

Nonqualified, nongovernmental deferred compensation plans are not eligible for subtraction modification in Section 203(a)(2)(F). (This is a GIL.)

December 13, 2019

NAME

ADDRESS

Re: Illinois income tax

Dear NAME:

This is in response to your letter received November 26, 2019, in which you request 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 2 Ill. Adm. Code 1200.120(b) and (c), which may be found on the Department's web site at [www.tax.illinois.gov](http://www.tax.illinois.gov).

Your letter states as follows:

My name is NAME, a resident of CITY, IL for the past 5 years and approaching retirement, currently scheduled for June of 2020. Having reviewed the Illinois Department of Revenue Publication 120 on Retirement Income I was disappointed to read that you may not subtract income from deferred compensation plans that are not local or government-based deferred compensation plans.

As I researched the topic approximately 5 years ago, I did not pick up on the differentiation between private and government deferred compensation distributions and made the assumption that our first 10 years of retirement would be tax free in the State of Illinois, ultimately viewing this as a bit of a reward for enduring the otherwise high tax rates and cost of living, as well as incentive for retirees staying in Illinois after retirement.

I am writing to seek clarification on what makes a local or state government deferred compensation distribution eligible for subtraction from income and why a private deferred compensation distribution is not. My deferred compensation plan is set up specifically as a retirement account. It is

intended income for retirement purposes and to that end, set up for distribution over a 10-year period.

Anticipating confirmation of what is stated in Publication 120, is there an appeal or petition process that you would be able to advise?

Thank you for your attention and reply to this very important matter for my wife and myself as we prepare for and enter into the next chapter of our lives.

### **RESPONSE**

Under Section 203(a) of the Illinois Income Tax Act ("IITA"), 35 ILCS 5/203, the computation of an individual's "net income" taxed by Illinois begins with the taxpayer's federal adjusted gross income, as properly computed for the taxable year. Various addition and subtraction modifications are then made, and the resulting "base income" is then allocated and apportioned to Illinois. Section 203(h) of the IITA provides that no modification may be made to adjusted gross income unless expressly provided in Section 203.

Section 203(a)(2)(F) allows an individual to subtract from his or her adjusted gross 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.

The Internal Revenue Code ("IRC") classifies deferred compensation plans as either qualified or nonqualified plans. The IRC sections cited in Section 203(a)(2)(F) are all considered qualified plans under the IRC. Such qualified plans are granted a subtraction modification under Section 203(a)(2)(F). Unlike nongovernmental plans, according to Section 203(a)(2)(F), the subtraction allowed for distributions from government retirement plans does not depend on whether the plan is a qualified plan under federal income tax law. Regardless of whether it is qualified under the IRC or not, a government plan is eligible for the deduction under IITA Section 203(a)(2)(F) because the plan constitutes a "retirement or disability plan for employees of any governmental agency or unit"

Section 402 of the Internal Revenue Code ("IRC") deals with distributions from employee trusts exempt under Section 401(a) of the IRC, which provides an exemption for certain employee trusts "created or organized in the United States."

Section 403(a) of the IRC deals with annuities described in Section 404(a)(2) of the IRC, which describes certain annuities purchased by employee trusts exempt under Section 401(a) of the IRC.

Section 403(b) of the IRC deals with annuities for employees of exempt organizations.

Sections 406 and 407 of the IRC deal with employee benefit plans under Section 401 that cover overseas employees of affiliates of the employer that created the plan.

Section 408 of the IRC deals with individual retirement accounts.

You did not provide enough information to determine if your nongovernmental deferred compensation plan would fall under one of the above stated sections of the Internal Revenue Code. Your employer may be able to tell you whether your plan is qualified and eligible for the subtraction.

The Department must enforce the IITA as written, as a result, it must follow Section 203(h) and only allow modifications expressly provided for in Section 203. As a result, there is no appeal or petition process if your deferred compensation plan does not fit within any of the modifications listed in Section 203. The only way to include a deferred compensation plan not listed in Section 203 would be to amend the IITA.

If, after you begin receiving distributions from your deferred compensation plan, you feel that your distributions are eligible for a subtraction modification, you may file a Form IL-1040 and claim the subtraction. If it is denied, you may protest the denial.

The Illinois Income Tax Act, associated Rules, forms and other guidance may be found at the Department's website: [www.tax.illinois.gov](http://www.tax.illinois.gov).

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 1200.11O(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