

Important News -- Illinois Amnesty Program

The state of Illinois recently implemented an amnesty program (the "Illinois Amnesty" or "Amnesty"). Unlike amnesty programs that are principally designed for delinquent taxpayers, the Illinois Amnesty is relevant to all taxpayers who file Illinois tax returns, whether or not they believe they currently owe any Illinois taxes. The Illinois Amnesty is particularly relevant to corporate taxpayers undergoing IRS audits.

The Illinois Amnesty is open only until November 17, 2003. It is therefore critical that any taxpayer who files Illinois tax returns review the Illinois Amnesty ASAP to determine whether to participate.

The Illinois Amnesty adopts a carrot and stick approach. Participate in the Illinois Amnesty and the state will reward you. But if you do not participate, the state will seek to punish you.

The Stick. Under the Illinois Amnesty, any taxpayer who owes or will owe liabilities for past periods and who does not participate in the Amnesty will be penalized. The penalty is that the state will double the interest and penalties that the taxpayer will otherwise ultimately owe on any past liabilities. For example, if a taxpayer is currently undergoing an audit, either a federal audit or an Illinois audit, and that audit will ultimately result in a deficiency of Illinois taxes, the interest that the taxpayer will be charged on that deficiency will be twice the regular rate. This doubling of interest will apply to both interest that has already accrued and to all future interest.

We expect that some taxpayers may decide to challenge the legality of this provision. Nonetheless, the effect of this harsh provision is to compel every taxpayer to look at its open tax years and determine whether it should pay any possible deficiencies now.

The Carrot. Under the Illinois Amnesty, a taxpayer who pays any past liabilities, whether or not those liabilities have been finally determined, will not be charged interest or penalties on those liabilities. What is unique about this provision is that Illinois permits a taxpayer who is undergoing an IRS audit, and who expects that the audit will cause adjustments to its taxable income, to make a good faith estimate of the additional Illinois tax that those adjustments will cause. If the taxpayer then remits to the state that estimate by November 17, all interest with respect to that amount will be abated. But if the taxpayer ultimately overstates the amount of its liability, Illinois will credit the taxpayer for the overpayment, with interest.

For example, assume a taxpayer has been engaged in a dispute with the IRS regarding its 1990 tax year. The taxpayer expects that it will ultimately settle this dispute and a deficiency will result, which deficiency will have to be reported to every state where the taxpayer files a tax return. If the taxpayer voluntarily estimates that liability for Illinois purposes by November 17 and pays it, the taxpayer will avoid all interest from 1990 forward. But if the taxpayer does not do so, the interest from 1990 forward will be doubled.

As a result of these provisions, any taxpayer who files Illinois tax returns and who may be subject to an IRS audit or otherwise faces a potential tax exposure should make an estimate of what impact that audit may have on its past Illinois liability. If the taxpayer remits that amount to Illinois by November 17, the taxpayer will permanently avoid all interest on that liability. If, however, the taxpayer does not estimate its liability and merely waits for the conclusion of the audit, Illinois will attempt to double the interest that the taxpayer will ultimately have to pay.

We urge each of our clients who file Illinois tax returns and who may have the possibility of future adjustments to its tax liability to consider whether it should participate in the Illinois Amnesty. Please feel free to

contact Greg Gallagher of Kirkland & Ellis (312 861-2087) or any other Kirkland & Ellis tax attorney if you have any questions or wish to discuss whether the Illinois Amnesty may be relevant to you.

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