

General Information Letter: State income tax withholding is generally required from compensation “paid in this State” from which federal income tax withholding is required.

August 14, 2012

Dear:

This is in response to your letter dated August 10, 2012, in which you request a letter ruling. 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 86 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).

In your letter you have stated the following:

I would like clarification on the amount of Illinois earnings to be placed on the W-2 when there are multiple states and multiple withholding.

For example

Illinois earnings	\$127,000
Indiana Earnings	\$16,000
2011 Form W-2 (US) Box 1 – Wages	\$143,000

The employer in this case states that IL instructions say that the entire \$143,000 must be placed on the W-2 as Illinois wages, and then issue a W-2 for Indiana showing the wage as \$16,000, thus in total reporting a total of \$159,000 in combined state earnings, when the total earnings are a total of \$143,000. This causes a correction notice eliminating a credit for taxpayers for tax paid to other states.

If you would clarify the reporting requirements and give some publication, letter or instructions as how these wages are to be correctly reported it would be helpful for the future years.

Response

Section 701(a) of the Illinois Income Tax Act (35 ILCS 5/701) provides, in part:

Every employer maintaining an office or transacting business within this State and required under the provisions of the Internal Revenue Code to withhold a tax on . . . compensation paid in this State (as determined under Section 304 (a)(2)(B)) to an individual.

Section 304(a)(2)(B) of the Illinois Income Tax Act (35 ILCS 5/304) provides, in part:

Compensation is paid in this State if:

- (i) The individual's service is performed entirely within this State;

(ii) The individual's service is performed both within and without this State, but the service performed without this State is incidental to the individual's service performed within this State; or

(iii) Some of the service is performed within this State and either the base of operations, or if there is no base of operations, the place from which the service is directed or controlled is within this State, or the base of operations or the place from which the service is directed or controlled is not in any state in which some part of the service is performed, but the individual's residence is in this State.

The amount of Illinois wages that should be reported on the Form W-2 is the amount "paid in this State" on which withholding is required. Your letter does not contain any facts relevant to making this determination. The fact that, under Indiana law, some or all of the compensation may be taxable by Indiana and subject to Indiana withholding is not relevant. Guidance on when compensation is "paid in this State" can be found at 86 Ill. Adm. Code Section 100.7010, which can be found at:

<http://www.ilga.gov/commission/jcar/admincode/086/086001000Q70100R.html>

and in Publication 130, which can be found at:

<http://www.iltax.com/Publications/Pubs/Pub-130.pdf>

Regarding the credit for taxes paid to other states, Section 601(b)(3) of the Illinois Income Tax Act (35 ILCS 5/601), which allows the credit, provides in part:

the credit provided under this paragraph for tax paid to other states shall not exceed that amount which bears the same ratio to the tax imposed by subsections 201(a) and (b) otherwise due under this Act as the amount of the taxpayer's base income that would be allocated or apportioned to other states if all other states had adopted the provisions in Article 3 of this Act bears to the taxpayer's total base income subject to tax by this State for the taxable year.

In Article 3 of the Illinois Income Tax Act, Section 302(a) of the Illinois Income Tax Act (35 ILCS 5/302) provides:

All items of compensation paid in this State (as determined under Section 304(a)(2)(B)) to an individual who is a nonresident at the time of such payment and all items of deduction directly allocable thereto, shall be allocated to this State.

Under these two provisions, compensation "paid in this State" is allocated to Illinois and cannot be treated as "base income that would be allocated . . . to other states if all other states had adopted the provisions in Article 3 of this Act" in computing the limitation on the credit for taxes paid to other states. Accordingly, to use your example, if the entire \$143,000 in wages are "paid in this State," and the taxpayer has no other income, the amount of base income that would be allocated to other states using Illinois' rules is zero, and the limit on the taxpayer's credit for taxes paid to other states is zero.

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 1200.110(b). If you have

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any further questions, you may contact me at (217) 782-7055.

Sincerely,

Paul S. Caselton
Deputy General Counsel – Income Tax