

General Information Letter: Individual who was required to include income from Madoff Investments in federal adjusted gross income in years prior to 2008, and who is entitled to a federal itemized deduction for theft loss from the investment in 2008, must include the income in Illinois base income in the prior years and is not entitled to deduct the theft loss in computing base income in 2008.

August 7, 2009

Dear:

This is in response to your letter dated May 19, 2009 in which you state the following:

We are writing on behalf of our above-referenced clients. During 2008, they filed Amended Illinois Income Tax Returns for years 2003 through 2006, as a result of Federal amendments to include previously unreported income. Remittance was not made at the time of filing pending acceptance of the Federal amendments.

In the period since these amendments have been prepared and filed, it has come to light that the unreported income was due entirely to income as reported by Madoff Investments, which has been confirmed as being entirely fictitious. The Internal Revenue Service, in Revenue Procedure 2009-20 has issued guidance with regard to treatment of these losses. As per the guidelines, in order to claim a theft loss for tax year 2008, the taxpayers agree not to file amended returns recharacterizing the income originally reported. Accordingly, newly amended Federal returns will not be prepared for the years previously referenced.

We are unaware that the Department of Revenue has issued similar guidance as to the treatment of these losses. Accordingly, we respectfully request permission to reverse these previous amendments without applying similar treatment to the Federal returns for the corresponding years. The Illinois Individual Income Tax Returns would therefore revert to the original filings with the amended returns and the additional liabilities generated by them being disregarded. Please advise the procedure to be followed under these circumstances.

According to the Department of Revenue ("Department") regulations, the Department may issue only two types of letter rulings: Private Letter Rulings ("PLR") and General Information Letters ("GIL"). The regulations explaining these two types of rulings issued by the Department can be found in 2 Ill. Adm. Code §1200, or on the website <http://www.tax.illinois.gov/LegalInformation/regs/part1200>.

Due to the nature of your inquiry and the information presented in your letter, we are required to respond with a GIL. GILs are designed to provide background information on specific topics. GILs, however, are not binding on the Department.

Your letter refers to Revenue Procedure 2009-20 which was issued simultaneously with Revenue Ruling 2009-09. The Illinois Department of Revenue has not issued anything similar to IRS Revenue Ruling 2009-09 and IRS Revenue Procedure 2009-20 to allow for a theft loss deduction in the year the lead figure in a ponzi scheme is indicted. These IRS actions provide an option to taxpayers to avoid the need to file federal amended returns reversing the "fictitious income" from the ponzi schemes.

Under Section 203 of the Illinois Income Tax Act (35 ILCS 5/203), the computation of a taxpayer's "net income" taxed by Illinois begins with the taxpayer's federal taxable income or, in the case of an

individual, 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) provides that no modification may be made to taxable income or adjusted gross income unless expressly provided in Section 203. There is no provision in Section 203 that modifies the federal treatment in the case you describe.

As you may know, theft losses are reported on Schedule A as an itemized deduction. Because the starting point for calculating an individual's Illinois income tax liability for a given taxable year is that individual's federal adjusted gross income, it does not reflect the itemized deductions found in Schedule A. Your clients will therefore be taxed on the income in 2003 through 2006 and will not receive any benefit from the theft loss in 2008 because it is an itemized deduction.

As stated above, this is a general information letter which does not constitute a statement of policy that either applies, interprets or prescribes tax law. It is not binding on the Department. Should you have additional questions, please do not hesitate to contact our office.

Sincerely,

Heidi Scott
Staff Attorney -- Income Tax