

Private Letter Ruling. Under the facts represented, the commercial domicile of the taxpayer is not in Illinois.

June 13, 2013

Dear:

This is in response to your letter dated March 5, 2013 in which you request a Private Letter Ruling on behalf of COMPANY1. Your request for a Private Letter Ruling includes the information required under paragraphs 1 through 8 of subsection (b) of 2 Ill. Adm. Code 1200.110. The Private Letter Ruling will bind the Department only with respect to COMPANY1 for the issues presented in this ruling. Issuance of this ruling is conditioned upon the understanding that COMPANY1 and/or any related taxpayer(s) is not currently under audit or involved in litigation concerning the issues that are the subject of this ruling request.

The facts and analysis as you have presented them are as follows:

We respectfully request, as described below pursuant to Section 1502(a)(2) of the Illinois Income Tax Act ("IITA") and 86 Ill. Adm. Code Section 100.3210, confirmation that COMPANY1's commercial domicile is considered to be located outside of Illinois based on the facts presented.

#### General Information

1. Enclosed please find an original Form IL-2848, Power of Attorney, authorizing COMPANY2 to represent COMPANY1 before the Department.
2. This PLR is not requested with regard to hypothetical or alternative proposed transactions. This PLR is requested to determine the Illinois income tax consequences of the actual business practices of COMPANY1 for its taxable year ended December 31, 2012.
3. To the best of the knowledge of both COMPANY1 and COMPANY2, the Department has not previously ruled regarding this matter for COMPANY1. In addition, COMPANY1 has not submitted the same or similar issue to the Department.
4. No audit or litigation regarding the tax period or issues presented is pending with the Department with respect to COMPANY1.
5. COMPANY1 respectfully requests that identifying information be deleted from the PLR prior to dissemination to others; specifically that the respective entity names, business descriptions, addresses, and the name of its representative be deleted.
6. COMPANY1 is not aware of any authority contrary to the authorities referred to and cited below.

#### Statement of Material Facts

COMPANY1 was formed in 20XX as a Company Limited by Shares under The Companies Law of the LOCATION (20XX Revision). Under its Articles of Association, the registered office of COMPANY1 is at the offices of COMPANY3 in LOCATION, where its attorney is also

located. The share capital of COMPANY1 is divided into X ordinary shares held by a Private Equity Investment Firm ("Private Equity") and XX participating shares authorized with approximately XXX shares issued as of December 31, 2012 to non-U.S. entities that maintain a commercial domicile outside of the United States (collectively, the "Participants or Members"). The sole assets of COMPANY1 are a limited partnership interest in Fund, L.P. ("Fund") and nominal cash held in a bank account located outside of Illinois. COMPANY1 has income/loss from its investment in Fund and earns interest income from its bank account. Expenses consist of management fee payments to Private Equity and payments to unrelated third parties for compliance work, including legal fees, audit fees, tax fees, and custody fees. Each partner in Partnership, including COMPANY1, is allocated a management fee in accordance with Private Equity's standard management fee schedule.

COMPANY1 holds a XXXX% limited partner capital interest in Fund as of December 31, 2012. Fund was formed in STATE and maintains its registered office in Illinois along with its address for service of process through The Corporation Trust Company. Under Fund's Limited Partnership Agreement, item 4(e) provides that limited partners such as COMPANY1 shall not "...take any part in the control of the business of, or transact any business for, or have any power to sign for or to bind..." this partnership. The general partner in Fund is Private Equity. Private Equity is based in CITY, Illinois, and its employees undertake management activities on behalf of multiple funds.

COMPANY1 does not have employees or officers. COMPANY1 has a single Director appointed by the participants who may appoint officers as provided for in COMPANY1's Articles of Association. However, no officers have been appointed since the inception of COMPANY1. That single Director is Private Equity who was appointed through the Articles of Association at the formation of COMPANY1. Private Equity does not receive any compensation from COMPANY1 in exchange for its services as Director. The Articles of Association specifically mandate that COMPANY1 shall acquire a limited partnership interest in Fund and further provide that "the Directors shall, subject to applicable law, manage and operate the Company in such manner as necessary to replicate as closely as possible a direct investment by each Member in the Partnership." Upon the final liquidation distribution by the Fund, the Articles of Association provide for the automatic wind-up and dissolution of COMPANY1 without further action by the Participants.

The Director is granted authority to manage the business of COMPANY1 which consists primarily of causing COMPANY1 to comply with the terms of the Limited Partnership Agreement of Fund. However, to the extent COMPANY1 is called upon to take any action as a limited partner of the Partnership, the Director's authority is expressly limited by the Articles of Association. To the extent any action of COMPANY1 as a limited partner is required, the Director must submit the proposed action to the Participants who will vote on the proposed action. No action can be taken by COMPANY1 until a resolution causing the Company to take action is adopted based on a vote of the Participants. To the extent any meetings of the board of directors are required to be held, such meetings will be held outside of Illinois.

#### Ruling Requested

We respectfully request that the Department confirm our determination that COMPANY1's commercial domicile is not in Illinois.

## Summary of Relevant Law

Section 1501(a)(2) of the Illinois Income Tax Act defines “commercial domicile” as “...the principal place from which the trade or business of the taxpayer is directed or managed.” Illinois regulation 86 Ill. Adm. Code Section 100.3210(a) further provides “in general, this is the place at which the offices of the principal executives are located. Where executive authority is scattered, the place of daily operational decision making controls. Such determinations must be made on the basis of all the facts and circumstances.”

Illinois regulations also provide an example to further illustrate the meaning of the term “commercial domicile” as follows:

(b) Example. 86 Ill. Adm. Code 100.3210 may be illustrated by the following example: Company A has a board of directors which meets quarterly, each meeting being held at a different plant in a different state. A’s chairman is designated as its chief executive officer and all top policy decisions are made by him. A’s president makes the day-to-day decisions involved in management and it is to him that the manufacturing and sales vice presidents report. He reports to the chairman. A’s treasurer is the company’s top financial officer, reporting directly to the chairman, and being reported to by financial vice presidents and the controller. A’s chairman operates largely out of his home in Wisconsin, communicating with other executives by telephone and periodic visits to their offices. A’s president has his office at the company office in Chicago. The manufacturing and sales vice presidents also have offices at the company office in Illinois, as do the sales manager and the controller. A’s treasurer and financial vice president have their offices at the company office in New York City. The company’s attorneys and accountants are located in Chicago; its investment banker in New York City. On the basis of the foregoing facts, A’s commercial domicile would be Illinois, because daily operational decision making occurs principally within Illinois.

## Analysis

First, the definition of commercial domicile assumes that the entity is engaged in a “trade or business.” Illinois law offers little guidance on the question of when a “trade or business” is deemed to exist. In a general information letter (IT 95-0073 GIL, 05/01/1995) issued by the Department, the Department was asked to consider the term “business” as the term applied to the application of the State’s bulk sales reporting rules under Section 902(d) of the Illinois Income Tax Act. Specifically, the bulk sales reporting rules considered in the general information letter apply to “any taxpayer who, outside the usual course of business, sells or transfers the major part of any one or more of the following business assets: (A) stock of goods; (B) furniture and fixtures; (C) machinery and equipment; and (D) real property. The Taxpayer, requesting the letter ruling from the Department, owned a parcel of real estate that it leased to a closely held business. The Department stated that it considered a “reasonable interpretation of the term ‘business’, for purposes of applying the bulk sales reporting rules, to be any trade or business under Section 162 of the Internal Revenue Code.” The Department, citing the U.S. Tax Court decision *Commissioner of Internal Revenue v. Robert P. Groetziner*, 480 U.S. 23, 87-1 USTC (1987), stated that “to be engaged in a trade or business, for purposes of the Internal Revenue Code, the taxpayer must be involved in an activity with continuity and regularity, and the taxpayer’s primary purpose for engaging in the activity must

be for income or profit.” In considering the Taxpayer’s activity of leasing real property, the Department determined that the Taxpayer was in fact engaged in a trade or business since it was allowed a business expense deduction for the property on its federal income tax return and therefore was subject to the bulk sales reporting requirements.

Unlike the activities of the Taxpayer in IT 95-0073 GIL, COMPANY1 does not conduct any activity “with continuity and regularity” such as renting or leasing property to another party. Similar to the activities of an Investment Partnership, an entity afforded special treatment under Illinois law given its passive investment activities, COMPANY1 merely holds a passive and limited interest in Fund, which itself is characterized as an investment partnership under Illinois law. See, 35 ILCS 5/1501(a)(11.5); 86 Ill. Adm. Code Section 100.9730. Under its Articles of Association, COMPANY1 exists only as a conduit for passive investment purposes. Specifically, the Articles of Association of COMPANY1 expressly provides that the Director shall “manage and operate the Company in such manner as is necessary to replicate as closely as possible a direct investment by each Member in the Partnership.” The effect of this mandate is to ensure that COMPANY1 operates as a passive conduit; its only purpose is to pool the interests of the foreign investors through their purchases of shares in COMPANY1, for purposes of investing in the Fund. In fact, under the Articles of Association, COMPANY1 will be automatically wound up upon the date of receipt by COMPANY1 of the final liquidation distribution from the Fund. As COMPANY1 is not operating a “trade or business,” this entity does not have a commercial domicile under the Illinois definition of this term and therefore cannot have a commercial domicile in Illinois.

To the extent COMPANY1 is considered to have a commercial domicile, it would be located in the LOCATION where daily operational decision making principally occurs. Similar to the example in Illinois regulation 86 Ill. Adm. Code Section 100.3210(b), COMPANY1’s executive authority is scattered. COMPANY1’s registered office is located in the LOCATION and that is the location where the register of its Members is maintained in accordance with the Companies Law of the LOCATION. In addition, COMPANY1’s attorney is located in the LOCATION. While no board meetings have been held to date, any and all board meetings would be held in the LOCATION. COMPANY1’s sole Director, while located in Illinois, has extremely limited authority to make operating decisions that bind COMPANY1. All operating decisions that bind COMPANY1, including any action of COMPANY1 as a limited partner of Fund, are made by the Participants by resolution based on a vote on proposed action submitted to the Participants by the Director. All such votes would occur in the LOCATION. No action can be taken by COMPANY1 until a resolution causing the Company to take action is adopted based on a vote of the Participants. In effect, the only “operational decision making” required for COMPANY1, is made by the Participants consistent with the Articles of Association’s provision that the entity be managed to “replicate as closely as possible a direct investment by each Member in the Partnership.” Since any operational decision making for COMPANY1 principally occurs in the LOCATION, the commercial domicile of COMPANY1, to the extent one exists, would be the LOCATION.

## **RULING**

Section 1501(a)(2) of the Illinois Income Tax Act (“IITA”; 35 ILCS 5/1501(a)(2)) defines the term “commercial domicile” as follows:

The term “commercial domicile” means the principal place from which the trade or business of the taxpayer is directed or managed.

Department Regulations Section 100.3210 further provides:

(a) General definition. The term “commercial domicile” is defined in IITA Section 1501(a)(2) to mean the principal place from which the trade or business of the taxpayer is directed or managed. In general, this is the place at which the offices of the principal executives are located. Where executive authority is scattered, the place of daily operational decision making controls. Such determinations must be made on the basis of all the facts and circumstances.

(b) Example. 86 Ill. Adm. Code 100.3210 may be illustrated by the following example: Company A has a board of directors which meets quarterly, each meeting being held at a different plant in a different state. A’s chairman is designated as its chief executive officer and all top policy decisions are made by him. A’s president makes the day-to-day decisions involved in management and it is to him that the manufacturing and sales vice presidents report. He reports to the chairman. A’s treasurer is the company’s top financial officer, reporting directly to the chairman, and being reported to by financial vice presidents and the controller. A’s chairman operates largely out of his home in Wisconsin, communicating with other executives by telephone and periodic visits to their offices. A’s president has his office at the company office in Chicago. The manufacturing and sales vice presidents also have offices at the company office in Illinois, as do the sales manager and the controller. A’s treasurer and financial vice-presidents have their offices at the company office in New York City. The company’s attorneys and accountants are located in Chicago; its investment banker in New York City. On the basis of the foregoing facts, A’s commercial domicile would be Illinois, because daily operational decision making occurs principally within Illinois.

In Associated Partnership I, Inc. v. Huddleston, 889 S.W.2d 190 (Tenn. 1994), the Tennessee Supreme Court considered the commercial domicile of a corporation whose only business activity was holding and managing a general partnership interest. The taxpayer was a general partner of a partnership engaged in a publishing business. However, the day-to-day operations of the partnership were conducted by a second general partner. This partner had sole and exclusive authority to hire and fire employees, conduct product development, execute routine contracts and documents, and perform other operational activities. Taxpayer’s involvement in the day-to-day operations was limited to major issues such as borrowing and certain asset sales. Taxpayer’s chief accounting officer, who was also a full-time employee of the partnership, performed bookkeeping functions in Tennessee relating to a bank account the taxpayer maintained in Tennessee for the purpose of receiving distributions of partnership income. The chief accounting officer never attended a meeting of the officers and directors of taxpayer, where all management and investment policy decisions of the taxpayer were made. These meetings were all held outside Tennessee. In addition, the taxpayer’s lawyers, accountants, and investment bankers were located outside Tennessee, along with the corporation’s books and records.

The taxpayer later sold a portion of its partnership interest, generating capital gain income. The state argued, *inter alia*, that if the gain is nonbusiness income, it should be allocated entirely to Tennessee because Tennessee was the taxpayer’s commercial domicile. Under Tennessee law, the term commercial domicile is defined exactly as it is in Illinois, as the “principal place from which the trade

or business of the taxpayer is directed or managed. (Assoc. Ptsp I, Inc., 889 S.W.2d at 194, fn.2) The court rejected the state's argument, finding that the taxpayer's commercial domicile was located outside Tennessee. The court noted that under the plain language of the statute, the commercial domicile is the place from which the business is directed or managed, rather than the location of the assets and operations. Accordingly, the court relied on the fact that all management personnel resided outside of Tennessee, and that all management meetings were held outside of Tennessee. In addition, the taxpayer's corporate advisors, including its lawyers, accountants and bankers, were all located outside of Tennessee. Although taxpayer's chief accounting officer was based in Tennessee, she had no duties at, and received no compensation from, the taxpayer. The court also rejected the argument that the management activities of the partnership should be attributed to the taxpayer in determining the commercial domicile of the taxpayer. In the absence of statutory authority, the court found no basis for attributing the assets and activity of the partnership to one of its corporate partners for purposes of determining the commercial domicile of the partner.

The facts in this case are similar to the facts in Associated Partnership I, Inc. The only business activity of COMPANY1 is holding and managing its partnership interest in Fund. In addition, there is no statutory basis in this case for attributing activities of Fund to COMPANY1 for purposes of determining COMPANY1's commercial domicile. With respect to the activities directly conducted by COMPANY1, you have not represented any facts sufficient to support a determination that COMPANY1's commercial domicile is Illinois. You indicate that any management activity required to be conducted by COMPANY1 will take place in the LOCATION. In particular, your letter states that "all" operating decisions that bind COMPANY1 must be made by resolution of the Participants of COMPANY1, and that any vote on such resolution would occur in the LOCATION. In addition, none of the Participants are residents of Illinois, COMPANY1's registered office is the LOCATION, and its attorney is located in the LOCATION.

While COMPANY1's sole Director is based in Illinois, it appears from your letter that Director's sole duty with respect to COMPANY1 is to submit to the Participants any matter that requires action to be taken by COMPANY1 in its role as limited partner. Although your letter states that Director is charged with authority to manage and operate the business of COMPANY1, which consists primarily of causing COMPANY1 to comply with the terms of the limited partnership agreement, except as stated above your letter does not detail any activities undertaken by Director to manage the business of COMPANY1 nor any specific duties that Director must undertake to cause COMPANY1 to comply with the terms of the limited partnership agreement. Rather, Director's only duty is to submit matters that require action by COMPANY1 to the COMPANY1 Participants. Moreover, Director is uncompensated. Under these facts, it cannot be concluded that the principle place from which the trade or business of COMPANY1 is directed or managed is Illinois. To the contrary, based on the facts you have represented any management activities that take place will occur in the LOCATION. Therefore, based on the facts you have provided, the commercial domicile of COMPANY1 is not Illinois.

The facts upon which this ruling is based are subject to review by the Department during the course of any audit, investigation or hearing and this ruling shall bind the Department only if the material facts as recited in this ruling are correct and complete. This ruling shall bind the Department for all taxable years, except as limited pursuant to 2 Ill. Adm. Code 1200.110(d) and (e). This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules or in the material facts recited in this ruling.

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Sincerely,

Brian L. Stocker  
Chairman, PLR Committee (Income Tax)