

PLYMOUTH INSTITUTE FOR FREE ENTERPRISE

**BUSINESS LOSS LIMITATION EXTENSION**

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APRIL 2026

**ADVANCING AMERICAN  
FREEDOM FOUNDATION**

**TOPLINE:** The One Big Beautiful Bill (OB BB) permanently extended the 2017 Tax Cuts and Jobs Act's (TCJA's) limitation on deductions for business losses.

**BACKGROUND:** Individual taxpayers with business income or losses must include that income or loss on their individual tax returns. Business income is added to other ordinary income and taxed at the same rate (ranging from 10% to 37% depending on the taxpayer's income). Prior to TCJA, active business owners with net business losses could use those losses to offset an unlimited amount of other income. So, for example, a taxpayer who suffered a \$1.5 million business loss in the same year as he earned \$1 million in wages would have no net income to be taxed and he would be able to carry a \$500,000 loss forward to the next year's return.

TCJA limited business losses to an inflation-adjusted \$250,000/\$500,000 (single/married filing jointly) in the 2018 tax year (though the COVID-era CARES Act retroactively pushed the start of the limitation to 2021), with the limitation amount inflation-adjusted each year. Under TCJA, a single taxpayer with \$1 million in wages and a \$1.5 million business loss would only be allowed to deduct the first \$250,000 of business loss, leaving him with \$750,000 in taxable income for the year. However, any business losses disallowed could be carried forward to future years. TCJA set the business loss limitation provision to expire after 2025, but the expiration date was later pushed back to 2026 and then to 2028.

**What OB BB Did:**

- Made TCJA's business loss limitation permanent law.
- Reset the business loss limitation inflation adjustment, effectively reducing the limitation.
  - Reduced the limitation from \$313,000/\$626,000 in 2025 to \$256,000/\$512,000 in 2026.

**Why It Matters?**

- Overtaxing business owners after they suffer losses is bad policy. It further discourages entrepreneurs from taking risks that are necessary for success.
- This policy is effectively an \$18 billion tax increase between 2029 and 2034.

**Where Can I Find the Changes?** OB BB Section 70601; 26 U.S.C. § 461(l).

**BOTTOMLINE:** Congress faced difficult tradeoffs in extending TCJA's tax cuts without exacerbating the deficit. The extension of the business loss limitation isn't ideal, though it should be considered in the context of a strong overall tax package.

