

Federal net loss carryforward does not affect eligibility for Section (a)(2)(F) subtraction modification for realized NUA benefit. (This is a GIL).

June 6, 2023

NAME/ADDRESS

Re: Illinois income tax

Dear NAME:

This is in response to your letter dated August 17, 2020, in which you request additional information regarding Illinois income tax. The nature of your request and the information you have provided require that we respond with a General Information Letter, which 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 found on the Department's web site at www.tax.illinois.gov.

Your letter states as follows:

Per my email conversation with NAME., I am writing to request a letter ruling. I retired in YEAR and took advantage of the Net Unrealized Appreciation (NUA). Per my understanding of Pub 120, I can reduce my Federal AGI by my NUA using line 5 of the IL 1040 (Pub 120 states I can reduce the following income on line 5 of my IL 1040 "capital gains on employer securities received in a lump-sum distribution, to the extent the gains are due to net unrealized appreciation on the securities at the time of distribution and reported on your U.S. 1040 or 1040-SR, Line 6."). Completing IL-4644 seems to confirm that I can reduce my federal AGI by my NUA. However, because I have a net loss carryforward from YEAR, my US 1040 line 6 is (\$\$\$\$). So, I was advised to obtain a letter ruling before I deduct my NUA on my IL line 5. Therefore, I did not deduct it on my original IL return.

I am contending that by not deducting it, I will forever lose the NUA benefit, in my case \$\$\$\$. The NUA is included in my income on my IL 1040 line 1. It is just being offset by the net loss carryforward. Here is the simplified example I provided to NAME that he suggested I send to you. Supposed my wife and my wages total \$\$\$\$ for YEAR, YEAR, and YEAR. Suppose we have a net loss in YEAR of \$\$k. In YEAR we have an NUA gain of \$\$k. No gain or loss in YEAR. Thus, on my Fed return for YEAR, I report a net loss of \$\$\$\$, and an AGI of \$\$\$\$\$. Same with YEAR (as I have a net loss carryforward of \$\$\$\$ and an NUA gain of \$\$\$\$ for a reported NL of \$\$\$\$). Then in YEAR, my AGI would be \$\$\$\$\$. Thus, my 3 year Fed AGI total is \$\$\$k (\$\$k from YEAR, \$\$\$k from YEAR, and \$\$\$k from YEAR). If I can't report the \$\$k on line 5 of my IL taxes for YEAR,

then my IL line 9 income would be identical to my Fed AGI, for a 3-year total taxable income for both of \$\$\$\$\$. So, I never get the benefit of reducing my Fed AGI by the \$\$k NUA. This is illustrated in the first section of the attached excel spreadsheet.

If the IRS would have allowed me to take the entire \$\$k loss in YEAR, my AGI's would be \$\$k for YEAR, \$\$\$\$k for YEAR, and \$\$\$\$k for YEAR for the same \$\$\$\$k. Then my IL line 9 totals would be \$\$k, \$\$\$\$k (the \$\$\$\$k AGI less the \$\$k NUA) and \$\$\$\$k for a total of \$\$\$\$k (thus I receive the \$\$k NUA benefit). Please see the second section of the excel spreadsheet.

If I get to take the \$\$k NUA in YEAR for IL (despite reporting a NL in YEAR), my Fed reporting would be \$\$k, \$\$k, and \$\$\$\$k, again totaling \$\$\$\$k. However, my IL reporting on line 9 would be \$\$k, \$\$k, and \$\$\$\$k for a total of \$\$\$\$k, allowing me the \$\$k NUA benefit. So, the only way I get the NUA benefit is if I take it for YEAR, despite the NOL I am reporting on my Fed return for YEAR (Third section of the excel spreadsheet).

(Excel Spreadsheet removed)

RULING

Section 203(a)(2)(F) of the Illinois Income Tax Act ("ITA", 35 ILCS 5/203(a)(2)(F)) provides the following deduction in the computation of an individual's Illinois base income:

An amount equal to all amounts included in such total pursuant to the provisions of Sections 402(a), 402(c), 403(a), 403(b), 406(a), 407(a), and 408 of the Internal Revenue Code, or included in such total as distributions under the provisions of any retirement or disability plan for employees of any governmental agency or unit, or retirement payments to retired partners, which payments are excluded in computing net earnings from self employment by Section 1402 of the Internal Revenue Code and regulations adopted pursuant thereto. (Emphasis added)

Step 3, Line 5 on page 7 of the *2019 Form IL-1040 Instructions* ("2019 Instructions") states, in pertinent part, as follows:

Line 5 Social Security benefits and certain retirement plans...Enter the amount of federally taxed Social Security and retirement income included in your adjusted gross income on Form IL-1040, Line 1 that you received from...**certain capital gains on employer securities** reported on federal Form 1040 or 1040-SR, Line 6.

Page 2 of Illinois Department of Revenue *Publication 120: Retirement Income* ("*Publication 120*"), states, in pertinent part, as follows:

You may subtract the amount of any federally taxed portion (not the gross amount) included in your Form IL-1040, Line 1 that you received from... capital gains on employer securities received in a lump-sum distribution, to the extent the gains are due to net unrealized appreciation on the securities at the time of distribution and reported on your U.S. 1040 or 1040-SR, Line 7.

Based on the examples you provided, your last example appears correct. According to Section 203(a)(2)(F), the *2019 Instructions* and *Publication 120*, any gains due to net unrealized appreciation ("NUA") on employer securities received in a lump-sum distribution reported on your U.S. 1040 or 1040-SR, Line 7, which are included in your AGI, are eligible for the subtraction modification afforded by Section 203(a)(2)(F). The net loss carryforward you describe does not appear to affect the application of Section 203(a)(2)(F). Therefore, if, as described, the NUA you realized meets these requirements, you may file a 2019 Form IL-1040-X and include the NUA on Line 5.

As stated above, this is a general information letter which 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 are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b). If you have any further questions regarding this letter, you may contact me at (217) 782-2844.

Sincerely,

Michael D. Mankowski
Associate Counsel - Income Tax

cc: Daily File
Correspondence file: