

Using tentative refund procedures to access cash from estimated tax overpayment, new NOL carryback

April 3, 2020

In brief

The Coronavirus Aid, Relief, and Economic Security Act (CARES Act or Act), enacted March 27, includes a net operating loss (NOL) carryback provision allowing an NOL from tax years beginning in 2018, 2019, or 2020 to be carried back five years. The provision temporarily removes the current-law taxable income limitation and allows an NOL to fully offset income. The provision also makes a retroactive correction to the 2017 tax reform legislation to allow NOLs arising in a fiscal tax year beginning in 2017 and ending in 2018 to be carried back two years.

These NOL provisions can provide an opportunity for companies that previously paid federal income taxes for their 2013 to 2017 tax years to access cash from these NOL carrybacks quickly via tentative refund procedures. The mechanisms of claiming refunds from these NOL carrybacks can be complex and driven by a company's specific fact pattern. In some cases, the slower amended return (Form 1120X, *Amended U.S. Corporation Income Tax Return*) refund process may have to be used. In that regard, it is unclear whether a taxpayer with a 2018 calendar-year NOL can use Form 1139, *Corporation Application for Tentative Refund*, or instead must carry back the loss on Form 1120X.

Given the March 27 date of enactment of the CARES Act, companies have a short window to work through the mechanisms of carrying back eligible NOLs. Companies with eligible NOLs should file quickly as the IRS generally works these claims on a strict 'first in, first out' basis. The IRS typically processes an application for a tentative refund pursuant to Section 6411 in 45 to 90 days; however, timing could be impacted by COVID-19 related circumstances.

Taxpayers may use various tentative or quick refund procedures to obtain refunds from these NOL carrybacks or the overpayment of estimated taxes. This insight discusses the mechanisms of each refund option.

In detail

Form 1139, Corporation Application for Tentative Refund

The IRS typically processes a taxpayer's Form 1139 application within 90 days of the later of either (1) the date the company files the complete application or (2) the last day of the month that includes the due date for filing the company's return for the loss year, including extensions.

The filing deadline and other key administrative issues are crucial to receiving an expedited refund. A Form 1139 cannot be filed until the return for the NOL year has been filed. Therefore, the Form 1139 can be filed after, or at the same time as, the loss year return, but not before that return. The 1139 also must be filed within 12 months after the end of that same loss year. Form 1139 must be filed with the Ogden IRS Center and may not be e-filed.

Like the Form 4466, *Corporation Application for Quick Refund of Overpayment of Estimated Tax*, an application for a tentative refund is not treated as a claim for credit or refund. It may be rejected if there are any material omissions or math errors that are not corrected within the 90-day period. The IRS has rejected Forms 1139 due to minor math errors, missing schedules, and other administrative reasons.

If the Form 1139 is rejected and the taxpayer does not have time to perfect and resubmit the application before the 12-months from the end of the loss year, the corporation then must file a Form 1120X to claim a credit or refund. Unlike with the Form 1139, the IRS has authority to examine the Form 1120X prior to issuance of a refund (and may have to conduct an audit if the claimed refund exceeds the \$5 million threshold for Joint Committee on Taxation review).

Observation: The taxpayer's goal should be to provide the IRS with the most complete and accurate Form 1139 package as possible to avoid questions or other procedural reasons to reject the application for tentative refund.

Below are the attachments a taxpayer should file with a Form 1139 and the suggested order in which they should be attached.

Attachments behind Form 1139 include the following:

- Statement reflecting amounts of regular and alternative minimum tax (AMT) NOL being applied to each year and any NOL/AMT NOL calculation
- Any CARES Act statement the IRS may decide to require
- Form 8302, *Electronic Deposit of Tax Refund of \$1 Million or More*, if applicable (for refunds over \$1 million on a year-by-year rather than an aggregate basis).

Loss Year (Label "Loss Year" on each page)

- Loss year 1120 pages 1-4
- Form 4626, *Alternative Minimum Tax - Corporations*
- Form 3800, *General Business Credit*, if carrying back general business credit
- Schedule D/Form 8949, *Sales and other Dispositions of Capital Assets*, if carrying back a Net Capital Loss (NCL)
- Form 8886, *Reportable Transaction Disclosure Statement*, if applicable.

Gain Year - both before and after carryback (label "Before Carryback" or "As Last Adjusted" and "After Carryback" on each page) *

- Form 1120 pages 1-4
- Form 4626/ACE worksheet and related statements
- Schedule O if applicable
- Schedule D if NCL carryback
- Form 8903, *Domestic Production Activities Deduction*, if applicable
- Form 1118, *Foreign Tax Credit – Corporations*, if applicable (could be optional)
- Form 3800/individual credit form if applicable
- Form 8827, *Credit for Prior Year Minimum Tax—Corporations*, if applicable.

**If the gain year has been amended or been the subject of an examination, the documentation should be “As Last Adjusted” for the pre-carryback calculations to reflect what the IRS currently has on its records. We also suggest including a copy of the first few pages of the Revenue Agent’s Report if there has been an exam, or a copy of the first two pages of the previously filed amended return (in which case there is no need to attach returns as originally filed).*

The order of the attachments should be:

- Form 1139
- NOL statement
- Form 8302
- Loss year 1120 and related forms
- Earliest Gain year 1120 and related forms before carryback (or as last adjusted)
- Earliest Gain year 1120 and related forms after carryback
- Next Earliest Gain year 1120, etc.

Note: The starting point for each year should tie to what the IRS has in its records. If the starting point on the Form 1139 does not match IRS records, it will be rejected. The taxable income on line 11 of Form 1139 includes any NOL carryovers or prior NOL carrybacks that have been processed by the IRS. **Do not** total the overpayments from line 28 of the Form 1139 and list them on line 29.

Do not recompute the charitable contribution deduction but do recompute any Section 199 deduction. As a reminder, **Form 1139 cannot be used to carry back foreign tax credit (FTC) or FTC released by the NOL carryback itself.**

Verify that the banking information provided on Form 8302 is accurate and compatible with the type of request being made (some accounts are fedwire only, some accounts are direct deposit (ACH) only). If the banking information is incorrect, the refund(s) will be delayed a substantial amount of time.

The Form 1139 cannot be filed until the loss year Form 1120 has been filed. If a “bare bones” return (discussed below) will be filed to satisfy this requirement, the proper order would be to file Form 7004, *Application for Automatic Extension of Time to File Certain Business Income Tax, Information, and Other Returns*, for the loss year, file the bare bones return for the loss year, insert on Line 2b of the Form 1139 the date the loss year was filed, and file the Form 1139. The IRS will reject any Form 1139 without a date entered in line 2b, and it will reject it if the date is in the future. The loss year return and Form 1139 can be filed at the same time, but not together.

Form 1139 can be filed only on paper, must have original signatures from the taxpayer, and should be sent to the following address (good for both US mail and private delivery services):

Internal Revenue Service
Mail Stop 6713
1973 Rulon White Blvd.
Ogden, UT 84201

Observation: Current IRS procedures provide that Form 1139 cannot be used to carry back an NOL to a taxable year in which an amount is includible in gross income by reason of Section 965(a). It is unclear whether the IRS will maintain that restriction. In any event, if one or more such “Section 965(a) taxable years of inclusion” is included in the five-year NOL carryback period, the taxpayer may elect to exclude all such taxable years from the carryback period, and thus should be able to use Form 1139. Otherwise, the taxpayer is treated as having made the election under Section 965(n) with respect to each such taxable year.

Observation: Individuals generally can file Form 1045 -- the equivalent to corporate Form 1139 -- to apply for a quick tax refund resulting from the carryback of an NOL. Certain procedural rules apply to the filing of this form as well. Note that there may be an issue for 2018 NOLs for individuals and additional guidance from the IRS is being requested.

Form 4466, Corporation Application for Quick Refund of Overpayment of Estimated Tax

Section 6425 provides that a company may obtain an expedited refund of overpaid estimated tax by filing a Form 4466. Any corporate taxpayer may file a Form 4466 if its overpayment is at least \$500 and 10% of the expected tax liability. A Form 4466 must be:

- Filed after the end of the taxable year
- Filed before the original due date of the corporation's tax return [**Note:** The April 15, 2020, deadline to file a Form 4466 with respect to calendar year 2019 was not postponed to July 15, 2020, by the COVID-19 related grants of relief.]
- Because the April 15 deadline is fast approaching, as an alternative to filing a Form 4466 a corporation could file a 'bare bones' return to request a refund of what it has determined to be excess estimated tax payments. The same "Form 7004 extension, 'bare bones' return, and superseding return" process described below should be followed.
- Filed before the corporation files its return
- Completed in duplicate with the original filed with the IRS Service Center where the corporation files its return with a copy attached to the original return.

Observation: The IRS is supposed to act upon the Form 4466 within 45 days from the date that it is filed, thus providing taxpayers a quick way to recover cash. However, since the filing is not a claim for refund there is no interest liability or other detriment to the IRS in delaying its processing; thus, it may take as long as the extended due date of the tax return for the refund to be made. Furthermore, taxpayers should use caution when utilizing this method. If a refund is later found to be excessive, the taxpayer may be subject to a penalty for underpayment of estimated tax. Electronic deposit of refunds in excess of \$1 million dollars (via Form 8302) can further expedite the receipt of the cash.

Expediting receipt of NOL carryback refund using the superseding return procedures

In the circumstances described below, a corporate taxpayer filing its Form 1120, *U.S. Corporation Income Tax Return*, reporting an NOL should file key documents in the following order:

1. Form 7004, *Application for Automatic Extension of Time to File Corporate Income Tax Return*
2. A 'barebones' Form 1120
3. A Form 1139 based upon the losses calculated on barebones return
4. A 'superseding' Form 1120 filed before the extended due date.

Observation: This process can afford a corporate taxpayer the opportunity to obtain a refund of prior year taxes early in the filing season while providing, if necessary, a means to revise the original return with a superseding original return to report final figures or subsequently received information. It is imperative that the first Form 1120 be conservatively filed with sufficient (albeit not complete) information for it to be considered a valid return. It is important to note that if a company files two returns for the same period on or before the statutorily prescribed due date, the IRS generally will consider the second return filed as the original return.

To summarize, the bare bones process includes the following steps:

- File a Form 7004 extension for the tax return. **Note:** It is a best practice to confirm that the extension has been processed by the IRS and posted with the correct extended due date., However, in light of limited IRS resources available to provide account transcripts, obtaining confirmation via the e-file system that the extension was filed is sufficient.
- Prepare a 'barebones' filing
 - The bare bones return should meet the minimum filing requirements (basically a return that will be processable in the IRS's E File system)

- Consider including a brief statement indicating that a final perfected return will be filed before the extended due date
- E-file the 'barebones' filing
- If applicable and NOL/credit carrybacks are generated, prepare and file Form 1139 for quick refund of overpayments attributable to carrybacks
- File a superseding return on or before the extended due date of the tax return.

The minimum bare bones return requirements include:

- Form 1120 - Pages 1-6
- All lines on 1120 that have an amount that also require a corresponding schedule must have the required schedule attached such as Sch. D, Form 4562, etc.
- At least one return if taxpayer files consolidated otherwise it will be rejected due to the fact the consolidated group box is checked on page one but no subgroup included (and Form 851)
- Consolidated M-3
- Credit schedules 3800, 5884, 6785, 6765, etc. (bare bones)
- If desired, a single consolidated Form 5471/5472 could be included, if applicable, but is not required, as the superseding return will include all required 5471/5472 forms
- Any election(s) required to be made by the original due date of a return excluding extension.
- Form 8050 for deposit of refund.

AMT implications for NOL carrybacks

Although this is an issue that PwC is continuing to review, for NOL carrybacks, it is important to remember that although there is no AMT for corporations post-TCJA, corporations were subject to the AMT in pre-2018 years. Therefore, based on a reasonable interpretation of the current rules, for 2018, 2019 and 2020 tax years, there may not be an AMT NOL to carryback to the prior five taxable years, as there was no AMT for those years. As a result, the regular NOL that a corporation is carrying back now pursuant to the CARES Act may generate AMT in a pre-2018 tax year. Any AMT that is generated in a carryback year is then carried forward to a future year. That carry forward is then applied to a future year, and if the carry forward (after applying to any intermediate years) goes into the 2018 and 2019 years, then that carry forward is refundable in those years. As a result, based on PwC's initial review of this issue, an additional amended filing may be required as a result of the carryback of the NOL five years if the AMT generated in the carryback year results in a benefit in a later year.

With respect to AMT credits, Section 2305 of the CARES Act accelerates the ability to receive refunds of remaining AMT credits for 2019, 2020 & 2021. At this time, the procedures for making these claims are outlined below:

- Claiming the remaining credits on an original or superseding Form 1120 for tax years beginning in 2019 (including a "bare bones" return filed specifically for that purpose) or,
- Claiming the entire refundable AMT credit in tax years beginning in 2018 by filing a Form 1139 by December 31, 2020. The IRS has not yet issued guidance regarding how to label the Form 1139 or requested attachments.

The takeaway

In light of the extended carryback period in the CARES Act, and the ability to obtain quick refunds through the Form 1139 and 4466 processes as described above, time is of the essence. A corporation that intends to carry back a loss and still is within the one-year time period from the end of its loss year should submit a Form 1139 as soon as possible in order to expedite its tentative refund. As noted above, the IRS will be working these submissions on a strict 'first in, first out' basis.

PwC can assist companies in navigating the many procedural issues in considering options with respect to the Form 1139, Form 4466, and/or bare bones return processes. As discussed, companies must take care that their submissions are complete and include all information required by the IRS for processing, as any missteps are likely to result in significant delays in the issuance of refunds. If a Form 1139 or 4466 is rejected, it will have to be corrected/perfected and then resubmitted, putting it at the bottom of what is sure to be an extremely large inventory of cases at the IRS.

Let's talk

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