent that:

- (1) Maine taxable income is not reduced below zero;*
- (2) The taxable year is within the allowable federal period for carry-over;*
- (3) The amount has not been previously used as a modification pursuant to this subsection;*
- (4) For taxable years beginning in 2008, the amount does not exceed \$100,000. In the case of an affiliated group of corporations engaged in a unitary business, the \$100,000 threshold applies with respect to the entire affiliated group of corporations; and*
- (5) The modification under this paragraph is not claimed for any tax year beginning in 2009, 2010 or 2011. The amount not deducted as the result of the restriction with respect to tax years beginning in 2009, 2010 or 2011 may be deducted in any tax year beginning after December 31, 2011, but only to the extent that the requirements of subparagraphs (1) and (3) are met and the taxable year is within the allowable federal period for carry-over plus the number of years that the net operating loss carry-over adjustment was not deducted as a result of the restriction with respect to tax years beginning in 2009, 2010 or 2011;*

L. An amount equal to the absolute value of any net operating loss arising from a tax year beginning or ending in 2001 for which federal taxable income was increased under subsection 1, paragraph M and that, pursuant to Section 102 of the federal Job Creation and Worker Assistance Act of 2002, Public Law 107-147, was carried back more than 2 years to the taxable year for federal income tax purposes, but only to the extent that:

- (1) Maine taxable income is not reduced below zero;*
- (2) The taxable year is either within 2 years prior to the year in which the loss arose or within the allowable federal period for carry-over of net operating losses;*
- (3) The amount has not been previously used as a modification pursuant to this subsection;*
- (4) For taxable years beginning in 2008, the amount does not exceed \$100,000. In the case of an affiliated group of corporations engaged in a unitary business, the \$100,000 threshold applies with respect to the entire affiliated group of corporations; and*
- (5) The modification under this paragraph is not claimed for any tax year beginning in 2009, 2010 or 2011. The amount not deducted as the result of the restriction with respect to tax years beginning in 2009, 2010 or 2011 may be deducted in any tax year beginning after December 31,*

2011, but only to the extent that the requirements of subparagraphs (1) and (3) are met and the taxable year is within the allowable federal period for carry-over plus the number of years that the net operating loss carry-over adjustment was not deducted as a result of the restriction with respect to tax years beginning in 2009, 2010 or 2011;

S. An amount equal to the value of any prior year addition modification under subsection 1, paragraph U, but only to the extent that:

(1) Maine taxable income is not reduced below zero;

(2) The taxable year is within the allowable federal period for carryover of the net operating loss plus one year; and

(3) The amount has not been previously used as a modification pursuant to this subsection;

T. An amount equal to the value of any prior year addition modification under subsection 1, paragraph V, but only to the extent that:

(1) Maine taxable income is not reduced below zero;

(2) The taxable year is within the allowable federal period for carry-over plus the number of years that the net operating loss carry-over adjustment was not deducted as a result of the restriction with respect to tax years beginning in 2009, 2010 and 2011;

(3) The amount has not been previously used as a modification pursuant to this subsection; and

(4) The modification under this paragraph is not claimed for any tax year beginning in 2009, 2010 or 2011;

Examples

Example #2.1 – NOL in 2008, all of the loss is carried forward

The taxpayer has a federal net operating loss of \$90,000 in tax year 2008. The entire amount of the loss is carried forward; \$25,000 is applied to 2009 and \$65,000 to 2010. All federal carryovers are deferred from tax years 2009, 2010, and 2011 to tax years 2012 and after. A \$25,000 Maine addition modification is entered in the column for tax year 2009 and a \$65,000 addition modification is entered in the column for tax year 2010. 36 M.R.S. § 5200-A(1)(V). These addition modifications may be recaptured in 2012 and later years. Here, the \$90,000 total additions in 2009 and 2010 are recaptured with a subtraction modification in the column for tax year 2012. Because the federal loss did not offset any Maine addition modifications in 2008, no other Maine adjustment is required.

| | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>2009</u> | <u>2010</u> | <u>2011</u> | <u>2012</u> |
|-----------------------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Federal income prior to NOL | \$40,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 | \$80,000 | \$90,000 |
| NOL carryback/carryforward | | | | (\$25,000) | (\$65,000) | | |
| Federal taxable income | \$40,000 | \$50,000 | (\$90,000) | \$0 | \$5,000 | \$80,000 | \$90,000 |
| NOL Modifications: | | | | \$25,000 | \$65,000 | | |
| § 5200-A(1)(V) | | | | | | | |
| § 5200-A(2)(T) | | | | | | | (\$90,000) |
| Maine taxable income | \$40,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 | \$80,000 | \$0 |

Example #2.2 – NOL in 2008, all of the loss is carried back

The taxpayer has a federal net operating loss of \$90,000 in tax year 2008. The entire loss is carried back; \$40,000 is applied to 2006 and \$50,000 to 2007. To reverse the federal carrybacks, a \$40,000 Maine addition modification is entered in the column for tax year 2006 and a \$50,000 addition modification is entered in the column for tax year 2007. The addition modifications in 2006 and 2007 are recaptured as a subtraction modification of \$90,000 in the column for tax year 2012, the first year that the subtraction modification is allowed.

| | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>2009</u> | <u>2010</u> | <u>2011</u> | <u>2012</u> |
|-----------------------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Federal income prior to NOL | \$40,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 | \$80,000 | \$90,000 |
| NOL carryback/carryforward | (\$40,000) | (\$50,000) | | | | | |
| Federal taxable income | \$0 | \$0 | (\$90,000) | \$25,000 | \$70,000 | \$80,000 | \$90,000 |
| NOL Modifications: | | | | | | | |
| § 5200-A(1)(H) | \$40,000 | \$50,000 | | | | | |
| § 5200-A(2)(H) | | | | | | | (\$90,000) |
| Maine taxable income | \$40,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 | \$80,000 | \$0 |

Example #2.3 – NOL in 2008, some of the loss is carried back, some is carried forward

The taxpayer has a federal net operating loss of \$90,000 in tax year 2008. Part of the loss (\$70,000) is carried back; \$20,000 is applied to 2006 and \$50,000 to 2007. The remaining loss (\$20,000) is carried forward to 2009. To reverse the federal carrybacks, a \$20,000 Maine addition modification is entered in the column for tax year 2006 and a \$50,000 addition modification is entered in the column for tax year 2007. The addition modifications in 2006 and 2007 are recaptured as a subtraction modification of \$70,000 in the column for tax year 2012, the first year that the subtraction modification is allowed. The \$20,000 federal carryforward to 2009 must also be reversed through an addition modification in that year. The addition modification in 2009 is recaptured with a \$20,000 subtraction modification in the column for 2012.

| | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>2009</u> | <u>2010</u> | <u>2011</u> | <u>2012</u> |
|-----------------------------|-----------------|-----------------|-------------------|-----------------|-----------------|-----------------|-------------|
| Federal income prior to NOL | \$20,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 | \$80,000 | \$90,000 |
| NOL carryback/carryforward | (\$20,000) | (\$50,000) | _____ | (\$20,000) | _____ | _____ | _____ |
| Federal taxable income | \$0 | \$0 | (\$90,000) | \$5,000 | \$70,000 | \$80,000 | \$90,000 |
| NOL Modifications: | | | | | | | |
| § 5200-A(1)(H) | \$20,000 | \$50,000 | | | | | |
| § 5200-A(1)(V) | | | | \$20,000 | | | |
| § 5200-A(2)(H) | | | | | | | (\$70,000) |
| § 5200-A(2)(T) | | | | | | | (\$20,000) |
| Maine taxable income | \$20,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 | \$80,000 | \$0 |

Example #2.4 – NOL in 2008, some of the loss is carried back, some is carried forward

The taxpayer has a federal net operating loss of \$90,000 in tax year 2008. Part of the loss (\$70,000) is carried back; \$20,000 is applied to 2006 and \$50,000 to 2007. The remaining loss (\$20,000) is carried forward to 2009. To reverse the federal carrybacks, a \$20,000 Maine addition modification is entered in the column for tax year 2006 and a \$50,000 addition modification is entered in the column for tax year 2007. The 2008 loss is available to offset unrelated Maine addition modifications. In this example, \$5,000 of Maine income in 2008 is offset by the federal loss. In order to prevent that portion of the federal loss used to offset Maine income from also reducing income in a carryforward year, Maine requires an adjustment. The recapture subtraction modification related to the carryback offsets in 2006 and 2007 must be reduced by the amount of addition modification offset in the loss year. In this example, the \$70,000 recapture modification must be reduced by \$5,000, resulting in a subtraction modification of \$65,000 in 2012. The \$20,000 federal carryforward to 2009 must also be reversed through an addition modification in that year. The addition modification in 2009 is recaptured with a \$20,000 subtraction modification in the column for 2012. In this example, the recapture reduction under section 36 M.R.S. § 5200-A(2)(H) keeps the taxpayer from avoiding tax on the \$5,000 unrelated modification in 2008 and also reducing income in 2012 by the full carryback recapture.

| | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>2009</u> | <u>2010</u> | <u>2011</u> | <u>2012</u> |
|------------------------------|-----------------|-----------------|-------------------|-----------------|-----------------|-----------------|----------------|
| Federal income prior to NOL | \$20,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 | \$80,000 | \$90,000 |
| NOL carryback/carryforward | (\$20,000) | (\$50,000) | _____ | (\$20,000) | _____ | _____ | _____ |
| Federal taxable income | \$0 | \$0 | (\$90,000) | \$5,000 | \$70,000 | \$80,000 | \$90,000 |
| Maine unrelated modification | | | \$5,000 | | | | |
| NOL Modifications: | | | | | | | |
| § 5200-A(1)(H) | \$20,000 | \$50,000 | | | | | |
| § 5200-A(1)(V) | | | | \$20,000 | | | |
| § 5200-A(2)(H) | | | | | | | (\$65,000) |
| § 5200-A(2)(T) | | | | | | | (\$20,000) |
| Maine taxable income | \$20,000 | \$50,000 | (\$85,000) | \$25,000 | \$70,000 | \$80,000 | \$5,000 |

PART 3 –TAX YEAR 2008

For all tax years after 2001, Maine has decoupled from federal carryback provisions. Any federal carryback must be offset by an addition modification of the same amount in the year of the carryback. 36 M.R.S. § 5200-A(1)(H). The addition modification can be recaptured in years subsequent to the year of the loss through a recapture subtraction modification. 36 M.R.S. § 5200-A(2)(H). The recapture modification must be reduced by any Maine income that is offset in the year of the loss. For tax years beginning in 2008, federal NOL carryover amounts in excess of \$100,000 are reduced (through an addition modification) by 10% of the carryover amount that exceeds \$100,000. 36 M.R.S. § 5200-A(1)(U). The denied federal carryover amounts may be recaptured beginning in 2009. 36 M.R.S. § 5200-A(2)(S). Also for tax years beginning in 2008, NOL recapture modifications are limited to \$100,000. 36 M.R.S. § 5200-A(2)(H)(4). The disallowed recapture amounts may be recaptured beginning with the 2012 tax year. 36 M.R.S. § 5200-A(2)(H)(5). Below are the statutory paragraphs related to NOL modifications in effect for tax year 2008.

§5200-A. Modifications

1. Additions. The taxable income of the taxpayer under the laws of the United States shall be increased by:

C. The amount of any deduction claimed for the taxable year under the Code, Section 172, which has previously been used to offset the modifications provided by this subsection;

H. The absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 1989 but before January 1, 1993 and the absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 2002 that, pursuant to the United States Internal Revenue Code, Section 172, are being carried back for federal income tax purposes to the taxable year by the taxpayer;

M. The absolute value of the amount of any net operating loss arising from a tax year beginning or ending in 2001 that the taxpayer, pursuant to Section 102 of the federal Job Creation and Worker Assistance Act of 2002, Public Law 107-147, carries back more than 2 years to the taxable year for federal income tax purposes;

U. For tax years beginning in 2008, 10% of the absolute value in excess of \$100,000 of any net operating loss that, pursuant to the Code, Section 172, is being carried over for federal income tax purposes to the taxable year by the taxpayer;

V. For any taxable year beginning in 2009, 2010 or 2011, an amount equal to the absolute value of any net operating loss carry-forward claimed for purposes of the federal income tax;

2. Subtractions. The taxable income of the taxpayer under the laws of the United States shall be decreased by:

H. For each taxable year subsequent to the year of the loss, an amount equal to the absolute value of the net operating loss arising from tax years beginning on or after January 1, 1989 but before

January 1, 1993 and the absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 2002, for which federal taxable income was increased under subsection 1, paragraph H and that, pursuant to the Code, Section 172, was carried back for federal income tax purposes, less the absolute value of loss used in the taxable year of loss to offset any addition modification required by subsection 1, but only to the extent that:

- (1) Maine taxable income is not reduced below zero;*
- (2) The taxable year is within the allowable federal period for carry-over;*
- (3) The amount has not been previously used as a modification pursuant to this subsection;*
- (4) For taxable years beginning in 2008, the amount does not exceed \$100,000. In the case of an affiliated group of corporations engaged in a unitary business, the \$100,000 threshold applies with respect to the entire affiliated group of corporations; and*
- (5) The modification under this paragraph is not claimed for any tax year beginning in 2009, 2010 or 2011. The amount not deducted as the result of the restriction with respect to tax years beginning in 2009, 2010 or 2011 may be deducted in any tax year beginning after December 31, 2011, but only to the extent that the requirements of subparagraphs (1) and (3) are met and the taxable year is within the allowable federal period for carry-over plus the number of years that the net operating loss carry-over adjustment was not deducted as a result of the restriction with respect to tax years beginning in 2009, 2010 or 2011;*

L. An amount equal to the absolute value of any net operating loss arising from a tax year beginning or ending in 2001 for which federal taxable income was increased under subsection 1, paragraph M and that, pursuant to Section 102 of the federal Job Creation and Worker Assistance Act of 2002, Public Law 107-147, was carried back more than 2 years to the taxable year for federal income tax purposes, but only to the extent that:

- (1) Maine taxable income is not reduced below zero;*
- (2) The taxable year is either within 2 years prior to the year in which the loss arose or within the allowable federal period for carry-over of net operating losses;*
- (3) The amount has not been previously used as a modification pursuant to this subsection;*
- (4) For taxable years beginning in 2008, the amount does not exceed \$100,000. In the case of an affiliated group of corporations engaged in a unitary business, the \$100,000 threshold applies with respect to the entire affiliated group of corporations; and*
- (5) The modification under this paragraph is not claimed for any tax year beginning in 2009, 2010 or 2011. The amount not deducted as the result of the restriction with respect to tax years beginning in 2009, 2010 or 2011 may be deducted in any tax year beginning after December 31, 2011, but only to the extent that the requirements of subparagraphs (1) and (3) are met and the taxable year is within the allowable federal period for carry-over plus the number of years that the net operating loss carry-over adjustment was not deducted as a result of the restriction with respect to tax years beginning in 2009, 2010 or 2011;*

S. An amount equal to the value of any prior year addition modification under subsection 1, paragraph U, but only to the extent that:

- (1) Maine taxable income is not reduced below zero;
- (2) The taxable year is within the allowable federal period for carryover of the net operating loss plus one year; and
- (3) The amount has not been previously used as a modification pursuant to this subsection;

T. An amount equal to the value of any prior year addition modification under subsection 1, paragraph V, but only to the extent that:

- (1) Maine taxable income is not reduced below zero;
- (2) The taxable year is within the allowable federal period for carry-over plus the number of years that the net operating loss carry-over adjustment was not deducted as a result of the restriction with respect to tax years beginning in 2009, 2010 and 2011;
- (3) The amount has not been previously used as a modification pursuant to this subsection; and
- (4) The modification under this paragraph is not claimed for any tax year beginning in 2009, 2010 or 2011;

Examples

Example #3.1 – NOL in 2007, all of the loss is carried forward

The taxpayer has a federal net operating loss of \$125,000 in tax year 2007. The entire amount of the loss is carried forward to 2008. Because the allowable amount of carryforward in 2008 is limited, an addition modification of \$2,500 is required in 2008. The addition modification is equal to ten percent of the carryforward amount in excess of \$100,000 ($\$25,000 \times 0.10 = \$2,500$). This addition is recaptured through a \$2,500 subtraction modification in 2009. Because the federal loss did not offset any Maine addition modifications in 2007, no other Maine adjustment is required in 2008.

| | 2005 | 2006 | 2007 | 2008 | 2009 |
|-----------------------------------|-------------|-------------|-------------|-------------|-------------|
| Federal income prior to NOL | \$40,000 | \$50,000 | (\$125,000) | \$125,000 | \$70,000 |
| NOL carryback/carryforward | | | | (\$125,000) | |
| Federal taxable income | \$40,000 | \$50,000 | (\$125,000) | \$0 | \$70,000 |
| NOL Modifications: § 5200-A(1)(U) | | | | \$2,500 | |
| § 5200-A(2)(S) | | | | | (\$2,500) |
| Maine taxable income | \$40,000 | \$50,000 | (\$125,000) | \$2,500 | \$67,500 |

Example #3.2 – NOL in 2007, all of the loss is carried back

The taxpayer has a federal net operating loss of \$125,000 in tax year 2007. The entire loss is carried back; \$75,000 is applied to 2005 and \$50,000 to 2006. To reverse the federal carrybacks, a \$75,000 Maine addition modification is entered in the column for tax year 2005 and a \$50,000 addition modification is entered in the column for tax year 2006. The addition modifications in 2005 and 2006 may be recaptured through subtraction modifications in years following 2007. In 2008, the recapture is limited to \$100,000. The remaining \$25,000 recapture is postponed to 2012 because most NOL subtraction modifications are disallowed for tax years 2009, 2010 and 2011. The exception to the disallowed modifications is the recapture of the addition related to the limitation of federal carryforwards in excess of \$100,000 for tax year 2008. See example #4.1.

| | <u>2005</u> | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>2009</u> |
|-----------------------------------|----------------|----------------|-------------------|----------------|----------------|
| Federal Income prior to NOL | \$75,000 | \$50,000 | (\$125,000) | \$125,000 | \$70,000 |
| NOL carryback/carryforward | (\$75,000) | (\$50,000) | _____ | _____ | _____ |
| Federal Taxable Income | \$0 | \$0 | (\$125,000) | \$125,000 | \$70,000 |
| NOL Modifications: § 5200-A(1)(H) | \$75,000 | \$50,000 | | | |
| § 5200-A(2)(H) | | | | (\$100,000) | |
| Maine taxable income | <hr/> \$75,000 | <hr/> \$50,000 | <hr/> (\$125,000) | <hr/> \$25,000 | <hr/> \$70,000 |

Example #3.3 – NOL in 2007, some of the loss is carried back, some is carried forward

The taxpayer has a federal net operating loss of \$125,000 in tax year 2007. Part of the loss (\$70,000) is carried back; \$20,000 is applied to 2005 and \$50,000 to 2006. The remaining \$55,000 loss is carried forward to 2008. To reverse the federal carrybacks, a \$20,000 Maine addition modification is entered in the column for tax year 2005 and a \$50,000 addition modification is entered in the column for tax year 2006. The addition modifications in 2005 and 2006 are recaptured as a subtraction modification of \$70,000 in the column for tax year 2008. Although the total federal carryover plus the recapture for 2008 exceed \$100,000, no adjustment is necessary because the separate amounts are each below that threshold.

| | <u>2005</u> | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>2009</u> |
|----------------------------------|----------------|----------------|-------------------|-------------|----------------|
| Federal Income prior to NOL | \$20,000 | \$50,000 | (\$125,000) | \$125,000 | \$70,000 |
| NOL carryback/carryforward | (\$20,000) | (\$50,000) | _____ | (\$55,000) | _____ |
| Federal Taxable Income | \$0 | \$0 | (\$125,000) | \$70,000 | \$70,000 |
| NOL Modification: § 5200-A(1)(H) | \$20,000 | \$50,000 | | | |
| § 5200-A(2)(H) | | | | (\$70,000) | |
| Maine taxable income | <hr/> \$20,000 | <hr/> \$50,000 | <hr/> (\$125,000) | <hr/> \$0 | <hr/> \$70,000 |

Example #3.4 – NOL in 2007, some of the loss is carried back, some is carried forward

The taxpayer has a federal net operating loss of \$125,000 in tax year 2007. Part of the loss (\$70,000) is carried back; \$20,000 is applied to 2005 and \$50,000 to 2006. The remaining \$55,000 loss is carried forward to 2008. To reverse the federal carrybacks, a \$20,000 Maine addition modification is entered in the column for tax year 2005 and a \$50,000 addition modification is entered in the column for tax year 2006. In this example, \$5,000 of Maine income in 2007 is offset by the federal loss. In order to prevent that portion of the federal loss used to offset Maine income from also reducing income in a carryforward year, Maine requires an adjustment. The recapture subtraction modification related to the carryback offset in 2005 and 2006 must be reduced by the amount of addition modification offset in the loss year. In this example, the \$70,000 recapture modification must be reduced by \$5,000, resulting in a subtraction modification of \$65,000 in 2008. Although the total federal carryover plus the recapture for 2008 exceed \$100,000, no adjustment is necessary because the separate amounts are each below that threshold. In this example, the recapture reduction under section 36 M.R.S. § 5200-A(2)(H) keeps the taxpayer from avoiding tax on the \$5,000 unrelated modification in 2007 and also reducing income in future years by the full carryback recapture.

| | 2005 | 2006 | 2007 | 2008 | 2009 |
|--|-------------------|-------------------|-------------------|-------------------|----------------|
| Federal Income prior to NOL | \$20,000 | \$50,000 | (\$125,000) | \$125,000 | \$70,000 |
| NOL carryback/carryforward | <u>(\$20,000)</u> | <u>(\$50,000)</u> | _____ | <u>(\$55,000)</u> | _____ |
| Federal Taxable Income | \$0 | \$0 | (\$125,000) | \$70,000 | \$70,000 |
| Maine unrelated modifications | (\$3,000) | \$4,000 | \$5,000 | (\$3,000) | \$7,000 |
| NOL Modifications: § 5200-A(1)(H) | \$20,000 | \$50,000 | | | |
| § 5200-A(2)(H) | | | | (\$65,000) | |
| Maine taxable income | <hr/> \$17,000 | <hr/> \$54,000 | <hr/> (\$120,000) | <hr/> \$2,000 | <hr/> \$77,000 |

PART 4 –TAX YEARS 2002 THROUGH 2007

For tax years beginning on or after January 1, 2002, Maine decoupled from the Internal Revenue Code regarding net operating loss carrybacks. Unlike prior years, the taxpayer was no longer required to add to income an amount equal to the total NOL incurred in the year of the loss and carried back federally, regardless of how many years the loss was carried back. Any federal carryback, however, was required to be offset by an addition modification in the year to which the carryback was applied. 36 M.R.S. § 5200-A(1)(H). A recapture of the carryback addition modification was allowed in years subsequent to the year of the loss. 36 M.R.S. § 5200- A(2)(H). Net operating loss modification recaptures are limited in tax years 2008 through 2011. For details about these restrictions, see Parts 4 and 5. Below are the statutory paragraphs related to NOL modifications in effect for tax years 2002 through 2007.

§5200-A. Modifications

1. Additions. The taxable income of the taxpayer under the laws of the United States shall be increased by:

C. The amount of any deduction claimed for the taxable year under the Code, Section 172, which has previously been used to offset the modifications provided by this subsection;

H. The absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 1989 but before January 1, 1993 and the absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 2002 that, pursuant to the United States Internal Revenue Code, Section 172, are being carried back for federal income tax purposes to the taxable year by the taxpayer;

M. The absolute value of the amount of any net operating loss arising from a tax year beginning or ending in 2001 that the taxpayer, pursuant to Section 102 of the federal Job Creation and Worker Assistance Act of 2002, Public Law 107-147, carries back more than 2 years to the taxable year for federal income tax purposes;

2. Subtractions. The taxable income of the taxpayer under the laws of the United States shall be decreased by:

H. For each taxable year subsequent to the year of the loss, an amount equal to the absolute value of the net operating loss arising from tax years beginning on or after January 1, 1989 but before January 1, 1993 and the absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 2002, for which federal taxable income was increased under subsection 1, paragraph H and that, pursuant to the Code, Section 172, was carried back for federal income tax purposes, less the absolute value of loss used in the taxable year of loss to offset any addition modification required by subsection 1, but only to the extent that:

(1) Maine taxable income is not reduced below zero;

- (2) The taxable year is within the allowable federal period for carry-over; and
- (3) The amount has not been previously used as a modification pursuant to this subsection;

L. An amount equal to the absolute value of any net operating loss arising from a tax year beginning or ending in 2001 for which federal taxable income was increased under subsection 1, paragraph M and that, pursuant to Section 102 of the federal Job Creation and Worker Assistance Act of 2002, Public Law 107-147, was carried back more than 2 years to the taxable year for federal income tax purposes, but only to the extent that:

- (1) Maine taxable income is not reduced below zero;
- (2) The taxable year is either within 2 years prior to the year in which the loss arose or within the allowable federal period for carry-over of net operating losses; and
- (3) The amount has not been previously used as a modification pursuant to this subsection;

Examples

Example #4.1 – NOL in 2005, all of the loss is carried forward

The taxpayer has a federal net operating loss of \$90,000 in tax year 2005. The entire amount of the loss is carried forward; \$25,000 is applied to 2006 and \$65,000 to 2007. Because the federal loss did not offset any unrelated Maine addition modifications in 2005, no Maine adjustment is required in 2006 or 2007.

| | 2003 | 2004 | 2005 | 2006 | 2007 |
|-------------------------------------|-------------|-------------|-------------|-------------|-------------|
| Federal income, prior to NOL | \$40,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | | | | (\$25,000) | (\$65,000) |
| Federal taxable income | \$40,000 | \$50,000 | (\$90,000) | \$0 | \$5,000 |
| Maine net/taxable income | \$40,000 | \$50,000 | (\$90,000) | \$0 | \$5,000 |

Example #4.2 – NOL in 2005, all of the loss is carried back

The taxpayer has a federal net operating loss of \$90,000 in tax year 2005. The entire loss is carried back; \$40,000 is applied to 2003 and \$50,000 to 2004. To reverse the federal carrybacks, a \$40,000 Maine addition modification is entered in the column for tax year 2003 and a \$50,000 addition modification is entered in the column for tax year 2004. The addition modifications in 2003 and 2004 are recaptured as subtraction modifications of \$25,000 in the column for tax year 2006 and \$65,000 for tax year 2007. Because the federal loss did not offset any unrelated Maine addition modifications in 2005, no other Maine adjustment is required in 2006 or 2007.

| | 2003 | 2004 | 2005 | 2006 | 2007 |
|-----------------------------------|-----------------|-----------------|-------------------|-------------|----------------|
| Federal Income prior to NOL | \$40,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | (\$40,000) | (\$50,000) | _____ | _____ | _____ |
| Federal Taxable Income | \$0 | \$0 | (\$90,000) | \$25,000 | \$70,000 |
| NOL Modifications: § 5200-A(1)(H) | \$40,000 | \$50,000 | | | |
| § 5200-A(2)(H) | | | | (\$25,000) | (\$65,000) |
| Maine net/taxable income | \$40,000 | \$50,000 | (\$90,000) | \$0 | \$5,000 |

Example #4.3 – NOL in 2005, some of the loss is carried back, some is carried forward

The taxpayer has a federal net operating loss of \$90,000 in tax year 2005. Part of the loss (\$70,000) is carried back; \$20,000 is applied to 2003 and \$50,000 to 2004. The remaining loss (\$20,000) is carried forward to 2006. To reverse the federal carrybacks, a \$20,000 Maine addition modification is entered in the column for tax year 2003 and a \$50,000 addition modification is entered in the column for tax year 2004. The addition modifications in 2003 and 2004 are recaptured as subtraction modifications of \$5,000 in the column for tax year 2006 and \$65,000 for tax year 2007. Because the federal loss did not offset any unrelated Maine addition modifications in 2005, no other Maine adjustment is required in 2006 or 2007.

| | 2003 | 2004 | 2005 | 2006 | 2007 |
|----------------------------------|-----------------|-----------------|-------------------|-------------|----------------|
| Federal Income prior to NOL | \$20,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | (\$20,000) | (\$50,000) | _____ | (\$20,000) | _____ |
| Federal Taxable Income | \$0 | \$0 | (\$90,000) | \$5,000 | \$70,000 |
| NOL Modification: § 5200-A(1)(H) | \$20,000 | \$50,000 | | | |
| § 5200-A(2)(H) | | | | (\$5,000) | (\$65,000) |
| Maine net/taxable income | \$20,000 | \$50,000 | (\$90,000) | \$0 | \$5,000 |

Example #4.4 – NOL in 2005, some of the loss is carried back, some is carried forward

The taxpayer has a federal net operating loss of \$90,000 in tax year 2005. Part of the loss (\$70,000) is carried back; \$20,000 is applied to 2003 and \$50,000 to 2004. The remaining loss (\$20,000) is carried forward to 2006. To reverse the federal carrybacks, a \$20,000 Maine addition modification is entered in the column for tax year 2003 and a \$50,000 addition modification is entered in the column for tax year 2004. Since no addition modification is necessary in 2005, the full amount of the federal loss is available to offset unrelated Maine addition modifications in that year. In this example, \$5,000 of Maine income in 2005 is offset by the federal loss. In order to prevent that portion of the federal loss used to offset Maine income in 2005 from also reducing income in a carryforward year, Maine requires an adjustment. The amount of the recapture subtraction modification claimed in 2007, which is related to the carryback offsets in 2003 and 2004, must be reduced by the amount of addition modification that is offset in the loss year. In this example, the \$70,000 recapture modification must be reduced by \$5,000, resulting in a subtraction modification of \$65,000 in the column for 2007. In this example, the recapture reduction under section 36 M.R.S. § 5200-A(2)(H) keeps the taxpayer from avoiding tax on the \$5,000 unrelated modification in 2005 and also reducing income in future years by the full carryback recapture. Notice that, in 2006, the NOL carryforward

combined with a Maine subtraction modification unrelated to the NOL results in a negative amount for Maine net income. Since Maine has no state-level NOL, negative income amounts have no effect on Maine income tax.

| | <u>2003</u> | <u>2004</u> | <u>2005</u> | <u>2006</u> | <u>2007</u> |
|--|--------------------|--------------------|--------------------|--------------------|--------------------|
| Federal Income prior to NOL | \$20,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | <u>(\$20,000)</u> | <u>(\$50,000)</u> | <u> </u> | <u>(\$20,000)</u> | <u> </u> |
| Federal Taxable Income | \$0 | \$0 | (\$90,000) | \$5,000 | \$70,000 |
| Maine unrelated modifications | (\$3,000) | \$4,000 | \$5,000 | (\$6,000) | \$7,000 |
| NOL Modifications: § 5200-A(1)(H) | \$20,000 | \$50,000 | | | |
| § 5200-A(2)(H) | | | | | (\$65,000) |
| Maine net/taxable income | <hr/> \$17,000 | <hr/> \$54,000 | <hr/> (\$85,000) | <hr/> (\$1,000) | <hr/> \$12,000 |

PART 5 –TAX YEAR 2001

For tax years beginning or ending in 2001, Maine was in conformity with the Internal Revenue Code regarding net operating losses carried back two years, but decoupled from federal carrybacks of more than two years. In the year of the loss, the taxpayer was required to add to income an amount equal to the total NOL incurred in that year and carried back federally. This addition modification was required under 36 M.R.S. § 5200-A(1)(B). A second addition modification was required for 2001 losses carried back to tax years 1996, 1997, or 1998. This carryback addition modification was equal to the amount of the federal NOL carried back and applied against income in those years. 36 M.R.S. § 5200-A(1)(M). A third addition modification was required in a carryforward year if a portion of the loss was carried forward federally and a Maine addition modification was offset in the loss year. 36 M.R.S. § 5200-A(1)(C) and Example #2.4. Below are the statutory paragraphs related to NOL modifications in effect for tax year 2001.

§5200-A. Modifications

1. Additions. The taxable income of the taxpayer under the laws of the United States shall be increased by:

B. The amount of any net operating loss in the taxable year which has been carried back to previous taxable years pursuant to the Code, Section 172;

C. The amount of any deduction claimed for the taxable year under the Code, Section 172, which has previously been used to offset the modifications provided by this subsection;

H. The absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 1989 but before January 1, 1993 and the absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 2002 that, pursuant to the United States Internal Revenue Code, Section 172, are being carried back for federal income tax purposes to the taxable year by the taxpayer;

M. The absolute value of the amount of any net operating loss arising from a tax year beginning or ending in 2001 that the taxpayer, pursuant to Section 102 of the federal Job Creation and Worker Assistance Act of 2002, Public Law 107-147, carries back more than 2 years to the taxable year for federal income tax purposes;

2. Subtractions. The taxable income of the taxpayer under the laws of the United States shall be decreased by:

H. For each taxable year subsequent to the year of the loss, an amount equal to the absolute value of the net operating loss arising from tax years beginning on or after January 1, 1989 but before January 1, 1993 and the absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 2002 that, pursuant to the Code, Section 172, was carried back for federal income tax purposes, but only to the extent that:

- (1) *Maine taxable income is not reduced below zero;*
- (2) *The taxable year is within the allowable federal period for carry-over; and*
- (3) *The amount has not been previously used as a modification pursuant to this subsection;*

L. An amount equal to the absolute value of any net operating loss arising from a tax year beginning or ending in 2001 for which federal taxable income was increased under subsection 1, paragraph M and that, pursuant to Section 102 of the federal Job Creation and Worker Assistance Act of 2002, Public Law 107-147, was carried back more than 2 years to the taxable year for federal income tax purposes, but only to the extent that:

- (1) *Maine taxable income is not reduced below zero;*
- (2) *The taxable year is either within 2 years prior to the year in which the loss arose or within the allowable federal period for carry-over of net operating losses;*
- (3) *The amount has not been previously used as a modification pursuant to this subsection;*

Examples

Example #5.1 – NOL in 2001, all of the loss is carried forward

The taxpayer has a federal net operating loss of \$90,000 in tax year 2001. The entire amount of the loss is carried forward; \$25,000 is applied to 2002 and \$65,000 to 2003. No addition modification is required in the loss year because none of the loss was carried back at the federal level. Further, because the federal loss did not offset any Maine addition modifications in 2001, no Maine adjustment is required in 2002 or 2003.

| | 1999 | 2000 | 2001 | 2002 | 2003 |
|------------------------------------|-------------|-------------|-------------|-------------|-------------|
| Federal income prior to NOL | \$40,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | _____ | _____ | _____ | (\$25,000) | (\$65,000) |
| Federal taxable income | \$40,000 | \$50,000 | (\$90,000) | \$0 | \$5,000 |
| Maine net income | \$40,000 | \$50,000 | (\$90,000) | \$0 | \$5,000 |

Example #5.2 – NOL in 2001, all of the loss is carried back

The taxpayer has a federal net operating loss of \$90,000 in tax year 2001. The entire loss is carried back; \$40,000 is applied to 1998 and \$50,000 to 1999. A \$90,000 Maine addition modification equal to the federal loss carryback is entered in the column for tax year 2001 and a second addition modification of \$40,000 is entered in the column for tax year 1998. Maine accepts the federal carryback to 1999, since it is within the allowable two-year carryback window. The carryback to 1998, however, must be reversed through an addition modification because that carryback is beyond the allowable two-year time period. The addition modification in 1998 may be recaptured as a subtraction modification in subsequent years, within the ordinary carryback/carryover time period

for federal losses. In this example, a subtraction modification is entered in the column for tax year 2000 to accomplish that recapture.

| | <u>1998</u> | <u>1999</u> | <u>2000</u> | <u>2001</u> | <u>2002</u> | <u>2003</u> |
|-----------------------------|-----------------|-------------|-----------------|-------------|-----------------|-----------------|
| Federal Income prior to NOL | \$40,000 | \$50,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | (\$40,000) | (\$50,000) | | | | |
| Federal Taxable Income | \$0 | \$0 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL Modifications: | | | | \$90,000 | | |
| § 5200-A(1)(B) | | | | | | |
| § 5200-A(1)(M) | \$40,000 | | | | | |
| § 5200-A(2)(L) | | | (\$40,000) | | | |
| Maine net income | \$40,000 | \$0 | \$10,000 | \$0 | \$25,000 | \$70,000 |

Example #5.3 – NOL in 2001, some of the loss is carried back, some is carried forward

The taxpayer has a federal net operating loss of \$90,000 in tax year 2001. Part of the loss (\$70,000) is carried back; \$20,000 is applied to 1999 and \$50,000 to 2000. In this example, since only a portion of the loss is carried back, only that portion must be added back to Maine income in the loss year. Also, because the loss is not carried back more than two years at the federal level, an addition modification is not required in any carryback year. The addition modification in 2001 brings Maine net income for the taxpayer to negative \$20,000. Since Maine law does not accommodate a separate NOL, there are no adjustments for this \$20,000 of negative Maine income. The negative \$20,000 is equal to the amount of the federal loss carryforward which, in this example, is applied to reduce the 2002 federal taxable income. No other Maine adjustment is required.

| | <u>1999</u> | <u>2000</u> | <u>2001</u> | <u>2002</u> | <u>2003</u> |
|----------------------------------|-------------|-------------|-------------------|----------------|-----------------|
| Federal Income prior to NOL | \$20,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | (\$20,000) | (\$50,000) | | (\$20,000) | |
| Federal Taxable Income | \$0 | \$0 | (\$90,000) | \$5,000 | \$70,000 |
| NOL Modification: § 5200-A(1)(B) | | | \$70,000 | | |
| Maine net income | \$0 | \$0 | (\$20,000) | \$5,000 | \$70,000 |

Example #5.4 – NOL in 2001, some of the loss is carried back, some is carried forward

The taxpayer has a federal net operating loss of \$90,000 in tax year 2001. Part of the loss (\$70,000) is carried back; \$20,000 is applied to 1999 and \$50,000 to 2000. The remaining loss (\$20,000) is carried forward to 2002. Only that portion of the loss carried back must be added back to Maine income in the loss year. As a result, the amount that is used as a federal carryforward is available in the year of the loss to offset unrelated Maine addition modifications. In this example, \$5,000 of Maine income in 2001 is offset by the federal loss. To prevent that portion of the federal loss used to offset Maine income in 2001 from also reducing income in a carryforward year, Maine requires an adjustment. This modification is located in the table below under tax year 2002 as an addition of \$5,000. The addition modification under section 36 M.R.S. § 5200-A(1)(C) keeps the

taxpayer from avoiding tax on the \$5,000 unrelated modification in 2001 and also reducing income in future years by the full carryover amount. Of the \$20,000 loss carryforward, \$5,000 is used to offset Maine income in 2001. Therefore, the \$20,000 carryforward must be reduced by that \$5,000 in 2002. Notice that, in 1999, the NOL carryback combined with a Maine subtraction modification unrelated to the NOL results in a negative amount for Maine net income. Since Maine has no state-level NOL, negative income amounts have no effect on Maine income tax.

| | <u>1999</u> | <u>2000</u> | <u>2001</u> | <u>2002</u> | <u>2003</u> |
|--|--------------------|--------------------|--------------------|--------------------|--------------------|
| Federal Income prior to NOL | \$20,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | <u>(\$20,000)</u> | <u>(\$50,000)</u> | _____ | <u>(\$20,000)</u> | _____ |
| Federal Taxable Income | \$0 | \$0 | (\$90,000) | \$5,000 | \$70,000 |
| Maine unrelated modifications | (\$3,000) | \$4,000 | \$5,000 | (\$6,000) | \$7,000 |
| NOL Modifications: § 5200-A(1)(B) | | | \$70,000 | | |
| § 5200-A(1)(C) | | | | \$5,000 | |
| Maine net income | <hr/> (\$3,000) | \$4,000 | (\$15,000) | \$4,000 | <hr/> \$77,000 |

PART 6 -- TAX YEAR 2000 AND EARLIER

From 1993 through 2000, Maine was in conformity with the Internal Revenue Code regarding net operating losses, so all federal carryback amounts were accepted for Maine income tax purposes. In the year of the loss, however, the taxpayer was required to add to income an amount equal to the NOL incurred in that year and carried back federally. This addition modification was required by 36 M.R.S. § 5200-A(1)(B). A second addition modification was required in a carryforward year if a portion of the loss was carried forward federally and a Maine addition modification was offset in the loss year. See 36 M.R.S. § 5200-A(1)(C) and Example #1.4. Below are the statutory paragraphs related to NOL modifications in effect for tax year 2000.

§5200-A. Modifications

1. Additions. The taxable income of the taxpayer under the laws of the United States shall be increased by:

B. The amount of any net operating loss in the taxable year which has been carried back to previous taxable years pursuant to the Code, Section 172;

C. The amount of any deduction claimed for the taxable year under the Code, Section 172, which has previously been used to offset the modifications provided by this subsection;

H. The absolute value of the amount of any net operating loss arising from tax years beginning on or after January 1, 1989 but before January 1, 1993 that, pursuant to the United States Internal Revenue Code, Section 172, is being carried back for federal income tax purposes to the taxable year by the taxpayer;

2. Subtractions. The taxable income of the taxpayer under the laws of the United States shall be decreased by:

H. For each taxable year subsequent to the year of the loss, an amount equal to the absolute value of the net operating loss arising from tax years beginning on or after January 1, 1989 but before January 1, 1993 and that, pursuant to the Code, Section 172, was carried back for federal income tax purposes, but only to the extent that:

(1) Maine taxable income is not reduced below zero;

(2) The taxable year is within the allowable federal period for carry-over; and

(3) The amount has not been previously used as a modification pursuant to this subsection;

Examples

Example #6.1 – NOL in 2000, all of the loss is carried forward

The taxpayer has a federal net operating loss of \$90,000 in tax year 2000. The entire amount of the loss is carried forward; \$25,000 is applied to 2001 and \$65,000 to 2002. No addition modification is required in the loss year because none of the loss was carried back at the federal level. Further, because the federal loss did not offset any Maine addition modifications in 2000, no Maine adjustment is required in 2001 or 2002.

| | <u>1998</u> | <u>1999</u> | <u>2000</u> | <u>2001</u> | <u>2002</u> |
|------------------------------------|-------------|-------------|-------------|-------------|-------------|
| Federal income prior to NOL | \$40,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | | | | (\$25,000) | (\$65,000) |
| Federal taxable income | \$40,000 | \$50,000 | (\$90,000) | \$0 | \$5,000 |
| Maine net income | \$40,000 | \$50,000 | (\$90,000) | \$0 | \$5,000 |

Example #6.2 – NOL in 2000, all of the loss is carried back

The taxpayer has a federal net operating loss of \$90,000 in tax year 2000. The entire loss is carried back; \$40,000 is applied to 1998 and \$50,000 to 1999. A \$90,000 Maine addition modification equal to the federal loss carryback is entered in the column for tax year 2000. The addition modification in the year of the loss brings federal income for the taxpayer to zero for 2000. No other adjustment is required.

| | <u>1998</u> | <u>1999</u> | <u>2000</u> | <u>2001</u> | <u>2002</u> |
|---|-------------|-------------|-------------|-------------|-------------|
| Federal Income prior to NOL | \$40,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | (\$40,000) | (\$50,000) | | | |
| Federal Taxable Income | \$0 | \$0 | (\$90,000) | \$25,000 | \$70,000 |
| NOL Modification: § 5200-A(1)(B) | | | \$90,000 | | |
| Maine net income | \$0 | \$0 | \$0 | \$25,000 | \$70,000 |

Example #6.3 – NOL in 2000, some of the loss is carried back, some is carried forward

The taxpayer has a federal net operating loss of \$90,000 in tax year 2000. Part of the loss (\$70,000) is carried back; \$20,000 is applied to 1998 and \$50,000 to 1999. The remaining loss (\$20,000) is carried forward to 2001. Only that portion of the loss carried back must be added back to Maine income in the loss year. The addition modification in 2000 brings Maine net income for the taxpayer to a loss of \$20,000. This \$20,000 loss is equal to the amount of the federal loss carryforward which, in this example, is applied to reduce the 2001 federal taxable income. No other Maine adjustment is required.

| | 1998 | 1999 | 2000 | 2001 | 2002 |
|----------------------------------|-------------|-------------|-------------------|----------------|-----------------|
| Federal Income prior to NOL | \$20,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | (\$20,000) | (\$50,000) | _____ | (\$20,000) | _____ |
| Federal Taxable Income | \$0 | \$0 | (\$90,000) | \$5,000 | \$70,000 |
| NOL Modification: § 5200-A(1)(B) | | | \$70,000 | | |
| Maine net income | \$0 | \$0 | (\$20,000) | \$5,000 | \$70,000 |

Example #6.4 – NOL in 2000, some of the loss is carried back, some is carried forward

The taxpayer has a federal net operating loss of \$90,000 in tax year 2000. Part of the loss (\$70,000) is carried back; \$20,000 is applied to 1998 and \$50,000 to 1999. The remaining loss (\$20,000) is carried forward to 2001. Only that portion of the loss carried back must be added back to Maine income in the loss year. As a result, the amount that is used as a federal carryforward is available in the year of the loss to offset unrelated Maine addition modifications. In this example, \$5,000 of Maine income in 2000 is offset by the federal loss. To prevent that portion of the federal loss used to offset Maine income in 2000 from also reducing income in a carryforward year, Maine requires an adjustment. This adjustment is located in the table below under tax year 2001 as an addition of \$5,000. The addition modification under section 36 M.R.S. § 5200-A(1)(C) keeps the taxpayer from avoiding tax on the \$5,000 unrelated modification in 2000 and also reducing income in future years by the full carryover amount. Of the \$20,000 loss carryforward, \$5,000 is used to offset Maine income in 2000. Therefore, the \$20,000 carryforward must be reduced by that \$5,000 in 2001. Notice that, in 1998, the NOL carryback combined with a Maine subtraction modification unrelated to the NOL results in a negative amount for Maine net income. Since Maine has no state-level NOL, negative income amounts have no effect on Maine income tax.

| | 1998 | 1999 | 2000 | 2001 | 2002 |
|-----------------------------------|------------------|----------------|-------------------|----------------|-----------------|
| Federal Income prior to NOL | \$20,000 | \$50,000 | (\$90,000) | \$25,000 | \$70,000 |
| NOL carryback/carryforward | (\$20,000) | (\$50,000) | _____ | (\$20,000) | _____ |
| Federal Taxable Income | \$0 | \$0 | (\$90,000) | \$5,000 | \$70,000 |
| Maine unrelated modifications | (\$3,000) | \$4,000 | \$5,000 | (\$6,000) | \$7,000 |
| NOL Modifications: § 5200-A(1)(B) | | | \$70,000 | | |
| § 5200-A(1)(C) | | | | \$5,000 | |
| Maine net income | (\$3,000) | \$4,000 | (\$15,000) | \$4,000 | \$77,000 |