Support legislation to minimize the financial reporting impact of the permanent tax rate increase enacted by P.A. 100-0022

We propose legislation to amend Section 203 of the Illinois Income Tax Act to minimize the financial statement (book) impact of the permanent tax rate increase enacted by P.A. 100-0022.

Companies are required to record deferred tax liabilities for financial reporting purposes under GAAP. Tax law changes, such as the enactment of a permanent tax rate increase, mandate a recalculation of deferred tax liabilities (future tax liabilities recorded on the company's books). When a state increases the statutory income tax rate, a company is required for financial statement purposes to restate existing deferred tax liabilities at the higher rate. Such an increase in deferred tax liability requires companies to recognize an expense to the income statement in the quarter the rate change is enacted. The recognition of these additional expenses will impact a company's overall financial performance, which in turn could affect its stock price.

Some states have amended their laws to lessen the financial statement impact of major income tax law changes. For example, several years ago, Massachusetts enacted legislation to establish a deduction for corporate taxpayers that experienced an increase in a combined group's net deferred tax liability because of the state's change to combined reporting. This offsetting deduction was to reduce the potential financial statement impact resulting from the state's enactment of a major income tax law change. However, the deduction was not effective immediately.

The Massachusetts provision was originally scheduled to provide a tax deduction to the affected companies over a seven-year period beginning in 2012. However, as the 2012 date approached, because of fiscal constraints, the state delayed the implementation of the deduction. Current Massachusetts law provides a deduction over a thirty-year period beginning in 2021. Washington, DC and Connecticut have enacted similar legislative relief.

Even though the deduction is not yet available, the presence of the Massachusetts deduction (despite periodic delays in implementing it) has been a benefit to the companies directly impacted by the tax law change. The continuation of the deduction in some form has allowed the affected companies to avoid the financial statement impact they were originally seeking to mitigate, while delaying and minimizing the revenue impact to the state of Massachusetts.

We are proposing an amendment to Section 203 of the Illinois Income Tax Act to establish a subtraction modification (deduction) that would, similar to the Massachusetts language, offset the adverse impact of a permanent tax rate increase on the financial statements of publicly traded companies.

The draft legislation proposed makes the deduction effective beginning with tax years beginning on or after July 1, 2025 and is spread over a 10-year period. In other words, there would be no revenue impact to the state until tax years beginning on or after July 1, 2025. The Illinois General Assembly would have plenty of opportunity to evaluate the deduction and, if it so chooses, modify it by deferring the date amortization of the deduction begins or lengthening the time period the deduction can be claimed.

In order to provide financial statement relief to affected companies, this issue must be addressed before publicly traded companies are required to complete their third quarter reporting for financial statement purposes. Accordingly, legislative relief must be enacted by September 30, 2017.