



# *i*nformational

## Bulletin

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## 2017 Illinois Income Tax Guidance - Foreign Income Repatriation Transition Tax

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This bulletin is written to inform you of recent changes; it does not replace statutes, rules and regulations, or court decisions.

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[tax.illinois.gov](http://tax.illinois.gov)

File your return online at:  
[mytax.illinois.gov](http://mytax.illinois.gov)

Call us at:  
1 800 732-8866 or  
217 782-3336

Call our TDD  
(telecommunications device  
for the deaf) at:  
1 800 544-5304

To: All tax practitioners and businesses who file:

- IL-1120, Corporation Income and Replacement Tax Return,
- IL-1120-ST, Small Business Corporation Replacement Tax Return,
- IL-1065, Partnership Replacement Tax Return,
- IL-1041, Fiduciary Income and Replacement Tax Return,
- IL-990-T, Exempt Organization Income and Replacement Tax Return,
- Schedule M, Other Additions and Subtractions (for businesses), or
- Schedule J, Foreign Dividends

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Public Law 115-97, commonly known as the Tax Cuts and Jobs Act, created a new provision under Internal Revenue Code (IRC) Section 965 requiring taxpayers with [untaxed foreign earnings and profits](#) to pay a tax as if those earnings and profits had been repatriated to the United States. The provision will increase federal taxable income. However, the Illinois subtraction modification for foreign dividends will exclude a portion of the increase from Illinois base income for certain taxpayers. This bulletin addresses how the IRS guidance affects Illinois business income tax returns.

Illinois does not follow either the election under IRC Section 965(h) to pay the tax liability in installments over eight years, or the election under IRC Section 965(i) in the case of S corporation shareholders to defer payment of the tax liability until the taxable year which includes a triggering event. Failure to accurately report IRC Section 965 net income and pay the applicable tax, by the original due date of your Illinois income tax return, could result in penalties and interest.

For 2017, according to IRS guidance, a taxpayer who has income under IRC Section 965 is required to include an [IRC 965 Transition Tax Statement](#) with their return, signed under penalties of perjury. This statement is separate from the federal income tax return. Due to the separate nature of the IRC 965 Transition Tax Statement, the income reported may not be included in federal taxable income; however, it must be included when determining Illinois base income. See the revised instructions associated with your specific return type for information on how to report IRC Section 965 net income.

Taxpayers who have already filed a 2017 Illinois income tax return and did not include IRC Section 965 net income must amend their return to account for that income.

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## News

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### Explanation of the Impact on Illinois Tax Revenue Resulting from the Federal Tax Cuts and Jobs Act - 03/01/2018

On December 22, 2017, [Public Law 115-97](#), the Tax Cuts and Jobs Act (the Act) was signed into law. This Act will impact Illinois' income tax base and therefore the state's income tax revenue. The Department has analyzed the Act based on current Illinois law, federal law, and Internal Revenue Service (IRS) rulings and interpretations to provide the following information. This is not a comprehensive list of how the Act changes Illinois adjusted gross income (AGI) or federal taxable income (FTI); however, it addresses major areas of concern.

#### Potential increases to Illinois base income and/or tax revenue

##### Limitation on Business Deductions

- **Excess Losses** — Internal Revenue Code (IRC) Section 461(1) is created to disallow a deduction to taxpayers, other than corporations, generally equal to the amount of the taxpayer's "excess business loss" for the taxable year. The amount disallowed under this provision is deemed a net operating loss carryover to the following taxable year(s) and therefore generally results in only a timing difference. However, in the case of a trust or estate, because Illinois decouples from the federal net operating loss provisions, unless the Illinois Income Tax Act (IITA) is amended, an excess business loss is permanently disallowed to a trust or estate.
- **Interest Deduction Limited** — IRC Section 163(j) is amended to limit the amount of interest expense that may be deducted in a taxable year to the amount not exceeding the sum of the taxpayer's interest income plus 30 percent of adjusted taxable income. Interest expense disallowed under this provision is deemed to be interest paid or accrued in the succeeding year.
- **Net Operating Loss (NOL) Deduction Limited** — IRC Section 172(a) is amended to limit the NOL deduction to 80 percent of taxable income (computed without regard to the NOL deduction). In addition, carryback provisions (except in the case of certain farming losses) are repealed, and unlimited carryforward of net operating losses is enacted.
- **Business Entertainment Expenses** — IRC Section 274 is amended to disallow a deduction for business entertainment expenses (business meals continue to be allowed up to 50%) and certain other deductions.
- **Federal Deposit Insurance Company (FDIC) Premiums** — IRC Section 162(r) is amended to disallow a deduction for a portion of the FDIC premiums paid by certain large banks.
- **Executive Compensation** — IRC Section 162(m) is amended to repeal the exceptions to the \$1 million deduction limit for commission- and performance-based compensation.

- **Related Party Expenses** — IRC Section 267A is created to disallow a deduction for certain interest and royalty payments made to foreign related parties.

### Accounting Method Changes

- **Required Amortization of Research Expenses** — IRC Section 174 is amended to disallow the deduction for research and experimental expenses for taxable years beginning after December 31, 2021. Such expenses must be amortized over five years (15 years for foreign research).
- **Generally Accepted Accounting Principles (GAAP) Revenue Recognition** — IRC Section 451 is amended so that an accrual basis taxpayer may not recognize an item of gross income later than it reports the same item on an applicable financial statement prepared in conformance with GAAP.

### Business Dividends

- **Reduction in Dividends Received Deduction** — IRC Section 243(a) is amended by reducing the dividends received deduction allowed to corporate taxpayers. The 70-percent dividends received deduction is reduced to 50 percent and the 80 percent dividends received deduction is reduced to 65 percent. This provision will also have the effect of reducing, in certain cases, the subtraction modification allowed to corporations for foreign dividends under IITA Section 203(b)(2)(O), which is based on the percentage allowed under IRC Section 243.
- **Repatriation Transition Tax** — IRC Section 965 is amended to require certain shareholders of controlled foreign corporations to include in gross income certain amounts of deemed subpart F income (net of a related deduction). This provision will increase FTI. However, the Illinois subtraction modification for foreign dividends will exclude a portion of the increase from Illinois base income.
- **Global Intangible Low-Taxed Income** — IRC Section 951A added a new subpart F inclusion for each U.S. shareholder's share of the global intangible low-taxed income of a controlled foreign corporation (net of a related deduction). This provision will increase FTI. However, the Illinois subtraction modification for foreign dividends will exclude a portion of the increase from Illinois base income.

### Other Miscellaneous Potential Increases (minimal impact)

- **Suspension of Certain Fringe Benefits** — IRC Section 132 is amended so that certain fringe benefits are no longer excludable.
- **Suspension of Moving Expense Deduction** — IRC Section 217 is amended to disallow a deduction for moving expenses.
- **Settlement Payments** — IRC Section 162(f) is amended to expand the disallowance of deductions for fines to include settlements paid to or at the direction of a governmental entity for violations of the law. This generally does not apply to amounts paid to come into compliance with the tax laws. In addition, no deduction is allowed for sexual harassment settlements subject to a nondisclosure agreement. The IRC Section 162(e) deduction for local lobbying expenses is repealed. These provisions apply to amounts paid after the December 22, 2017, date of enactment.
- **Contributions to Capital** — IRC Section 118 is amended to deny the exclusion for contributions to capital of a corporation in the case of certain amounts transferred by a governmental entity made after December 22, 2017. This provision accelerates recognition of income from contributions of capital; therefore, generally resulting in only a timing difference.

- **Life Insurance Proceeds** — IRC Section 101 is amended to limit the exclusion for life insurance proceeds in the case of certain transfers of life insurance contracts for valuable consideration.

## **Potential decreases to Illinois base income and/or tax revenue**

### **Business Asset Expensing**

- **Small Business Expensing (IRC Section 179 Deduction)** — IRC Section 179 is amended to increase the maximum deduction to \$1 million and increases the phase-out threshold to \$2.5 million. Illinois is not decoupled from IRC Section 179.
- **Bonus Depreciation** — IRC Section 168(k) is amended to allow 100-percent bonus depreciation for qualified property acquired and placed in service after September 27, 2017, and before January 1, 2023. Illinois is not decoupled from 100-percent bonus depreciation.

### **Accounting Method Changes**

- **Cash Method for Small Business** — IRC Section 448(c) is amended to increase the gross receipts threshold that applies when determining whether a corporation may use the cash method of accounting.

### **Dividend Deduction**

- **Foreign Dividends-Received Deduction** — IRC Section 245A is created to provide a deduction for the foreign-sourced portion of dividends received by a U.S. corporation from a foreign corporation in which the taxpayer owns at least ten percent of the stock.

### **Other Provisions Affecting Individuals**

- **Achieving a Better Life Experience (ABLE) Accounts** — IRC Section 529A(a)(1) is amended to increase the contribution limit to so-called ABLE accounts. ABLE accounts are exempt from income taxes, and distributions from such accounts are generally excluded from gross income.
- **Discharge of Education Loans** — IRC Section 108(f) is amended to exclude from AGI the discharge of an education loan due to the death or disability of the student.

### **Other Miscellaneous Potential Decreases (minimal impact)**

- **Opportunity Zones** — IRC Section 1400Z-1 is created to allow the chief executive officer of a State to nominate certain population census tracts of low-income property for designation as a qualified opportunity zone. Taxpayers may make investments in qualified opportunity funds with favorable tax treatment given to such investments, including exclusion of gain on sale or exchange.

## **No impact to Illinois base income and/or tax revenue**

**Pass-Through Business Income Deduction** — IRC Section 199A is created to allow taxpayers other than corporations a deduction generally equal to 20 percent of the taxpayer's qualified business income for the taxable year. For federal income tax purposes, the deduction is not allowed in computing AGI. Therefore, there is no impact on Illinois base income. Additionally, partnerships and S corporations do not get this deduction when computing Personal Property Replacement tax.

**Standard Deduction, Personal Exemptions, SALT, and other Itemized Deductions taken after the calculation of Adjusted Gross Income** — These amendments to

the Act do not impact Illinois base income because the deductions are applied after the calculation of AGI (the start of Illinois returns). The Act did not repeal the personal exemption deduction but instead reduced it to zero for certain taxable years. Illinois taxpayers will remain entitled to an exemption of the basic amount for the taxpayer and each eligible dependent. The Illinois exemption amount is currently \$2,000. This provision should have no impact on Illinois base income, except for the decreased exemption that was not a result of the federal tax law change.

**Section 529 Plans** — IRC Section 529(c) is amended to expand the definition of “qualified higher education expenses” to include expenses for tuition in connection with enrollment or attendance at an elementary or secondary public, private, or religious school. The Illinois subtraction modification for contributions to IRC Section 529 plans only applies to Illinois 529 plans. Illinois 529 plans define “eligible educational institution” as public and private colleges, junior colleges, graduate schools, and certain vocational institutions. Illinois law requires an addition modification for the portion of a distribution attributable to the taxpayer’s previously subtracted contributions in cases where the taxpayer uses a distribution from an Illinois 529 plan to pay for expenses other than qualified expenses at an eligible educational institution. In addition, the Treasurer’s Act imposes a penalty equal to 10 percent of the earnings portion of a distribution used for expenses other than qualifying expenses at an eligible educational institution.

## Frequently Asked Questions

### **Pre-Paid Property Tax — Can we claim pre-paid property tax on our Illinois return?**

Any property tax paid in 2017 will be allowed as an Illinois Property Tax Credit on 2017 IL-1040 forms. This provision should decrease Illinois tax revenue due to increased property tax credit claimed.

### **Estate Tax — Does the change in the federal law affect Illinois estate tax?**

The federal tax law doubles the exemption amount for estate, gift, and generation-skipping taxes. This will have no effect on Illinois estate taxes. Illinois estate taxes are managed by the Attorney General’s office.

### **Standard Deduction, Personal Exemptions, SALT, and other Itemized Deductions taken after the calculation of Adjusted Gross Income — How do these changes affect Illinois?**

These amendments to the Act do not impact Illinois base income because the deductions are applied after the calculation of AGI (the start of Illinois returns). The Act did not repeal the personal exemption deduction but instead reduced it to zero for certain taxable years. Illinois taxpayers will remain entitled to an exemption of the basic amount for the taxpayer and each eligible dependent, which is currently \$2,000. This provision should have no impact on Illinois base income except for the decreased exemption that was not a result of the federal tax law change.

### **Net Operating Loss (NOL) Deduction Limitation — Will the NOL limitation affect Illinois income?**

The new limitations on the deduction may increase Illinois base income in the case of

individual taxpayers; however, due to the carryforward provision, Illinois base income may be reduced in subsequent years.

**Bonus Depreciation — Do I need to subtract or add back the 100-percent bonus depreciation?**

Illinois is not decoupled from 100-percent bonus depreciation. Bonus depreciation is considered when computing AGI and FTI. Taxpayers do not need to make any adjustment on their Illinois return for taking 100-percent bonus depreciation federally.

**Section 529 Plans — Will Illinois taxpayers be able to use Illinois 529 plans to pay for elementary or secondary schools?**

Illinois law requires an addition modification for the portion of a distribution attributable to the taxpayer's previously subtracted contributions in cases where the taxpayer uses a distribution from an Illinois 529 plan to pay for expenses other than qualified expenses at an eligible educational institution, which does not include elementary or secondary schools. In addition, the Treasurer's Act imposes a penalty equal to ten percent of the earnings portion of a distribution used for expenses other than qualifying expenses at an eligible educational institution.

## Preliminary Revenue Impact Estimates on Illinois Taxes Resulting from the Tax Cuts and Jobs Act

This table provides information about the potential impact of Public Law 115-97, the Tax Cuts and Jobs Act (the Act), on Illinois' individual income tax, corporate income tax, and personal property replacement tax. The estimates are subject to revision as our understanding of the Act's impact on Illinois taxpayers continues to evolve. To calculate the revenue impact of each provision, the Department relied on Illinois tax return data, the IRS's Statistics of Income datasets, and estimates produced by the Joint Committee on Taxation (JCT).

<i>All dollar amounts are in millions</i>		Individual Income Tax		Corporate Income Tax		Personal Property Replacement Tax	
		FY18	FY19	FY18	FY19	FY18	FY19
		Estimate	Estimate	Estimate	Estimate	Estimate	Estimate
<b>Potential Increases</b>							
Limitations on Business Deductions							
	Excess losses	\$70 - 80	\$120 - 130	\$0	\$0	\$21 - 24	\$36 - 39
	Interest expense	3 - 4	6 - 8	12 - 16	30 - 40	5 - 7	13 - 17
	Net operating loss	45 - 50	70 - 80	0	0	14 - 15	21 - 24
	Business entertainment	5 - 7	7 - 9	7 - 9	17 - 23	4 - 5	8 - 11
	FDIC premiums	0	0	5 - 6	12 - 16	1 - 2	4 - 6
	Executive compensation	0	0	2 - 4	6 - 10	1 - 2	2 - 4
	Related-Party expenses	0	0	0 - 1	0 - 2	0 - 1	0 - 1
Accounting method changes							
	Research expenses	0	0	0	0	0	0
	Accrual method changes	0	0	4 - 6	10 - 14	1 - 2	4 - 5
Business Dividends*		390 - 430	60 - 80	70 - 90	43-93	120 - 140	15 - 25
	Domestic dividends	-Included in Business Dividends-		-Included in Business Dividends-		-Included in Business Dividends-	
	Repatriation Transition	-Included in Business Dividends-		-Included in Business Dividends-		-Included in Business Dividends-	
	Global intangible income	-Included in Business Dividends-		-Included in Business Dividends-		-Included in Business Dividends-	
<b>Total Increases</b>		<b>513 - 571</b>	<b>263 - 307</b>	<b>100 - 132</b>	<b>85 - 125</b>	<b>167 - 198</b>	<b>103 - 132</b>
<b>Potential Decreases</b>							
Business asset expensing							
	Small business expensing	(30) - (40)	(55) - (60)	(2) - (3)	(6) - (8)	(10) - (13)	(19) - (21)
	Bonus depreciation	(39) - (50)	(45) - (55)	(46) - (50)	(230) - (250)	(28) - (33)	(96) - (106)
Accounting method changes							
	Cash method	(55) - (60)	(55) - (60)	(5) - (7)	(5) - (7)	(18) - (21)	(18) - (21)
Foreign dividends deduction		-Netted out of Business Dividends-		-Netted out of Business Dividends-		-Netted out of Business Dividends-	
Other provisions affecting individuals							
	ABLE accounts	Little revenue impact		0	0	0	0
	Education loans	Little revenue impact		0	0	0	0
<b>Total Decreases</b>		<b>(124) - (150)</b>	<b>(155) - (175)</b>	<b>(53) - (60)</b>	<b>(241) - (265)</b>	<b>(56) - (67)</b>	<b>(133) - (148)</b>
<b>Net Effect</b>		<b>\$363 - 447</b>	<b>\$88 - 152</b>	<b>\$40 - 79</b>	<b>\$(180) - (116)</b>	<b>\$100 - 142</b>	<b>\$(45) - (1)</b>

\*Repatriation is a one-time revenue source mostly impacting FY18. All other components are expected to continue in FY 19.