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Computation of Federal Modified Taxable Income (FMTI) for Household Income Only

NOTE: Do not complete Part 3 if you are electing to forego your carryback. Effective 2012, FMTI is not used and an NOL is not allowed in determining Total Household Resources.

PART 3: ADJUSTING YOUR NOL FOR HOUSEHOLD INCOME

Step 1. Figure Your FMTI

	A	B	C
41. Year to which NOL is being carried			
42. Reported AGI for year shown on line 41 without NOLD	00	00	00
43. a. Adjustments to AGI including DPAD (see instructions).....	00	00	00
b. Capital losses, in excess of capital gains (\$3,000 maximum) ...	00	00	00
44. MODIFIED federal AGI. Add lines 42 and 43a or 43b	00	00	00
45. a. Medical (see instructions for limitations).....	00	00	00
b. Taxes	00	00	00
c. Contributions.....	00	00	00
d. Interest.....	00	00	00
e. Casualty loss	00	00	00
f. Moving expenses.....	00	00	00
g. Miscellaneous (attach U.S. <i>Schedule A</i> ; see instructions)	00	00	00
h. Limit on itemized deductions	00	00	00
i. If you did not itemize, use the standard deduction	00	00	00
46. Enter the total of of 45a through 45h, or 45i if you did not itemize	00	00	00
47. FMTI. Subtract line 46 from line 44. If less than zero, enter "0"	00	00	00

Step 2. Figure Your Carryback (If you are not carrying the loss back, go to Step 3.)

48. Unabsorbed NOL. Enter in column A your federal NOL as a positive amount	00	00	00
49. NOL to be carried to next succeeding year through 2011. Subtract line 47 from line 48. Carry the amount on this line to the next column, line 48. If less than zero, enter "0".....	00	00	00

Step 3. Figure Your Carryforward

50. Year the federal NOL occurred			
51. Enter the amount of the original federal NOL as a positive amount	00	00	00
52. Total of all NOLs used for previous years	00	00	00
53. Subtract line 52 from line 51. This is the remaining NOL that can be carried forward to the year on line 41	00	00	00
54. Subtract line 47 (FMTI) from line 53. This is the remaining NOL to carry forward. If less than zero, enter "0"	00	00	00

Line-by-Line Instructions for Part 3

Part 3: Adjusting Your NOL for Household Income

Line 41: May be applied to tax years 2011 and prior only.

Line 42: Include NOL carryovers or carrybacks from earlier years.

Line 43a: Add back any domestic production activities deduction (DPAD). Also, adjustments to AGI, such as taxable Social Security benefits and IRA deductions, must be recalculated based on federal modified AGI.

Line 45: Use 45a through 45h if you itemized. If you didn't itemize, use 45i.

45a: Medical adjustments. The amount of medical adjustments allowed varies with federal law from year to year. You must recalculate your medical expense deduction based on modified federal AGI and the federal limitation in effect for the year entered on line 41.

45c: Percentage limitations on charitable contributions are based on modified federal AGI.

45g: Miscellaneous deductions are limited to 2 percent of AGI. This amount cannot exceed 2 percent of modified federal AGI.

45h: If modified AGI exceeds certain amounts, itemized deductions may be limited. See limitations in effect for the year entered on line 41.

Line 47: This is your FMTI. Your Michigan NOLD will be the amount on this line or the amount from line 48 (or line 53 for carryforwards), whichever is smaller. This amount cannot be less than zero.

Line 48: Enter your federal NOL in column A as a positive amount. Each succeeding year will be the excess portion (if any) from line 49 of the preceding column.

Line 49: Subtract line 47 from line 48. If the result is more than zero, this is the excess NOL to be carried forward to the next year. If it is less than zero, the NOLD is limited to the excess on line 48. This is the last year affected by the NOL.

NOTE: Effective January 1, 2012 an NOLD cannot reduce total household resources and is no longer used on Michigan Property Tax Credit and Home Heating Credit claims.

Line 54: If line 47 is less than line 53, subtract line 47 from line 53 and enter here; then use line 47 as your NOLD to recalculate your credit. If line 47 is greater than line 53 enter "0" and use line 53 as your NOLD to recalculate your Michigan credits.

Instructions for Form MI-1045, Application for Michigan Net Operating Loss Refund

What is a Net Operating Loss?

A net operating loss (NOL) occurs when a business has losses in excess of its gains. In general terms, a federal NOL is computed by starting with federal taxable income and making the following modifications: (1) eliminate the personal exemption allowance, (2) eliminate capital losses in excess of capital gains and any excluded capital gains, (3) eliminate NOL carryovers from other years, and (4) eliminate the excess of nonbusiness deductions over nonbusiness income. If the end result is negative, a federal NOL has been created for use in another tax year.

The excess capital loss deduction is calculated on a U.S. Form *1045 Schedule A*, line 21 or 22. An excess capital loss includes a U.S. Form *1040 Schedule D* loss that is limited to \$3,000. The capital loss may be greater than \$3,000 if nonbusiness capital losses were offset by business gains that are also reported on U.S. Form *1040 Schedule D*. Example: \$10,000 nonbusiness stock loss and \$50,000 gain from the sale of a business asset (U.S. Form *4797*) produce a U.S. Form *Schedule D* gain of \$40,000. The \$10,000 stock loss is an excess capital loss.

The Michigan NOL

The Michigan NOL and net operating loss deduction (NOLD) are computed independently from the federal NOL and NOLD. The calculation of a Michigan NOL (for taxable income purposes) follows the same general format of the federal NOL calculation but uses federal adjusted gross income (AGI) as a starting point rather than federal taxable income. Therefore, federal itemized deductions that may be used to create or contribute to the federal NOL are not taken into consideration in the calculation of the Michigan NOL.

In addition, the Michigan NOL calculation must be further modified to remove, to the extent included in federal AGI, any income and losses sourced to other states, income and related expenses from Michigan oil and gas production and nonferrous metallic minerals extraction subject to Michigan severance tax and a federal NOLD. The Michigan NOLD is subject to allocation and apportionment as required by the Michigan Income Tax Act. See *Revenue Administrative Bulletin 1998-3* for additional guidance.

In order to determine whether an NOL was incurred from Michigan sources, regardless of whether or not there is a corresponding federal NOL, complete page 1 of Form MI-1045.

Carryover of a Michigan NOL

The Michigan NOL may be carried over in the same manner and to the same time periods as provided for in Section 172 of the Internal Revenue Code (IRC) in effect for the year the loss was incurred. If the NOL is not exhausted in the carryback years, or if an election is made to forego the carryback (election is irrevocable), an NOL carryforward will exist for subsequent years. The carryback period is generally limited to two years for both federal and Michigan taxes, and any unused loss may

be carried forward for 20 consecutive years. Exceptions to the general carryover periods used for federal NOLs also apply to Michigan.

When there is a change in filing status, special rules apply to carrying over a Michigan NOL, which follow the federal rules. See Internal Revenue Service (IRS) Publication 536. A schedule showing the calculations for the Michigan carryover must be attached to the Form MI-1045.

The amount of the Michigan NOL used in carryover years must be reduced by any domestic production activities deduction (DPAD), attributable to Michigan, claimed in the carryover year. For example, an NOL carryforward claimed in 2015 must be reduced by any Michigan sourced DPAD included in your 2015 AGI.

When to File Form MI-1045

When carrying back a Michigan NOL to prior years, Form MI-1045 must be filed within four years after the date set for filing the return in which the NOL was incurred. For example, if the original NOL was incurred in 2010, the original 2010 return was due April 15, 2011. Form MI-1045 must be filed by April 15, 2015 to carryback the 2010 Michigan NOL to a year that is otherwise outside of the general four-year statute of limitations.

For the first year that a loss is used, a copy of the federal income tax return (U.S. Form *1040*) and all supporting federal tax schedules and statements that substantiate the NOL (see Required Attachments) must be attached to the Form MI-1045. If a carryover remains and until that loss is exhausted, include a copy of the originally filed Form MI-1045 with each Form MI-1040 that claims the NOLD. A schedule demonstrating how the Michigan NOL has been used must also be included.

If an election to forego the carryback is made, you are not required to file a Form MI-1045 until the year the loss is actually used to offset Michigan income (the first year in which there is taxable income). Keep all records for the loss year(s) until the NOL has been used and exhausted. If a Michigan NOL is carried forward, Form MI-1045 should be filed with Form MI-1040 to claim the Michigan NOLD. The NOL carryover must be used in consecutive years.

Using Form MI-1045

Use page 1 of Form MI-1045 to calculate the Michigan NOL for the year of the loss. If the loss is carried back, also complete "Redetermining Michigan Income Tax" on page 2. Page 3 is used to determine the amount of the federal NOLD that may be used to compute household income for the homestead property tax credit for tax years prior to 2012. Page 3 is also used to compute the federal NOLD used in household income for the farmland preservation tax credit.

When filing a refund claim from the carryback of a Michigan NOL, prepare the appropriate amended credit claim forms for each year the loss is being carried back and attach to Form MI-1045.

The total amount of the federal NOLD used to arrive at federal AGI must be added back on Form MI-1040, Schedule 1. The Michigan NOLD is then subtracted on Form MI-1040, Schedule 1. This amount is the NOL determined on Form MI-1045, page 1, line 22, less any of the loss used in previous years. See the MI-1040 instruction booklet for specific line references for the years involved.

If there are Michigan NOLs from multiple tax years, the total unused losses must be combined and reported on Form MI-1040, Schedule 1.

Nonresidents and Part-Year Residents

Nonresidents and part-year residents may also be entitled to a Michigan NOLD. In order to determine whether a Michigan NOL was incurred, complete Part 1 of Form MI-1045 in the same manner as described in the section, "The Michigan NOL." Only items sourced to Michigan may create a Michigan NOL.

A federal NOLD must be removed from taxable income to the extent included in federal AGI. Nonresidents and part-year residents accomplish this by allocating the entire federal NOLD to Column C on Michigan Schedule NR. Do not add back the federal NOLD as an addition on Michigan Schedule 1.

In a carryforward year, the Michigan NOL must be claimed on the Michigan Schedule 1 as a subtraction. Do not report a Michigan NOL on Michigan Schedule NR.

Required Attachments

Attach a copy of the federal income tax return (U.S. Form 1040) and all supporting federal tax schedules and statements that substantiate the NOL. Be sure to indicate the location (city and state) of each source of income or loss. If there is income or loss subject to apportionment, see Schedule of Apportionment (Form MI-1040H).

Include any of the following schedules and accompanying statements that support the Michigan NOL:

- U.S. Form 1040, pages 1 and 2
- U.S. Form 1040 Schedule(s) A, B, C, D, E, F
- U.S. Form 4797
- U.S. Form 4835
- Any other applicable documents, including U.S. Form 1040 or 1041 Schedule(s) K-1.

NOL Effects on Household Income

An NOLD allowed in household income cannot exceed Federal Modified Taxable Income (FMTI) as defined in section 172(b)(2) of the IRC.

An NOL is not used to determine total household resources. An NOLD requiring an FMTI adjustment is only applicable when computing household income for a homestead property tax credit (Form MI-1040CR) for a carryback year prior to 2012.

Alternatively, an NOLD requiring an FMTI adjustment is applicable when computing household income for a farmland preservation tax credit (Form MI-1040CR-5) for any year, subject to the statute of limitations. The farmland preservation tax credit continues to be computed using household income, not total household resources.

The amount of the NOLD that is allowed cannot exceed FMTI in the year to which it is being carried back or carried forward.

FMTI is computed by modifying federal taxable income to remove the federal exemption allowance, the capital loss deduction, DPAD, and the NOLD. For more information about FMTI, see IRS Publication 536.

The amount of the allowable NOLD for use in household income is calculated on page 3 of the MI-1045 form for both carrybacks and carryforwards. The amount of the carryback deduction is the smaller of lines 47 or 48, and the amount of the carryforward deduction is the smaller of lines 47 or 53.

Example: Your 2012 FMTI is \$20,000, and your 2012 federal NOLD is \$50,000. The amount of the 2012 NOLD of \$50,000 that may be used in 2012 household income for a farmland preservation tax credit is limited to \$20,000. The balance of \$30,000 will be available for use in a 2013 farmland preservation tax credit, to the extent of 2013 FMTI. There is no NOLD allowed for a homestead property tax credit for tax years 2012 and later.

Claim the amount of the NOLD allowed on the "other adjustments line" on the appropriate credit forms for each applicable year.

NOTE: To deduct an NOLD from household income, there must be a corresponding federal NOLD. If there is no federal NOLD in AGI, there is no NOLD to claim in household income. Income and losses from other states, income and losses from oil and gas production and nonferrous metallic minerals extraction subject to Michigan severance tax, and federal itemized deductions must be considered when calculating the NOL and NOLs used for household income.

Forms or Questions

Michigan tax forms are at www.michigan.gov/taxes. Call (517) 636-4486 if you have questions or to request tax forms.

Michigan NOL Carryforward Example

A full-year Michigan resident born in 1942 has the following business and rental activity reported on their U.S. Form 1040 in tax **Year 00**: Form MI-1040 for tax **Year 00** reports the following:

- Schedule C
\$18,000 Michigan and \$2,500 Indiana
- Schedule E, Part 1, rental income
\$6,500 Arizona
- Schedule E, Part 2, flow-through income (loss)
(\$87,000) Michigan and (\$8,500) Ohio
- Self-employment tax deduction
\$202 Michigan and \$28 Indiana
- Domestic Production Activities Deduction [DPAD]
\$2,000 Michigan and \$1,200 Ohio

Federal adjusted gross income [AGI] is (\$41,170) for **Year 00**.

- Federal AGI (\$41,170)
- Additions
 - Schedule 1, line 2: Deduction for SE taxes \$230
 - Schedule 1, line 4: Business loss, Ohio \$8,500
 - Schedule 1, line 4: DPAD, Ohio \$1,200
 - Schedule 1, line 7: Federal NOLD \$4,000
- Subtractions
 - Schedule 1, line 13: Business income, Indiana \$2,500
 - Schedule 1, line 13: Rental income, Arizona \$6,500
 - Schedule 1, line 16: Michigan income tax refunds included in AGI \$560
 - Schedule 1, line 25: Pension subtraction \$12,500
- Michigan income subject to tax (\$49,300)

The taxpayer must complete the first page of the MI-1045 to determine (1) if a **Year 00** Michigan NOL exists, and (2) the amount of the **Year 00** Michigan NOL. In this example, a Michigan NOL exists and the taxpayer elects to forgo an NOL carryback. The full NOL will be carried forward beginning with **Year 01**. The Michigan **Year 00** NOL is calculated below.

Federal AGI Year 00	Michigan Adjustments	MI-1045 Part 1 Year 00
Wages \$25,000		\$25,000
Interest Income 120		120
Dividend Income 80		80
Schedule C Income (Loss) 20,500	2,500 Indiana	18,000 Business income attributable to Michigan
Capital Gain (Loss) (3,000)		(3,000)
Pension 12,500		12,500
Schedule E, Part 1, Income (Loss) 6,500	6,500 Arizona	0
Schedule E, Part 2, Income (Loss) (95,500)	(8,500) Ohio	(87,000) Business loss attributable to Michigan
Misc: State Tax Refunds 560		560
Other: Prior Year Federal NOL (4,000)		0 A federal NOL does not affect a Michigan NOL calculation.
<i>Total Income</i> (\$37,240)		(\$33,740)
Adjustments		
Retirement Plan Contributions 500		500
Deductions for Self-Employment Tax 230	28 Indiana	202
DPAD 3,200	1,200 Ohio	2,000 DPAD attributable to Michigan
<i>Total Adjustments</i> 3,930		2,702
<i>Federal AGI</i> (\$41,170)		(\$36,442) <i>Federal AGI attributable to Michigan</i>
**For demonstration purposes assume for Year 00 the federal NOL computes to: (\$63,000)		3,000 Excess capital loss deduction (MI-1045, line 19)
		2,000 DPAD (MI-1045, line 20)
		(\$31,442) Michigan NOL for Year 00

The **Year 01** federal AGI is (\$30,000), which consists of the following:

Wages	\$10,000
Schedule C - MI	(2,000)
Schedule C - IN	3,000
Schedule E, Part 1 – AZ	(4,000)
Schedule E, Part 2 – MI	15,000
Schedule E, Part 2 – OH	(1,500)
Pension	12,500
Total Income	\$33,000
Federal NOLD from Year 00 carryforward	(63,000)
Federal AGI	(\$30,000)

To determine how much, if any, of a Michigan NOL remains after being carried to another year, a calculation must be made to determine how much Michigan income was offset in the carryover year. To calculate this amount, determine income subject to Michigan tax (before the exemption allowance) without regard to the subtraction allowed for the Michigan NOLD. If this amount is greater than the Michigan NOLD, the entire NOL is used up, and none is available to carry to the next year. If this figure is less than the Michigan NOLD, the difference will be the NOL amount carried to the next tax year.

The NOL available for carryover from **Year 00** (\$31,442) exceeds Michigan taxable income (\$23,000) in **Year 01**, which is calculated without regard to the Michigan NOLD and Michigan exemptions. As such, the Michigan NOL absorbed in **Year 01** equals Michigan taxable income without regard to the Michigan NOLD and Michigan exemptions. A subtraction is taken on the Michigan Schedule 1 for a Michigan NOLD, reporting the **entire** NOLD balance available in the tax year, in this case, \$31,442. The NOL carryforward for **Year 02** computes to \$8,442.

Year 01 Michigan NOL Carryforward Computation

Federal AGI	(\$30,000)
Michigan Additions:	
Schedule E, Part 1 – AZ	4,000
Schedule E, Part 2 – OH	1,500
Federal NOLD	63,000
Subtotal	38,500
Michigan Subtractions:	
Schedule C – IN	3,000
Pension	12,500
Total income subject to MI tax, without regard to the MI NOLD or MI exemptions	\$23,000
Michigan NOL carryover available from Year 00	31,442
Total income subject to MI tax, without regard to the MI NOLD or MI exemptions	23,000
MI NOL available for carryforward to Year 02	\$8,442

The **Year 02** federal AGI is \$19,350, which consists of the following:

Wages	\$15,000
Interest	250
Dividend	100
Schedule C – MI	14,000
Schedule C – IN	2,500
Schedule E, Part 1 – AZ	5,000
Schedule E, Part 2 – MI	(5,000)
Schedule E, Part 2 – OH	5,000
Pension	12,500
Total Income	\$49,350
Remaining federal NOLD from Year 01 carryforward	(30,000)
Adjustment for DPAD – MI	500
Adjustment for DPAD – IN	200
Federal AGI	\$20,050

The Michigan NOL must be reduced by the Michigan apportioned amount of the DPAD that was used to arrive at the AGI for the current year (**Year 02**). It is not the Michigan NOLD amount that is reduced when there is a DPAD amount allocated or apportioned to Michigan, but the overall available Michigan NOL amount that is reduced.

In **Year 02** a subtraction is taken on the Michigan Schedule 1 for a Michigan NOLD reporting the full amount available of \$7,942. The Michigan NOL available as a carryforward from the previous year, **Year 01**, (\$8,442) was reduced by a DPAD apportioned to Michigan (\$500), thereby decreasing the Michigan NOL amount to \$7,942. The available Michigan NOL does not exceed Michigan taxable income of \$25,050, calculated without regard to the Michigan NOLD and Michigan exemptions. The balance of the Michigan NOL from loss **Year 00** is exhausted in the carryforward used in **Year 02**.

Year 02 Michigan NOL Carryforward Computation

Federal AGI	\$20,050
Michigan Additions:	
Federal NOLD	30,000
Subtotal	50,050
Michigan Subtractions:	
Schedule C – IN	2,500
Schedule E, Part 1 – AZ	5,000
Schedule E, Part 2 – OH	5,000
Pension	12,500
Total income subject to MI tax, without regard to the MI NOLD or MI exemptions	\$25,050
Michigan NOL carryforward available from Year 01	8,442
Michigan apportioned DPAD	(500)
Total MI NOLD available for Year 02	\$7,942

Total income subject to MI tax, without regard to the MI NOLD or MI exemptions (NOL absorbed) **\$25,050**
MI NOL available for carryforward to Year 03 **\$0**