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Illinois Decouples from Federal QSBS Exclusion and Further Limits Corporate NOL Deductions

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On June 16, 2026, Governor Pritzker signed Public Act 104-0468 into law. The Illinois Act makes two significant income tax changes: it decouples Illinois from the federal qualified small business stock ("QSBS") gain exclusion under Code Section 1202 and further restricts the use of corporate net operating loss ("NOL") carryover deductions.

- Beginning with taxable years ending on or after December 31, 2026, Illinois will require taxpayers to add back federally excluded QSBS gain to the Illinois income tax base.
- Founders and investors may owe Illinois tax on gain that is excluded for federal income tax purposes.
- Beginning with taxable years ending on or after December 31, 2027, Illinois will limit the amount of corporate NOL carryover that a C corporation may use each year.

Decoupling of Code Section 1202

In our previous article, we discussed the expansion of the QSBS gain exclusion under the One Big Beautiful Bill Act (OBBBA). In general, Code Section 1202 allows a taxpayer to exclude gain from the sale of QSBS if the stock satisfies certain requirements, including holding period requirements. This exclusion can be especially valuable to founders and investors because it may allow a taxpayer to exclude the greater of 10 times the taxpayer's invested capital or $10,000,000 ($15,000,000 for stock acquired after enactment of the OBBBA).

As a general matter, Illinois starts with an entity's federal taxable income or an individual's federal adjusted gross income. Illinois then applies its own additions and subtractions to determine the taxpayer's Illinois income tax base.

As a result of the Illinois Act, federally excluded QSBS gain will be added back, dollar for dollar, to the Illinois income tax base. This change effectively decouples Illinois from the federal QSBS exclusion for taxable years ending on and after December 31, 2026.

In practical terms, founders and investors should evaluate the Illinois tax impact before an anticipated exit event. Depending on the facts, taxpayers may also want to consider whether transaction timing, negotiations, or a change in domicile before an exit could affect the Illinois tax result.

NOL Carryover

The Illinois Act also affects corporations with NOL carryovers, creating a separate set of planning considerations for businesses operating in Illinois.

Beginning with taxable years ending on or after December 31, 2027, a C corporation with an NOL carryover may use that carryover only up to 15% of the C corporation's net income or $500,000, whichever is greater. The 15% cap increases each year until taxable

years ending on or after December 31, 2031, when it reaches 80%.

Planning for the Illinois Tax Changes

The Illinois Act creates important new considerations for founders, investors, and businesses with Illinois tax exposure. With the QSBS change taking effect for taxable years ending on or after December 31, 2026, and the new NOL limitations following in 2027, taxpayers should evaluate how these provisions may affect upcoming transactions and broader tax planning.

For questions about these changes or their potential impact, contact Jennifer Tolsky, Chair of Gould & Ratner's Tax Planning and Structuring Practice.