

IT 17-0011-GIL 12/13/2017 TAX CHANGES

P.A. 100-22 Illinois Income Tax Changes (This is a GIL.)

December 13, 2017

Re: P.A. 100-22  
Illinois Income Tax Changes

Dear Xxxxx:

This is in response to your letter dated November 16, 2017 in which you requested information related to the Illinois income tax. The nature of your letter and the information provided require that we respond with a General Information Letter (GIL). A GIL is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), which may be accessed from the Department's web site at [www.Iltax.com](http://www.Iltax.com).

Your letter states as follows:

As we prepare for the upcoming tax filing season for 2017 returns, we are reminded of the many changes enacted with P.A. 100-0022 which became effective for tax years beginning on or after January 1, 2017 or ending on December 31, 2017. Reference is made to the Illinois Department of Revenue Informational Bulletins FY 2018-01, FY 2018-02 and FY 2018-03.

By way of background, the vast, vast majority of our individual and trust taxpayers use the calendar year for tax reporting purposes. We note among the various provisions of the tax legislation that the Illinois individual, trust and estate tax rate increased to 4.95% on July 1, 2017 and the corporate tax rate increased to 7%. We have questions regarding the computation of 2017 tax and other provisions of P.A. 100-0022:

- Bulletin FY 2018-02 makes specific reference to additional guidance and instructions to be released in January 2018 – is a draft of the form and/or instructions available now? Will taxpayers be allowed to specifically bifurcate their transactions into pre-versus post-tax law rate changes and how will this work? For example, if a taxpayer is redeemed out of a partnership in March of 2017 at a gain, will he be allowed to apply the tax rate in effect at that date or must he use the blended rate? Will a taxpayer be allowed to segregate his portfolio gains and losses from taxable brokerage account transactions into pre- versus post-tax law rate changes and how will this work? We believe that releasing information now (and not in January 2018) will help practitioners understand what options are available and how this information is to be reported to the Illinois Department of Revenue.
- We note that Schedule SA (IL-1040) Specific Accounting Method of Computing Net Income for Individuals is on the Department's website but that it only applies to fiscal-year filers with tax years ending on or after July 1, 2017 and on or before December 30, 2017. What form is to be used for calendar 2017 tax filers? What will it look like and,

given the impending tax filing season, why is it not yet released for practitioners to get up to speed?

- We note that the standard exemption allowance and property tax credit will be disallowed where a taxpayer's AGI exceeds \$500,000 (MFJ status) or \$250,000 (all other returns). Are these thresholds referring to Federal AGI or Illinois base income? Is the disallowance in the form of a cliff cut-off i.e., if the AGI limit is achieved, then no phase-out occurs, just total loss of deduction or credit? Please clarify.
- The research and development credit was reinstated retroactive to 2016. FY 2018-01 states that the Department will provide updated forms and instructions in order to claim a credit not previously allowed. When will this guidance be released?
- As to individuals, trusts, and estates, if such taxpayers have based their 2017 estimated tax payments using the 100% of prior year tax safe harbor, and have paid these installments on time and as scheduled, no penalties for underpayment of estimated tax would be applicable under the new law. Please confirm.

### **RULING**

Public Act 100-22 amended the Illinois Income Tax Act ("IITA" ; 35 ILCS 5/101 *et seq.*), including Sections 201(b) and 202.5. Subsection (a) of Section 201 imposes the regular income tax, and subsection (b) establishes the rate of tax.<sup>1</sup> As amended, IITA Section 201(b) provides, in relevant part, as follows:

(5.2) In the case of an individual, trust, or estate, for taxable years beginning on or after January 1, 2015, and ending prior to July 1, 2017, an amount equal to 3.75% of the taxpayer's net income for the taxable year.

(5.3) In the case of an individual, trust, or estate, for taxable years beginning prior to July 1, 2017 and ending after June 30, 2017, an amount equal to the sum of (i) 3.75% of the taxpayer's net income for the period prior to July 1, 2017, as calculated under Section 202.5, and (ii) 4.95% of the taxpayer's net income for the period after June 30, 2017, as calculated under Section 202.5.

(5.4) In the case of an individual, trust, or estate, for taxable years beginning on or after July 1, 2017, an amount equal to 4.95% of the taxpayer's net income for the taxable year.

...

(12) In the case of a corporation, for taxable years beginning on or after January 1, 2015, and ending prior to July 1, 2017, an amount equal to 5.25% of the taxpayer's net income for the taxable year.

(13) In the case of a corporation, for taxable years beginning prior to July 1, 2017, and ending after June 30, 2017, an amount equal to the sum of (i) 5.25% of the taxpayer's net income for the period prior to July 1, 2017, as calculated under Section 202.5, and (ii) 7% of the taxpayer's net income for the period after June 30, 2017, as calculated under Section 202.5.

(14) In the case of a corporation, for taxable years beginning on or after July 1, 2017, an amount equal to 7% of the taxpayer's net income for the taxable year.

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<sup>1</sup> IITA Sections 201(c) and (d) impose the personal property tax replacement income tax (replacement tax). The replacement tax is imposed at the rate of 2.5% of net income in the case of a corporation (other than an S corporation), and 1.5% of net income in the case of a partnership, trust or Subchapter S corporation. Public Act 100-22 did not amend IITA Sections 201(c) or (d).

IITA Section 202.5 sets forth the manner by which a taxpayer determines net income for the period prior to July 1, 2017 and after June 30, 2017. As amended, IITA Section 202.5 states:

(a) In general. With respect to the taxable year of a taxpayer beginning prior to the first day of a month and ending after the last day of the preceding month, net income for the period after the last day of the preceding month is that amount that bears the same ratio to the taxpayer's net income for the entire taxable year as the number of days in that taxable year after the last day of the preceding month bears to the total number of days in that taxable year, and the net income for the period prior to the first day of the month is that amount that bears the same ratio to the taxpayer's net income for the entire taxable year as the number of days in that taxable year prior to the first day of the month bears to the total number of days in that taxable year.

(b) Election to attribute income and deduction items specifically to the respective portions of a taxable year prior to the first day of a month and ending after the last day of the preceding month. In the case of a taxpayer with a taxable year beginning prior to the first day of a month and ending after the last day of the preceding month, the taxpayer may elect, instead of the procedure established in subsection (a) of this Section, to determine net income on a specific accounting basis for the 2 portions of the taxable year:

(1) from the beginning of the taxable year through the last day of that apportionment period; and

(2) from the first day of the next apportionment period through the end of the taxable year.

The election provided by this subsection must be made in the form and manner that the Department requires by rule, and must be made no later than the due date (including any extensions thereof) for the filing of the return for the taxable year, and is irrevocable.

(c) If the taxpayer elects specific accounting under subsection (b):

(1) there shall be taken into account in computing base income for each of the 2 portions of the taxable year only those items earned, received, paid, incurred or accrued in each such period;

(2) for purposes of apportioning business income of the taxpayer, the provisions in Article 3 shall be applied on the basis of the taxpayer's full taxable year, without regard to this Section;

(3) the exemption provided by Section 204 shall be divided between the respective periods in amounts which bear the same ratio to the total exemption allowable under Section 204 (determined without regard to this Section) as the total number of days in each period bears to the total number of days in the taxable year;

(4) for purposes of this subsection, net income may not be negative for either of the two portions of the taxable year and positive for the other; if net income for one portion of the taxable year would be positive and net income for the other portion would otherwise be negative, the net income for the entire taxable year shall be attributed to the portion

of the taxable year with positive net income and the net income for the other portion of the taxable year shall be zero; and

(5) the net loss carryforward deduction for the taxable year under Section 207 may not exceed combined net income of both portions of the taxable year, and shall be used against the net income of the portion of the taxable year from the beginning of the taxable year through the last day of the preceding month before any remaining amount is used against the net income of the latter portion of the taxable year.

As these provisions indicate, for purposes of applying the tax rates under IITA Sections 201(b)(5.3) and 201(b)(13), under IITA Section 202.5(a) a taxpayer's net income for the period prior to July 1, 2017 and for the period after June 30, 2017, is deemed to be received in each period based on the ratio of the number of days in such period to the total number of days in the taxable year. The Department implements the general rule of IITA Section 202.5(a) by computing a blended income tax rate.<sup>2</sup> Taxpayers must use the blended income tax rate to determine their tax liability unless a proper election is made to apply the specific accounting method under IITA Section 202.5(b). Where a taxpayer properly elects to apply the specific accounting method, net income for the period prior to July 1, 2017 and for the period after June 30, 2017 is determined by applying the taxpayer's method of accounting under IITA Section 402 as if each such period constituted a separate taxable year as well as the special rules set forth under IITA Section 202.5(c). Taxpayers make the election to apply specific accounting by properly completing Schedule SA. The election must be made no later than the due date (including any extensions thereof) for the filing of the return for the taxable year, and once made is irrevocable. The 2017 Schedule SA for corporate and individual filers will soon be available on the Department's website at [tax.illinois.gov](http://tax.illinois.gov).

Public Act 100-22 amended IITA Sections 204 and 208. IITA Section 204 allows the standard exemption and certain additional exemptions. Public Act 100-22 added subsection (g) to Section 204, which states as follows:

(g) Notwithstanding any other provision of law, for taxable years beginning on or after January 1, 2017, no taxpayer may claim an exemption under this Section if the taxpayer's adjusted gross income for the taxable year exceeds (i) \$500,000, in the case of spouses filing a joint federal tax return or (ii) \$250,000, in the case of all other taxpayers.

Section 208 of the IITA allows a tax credit for residential real property taxes. As amended, IITA Section 208 provides:

Beginning with tax years ending on or after December 31, 1991, every individual taxpayer shall be entitled to a tax credit equal to 5% of real property taxes paid by such taxpayer during the taxable year on the principal residence of the taxpayer. In the case of multi-unit or multi-use structures and farm dwellings, the taxes on the taxpayer's principal residence shall be that portion of such total taxes which is attributable to such principal residence. Notwithstanding any other provision of law, for taxable years beginning on or after January 1, 2017, no taxpayer may claim a credit under this Section if the taxpayer's adjusted gross income for the taxable year exceeds (i) \$500,000, in the case of spouses filing a joint federal tax return, or (ii) \$250,000, in the case of all other taxpayers.

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<sup>2</sup> For example, the tax imposed under IITA Sections 201(b)(5.3) and 202.5(a) in the case of a calendar year individual taxpayer for the 2017 taxable year is determined as follows:  $[(\text{net income} \times 181/365(.0375)) + (\text{net income} \times 184/365(.0495))] = \text{net income}(.043549)$ .

As these provisions indicate, the disallowance of exemptions and credit is based on federal adjusted gross income rather than Illinois base income, and applies in full once the AGI threshold is exceeded (i.e. there is no phase-out). See IITA Section 102.

Public Act 100-22 amended Section 201(k) of the IITA, which allows the research and development credit. As amended, Section 201(k) provides, in pertinent part, as follows:

(k) Research and development credit. For tax years ending after July 1, 1990 and prior to December 31, 2003, and beginning again for tax years ending on or after December 31, 2004, and ending prior to January 1, 2022, a taxpayer shall be allowed a credit against the tax imposed by subsections (a) and (b) of this Section for increasing research activities in this State.

...

It is the intent of the General Assembly that the research and development credit under this subsection (k) shall apply continuously for all tax years ending on or after December 31, 2004 and ending prior to January 1, 2022, including, but not limited to, the period beginning on January 1, 2016 and ending on the effective date of this amendatory Act of the 100th General Assembly. All actions taken in reliance on the continuation of the credit under this subsection (k) by any taxpayer are hereby validated.

The Department has prescribed 2016 Schedule 1299-D (R&D), and revised the 2016 Schedule 1299-D in order to allow taxpayers to claim the research and development credit for the 2016 tax year. In addition, if a taxpayer did not claim the research and development credit on a 2015 return because its tax year ended after December 31, 2015, the taxpayer may amend the 2015 return and the 2015 Schedule 1299-D to claim the credit.

Section 804 of the IITA imposes a penalty in the case of any underpayment of estimated tax. Section 804(b) defines an "underpayment" for this purpose as the excess of the amount of the required installment determined under Section 804(c) over the amount of the installment paid on or before the last date prescribed for payment. IITA Section 804(c) states that the required installment is equal to 25% of the "required annual payment." The required annual payment is defined as the lesser of: (i) 90% of the tax shown on the return for the taxable year (or if no return is filed, 90% of the tax for such year), or (ii) 100% of the tax shown on the return of the taxpayer for the preceding taxable year if a return showing a liability for tax was filed by the taxpayer for the preceding taxable year and such preceding taxable year was not a short year. Public Act 100-22 did not amend IITA Section 804.

As these provisions indicate, a taxpayer who makes timely estimated payments by properly calculating the required annual payment based on 100% of the tax shown on their return filed for the prior 12 month taxable year will not incur a penalty for underpayment of estimated tax.

As stated above, this is a GIL. A GIL does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department. If you have further questions regarding this GIL, please call (217) 782-7055. If you have additional questions regarding Illinois income tax laws, please visit the Department's website at [www.ILtax.com](http://www.ILtax.com).

Sincerely,

Brian L. Stocker  
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