Department of the Treasury

Internal Revenue Service

Publication 536
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Net Operating Losses

- Trade or business
- Employee business expenses
- Casualty and theft

For use in preparing

1997 Returns

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Contents

Important Change for 1997

Carrybacks and carryforwards. For an NOL occurring in a tax year beginning after August 5, 1997, the carryback period is reduced to 2 years and the carryforward period is increased to 20 years. However, the carryback period remains 3 years for the part of an NOL that:

1) Is from a casualty or theft, or
2) In the case of a farm business or other qualified small business, is attributable to a Presidentially declared disaster.

For more information, see *When To Use an NOL,* later.

Introduction

If your deductions for the year are more than your income for the year, you may have a net operating loss (NOL). You can use an NOL by deducting it from your income in another year or years. This publication discusses NOLs for individuals, estates, trusts, and corporations. It explains how to figure an NOL, when to use it, how to claim an NOL deduction, and how to figure an NOL carryover.

To have an NOL, your loss must be caused by:

1) Deductions from a trade or business,
2) Deductions from your work as an employee, or
3) Deductions for casualty and theft losses.

A loss from operating a business is the most common reason for an NOL.

Partnerships and S corporations generally cannot use an NOL. But partners or shareholders can use their separate shares of the partnership's or S corporation's business income and business deductions to figure their individual NOLs.

This publication does not discuss bankruptcy. If you need information on bankruptcy, see Publication 908, *Bankruptcy Tax Guide.*

Useful Items

You may want to see:

Publication

- ☐ **542** Corporations

Form (and Instructions)

- ☐ **1040X** Amended U.S. Individual Income Tax Return
- ☐ **1045** Application for Tentative Refund
- ☐ **1120X** Amended U.S. Corporation Income Tax Return
- ☐ **1138** Extension of Time for Payment of Taxes by a Corporation Expecting a Net Operating Loss Carryback
- ☐ **1139** Corporation Application for Tentative Refund

See *How To Get More Information,* near the end of this publication for information about getting these publications and forms.

NOL Steps

Figure and use your NOL in the following steps:

Step 1. Complete your tax return for the year. You may have an NOL if a negative figure appears on the line below:

Individuals — line 36 of Form 1040.

Estates and trusts — line 23 of Form 1041.

Corporations — line 30 of Form 1120 or line 26 of Form 1120–A.

If the amount on that line is zero or more, ***stop here —*** you do not have an NOL.

Step 2. Determine whether you have an NOL and its amount. See *How To Figure an NOL,* later. If you do not have an NOL, ***stop here.***

Step 3. Decide whether to carry the NOL back to a past year or to forgo any carryback and instead carry the NOL forward to a future year. See *When To Use an NOL,* later.

Step 4. Deduct the NOL in the carryback or carryforward year. See *How To Claim an NOL Deduction,* later. If your NOL deduction is equal to or smaller than your taxable income without the deduction, ***stop here —*** you have used up your NOL.

Step 5. Determine the amount of your unused NOL. See *How To Figure an NOL Carryover,* later. Carry over the unused NOL to the next carryback or carryforward year and begin again at Step 4.

Note. If your NOL deduction includes more than one NOL amount, apply Step 5 separately to each NOL amount, starting with the amount from the earliest year.

How To Figure an NOL

If your deductions for the year are more than your income for the year, you have a potential NOL.

There are rules that limit what you can deduct when figuring an NOL. In general, these rules do not allow:

1) Exemptions,
2) Net capital losses,
3) Nonbusiness losses,
4) Nonbusiness deductions, and
5) Net operating loss deductions.

Schedule A (Form 1045). You can use Schedule A (Form 1045) to figure an NOL for an individual, estate, or trust. This discussion explains Schedule A and includes an illustrated example.

First, complete lines 1–3 of Schedule A, using amounts from your return. If line 3 is a negative amount, you have a net loss and a potential NOL.

Next, complete the rest of Schedule A to figure your NOL. Adjust the amount on line 3 for deductions that are allowed when figuring your taxable income, but not when figuring an NOL. The following discussions explain these adjustments.

Adjustment for exemptions (line 4). You cannot deduct your personal exemption or exemptions for dependents. An estate or trust cannot deduct its exemption amount. Your adjustment is the total amount you deducted.

Adjustment for nonbusiness deductions (line 12). You can deduct your nonbusiness deductions (line 9) only up to the total of:

1) Your nonbusiness capital gains that are more than your nonbusiness capital losses (line 8), and
2) Your nonbusiness income (line 10).

Your adjustment is your nonbusiness deductions that are more than the total of (1) and (2).

Nonbusiness deductions (line 9). Enter on line 9 as your nonbusiness deductions only those that are unrelated to your trade or business or your employment. For example, enter your deductions for alimony, contributions to an IRA or other retirement plan, medical expenses, and charitable contributions. If you do not itemize deductions, include your standard deduction.

Do ***not*** include your deductions for personal casualty and theft losses or for one-half of self-employment tax. Treat these as business deductions.

Also do not include your deductions for expenses that are ordinary and necessary in carrying on your trade or business or your employment, your deduction for your share of a business loss from a partnership or S corporation, or the following related deductions for:

Moving expenses,

State income tax on business profits,

Interest and litigation expenses on state and federal income taxes related to your business income,

Payments by a federal employee to buy back sick leave used in an earlier year,

Loss on property you rent out,

Loss on the sale or exchange of business real estate or depreciable business property,

Loss on the sale of accounts receivable (if you use an accrual method of accounting),

Loss on the sale or exchange of stock in a small business corporation or a small business investment company, if treated as ordinary loss, and

Unrecovered investment in a pension or annuity claimed on a decedent's final return.

Nonbusiness income (line 10). Enter on line 10 as your nonbusiness income only income that is unrelated to your trade or business or your employment. For example, enter your annuity income, dividends, and interest from investments. Also, include your share of nonbusiness income from partnerships and S corporations.

Do ***not*** include the income you receive from your trade or business or your employment. This includes salaries and wages, self-employment income, and your share of business income from partnerships and S corporations. Also, do not include rental income or ordinary gain from the sale or other disposition of business real estate or depreciable business property.

Adjustment for capital losses (line 22). You can deduct your nonbusiness capital losses (line 5) only up to the amount of your nonbusiness capital gains (line 6). If your nonbusiness capital losses are more than your nonbusiness capital gains, you cannot deduct the excess.

You can deduct your business capital losses (line 14) only up to the total of:

1) Your nonbusiness capital gains that are more than the total of your nonbusiness capital losses and excess nonbusiness deductions (line 13), and
2) Your business capital gains (line 15).

Your adjustment is your nondeductible capital losses (line 18) that are more than the nondeductible net capital loss on your return (line 21). (You had a nondeductible net capital loss if your net capital loss was more than your capital loss deduction.)

Adjustment for NOL deduction (line 23). You cannot deduct any NOL carryovers or carrybacks from other years. Your adjustment is the total amount of your NOL deduction for losses from other years.

Illustrated Schedule A (Form 1045)

The following example illustrates how to figure an NOL. It includes filled-in pages 1 and 2 of Form 1040 and Schedule A (Form 1045).

Form **1040** Department of the Treasury—Internal Revenue Service
U.S. Individual Income Tax Return 1997

IRS Use Only—Do not write or staple in this space.

For the year Jan. 1–Dec. 31, 1997, or other tax year beginning , 1997, ending , 19 OMB No. 1545-0074

Label

(See instructions on page 10.)

Use the IRS label. Otherwise, please print or type.

LABEL HERE

Your first name and initial: Glenn M.	Last name: Johnson		Your social security number: 765 00 4321
If a joint return, spouse's first name and initial	Last name		Spouse's social security number
Home address (number and street). If you have a P.O. box, see page 10.: 5603 E. Main Street		Apt. no.	
City, town or post office, state, and ZIP code. If you have a foreign address, see page 10.: Anytown, VA 20000			

For help in finding line instructions, see pages 2 and 3 in the booklet.

Presidential Election Campaign (See page 10.)

	Yes	No
Do you want $3 to go to this fund?	√	
If a joint return, does your spouse want $3 to go to this fund?		

Note: *Checking "Yes" will not change your tax or reduce your refund.*

Filing Status

Check only one box.

1 [√] Single
2 [ ] Married filing joint return (even if only one had income)
3 [ ] Married filing separate return. Enter spouse's social security no. above and full name here. ▶
4 [ ] Head of household (with qualifying person). (See page 10.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶
5 [ ] Qualifying widow(er) with dependent child (year spouse died ▶ 19). (See page 10.)

Exemptions

6a [√] **Yourself.** If your parent (or someone else) can claim you as a dependent on his or her tax return, **do not** check box 6a.

b [ ] **Spouse**

No. of boxes checked on 6a and 6b: 1

c **Dependents:**

(1) First name Last name	(2) Dependent's social security number	(3) Dependent's relationship to you	(4) No. of months lived in your home in 1997

If more than six dependents, see page 10.

No. of your children on 6c who:
- lived with you
- did not live with you due to divorce or separation (see page 11)

Dependents on 6c not entered above

d Total number of exemptions claimed

Add numbers entered on lines above ▶ 1

Income

Attach Copy B of your Forms W-2, W-2G, and 1099-R here.

If you did not get a W-2, see page 12.

Enclose but do not attach any payment. Also, please use **Form 1040-V.**

7	Wages, salaries, tips, etc. Attach Form(s) W-2		7	1,225	
8a	**Taxable** interest. Attach Schedule B if required		8a	425	
b	**Tax-exempt** interest. DO NOT include on line 8a	8b			
9	Dividends. Attach Schedule B if required		9		
10	Taxable refunds, credits, or offsets of state and local income taxes (see page 12)		10		
11	Alimony received		11		
12	Business income or (loss). Attach Schedule C or C-EZ		12	< 5,000 >	
13	Capital gain or (loss). Attach Schedule D		13	1,000	*
14	Other gains or (losses). Attach Form 4797		14		
15a	Total IRA distributions 15a	b Taxable amount (see page 13)	15b		
16a	Total pensions and annuities 16a	b Taxable amount (see page 13)	16b		
17	Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E		17		
18	Farm income or (loss). Attach Schedule F		18		
19	Unemployment compensation		19		
20a	Social security benefits 20a	b Taxable amount (see page 14)	20b		
21	Other income. List type and amount—see page 15		21		
22	Add the amounts in the far right column for lines 7 through 21. This is your **total income** ▶		22	< 2,350 >	

Adjusted Gross Income

If line 32 is under $29,290 (under $9,770 if a child did not live with you), see EIC inst. on page 21.

23	IRA deduction (see page 16)	23			
24	Medical savings account deduction. Attach Form 8853	24			
25	Moving expenses. Attach Form 3903 or 3903-F	25			
26	One-half of self-employment tax. Attach Schedule SE	26			
27	Self-employed health insurance deduction (see page 17)	27			
28	Keogh and self-employed SEP and SIMPLE plans	28			
29	Penalty on early withdrawal of savings	29			
30a	Alimony paid b Recipient's SSN ▶	30a			
31	Add lines 23 through 30a			31	
32	Subtract line 31 from line 22. This is your **adjusted gross income** ▶			32	< 2,350 >

For Privacy Act and Paperwork Reduction Act Notice, see page 38. Cat. No. 11320B Form **1040** (1997)

* Net capital gain ($2,000 gain less $1,000 loss)

Tax Computation

33	Amount from line 32 (adjusted gross income)	33	< 2,350 >
34a	Check if: ☐ **You** were 65 or older, ☐ Blind; ☐ **Spouse** was 65 or older, ☐ Blind. Add the number of boxes checked above and enter the total here ▶ 34a		
b	If you are married filing separately and your spouse itemizes deductions or you were a dual-status alien, see page 18 and check here ▶ 34b ☐		
35	Enter the **larger** of your: **Itemized deductions** from Schedule A, line 28, **OR** **Standard deduction** shown below for your filing status. **But** see page 18 if you checked any box on line 34a or 34b **or** someone can claim you as a dependent. • Single—$4,150 • Married filing jointly or Qualifying widow(er)—$6,900 • Head of household—$6,050 • Married filing separately—$3,450	35	4,150
36	Subtract line 35 from line 33	36	< 6,500 >
37	If line 33 is $90,900 or less, multiply $2,650 by the total number of exemptions claimed on line 6d. If line 33 is over $90,900, see the worksheet on page 19 for the amount to enter	37	2,650
38	**Taxable income.** Subtract line 37 from line 36. If line 37 is more than line 36, enter -0-	38	-0-
39	**Tax.** See page 19. Check if any tax from **a** ☐ Form(s) 8814 **b** ☐ Form 4972 ▶	39	

If you want the IRS to figure your tax, see page 18.

Credits

40	Credit for child and dependent care expenses. Attach Form 2441	40			
41	Credit for the elderly or the disabled. Attach Schedule R	41			
42	Adoption credit. Attach Form 8839	42			
43	Foreign tax credit. Attach Form 1116	43			
44	Other. Check if from **a** ☐ Form 3800 **b** ☐ Form 8396 **c** ☐ Form 8801 **d** ☐ Form (specify) ________	44			
45	Add lines 40 through 44			45	
46	Subtract line 45 from line 39. If line 45 is more than line 39, enter -0- ▶			46	

Other Taxes

47	Self-employment tax. Attach Schedule SE	47	
48	Alternative minimum tax. Attach Form 6251	48	
49	Social security and Medicare tax on tip income not reported to employer. Attach Form 4137	49	
50	Tax on qualified retirement plans (including IRAs) and MSAs. Attach Form 5329 if required	50	
51	Advance earned income credit payments from Form(s) W-2	51	
52	Household employment taxes. Attach Schedule H	52	
53	Add lines 46 through 52. This is your **total tax** ▶	53	

Payments

54	Federal income tax withheld from Forms W-2 and 1099	54			
55	1997 estimated tax payments and amount applied from 1996 return	55			
56a	**Earned income credit.** Attach Schedule EIC if you have a qualifying child **b** Nontaxable earned income: amount ▶ ______ and type ▶ ______	56a			
57	Amount paid with Form 4868 (request for extension)	57			
58	Excess social security and RRTA tax withheld (see page 27)	58			
59	Other payments. Check if from **a** ☐ Form 2439 **b** ☐ Form 4136	59			
60	Add lines 54, 55, 56a, 57, 58, and 59. These are your **total payments** ▶			60	

Attach Forms W-2, W-2G, and 1099-R on the front.

Refund

61	If line 60 is more than line 53, subtract line 53 from line 60. This is the amount you **OVERPAID**	61	
62a	Amount of line 61 you want **REFUNDED TO YOU** ▶	62a	
▶ b	Routing number ▶ **c** Type: ☐ Checking ☐ Savings		
▶ d	Account number		
63	Amount of line 61 you want **APPLIED TO YOUR 1998 ESTIMATED TAX** ▶ 63		

Have it directly deposited! See page 27 and fill in 62b, 62c, and 62d.

Amount You Owe

64	If line 53 is more than line 60, subtract line 60 from line 53. This is the **AMOUNT YOU OWE**. For details on how to pay, see page 27 ▶	64	
65	Estimated tax penalty. Also include on line 64 — 65		

Sign Here

Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Keep a copy of this return for your records.

Your signature	Date	Your occupation
Glenn M. Johnson	2-5-98	Self-employed
Spouse's signature. If a joint return, BOTH must sign.	Date	Spouse's occupation

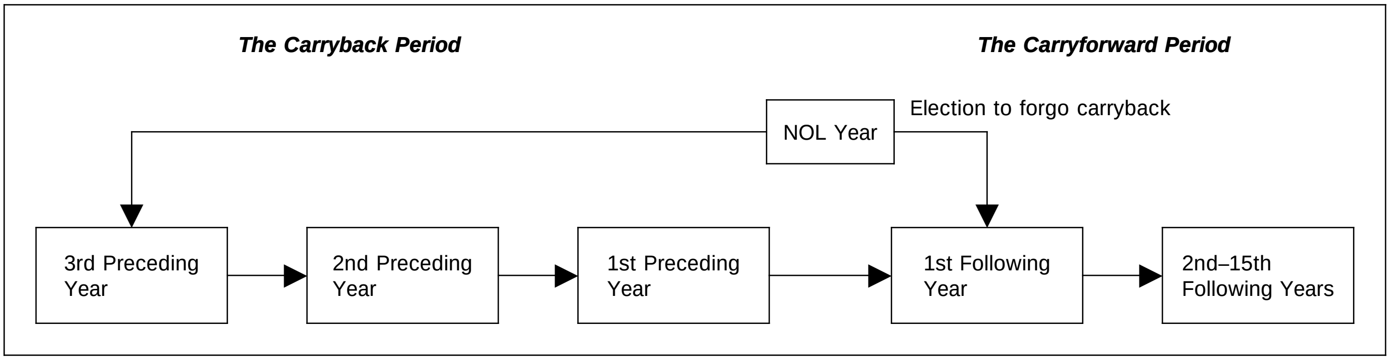
Paid Preparer's Use Only

Preparer's signature ▶	Date	Check if self-employed ☐	Preparer's social security no.
Firm's name (or yours if self-employed) and address ▶			EIN
			ZIP code

Schedule A—Net Operating Loss (NOL). See instructions.

1	Adjusted gross income from 1997 Form 1040, line 33. Estates and trusts, skip lines 1 and 2					**1**	< 2,350 >
2	Deductions (individuals only):						
a	Enter amount from your 1997 Form 1040, line 35			**2a**	4,150		
b	Enter your deduction for exemptions from 1997 Form 1040, line 37			**2b**	2,650		
c	Add lines 2a and 2b					**2c**	(6,800)
3	Combine lines 1 and 2c. Estates and trusts, enter taxable income					**3**	< 9,150 >
	Note: *If line 3 is zero or more, do not complete rest of schedule. You* ***do not*** *have a net operating loss.*						
	Adjustments:						
4	Deduction for exemptions from line 2b above. Estates and trusts, enter exemption amount from tax return			**4**	2,650		
5	Total nonbusiness capital losses before limitation. Enter as a positive number	**5**	1,000				
6	Total nonbusiness capital gains	**6**					
7	If line 5 is more than line 6, enter difference; otherwise, enter -0-	**7**	1,000				
8	If line 6 is more than line 5, enter difference; otherwise, enter -0-	**8**	-0-				
9	Nonbusiness deductions. See instructions	**9**	4,150				
10	Nonbusiness income other than capital gains. See instructions	**10**	425				
11	Add lines 8 and 10	**11**	425				
12	If line 9 is more than line 11, enter difference; otherwise, enter -0-			**12**	3,725		
13	If line 11 is more than line 9, enter difference; otherwise, enter -0-. Do not enter more than line 8	**13**	-0-				
14	Total business capital losses before limitation. Enter as a positive number	**14**					
15	Total business capital gains	**15**	2,000				
16	Add lines 13 and 15	**16**	2,000				
17	If line 14 is more than line 16, enter difference; otherwise, enter -0-	**17**	-0-				
18	Add lines 7 and 17	**18**	1,000				
19	Enter the loss, if any, from line 18 of Schedule D (Form 1040). (Estates and trusts, enter the loss, if any, from line 17, column (c), of Schedule D (Form 1041).) Enter as a positive number. If you do not have a loss on that line, skip lines 19 through 21 and enter on line 22 the amount from line 18	**19**					
20	Enter the loss from line 19 of Schedule D (Form 1040). (Estates and trusts, enter the loss from line 18 of Schedule D (Form 1041).) Enter as a positive number	**20**					
21	Subtract line 20 from line 19	**21**					
22	Subtract line 21 from line 18. If zero or less, enter -0-			**22**	1,000		
23	Net operating loss deduction for losses from other years. Enter as a positive number			**23**			
24	Add lines 4, 12, 22, and 23					**24**	7,375
25	**Net operating loss.** Combine lines 3 and 24. If the combined amount is less than zero, enter it here and on page 1, line 1a. If the combined amount is zero or more, you **do not** have a net operating loss					**25**	< 1,775 >

Figure A. **When To Use an NOL**



Example. Glenn Johnson is in the retail record business. He is single and has the following income and deductions on his Form 1040 for 1997.

INCOME	
Wages from part-time job	$1,225
Interest on savings	425
Net long-term capital gain on sale of real estate used in business	2,000
Glenn's total income	$3,650
DEDUCTIONS	
Net loss from business (sales of $67,000 minus expenses of $72,000)	$5,000
Net short-term capital loss on sale of stock	1,000
Standard deduction	4,150
Personal exemption	2,650
Glenn's total deductions	$12,800

Glenn's deductions exceed his income by $9,150 ($12,800 – $3,650). However, to figure whether he has an NOL, he must modify certain deductions. He can use Schedule A (Form 1045) to figure his NOL. See the illustrated Schedule A (Form 1045) included here.

Glenn cannot deduct the following:

Nonbusiness net short-term capital loss	1,000
Nonbusiness deductions (standard deduction, $4,150) minus nonbusiness income (interest, $425)	3,725
Personal exemption	$2,650
Total adjustments to net loss	$7,375

When these items are eliminated, Glenn's net loss is reduced to $1,775 ($9,150 – $7,375). This is his NOL for 1997.

When To Use an NOL

Generally, you carry back an NOL to the 3 tax years before the NOL year (the carryback period), and then carry forward any remaining NOL for up to 15 years after the NOL year (the carryforward period). See Figure A, *When To Use an NOL.* You may, however, choose not to carry back an NOL and carry it forward only. See *Forgoing the carryback period,* later. The "NOL year" is the year in which the NOL occurred. You cannot deduct any part of the NOL remaining after the 15-year carryforward period.

TIP *For an NOL occurring in a tax year beginning after August 5, 1997, the carryback period is reduced to 2 years and the carryforward period is increased to 20 years. However, the carryback period remains 3 years for the part of an NOL that:*

1) *Is from a casualty or theft, or*

2) *In the case of a farm business or other qualified small business, is attributable to a Presidentially declared disaster.*

You must first carry the entire NOL to the earliest carryback year. If your NOL is not used up, you can carry the rest to the next earliest carryback year, and so on.

If you do not use up the NOL in the 3 carryback years, carry forward what remains of it to the 15 tax years following the NOL year. Start by carrying it to the first tax year after the NOL year. If you do not use it up, carry over the unused part to the next year. Continue to carry over any unused part of the NOL until you complete the 15-year carryforward period.

Example. You started your business in 1997 and had a $42,000 NOL for the year. You begin using your NOL in 1994, the third year before the NOL year, as shown in the following chart.

Year	Carryback /Carryover	Unused Loss
1994	$42,000	$40,000
1995	40,000	37,000
1996	37,000	31,500
1997 (NOL year)		
1998	31,500	22,500
1999	22,500	12,700
2000	12,700	4,000
2001	4,000	–0–

If your loss were larger, you could carry it forward until the year 2012. If you still had an unused 1997 carryforward after the year 2012, you could not deduct it.

Forgoing the carryback period. You can choose not to carry back your NOL. If you make this choice, you use your NOL only in the 15-year carryforward period. (This choice means you also choose not to carry back any alternative tax NOL.)

To make this choice, attach a statement to your tax return for the NOL year or to an amended return for the NOL year filed within 6 months of the due date of the return (excluding extensions). This statement must show that you are choosing to forgo the carryback period under section 172(b)(3) of the Internal Revenue Code.

CAUTION *If you do not file this statement on time, you cannot forgo the carryback period. Once you make this choice, you cannot change it. If you want to forgo the carryback period for more than one NOL, you must make a separate choice for each NOL year.*

How To Claim an NOL Deduction

If you have not already carried the NOL to an earlier year, your NOL deduction is the total NOL. If you carried the NOL to an earlier year, your NOL deduction is the NOL minus the amount you used in the earlier year or years.

If you carry more than one NOL to the same year, your NOL deduction is the total of these carrybacks and carryovers.

NOL more than taxable income. If your NOL is more than the taxable income of the year you carry it to (figured before deducting the NOL), you generally will have an NOL carryover to the next year. See *How To Figure an NOL Carryover,* later, to determine how much NOL you have used and how much you carry to the next year.

Deducting a Carryback

If you carry back your NOL, you can use either Form 1045 or Form 1040X. You can get your refund faster by using Form 1045, but you have a shorter time to file it. You can use Form 1045 to apply an NOL to all three carryback years. If you use Form 1040X, you must use a separate Form 1040X for each carryback year to which you apply the NOL.

Estates and trusts not filing Form 1045 must file an amended Form 1041 (instead of Form 1040X) for each carryback year to which they apply the NOL. Use a copy of the appropriate year's Form 1041, check the "Amended return" box, and follow the Form 1041 instructions for amended returns. Include the NOL deduction with other deductions not subject to the 2% limit (line 15a for 1994, 1995, and 1996). Also, see the special procedures for filing an amended return due to an NOL carryback, explained under *Form 1040X,* later.

Form 1045. You can apply for a quick refund by filing Form 1045. This form results in a tentative adjustment of tax in the carryback year. See the Form 1045 illustrated at the end of this discussion.

If the IRS refunds or credits an amount to you from Form 1045 and later determines that the refund or credit is too much, the IRS may assess and collect the excess immediately.

You must file Form 1045 on or after the date you file the return for the NOL year, but not later than one year after the NOL year. For example, if you are a calendar year taxpayer with a carryback from 1997 to 1994, you must file Form 1045 on or after the date you file your tax return for 1997, but no later than December 31, 1998.

Form 1040X. If you do not file Form 1045, you can file Form 1040X to get a refund of tax because of an NOL carryback. File Form 1040X within 3 years after the due date, including extensions, for filing the return for the NOL year. For example, if you are a calendar year taxpayer and filed your 1994 return by the April 15, 1995, due date, you must file a claim for refund of 1991 tax because of an NOL carryback from 1994 by April 15, 1998.

Attach a computation of your NOL using Schedule A (Form 1045) and, if it applies, your NOL carryover using Schedule B (Form 1045), discussed later.

Refiguring your tax. To refigure your total tax liability for a carryback year, first refigure your adjusted gross income for that year. (On Form 1045, use lines 10 through 12, column (b), (d), or (f).) Use your adjusted gross income after applying the NOL deduction to refigure income or deduction items that are based on, or limited to, a percentage of your adjusted gross income. These are:

1) The special allowance for passive activity losses from rental real estate activities,
2) Taxable social security and tier 1 railroad retirement benefits,
3) IRA deductions, and
4) Excludable savings bond interest.

If more than one of these items apply, refigure them in the order listed above, using your adjusted gross income after applying the NOL deduction and any previous item. (On line 10 of Form 1045, column (b), (d), or (f), enter your adjusted gross income after applying the above refigured items, but without the NOL deduction. Enter your NOL deduction on line 11.)

Next, refigure your taxable income. (On Form 1045, use lines 13 through 16, column (b), (d), or (f).) Use your refigured adjusted gross income (line 12 of Form 1045, column (b), (d), or (f)) to refigure certain deductions and other items that are based on, or limited to, a percentage of your adjusted gross income. These are:

1) The itemized deduction for medical expenses,
2) The itemized deduction for casualty losses,
3) Certain miscellaneous itemized deductions,
4) The overall limit on itemized deductions, and
5) The phaseout of the deduction for exemptions.

Do not refigure the itemized deduction for charitable contributions.

Finally, use your refigured taxable income (line 16 of Form 1045, column (b), (d), or (f)) to refigure your total tax liability. Refigure your income tax, your alternative minimum tax, and any credits that are based on, or limited to, the amount of tax. (On Form 1045, use lines 17 through 26, column (b), (d), or (f).) The earned income credit, for example, may be affected by changes to adjusted gross income or the amount of tax (or both) and therefore must be recomputed. If you become eligible for a credit because of the carryback, complete the form for that specific credit (such as Schedule EIC) for that year.

While it is necessary to refigure your income tax, alternative minimum tax, and credits, **do not refigure self-employment tax.**

Deducting a Carryforward

If you carry forward your NOL to a tax year after the NOL year, list your NOL deduction as a negative figure on the “Other income” line of Form 1040 (line 21 for 1997). Estates and trusts include an NOL deduction on Form 1041 with other deductions not subject to the 2% limit (line 15a for 1997).

You must attach a statement that shows all the important facts about the NOL. Your statement should include a computation showing how you figured the NOL deduction. If you deduct more than one NOL in the same year, your statement must cover each of them.

Change in Marital Status

If you and your spouse were not married to each other in all years involved in figuring NOL carrybacks and carryovers, only the spouse who had the loss can take the NOL deduction. If you file a joint return, the NOL deduction is limited to the income of that spouse.

For example, if your marital status changes because of death or divorce, and in a later year you have an NOL, you can carry back that loss only to the part of the income reported on a joint return (filed with your former spouse) that was ***your*** taxable income. After you deduct the NOL in the carryback year, the joint rates apply to the resulting taxable income.

Refund limit. If you are not married in the NOL year (or are married to a different spouse), and in the carryback year you were married and filed a joint return, your refund for the overpaid joint tax may be limited. You can claim a refund for the difference between your share of the refigured tax and your contribution toward the tax paid on the joint return. The refund cannot be more than the joint overpayment. Attach a statement showing how you figured your claim.

Figuring your share of a joint tax liability. There are five steps for figuring your share of the refigured joint tax liability.

1) Figure your total tax as though you had filed as “married filing separately,”
2) Figure your spouse's total tax as though your spouse had also filed as “married filing separately,”
3) Add the amounts in (1) and (2),
4) Divide the amount in (1) by the amount in (3), and
5) Multiply the refigured tax on your joint return by the amount figured in (4). This is your share of the joint tax liability.

Figuring your contribution toward tax paid. Unless you have an agreement or clear evidence of each spouse's contributions toward the payment of the joint tax liability, figure your contribution by adding the tax withheld on your wages and your share of joint estimated tax payments or tax paid with the return. If the original return for the carryback year resulted in an overpayment, reduce your contribution by your share of the tax refund. Figure your share of a joint payment or refund by the same method used in figuring your share of the joint tax liability. Use your taxable income as originally reported on the joint return in steps (1) and (2), and substitute the joint payment or refund for the refigured joint tax in step (5).

Change in Filing Status

If you and your spouse were married and filed a joint return for each year involved in figuring NOL carrybacks and carryovers, figure the NOL deduction on a joint return as you would for an individual. However, treat the NOL deduction as a joint NOL. Figure it from the joint NOLs.

If you and your spouse were married and filed separate returns for each year involved in figuring NOL carrybacks and carryovers, the spouse who sustained the loss may take the NOL deduction on a separate return.

CAUTION *Special rules apply for figuring the NOL carrybacks and carryovers of married people whose filing status changes for any tax year involved in figuring an NOL carryback or carryover.*

Separate to joint return. If you and your spouse file a joint return for a carryback or carryforward year, and were married but filed separate returns for any of the tax years involved in figuring the NOL carryback or carryover, treat the separate carryback or carryover as a joint carryback or carryover.

Joint to separate returns. If you and your spouse file separate returns for a carryback or carryforward year, but filed a joint return for any or all of the tax years involved in figuring the NOL carryover, figure each of your carryovers separately.

Joint return in NOL year. Figure each spouse's share of the joint NOL in the following steps:

1) Figure each spouse's NOL as if he or she filed a separate return. See *How To Figure an NOL,* earlier. If only one spouse has an NOL, ***stop here.*** All of the joint NOL is that spouse's NOL.
2) If both spouses have an NOL, multiply the joint NOL by a fraction, the numerator of which is spouse A's NOL figured in (1) and the denominator of which is the total of the spouses' NOLs figured in (1). The result is spouse A's share of the joint NOL. The rest of the joint NOL is spouse B's share.

Example 1. Mark and Nancy are married and file a joint return for 1997. They have an NOL of $5,000. They carry the NOL back to 1994, a year in which Mark and Nancy filed separate returns. Figured separately, Nancy's 1997 deductions were more than her income, and Mark's income was more than his deductions. Mark does not have any NOL to carry back. Nancy may carry back the entire $5,000 NOL to her 1994 separate return.

Example 2. Assume the same facts as in Example 1 except that both Mark and Nancy had deductions in 1997 that were more than their income. Figured separately, his NOL is $1,800 and hers is $3,000. (The sum of their separate NOLs is less than their $5,000 joint NOL because his deductions included a $200 net capital loss that is not allowed in figuring his separate NOL. The loss is allowed in figuring their joint NOL because it was offset by Nancy's capital gains.) Mark's share of their $5,000 joint NOL is $1,875 ($5,000 × $1,800/$4,800) and Nancy's is $3,125 ($5,000 – $1,875).

Joint return in previous carryback or carryforward year. If only one spouse had an NOL deduction on the previous year's joint return, all of the joint carryover is that spouse's carryover. If both spouses had an NOL deduction (including separate carryovers of a joint NOL, figured as explained in the previous discussion), figure each spouse's share of the joint carryover in the following steps:

1) Figure each spouse's modified taxable income as if he or she filed a separate return. See *Modified taxable income* under *How To Figure an NOL Carryover,* later.

2) Multiply the joint modified taxable income you used to figure the joint carryover by a fraction, the numerator of which is spouse A's modified taxable income figured in (1) and the denominator of which is the total of the spouses' modified taxable incomes figured in (1). This is spouse A's share of the joint modified taxable income.

3) Subtract the amount figured in (2) from the joint modified taxable income. This is spouse B's share of the joint modified taxable income.

4) Reduce the amount figured in (3), but not below zero, by spouse B's NOL deduction.

5) Add the amounts figured in (2) and (4).

6) Subtract the amount figured in (5) from spouse A's NOL deduction. This is spouse A's share of the joint carryover. The rest of the joint carryover is spouse B's share.

Example. Sam and Wanda filed a joint return for 1994 and separate returns for 1995, 1996, and 1997. In 1997, Sam had an NOL of $18,000 and Wanda had an NOL of $2,000. They carry back both NOLs to their 1994 joint return and claim a $20,000 NOL deduction.

Their joint modified taxable income (MTI) for 1994 is $15,000, and their joint NOL carryover to 1995 is $5,000 ($20,000 – $15,000). They figure their shares of the $5,000 carryover as follows:

Step 1.	
Sam's separate MTI	$9,000
Wanda's separate MTI	+ 3,000
Total MTI	$12,000
Step 2.	
Joint MTI	$15,000
Sam's MTI ÷ total MTI ($9,000 ÷ $12,000)	× .75
Sam's share of joint MTI	$11,250
Step 3.	
Joint MTI	$15,000
Sam's share of joint MTI	– 11,250
Wanda's share of joint MTI	$3,750
Step 4.	
Wanda's share of joint MTI	$3,750
Wanda's NOL deduction	– 2,000
Wanda's remaining share	$1,750
Step 5.	
Sam's share of joint MTI	$11,250
Wanda's remaining share	+ 1,750
Joint MTI to be offset	$13,000
Step 6.	
Sam's NOL deduction	$18,000
Joint MTI to be offset	– 13,000
Sam's carryover to 1995	$5,000
Joint carryover to 1995	$5,000
Sam's carryover	– 5,000
Wanda's carryover to 1995	$–0–

Wanda's $2,000 NOL deduction offsets $2,000 of her $3,750 share of the joint modified taxable income and is completely used up. She has no carryover to 1995. Sam's $18,000 NOL deduction offsets all of his $11,250 share of joint modified taxable income and the remaining $1,750 of Wanda's share. His carryover to 1995 is $5,000.

Illustrated Form 1045

The following example illustrates how to use Form 1045 to claim an NOL deduction in a carryback year. It includes a filled-in page 1 of Form 1045.

Example. Martha Sanders is a self-employed contractor. Because of a business loss, Martha's 1997 deductions are more than her 1997 income. She uses Form 1045 to carry back her NOL and claim an NOL deduction in 1994. See the filled-in Form 1045 included here. Her filing status both years was “single.”

Martha figures her 1997 NOL on Schedule A, Form 1045 (not shown). (For an example using Schedule A, see *Illustrated Schedule A (Form 1045)* under *How To Figure an NOL,* earlier.) She enters the $10,000 NOL from line 25 of Schedule A on line 1a of page 1 of Form 1045.

Martha completes lines 10 through 26 under “3rd preceding tax year ended 12/31/94” on page 1 of Form 1045 using the following amounts from her 1994 return.

Adjusted gross income		$50,000
Itemized deductions:		
Medical expenses ($6,000 minus 7.5% of adjusted gross income)	$2,250	
State income tax	2,000	
Real estate tax	4,000	
Home mortgage interest	5,000	
Total		$13,250
Exemption		$2,450
Income tax		$6,654
Self-employment tax		$6,120

On line 11, column (b), Martha enters her $10,000 NOL deduction. Her new adjusted gross income on line 12, column (b), is $40,000 ($50,000– $10,000).

To complete line 13, column (b), she must refigure her medical expense deduction using her new adjusted gross income. Her refigured medical expense deduction is $3,000 [$6,000 – ($40,000 × 7.5%)]. This increases her total deductions to $14,000 [$13,250 + ($3,000 – $2,250)].

Martha uses her refigured taxable income ($23,550) from line 16, column (b), and the tax tables in her 1994 Form 1040 instructions to find her income tax. She enters the new amount, $3,644, on line 17, column (b), and her new total tax liability, $9,764, on line 26, column (b).

Martha uses up her $10,000 NOL in 1994, so she does not complete the columns for the second and first preceding tax years. The decrease in tax because of her NOL deduction (line 28) is $3,010.

Martha files Form 1045 after filing her 1997 return, but no later than December 31, 1998. She mails it to the Internal Revenue Service Center where she filed her 1997 return and attaches a copy of her 1997 return (including its attached forms and schedules).

Form **1045**

Department of the Treasury
Internal Revenue Service

Application for Tentative Refund

► **Before you fill in this form, read the separate instructions.**
► **Do not attach to your income tax return—mail in a separate envelope.**
► **For use by individuals, estates, or trusts.**

OMB No. 1545-0098

1997

Please type or print

Name (and name of spouse if filing jointly) Martha Sanders	**Social security or employer identification number** 123-00-4567
Number, street, and apt. or suite no. If you have a P.O. box or a foreign address, see the instructions. 9876 Holly Street	**Spouse's social security number**
City, town or post office, state, and ZIP code Yardley, PA 19067	Telephone no. (optional) (041) 123-4567

1 This application is filed to carry back: **a** Net operating loss (from Schedule A, page 2, line 25) $ $10,000 **b** Unused general business credit $

2a For the calendar year 1997, or other tax year beginning , 1997, ending , 19 . **b** Date tax return was filed 3-5-98

3 If this application is for an unused credit created by another carryback, give year of the first carryback ►

4 If you filed a joint return (or separate return) for some, but not all, of the tax years involved in figuring the carryback, list the years and specify whether joint (J) or separate (S) return for each ►

5 If social security number for carryback year is different from above, enter **a** SSN ► and **b** Year(s) ►

6 If you changed your accounting period, give date permission to change was granted ►

7 Have you filed a petition in Tax Court for the year(s) to which the carryback is to be applied? ☐ Yes ☑ No

8 Does this carryback include a loss or credit from a tax shelter required to be registered? ☐ Yes ☑ No

9 If you are carrying back a net operating loss, did this cause the release of foreign tax credits or the release of other credits because of the release of the foreign tax credit? See instructions ☐ Yes ☑ No

Computation of Decrease in Tax	3rd preceding tax year ended ► 12-31-94		2nd preceding tax year ended ►		1st preceding tax year ended ►	
Note: *If **1a** is blank, skip lines 10 through 16.*	**(a)** Before carryback	**(b)** After carryback	**(c)** Before carryback	**(d)** After carryback	**(e)** Before carryback	**(f)** After carryback
10 Adjusted gross income from tax return or as previously adjusted	50,000	50,000				
11 Net operating loss deduction after carryback. See instructions		10,000				
12 Subtract line 11 from line 10	50,000	40,000				
13 Deductions. See instructions	13,250	14,000				
14 Subtract line 13 from line 12	36,750	26,000				
15 Exemptions	2,450	2,450				
16 Taxable income. Line 14 minus line 15	34,300	23,550				
17 Income tax. See instructions—attach explanation	6,654	3,644				
18 General business credit						
19 Other credits. Identify						
20 Total credits. Add lines 18 and 19						
21 Subtract line 20 from line 17	6,654	3,644				
22 Recapture taxes						
23 Alternative minimum tax						
24 Self-employment tax	6,120	6,120				
25 Other taxes						
26 Total tax liability. Add lines 21 through 25	12,774	9,764				
27 Enter amount from line 26, cols. (b), (d), and (f)	9,764					
28 Decrease in tax. Line 26 minus line 27	3,010					

29 Overpayment of tax due to a claim of right adjustment under section 1341(b)(1)—attach computation

Sign Here

Keep a copy of this application for your records.

Under penalties of perjury, I declare that I have examined this application and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete.

Your signature: Martha Sanders — Date: 4-10-98

Spouse's signature (if Form 1045 is filed jointly, BOTH must sign) — Date

Preparer Other Than Taxpayer Name ► Address ► Date

For Paperwork Reduction Act Notice, see separate instructions. Cat. No. 10670A Form **1045** (1997)

How To Figure an NOL Carryover

If your NOL is more than your taxable income for the year to which you carry it (figured before deducting the NOL), you may have an NOL carryover. You must make certain modifications to your taxable income to determine how much NOL you will use up in that year and how much you can carry over to the next tax year. Your carryover is the excess of your NOL deduction over your modified taxable income for the carryback or carryforward year. If your NOL deduction includes more than one NOL, apply the NOLs against your modified taxable income in the same order in which you incurred them, starting with the earliest.

Modified taxable income. Your modified taxable income is your taxable income figured with the following changes:

1) You cannot claim an NOL deduction for the NOL whose carryover you are figuring or for any later NOL.
2) You cannot claim a deduction for capital losses in excess of your capital gains.
3) You cannot claim your exemptions for yourself or dependents.
4) You must figure any item affected by the amount of your adjusted gross income after making the changes in (1) and (2), above, and certain other changes to your adjusted gross income that result from (1) and (2). This includes income and deduction items used to figure adjusted gross income (for example, IRA deductions), as well as certain itemized deductions. To figure a charitable contribution deduction, do not include deductions for NOL carrybacks in the change in (1) but do include deductions for NOL carryforwards from tax years before the NOL year.

Your taxable income as modified cannot be less than zero.

Schedule B (Form 1045). You can use Schedule B (Form 1045) to figure your modified taxable income for carryback years and your carryover from each of those years. Do ***not*** use Schedule B for a carryforward year. If your 1997 return includes an NOL deduction from an NOL year before 1997 that reduced your taxable income to zero (to less than zero, if an estate or trust), see *NOL Carryover From 1997 to 1998,* later.

Illustrated Schedule B (Form 1045)

The following example illustrates how to figure an NOL carryover from a carryback year. It includes a filled-in Schedule B (Form 1045).

Example. Ida Brown runs a small clothing shop. In 1997, she has an NOL of $36,000 that she chooses to carry back to 1994. She has no other carrybacks or carryovers to 1994.

Ida's adjusted gross income in 1994 was $29,000, consisting of her salary of $30,000 minus a $1,000 capital loss deduction. She is single and claimed only one personal exemption of $2,450. During that year, she gave $1,450 in charitable contributions. Her medical expenses were $2,725. She also deducted $1,650 in taxes and $1,125 in home mortgage interest.

Her deduction for charitable contributions was not limited because her contributions, $1,450, were less than 50% of her adjusted gross income. The deduction for medical expenses was limited to expenses over 7.5% of adjusted gross income (.075 × $29,000 = $2,175; $2,725 – $2,175 = $550). The deductions for taxes and home mortgage interest were not subject to any limits. She was able to claim $4,775 ($1,450 + $550 + $1,650 + $1,125) in itemized deductions for 1994. She had no other deductions in 1994. Her taxable income for the year was $21,775.

Ida's $36,000 carryback will reduce her 1994 taxable income to zero. She completes column (a) of Schedule B (Form 1045) to figure how much of her NOL she uses up in 1994 and how much she can carry over to 1995. See the illustrated Schedule B shown here. Ida does not complete columns (b) and (c) because the $10,700 carryover to 1995 is completely used up that year. (See the information for line 8, below.)

Line 1. Ida enters $36,000, her 1997 net operating loss, on line 1.

Line 2. She enters $21,775, her 1994 taxable income, on line 2.

Line 3. Ida enters on line 3 her net capital loss deduction of $1,000.

Line 4. Although Ida's entry on line 3 modifies her adjusted gross income, that does not affect any other items included in her adjusted gross income. Ida enters zero on line 4.

Line 5. Since Ida had itemized deductions and entered $1,000 on line 3, she completes lines 9 through 33 to figure her adjustment to itemized deductions. On line 5, she enters the total adjustment from line 33.

Line 9. Ida's adjusted gross income for 1994 was $29,000.

Line 10. She adds lines 3 and 4 and enters $1,000 on line 10. (This is her net capital loss deduction added back, which modifies her adjusted gross income.)

Line 11. Her modified adjusted gross income for 1994 is now $30,000.

Line 12. Her actual medical expenses were $2,725.

Line 13. She multiplies her modified adjusted gross income, $30,000, by .075. She enters $2,250 on line 13.

Line 14. The difference between her actual medical expenses and the amount she is allowed to deduct is $475.

Line 15. On her 1994 tax return, she deducted $550 as medical expenses.

Line 16. The difference between her medical deduction and her modified medical deduction is $75. She enters this on line 16.

Line 17. She enters her modified adjusted gross income of $30,000 on line 17.

Line 18. She had no other carrybacks to 1994 and enters zero on line 18.

Line 19. Her modified adjusted gross income remains $30,000.

Line 20. She now refigures her charitable contributions based on her modified adjusted gross income. Since she is well below the 50% limit, she enters $1,450 on line 20.

Line 21. Her actual contributions for 1994 were $1,450, which she enters on line 21.

Line 22. The difference is zero.

Lines 23 through 32. Since Ida had no casualty losses or deductions for miscellaneous items in 1994, she leaves these lines blank.

Line 33. She combines lines 16, 22, 27, and 32 and enters $75 on line 33. She carries this figure to ***line 5.***

Line 6. Ida enters her personal exemption of $2,450 for 1994.

Line 7. After combining lines 2 through 6, Ida's modified taxable income is $25,300.

Line 8. Ida figures her carryover to 1995 by subtracting her modified taxable income (line 7) from her NOL deduction (line 1). She enters the $10,700 carryover on line 8. She also enters this $10,700 on page 1 of Form 1045, line 11 of column (d), as her NOL deduction for 1995. (For an illustrated example of page 1 of Form 1045, see *Illustrated Form 1045* under *How To Claim an NOL Deduction,* earlier.)

Schedule B—Net Operating Loss Carryover. See instructions.

Complete one column **before** going to the next column.	**(a)** 3rd preceding tax year ended ▶ 12-31-94	**(b)** 2nd preceding tax year ended ▶	**(c)** 1st preceding tax year ended ▶
1 **Net operating loss deduction.** In column (a), enter as a positive number the net operating loss from Schedule A, line 25. In columns (b) and (c), enter amounts from line 8 below, columns (a) and (b), respectively	36,000		
2 Taxable income from tax return (or as previously adjusted) before 1997 NOL carryback. (For individuals, if line 38 of Form 1040 is zero, subtract line 37 (Form 1040) from line 36 (Form 1040), and enter the difference as a negative number	21,775		
3 Net capital loss deduction from Sch. D (Form 1040), line 19, or from Sch. D (Form 1041), line 18. Enter as a positive number	1,000		
4 Adjustments to adjusted gross income. See instructions	-0-		
5 Adjustment to itemized deductions. See instructions	75		
6 Deduction for exemptions from tax return (or as previously adjusted). Estates and trusts, enter exemption amount	2,450		
7 Modified taxable income. Combine lines 2 through 6. If zero or less, enter -0-	25,300		
8 **Net operating loss carryover.** Subtract line 7 from line 1. If zero or less, enter -0-. See instructions	10,700		
Adjustment to Itemized Deductions (Individuals Only) Complete lines 9 through 33 **ONLY** if, for any of the 3 preceding years, you itemized deductions.			
9 Adjusted gross income per return (or as previously adjusted) before 1997 NOL carryback	29,000		
10 Add lines 3 and 4 above	1,000		
11 Modified adjusted gross income. Add lines 9 and 10	30,000		
12 Medical expenses from Sch. A (Form 1040), line 1	2,725		
13 Multiply line 11 by .075	2,250		
14 Subtract line 13 from line 12. If zero or less, enter -0-	475		
15 Medical expenses from Sch. A (Form 1040), line 4 (or as previously adjusted)	550		
16 Subtract line 14 from line 15	75		

Schedule B—Net Operating Loss Carryover *(Continued)*

Complete one column **before** going to the next column.	**(a)** 3rd preceding tax year ended ▶ 12-31-94		**(b)** 2nd preceding tax year ended ▶		**(c)** 1st preceding tax year ended ▶	
17 Modified adjusted gross income from line 11	30,000					
18 Enter as a positive number any NOL carryback from a year before 1997 that was deducted in figuring line 9 on page 3	-0-					
19 Add lines 17 and 18	30,000					
20 Refigure your charitable contributions using line 19 as your adjusted gross income. See instructions	1,450					
21 Charitable contributions from Sch. A (Form 1040), line 18	1,450					
22 Subtract line 20 from line 21		-0-				
23 Casualty and theft losses from Form 4684, line 16						
24 Multiply line 11 by .10						
25 Subtract line 24 from line 23. If zero or less, enter -0-						
26 Casualty and theft losses from Form 4684, line 18 (or as previously adjusted)						
27 Subtract line 25 from line 26						
28 Miscellaneous itemized deductions from Sch. A (Form 1040), line 23						
29 Multiply line 11 by .02						
30 Subtract line 29 from line 28. If zero or less, enter -0-						
31 Miscellaneous itemized deductions from Sch. A (Form 1040), line 26 (or as previously adjusted)						
32 Subtract line 30 from line 31						
33 Combine lines 16, 22, 27, and 32. If line 11 is more than $111,800 for 1994 ($55,900 if married filing separately), more than $114,700 for 1995 ($57,350 if married filing separately), or more than $117,950 for 1996 ($58,975 if married filing separately), complete the worksheet on page 4 of the instructions. Otherwise, enter the amount from this line on line 5 (page 3)		75				

NOL Carryover From 1997 to 1998

If you had an NOL deduction that reduced your taxable income on your 1997 return to zero (to less than zero, if an estate or trust), complete Table 1, *Worksheet for NOL Carryover From 1997 to 1998.* It will help you figure your NOL to carry to 1998. Keep the worksheet for your records.

Worksheet Instructions

At the top of the worksheet, enter the NOL year for which you are figuring the carryover.

CAUTION ***More than one NOL.*** *If your 1997 NOL deduction includes amounts for more than one loss year, complete this worksheet only for one loss year. To determine which year, start with your negative taxable income. (An individual's negative taxable income is figured by subtracting the amount on line 37 of Form 1040 from the amount on line 36 of Form 1040.) Then, beginning with the earliest NOL, add each NOL (treated as a positive amount) separately to your negative taxable income. Complete this worksheet for the earliest NOL that increases your taxable income to zero or more. Your earlier NOLs will be completely used up in 1997. Your NOL carryover to 1998 is the total of the amount on line 8 of the worksheet and all later NOL amounts.*

Example. Your negative taxable income is ($4,000). Your NOL deduction includes $2,000 for 1994, $7,000 for 1995, and $5,000 for 1996. Add your 1994 NOL of $2,000 to ($4,000). This gives you taxable income of ($2,000). Your 1994 NOL is now completely used up. Add your $7,000 1995 NOL to ($2,000). This gives you taxable income of $5,000. You now complete the worksheet for your 1995 NOL. Your NOL carryover to 1998 is the unused part of your 1995 NOL from line 8 of the worksheet, plus your $5,000 1996 NOL.

Line 2. Treat your NOL deduction for the NOL year entered at the top of the worksheet and later years as a positive amount. Add it to your negative taxable income. Enter the result on line 2.

Line 4. You must refigure certain income and deductions based on adjusted gross income. These are:

1) The special allowance for passive activity losses from rental real estate activities,
2) Taxable social security and tier 1 railroad retirement benefits,
3) IRA deductions, and
4) Excludable savings bond interest.

If none of these items apply to you, enter zero on line 4. Otherwise, increase your adjusted gross income by the total of line 3 and your NOL deduction for the NOL year entered at the top of the worksheet and later years. Using this increased adjusted gross income, refigure the items that apply, in the order listed above. Your adjustment for each item is the difference between the refigured amount and the amount included on your return. Add the adjustments for previous items to your adjusted gross income before refiguring the next item. Keep a record of your computations.

Enter your total adjustments for the above items on line 4.

Line 5. Enter zero if you claimed the standard deduction. Otherwise, use lines 9 through 40 of the worksheet to figure the amount to enter on this line. Complete only those sections that apply to you.

Estates and trusts. Enter zero on line 5 if you did not claim any miscellaneous deductions on line 15b (Form 1041) or a casualty or theft loss. Otherwise, refigure these deductions by substituting modified adjusted gross income (see below) for adjusted gross income. Subtract the recomputed deductions from those claimed on the return. Enter the result on line 5.

Modified adjusted gross income. To refigure miscellaneous itemized deductions of an estate or trust (Form 1041, line 15b), modified adjusted gross income is the total of:

1) The adjusted gross income on the return,
2) The amount from line 3 of the worksheet,
3) The exemption amount from Form 1041, line 21, and
4) The NOL deduction for the NOL year entered at the top of the worksheet and for later years.

To refigure the casualty and theft loss deduction of an estate or trust, modified adjusted gross income is the total of:

1) The adjusted gross income amount you used to figure the deduction claimed on the return,
2) The amount from line 3 of the worksheet, and
3) The NOL deduction for the NOL year entered at the top of the worksheet and for later years.

Line 9. Treat your NOL deduction for the NOL year entered at the top of the worksheet and for later years as a positive amount. Add it to your adjusted gross income. Enter the result on line 9.

Line 18. If you had a contributions carryover from 1996 to 1997 and your NOL deduction includes an amount from an NOL year before 1996, you may have to reduce your contributions carryover. This reduction is any adjustment you made to your 1996 charitable contributions deduction when figuring your NOL carryover to 1997. Use the reduced contributions carryover to figure the amount to enter on line 18.

Table 1. **Worksheet for NOL Carryover From 1997 to 1998 (For an NOL Year Before 1997)**

For Use by Individuals, Estates, and Trusts (Keep for your records)
See the instructions under *NOL Carryover From 1997 to 1998.*

NOL YEAR: ___________

USE YOUR 1997 FORM 1040 (OR FORM 1041) TO COMPLETE THIS WORKSHEET:

1. Enter as a positive number your NOL deduction for the NOL year entered above from line 21 (Form 1040)		
2. Enter your taxable income without the NOL deduction for the NOL year entered above or later years. (See instructions.)		
3. Enter as a positive number any net capital loss deduction on line 13 (Form 1040)		
4. Enter any adjustments to your adjusted gross income (See instructions.)		
5. Enter any adjustments to your itemized deductions from line 30 or line 40 below. (See instructions.)		
6. Enter your deduction for personal exemptions from line 37 (Form 1040)		
7. Modified taxable income. Combine lines 2 through 6. Enter the result (but not less than zero)		
8. NOL carryover to 1998. Subtract line 7 from line 1. Enter the result (but not less than zero)		

ADJUSTMENTS TO ITEMIZED DEDUCTIONS (INDIVIDUALS ONLY):

9. Enter your adjusted gross income without the NOL deduction for the NOL year entered above or later years. (See instructions.)		
10. Combine lines 3 and 4 above		
11. Modified adjusted gross income. Combine lines 9 and 10 above		

ADJUSTMENT TO MEDICAL EXPENSES:

12. Enter your medical expenses from Schedule A (Form 1040), line 4		
13. Enter your medical expenses from Schedule A (Form 1040), line 1		
14. Multiply line 11 above by 7.5% (.075)		
15. Subtract line 14 from line 13. Enter the result (but not less than zero)		
16. Subtract line 15 from line 12		

ADJUSTMENT TO CHARITABLE CONTRIBUTIONS:

17. Enter your charitable contributions deduction from Schedule A (Form 1040), line 18		
18. Refigure your charitable contributions deduction using line 11 above as your adjusted gross income. (See instructions)		
19. Subtract line 18 from line 17		

ADJUSTMENT TO CASUALTY AND THEFT LOSSES:

20. Enter your casualty and theft losses from Form 4684, line 18		
21. Enter your casualty and theft losses from Form 4684, line 16		
22. Multiply line 11 above by 10% (.10)		
23. Subtract line 22 from line 21. Enter the result (but not less than zero)		
24. Subtract line 23 from line 20		

ADJUSTMENT TO MISCELLANEOUS DEDUCTIONS:

25. Enter your miscellaneous deductions from Schedule A (Form 1040), line 26		
26. Enter your miscellaneous deductions from Schedule A (Form 1040), line 23		
27. Multiply line 11 above by 2% (.02)		
28. Subtract line 27 from line 26. Enter the result (but not less than zero)		
29. Subtract line 28 from line 25		

TENTATIVE TOTAL ADJUSTMENT:

30. Combine lines 16, 19, 24, and 29, and enter the result here. If line 11 above is $121,200 or less ($60,600 or less if married filing separately), also enter the result on line 5 above and **stop here.** Otherwise, go to line 31		

Table 1. **(Continued)**

ADJUSTMENT TO OVERALL ITEMIZED LIMIT:		
31. Enter the amount on Schedule A (Form 1040), line 28		
32. Add lines 15, 18, 23, and 28, and the amounts on Schedule A (Form 1040), lines 9, 14, and 27		
33. Add lines 15 and 23, the amount on Schedule A (Form 1040), line 13, and any gambling losses included on Schedule A (Form 1040), line 28		
34. Subtract line 33 from line 32. If the result is zero, enter the amount from line 30 on line 5 above and **stop here.** Otherwise, go to line 35		
35. Multiply line 34 by 80% (.80)		
36. Subtract $121,200 ($60,600 if married filing separately) from the amount on line 11		
37. Multiply line 36 by 3% (.03)		
38. Enter the smaller of line 35 or line 37		
39. Subtract line 38 rom line 32. Enter the result (but not less than your standard deduction amount)		
40. Subtract line 39 from 31. Enter the result here and on line 5		

Corporations

A corporation generally figures and deducts an NOL the same way an individual, estate, or trust does. The same carryback and carryforward periods apply, and the same sequence applies when it carries two or more NOLs to the same year. See *When To Use an NOL* and *How To Figure an NOL Carryover,* earlier.

A corporation's NOL generally differs from an individual's, estate's, or trust's in two ways:

1) A corporation can take different deductions when figuring an NOL, and

2) A corporation must make different modifications to its taxable income in the carryback or carryforward year when figuring how much of the NOL is used and how much is carried to the next year.

A corporation also uses different forms when claiming an NOL deduction from those used by individuals, estates, and trusts.

The following discussions explain these differences.

Figuring the NOL

A corporation figures an NOL in the same way it figures taxable income. It starts with its gross income and subtracts its deductions. If its deductions are more than its gross income, the corporation has an NOL.

However, there are rules for figuring the NOL that either limit what it can deduct, or permit deductions not ordinarily allowed. These rules are:

1) A corporation cannot deduct any NOL carrybacks or carryovers from other years,

2) A corporation can take the deduction for dividends received, explained later, without regard to the aggregate limits (based on taxable income) that normally apply, and

3) A corporation can figure the deduction for dividends paid on certain preferred stock of public utilities without limiting it to its taxable income for the year.

Dividends-received deduction. The corporation's deduction for dividends received from domestic corporations is generally subject to an aggregate limit of 70% or 80% of taxable income. However, if a corporation sustains an NOL for a tax year, the limit on this deduction based on taxable income does not apply. In determining if a corporation has an NOL, the corporation figures the dividends-received deduction without regard to the 70% or 80% of taxable income limit.

See Publication 542 for more information on the dividends-received deduction.

Example. A corporation had $500,000 gross income from business operations and $625,000 of allowable business expenses. It also received $150,000 in dividends from a domestic corporation for which it can take an 80% deduction, ordinarily limited to 80% of its taxable income before the deduction. It figures its NOL as follows:

Income from business	$500,000
Dividends	150,000
Gross income	$650,000
Deductions (expenses)	(625,000)
Taxable income before special deductions	$25,000
Minus: Deduction for dividends received, 80% of $150,000	(120,000)
Net operating loss	($95,000)

Claiming the NOL Deduction

The form a corporation uses to deduct its NOL depends on whether it carries the NOL back or forward.

For a carryback. If a corporation carries back the NOL, it can use either Form 1120X, *Amended U.S. Corporation Income Tax Return* or Form 1139, *Corporation Application for Tentative Refund.* A corporation can get a refund faster by using Form 1139. It cannot file Form 1139 before filing the return for the corporation's NOL year, but it must file Form 1139 no later than one year after the NOL year.

If the corporation does not file Form 1139, it must file Form 1120X within 3 years of the due date, plus extensions, for filing the return for the year in which it has the NOL.

For a carryforward. If a corporation carries forward its NOL, it enters the carryover on Schedule K (Form 1120), line 15. It also enters the deduction for the carryover (but not more than the corporation's taxable income after special deductions) on line 29(a) of Form 1120 or line 25(a) of Form 1120–A.

Carryback expected. If a corporation expects to have an NOL in its current year, it may automatically extend the time for paying all or part of its income tax for the immediately preceding year. It does this by filing Form 1138, *Extension of Time for Payment of Taxes by a Corporation Expecting a Net Operating Loss Carryback.* It must explain on the form why it expects the loss.

The extension applies to previously determined unpaid tax that must be paid after filing Form 1138. This amount cannot exceed the tax overpayment in the carryback years due to the NOL carryback.

Period of extension. The extension is in effect until the end of the month in which the return for the NOL year is due, including extensions.

If the corporation files Form 1139 before this date, the extension will continue until the date the IRS notifies the corporation that its Form 1139 is disallowed in whole or in part.

Figuring the NOL Carryover

If the NOL available for a carryback or carryforward year is greater than the taxable income for that year, the corporation must modify its taxable income to figure how much of the NOL it will use up in that year and how much it can carry to the next tax year. Its carryover is the excess of the available NOL over its modified taxable income for the carryback or carryforward year.

Modified taxable income. A corporation figures its modified taxable income in the same way it figures taxable income. But it can deduct NOLs only from years before the NOL year whose carryover is being figured. The corporation must figure its deduction for charitable contributions without considering any NOL carrybacks. The modified taxable income for any year cannot be less than zero.

Modified taxable income is used only to figure how much of an NOL the corporation uses up in the carryback or carryforward year and how much it carries to the next year. It is not used to fill out the corporation's tax return or figure its tax.

Ownership change. A loss corporation that has an ownership change is limited on the taxable income it can offset by NOL carryforwards arising before the date of the ownership change. This limit applies to any year ending after the change of ownership.

See sections 381, 382, 383, 384, and 269 of the Internal Revenue Code and the related regulations for more information about the limits on corporate NOL carryovers and corporate ownership changes.

Corporate equity reduction transactions. The portion of an NOL generated by certain interest deductions attributable to a corporate equity reduction transaction may not be carried back to a tax year before the tax year of the corporate equity reduction transaction. For more information, see sections 172(b)(1)(E) and 172(h) of the Internal Revenue Code.

Worksheet for Figuring the NOL Carryover

A corporation without a capital loss carryback or deduction for percentage depletion for oil and gas wells can use the worksheet in Table 2 to figure how much of its NOL is used up in a carryback or carryforward year and how much to carry over to the next year.

On line A, Part I, enter the carryback or carryforward year from which the NOL is being carried. For example, if the worksheet is used to figure the carryover from 1997 to 1998, enter 1997. On line B, enter the NOL year whose carryover must be figured.

More than one NOL. If more than one NOL is available for the carryback or carryforward year (year A), complete the worksheet only for one loss year (year B). To determine which year, start with the earliest NOL and subtract each NOL separately from the corporation's taxable income figured without the NOL deduction. Complete the worksheet for the earliest NOL that reduces the corporation's taxable income below zero. The earlier NOLs are completely used up in year A. The later NOLs are carried over in full.

Table 2. **Worksheet for Figuring a Corporation's NOL Carryover**

See the instructions under *Corporations.*

PART I			
A. Carryback or carryforward year—Enter the year from which the NOL is being carried			
B. NOL year—Enter the year in which the NOL occurred (the loss year). If the corporation has more than one NOL, see the instructions			
C. NOL amount—Enter the amount of year B's NOL that was carried to year A			
D. If more than one NOL was carried to year A, enter the total of all—			
1. Carryovers of NOLs that preceded both years A and B			
2. Carrybacks of NOLs that preceded year B			
PART II			
1. Taxable income for year A before the NOL deduction and special deductions—Enter the amount from line 28, Form 1120 (line 24, Form 1120-A)			
2. Enter the amount from line D1 of Part I			
3. Subtract line 2 from line 1			
4. If year A is a carryforward year, enter the deduction for charitable contributions figured by using the amount on line 3 as taxable income. Otherwise, enter zero			
5. Enter the amount from line D2 of PART I			
6. Dividends received deduction:			
a. Subtract line 4 from line 1			
b. Dividends received deduction figured by using the amount on line 6a as taxable income			
7. Add lines 4, 5, and 6b			
8. Modified taxable income—Subtract line 7 from line 3. (If line 7 is more than line 3, enter zero.)			
9. Carryover—Subtract line 8 from line C, PART I			

How To Get More Information

You can get help from the IRS in several ways.

Free publications and forms. To order free publications and forms, call 1–800–TAX–FORM (1–800–829–3676). You can also write to the IRS Forms Distribution Center nearest you. Check your income tax package for the address. Your local library or post office also may have the items you need.

For a list of free tax publications, order Publication 910, *Guide to Free Tax Services.* It also contains an index of tax topics and related publications and describes other free tax information services available from IRS, including tax education and assistance programs.

If you have access to a personal computer and modem, you also can get many forms and publications electronically. See *Quick and Easy Access to Tax Help and Forms* in your income tax package for details.

Tax questions. You can call the IRS with your tax questions. Check your income tax package or telephone book for the local number, or call 1–800–829–1040.

TTY/TDD equipment. If you have access to TTY/TDD equipment, you can call 1–800–829–4059 to ask tax questions or to order forms and publications. See your income tax package for the hours of operation.

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579SP Cómo Preparar la Declaración de Impuesto Federal
594SP Comprendiendo el Proceso de Cobro
850 English-Spanish Glossary of Words and Phrases Used in Publications Issued by the Internal Revenue Service
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Commonly Used Tax Forms

W-2 Wage and Tax Statement
W-4 Employee's Withholding Allowance Certificate
940 Employer's Annual Federal Unemployment (FUTA) Tax Return
940EZ Employer's Annual Federal Unemployment (FUTA) Tax Return
1040 U.S. Individual Income Tax Return
- **Sch A** Itemized Deductions
- **Sch B** Interest and Dividend Income
- **Sch C** Profit or Loss From Business
- **Sch C-EZ** Net Profit From Business
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- **Sch SE** Self-Employment Tax

1040-ES Estimated Tax for Individuals
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