

NOL Workgroup

Department of Taxation

July 1, 2025

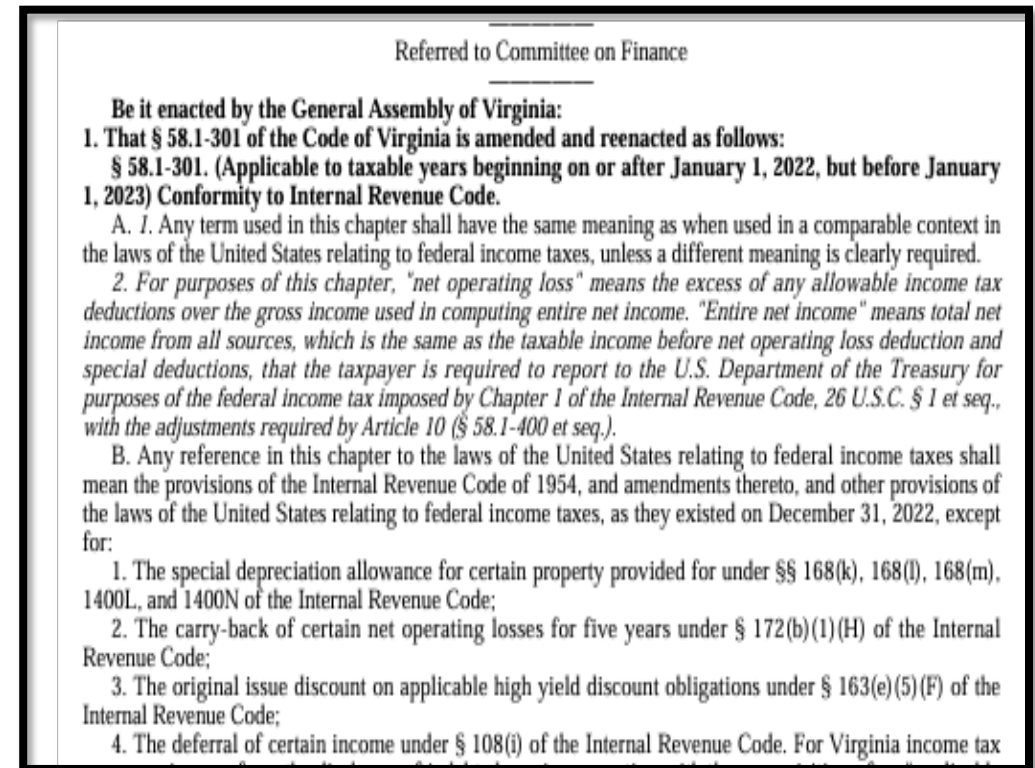
- ▶ Introductions
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- ▶ **Kristin Collins**, Deputy Commissioner
- ▶ **Charles Kennington**, Assistant Commissioner
- ▶ **James Savage**, Director of Tax Legislation
- ▶ **Ryan Cunningham**, Income Tax Team Lead
- ▶ **James Ford**, Senior Tax Law Analyst
- ▶ **John Josephs**, Senior Tax Law Analyst
- ▶ **Matt Style**, Principal Economist

HB 2681/SB 1426

As introduced these bills would have:

- ▶ Defined “net operating loss” as the excess of any allowable income tax deductions over the gross income used in computing entire net income.
- ▶ Defined “entire net income” as total net income from all sources, which is the same as the taxable income before net operating loss deduction and special deductions, that the taxpayer is required to report for purposes of the federal income tax, with the adjustments required by Article 10 (§ 58.1-400 et seq.).



HB 2681/SB 1426

Substitute versions of these bills would have:

- ▶ Required the Department of Taxation (“the Department”) to convene this workgroup to study Virginia’s treatment of NOLs.
- ▶ These bills ultimately failed to pass in the General Assembly.

(Paraphrase of Prior to Substitute—Delegate Banard)
A BILL to direct the Department of Taxation to convene a work group to analyze the treatment of net operating losses in Virginia when compared to other states; report.
Be it enacted by the General Assembly of Virginia:
1. § 1. *That the Department of Taxation shall convene a work group composed of tax practitioners experienced in the preparation of corporate tax returns involving net operating losses, including members recommended by the Taxation Section of the Virginia Bar Association and the Virginia Society of Certified Public Accountants. The work group shall study the treatment of net operating losses in Virginia when compared to other states and shall make recommendations to simplify such treatment in Virginia. The work group shall consider at a minimum: (i) transition rules to the proposed simplified method of determining net operating losses; (ii) the effective date of any such transition; and (iii) what legislative, regulatory, or guideline amendments would be necessary to best effectuate such transition. The work group shall complete its meetings by October 1, 2025, and the Department shall submit a report of the work group's findings and recommendations to the Chairmen of the Senate Committee on Finance and Appropriations, the House Committee on Finance, and the House Committee on Appropriations by November 1, 2025.*

Item 257 of the 2025 Appropriation Act (House Bill 1600, Chapter 725)

This item requires the Department to convene this workgroup to study the treatment of net operating losses in Virginia when compared to other states and to make recommendations to simplify such treatment in Virginia.

F. The Department of Taxation shall convene a work group composed of tax practitioners experienced in the preparation of corporate tax returns involving net operating losses, including members recommended by the Taxation Section of the Virginia Bar Association and the Virginia Society of Certified Public Accountants. The work group shall study the treatment of net operating losses in Virginia when compared to other states and shall make recommendations to simplify such treatment in Virginia. The work group shall consider at a minimum: (i) transition rules to the proposed simplified method of determining net operating losses; (ii) the effective date of any such transition; and (iii) what legislative, regulatory, or guideline amendments would be necessary to best effectuate such transition. The work group shall complete its meetings by October 1, 2025, and the Department shall submit a report of the work group's findings and recommendations to the Chairs of the Senate Finance and Appropriations, House Finance, and House Appropriations Committee by November 1, 2025.

The workgroup shall study the treatment of net operating losses in Virginia when compared to other states and shall make recommendations to simplify such treatment in Virginia.

The workgroup's considerations will include, but not be limited to:

- ▶ Transition rules to the proposed simplified method of determining net operating losses,
- ▶ The effective date of any such transition, and
- ▶ What legislative, regulatory, or guideline amendments would be necessary to best effectuate such transition.

- ▶ The majority of states (36 plus the District of Columbia) calculate a state NOL using post-apportionment rules.
- ▶ Only 11 states (including Virginia) calculate a state NOL using pre-apportionment rules.

- ▶ Before 1972, only manufacturers were allowed to claim NOLs carried from other taxable years (“NOLD”).
- ▶ In 1972, Virginia adopted federal taxable income as the starting point for computing corporate Virginia income tax.
- ▶ By starting with federal taxable income, Virginia incorporated:
 - ▶ the federal allowance of NOLD for any business, and
 - ▶ the federal allowance of NOLD to individuals to the extent that FAGI included business income.
- ▶ The NOLD for manufacturers was repealed.

- ▶ The 1972 changes brought in two NOLD policies:
 - ▶ First, Virginia required several additions and subtractions to federal taxable income, and the net Virginia modifications had to follow the NOLD as it was used to reduce the amount of federal taxable income that was taxable on the Virginia return.
 - ▶ Second, the federal return reported the entire NOLD available on Line 29a of the federal corporate income tax return (Form 1120), which often resulted in a negative Line 30. Therefore, Virginia did not recognize a federal NOLD to the extent that it reduced federal taxable income below zero. This effectively limited NOLD for Virginia purposes to the amount of a corporation's income before claiming NOLD on Line 29a of the federal return. This amount of NOLD absorbed was also used to calculate the portion of net Virginia modifications from the loss year that must be reported on the Virginia return.

- ▶ In 1982, in addition to changing how multistate income is allocated and apportioned, the General Assembly added a new way for affiliated corporations to report their income: a Virginia combined return.
 - ▶ This new type of return required that income, additions, subtractions, allocation and apportionment be computed separately for each corporation, then the bottom-line income and loss amounts are combined.
 - ▶ This meant that the 1972 policies for determining the NOLD absorbed and the applicable portion of net modifications had to be applied for each affiliate.

- ▶ In 1984, the Department published comprehensive regulations for corporate income tax, effective for taxable years beginning on and after January 1, 1985. These regulations explained:
 - ▶ The policies relevant to NOLD, including limiting NOLD to the amount absorbed each year and associated net modifications from the loss year.
 - ▶ How combined returns were to be prepared, but did not include specific explanations of how NOLD policies applied to combined returns.
 - ▶ That a consolidated return could not include corporations that used different apportionment factors.

- ▶ In 1990, the General Assembly said that permission to file a consolidated return shall not be denied because affiliates used different apportionment factors and directed the Department to issue regulations implementing this policy.
- ▶ This amended regulation was published in 1993 and specified how a consolidated return handled corporations with different apportionment factors. The amendment also clarified and expanded other policies, including detailed instructions and examples of how NOLD is reported under Virginia's statutory separate, consolidated, and combined filing methods.
 - ▶ It is the intersection of Virginia's statutory filing methods with Virginia's net operating loss rules that is the source of the complicated calculations that the Department is now required to study and report on simplification.

- ▶ In 2003, the General Assembly began selectively deconforming from specific provisions of the Internal Revenue Code.
- ▶ Originally, deconformity was limited to “bonus depreciation.”
- ▶ However in subsequent years, more deconformity provisions were added and deleted, which directly affected the computation of the NOLD.
- ▶ As a result, the complexity of NOLD calculations increased.



Open Forum

Questions and Comments

Step 1

Workgroup Meeting

- ▶ **Completed!**

Step 2

Provide Policy Options and Written Comments by **July 15, 2025**

- ▶ To: james.ford@tax.virginia.gov

Step 3

Circulate draft report to stakeholders by September 1, 2025

- ▶ Provide any additional written comments by October 1, 2025.

- ▶ Presentation will be made available on the Virginia Tax webpage:
<https://www.tax.virginia.gov/> (coming soon)
- ▶ Final Report Submitted by November 1, 2025, to the following:
 - ▶ The Chairperson of the House Committee on Finance;
 - ▶ The Chairperson of the House Committee on Appropriations; and
 - ▶ The Chairperson of the Senate Committee on Finance and Appropriations.

Thank you



James Savage

Tax Legislation Director

james.savage@tax.virginia.gov



Ryan Cunningham

Lead Income Tax Analyst

ryan.cunningham@tax.virginia.gov



James Ford

Senior Income Tax Analyst

james.ford@tax.virginia.gov