IT 16-0002-PLR 11/18/2016 APPORTIONMENT

Income from Intangible Property – Where taxpayer is a dealer, gain from sale of partnership interest is included in numerator of sales factor where gain is received from customer in Illinois

November 18, 2016

Re: Request for Private Letter Ruling
COMPANY

Dear Xxxxx:

This is in response to your letter dated April 14, 2016 in which you requested a Private Letter Ruling on behalf of COMPANY. Review of your request for a Private Letter Ruling indicates that all information described in paragraphs 1 through 8 of subsection (b) of 2 Ill. Adm. Code 1200.110 is contained in your request. This Private Letter Ruling will bind the Department only with respect to COMPANY. Issuance of this ruling is conditioned upon the understanding that COMPANY 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 are writing to request a Private Letter Ruling in accordance with 2 Ill. Admin. Code 1200.110 related to the disposition of partnership interests and the sourcing provisions under Illinois Compiled Statutes 5/304(a)(3)(C-5)(iii)(a). The transactions in question occurred during the tax year ended MONTH 31, 20XX.
>
> Disclosures
>
> 1. Enclosed please find an original Form IL-2848, Power of Attorney, authorizing LEGAL TEAM to represent COMPANY ("COMPANY") before the Illinois Department of Revenue (the "Department").
> 2. This Private Letter Ruling ("PLR") is not requested with regard to hypothetical or alternative proposed transactions.
> 3. The Taxpayer is not currently engaged in litigation with the Department in regard to this or any other tax matter.
> 4. The taxpayer is not currently under audit by the Department in regard to this matter, however, the Taxpayer is currently under audit related to its 20XX IL-1065 replacement tax return.
> 5. The Taxpayer requests that certain information be redacted from the PLR prior to dissemination to others. The Taxpayer requests that its name, all contractual parties' names, its exhibits, and the name of its representative be redacted.

6. The Taxpayer knows of no authority contrary to the authorities referred to and cited below.

Tax Year

This ruling is requested for the tax year ending MONTH 31, 20XX ("the 20XX tax year").

Ruling Requested

Based on our analysis of ILCS 5/304(a)(3)(C-5)(iii)(a), it is our understanding that the Taxpayer's sales of partnership interests in the COMPANY 1 should be sourced based on customer location. We respectfully request a Private Letter Ruling in accordance with 2 Ill. Adm. Code 1200.110 that confirms that the Taxpayer's sales of partnership interests should be sourced under ILCS 5/304(a)(3)(C-5)(iii)(a).

Executive Summary

Illinois Statute governs when other items of income from intangible personal property should be considered a sale within the state. ILCS 5/304(a)(3)(C-5)(iii)(b) provides that the location of the income-producing activity should be used in determining when such an item of income should be included in the sales factor numerator. However, if the taxpayer is a dealer in the item of intangible personal property within Illinois' modified meaning of Section 475 of the Internal Revenue Code, then ILCS 5/304(a)(3)(C-5)(iii)(a) requires a taxpayer to utilize a customer-based sourcing approach. For federal income tax purposes, the Taxpayer is not a dealer under IRC Section 475 because the sale of the partnership interests in the COMPANY 1 is not a "security" under IRC Section 475(c)(2). However, for Illinois income tax purposes, the state replaced the word "security" with "intangible personal property." While the sale of the COMPANY 1 is not a "security" for federal tax purposes, it is a sale of "intangible personal property" for purposes of Illinois' statutory sourcing provision. Additionally, as detailed in the below analysis, the Taxpayer regularly sells partnership interests to customers in the ordinary course of its business. As a result, for Illinois purposes, the Taxpayer is a dealer in an item of intangible personal property within the meaning of "dealer in securities" under IRC Section 475(c)(1).

Therefore, based on our analysis of IRC Section 475(c)(1) for purposes of Illinois' sourcing of income from intangible personal property and the Department's administrative guidance regarding ILCS 5/304(a)(3)(C-5)(iii)(a), the Taxpayer's sales of partnership interests should be sourced under the customer-based sourcing methodology required under ILCS 5/304(a)(3)(C-5)(iii)(a). We are requesting the Illinois Department of Revenue confirm our understanding of the application of ILCS 5/304(a)(3)(C-5)(iii)(a) to Taxpayer's fact pattern.

Facts

Organization and Activities

COMPANY ("the COMPANY"), a STATE organized limited liability company, has been a regarded partnership for U.S. federal income tax purposes since 20XX. Its

current owners are COMPANY 2 owning #, COMPANY 3 owning # percent, COMPANY 4 owning # percent, COMPANY 5 owning # percent and COMPANY 6 owning just under # percent. The Taxpayer, along with its affiliated companies, is CONTINENT's largest independent wind power generation company. It has fully developed and placed into service # wind farms across the COUNTRY, COUNTRY 1, and CONTINENT 1. Specifically, the Taxpayer develops, owns, operates, maintains, and sells these large-scale, capital intensive, renewable energy projects.

Due to the capital intensive nature of developing wind farms, wind farm project companies are held in separate legal entities for both legal and financing purposes. Generally, each wind farm is held by a disregarded entity during the project's development phase. As the project construction is completed and the wind farm becomes operational, the taxpayer introduces external equity finance investors (i.e., partners) as an alternative means to traditional financing (e.g. bank loans). The equity finance investors contribute capital to a disregarded holding company that's the single member of the disregarded project entity, and the disregarded holding company becomes a federally regarded partnership.

Wind farm developers and equity finance investors sought mutual benefits in the development and operations of wind farms, which evolved into the finance structures employed today. Internal Revenue Service Ruling 2007-65 was issued to encourage the development of the wind farm industry and to provide favorable guidelines for investors and developers to finance wind farms. Revenue Ruling 2007-65 affirmed the underlying legal, finance, regulatory and tax implications of building and financing these wind projects and generally led the industry to structure them as "Flip" partnership structures. The utilization of this type of partnership structure allows the Taxpayer to monetize certain tax attributes (e.g. depreciation expense and tax credits) to achieve an investment return required by the equity investor, while simultaneously providing critical financing for the project and Taxpayer. The equity finance investor is allocated a certain percentage (generally # percent) of taxable income/losses and credits until the investor has achieved a defined after-tax internal rate of return (the "Flip Point"). The Taxpayer is generally allocated 1 percent of taxable income/losses, and cash. Although the Flip Point may occur sooner, it is expected that the Flip Point will not occur until after the end of year 10 of the project. When the partnership reaches the Flip Point, the allocations flip, and the Taxpayer is allocated the majority of the partnership's activity.

During the life of the partnership, the Taxpayer manages, maintains, and controls the project company; the equity finance investors own a passive interest in the partnership. As the project company partnership matures, the Taxpayer will either (1) continue to own and operate the project company; or (2) the Taxpayer and /or equity finance investor purposefully (i.e. actively solicit to) dispose of significant portions of their interests in the project company partnership to third parties and large, generally publicly traded "Yield Companies." The sale to third party investors

and Yield Companies serves the market's demand for the Taxpayer's high quality, valuable assets with a track record of operational excellence. In instances where the Taxpayer sells partnership interests, it may either maintain some portion of ownership and operation of the project company, or will fully divest of its interest in the partnership. Under either scenario, the income and profit from the partnership interest sale transactions are used to pay down existing debt, and to a larger extent, used to finance the Taxpayer's next development projects.

Given the life cycle of these projects, the Taxpayer at any given point holds various projects through disregarded single member limited liability companies, or as a partner in federally regarded partnerships. During the 2015 tax year, the Taxpayer held 21 federally regarded domestic (U.S.) partnership interests, and 25 federally regarded foreign (non-U.S.) partnership interests in operational wind project companies, as well as numerous projects under development through SMLLCs. Given the large scale nature of these projects (e.g. a single wind farm project can cost several hundreds of millions of dollars), it can take several years from development company ground breaking, to project company commercial operation, to the point when equity investors are introduced, and ultimately to the point where the project company is sold to a Yield Company, or the partnership flips. As a result of market conditions and performance of the wind farms, partnership interests have historically been sold prior to project company partnerships reaching the Flip Point. The Taxpayer has yet to reach a Flip Point with regards to any project company.

Taxpayer's Operations

On an annual basis, the Taxpayer generates gross income from several activities that are core to its business. The majority of the Taxpayer's gross income is generated from the following: (1) development fees; (2) sales of partnership interests; (3) sales of wind farms under a build/transfer agreement; (4) distributive shares of partnership income from the Taxpayer's interest in underlying project company partnerships; (5) income from wholly-owned wind farms; and (6) interest income generated from loans to project companies. Below is a detailed description of each activity of the Taxpayer.

Development fees – A fee paid to the Taxpayer for development services, which include negotiating construction financing terms, negotiating the project and any necessary operational documents, obtaining permits, and performing other services relating to the project. The development fee is earned upon completion of the development services, which occurs upon commercial operation of the project company facilities. Development fees vary year to year depending on when projects are completed and operational, but have historically contributed substantial amounts to gross and taxable income.

Sales of Partnership Interests – As described above, the Taxpayer will actively solicit buyers (e.g. Yield Companies) for wind farm project companies. The Taxpayer has sold # partnership interests since 20XX (approximately # per year

including the current transaction; # per year excluding this transaction) which has consistently contributed substantial amounts to gross and taxable income.

Build/Transfers – Under build/transfer agreements, the Taxpayer will contract with customers to build a wind farm. Upon completion of the wind farm, the assets are sold (transferred) to the customer. The Taxpayer will generally contract for several build transfer projects throughout a tax year, which contributes substantially to gross and taxable income.

Distributive Share of Partnership Income/Loss – As a project company becomes operational, electricity produced by the project company is sold to a regional power authority under a multi-decade master power and sale agreement. During the first several years of a project company, the project company partnership will generate substantial losses as depreciation expense on wind farm turbines exceeds the taxable income generated from the sale of electricity. It is generally not until after the assets have been fully depreciated (five plus years) that the partnership will generate taxable income that is distributed to the Taxpayer. Note, the Taxpayer's allocation of partnership income/loss is generally small (e.g. 1 percent) until the partnership flip occurs.

Income from Wholly Owned Wind Farms – The Taxpayer generates taxable income/loss from two wholly owned operational wind farms.

Interest Income – In addition to other methods of financing project company construction (e.g. traditional bank loans, equity finance investors), the Taxpayer will lend project companies capital that generates interest income.

Transaction in Question

On MONTH 15, 20XX, COMPANY 7, a single member LLC disregarded subsidiary of the Taxpayer, executed a purchase and sale agreement, whereby it sold # percent of its partnership interests in COMPANY 8, COMPANY 9, COMPANY 10 and COMPANY 11 (collectively, the "COMPANY 1"). The interests were purchased by three limited liability companies owned in whole or in part by COMPANY 12. – COMPANY 13, COMPANY 14, and COMPANY 15. (As the structure of the purchaser's group is not relevant for purposes of this ruling request, the COMPANY 12 group will be treated generally as a single entity and referred to collectively as "COMPANY 16".) For federal income tax purposes, the sale of the partnership interests in the COMPANY 1 by the Taxpayer is treated as the sale of intangible assets.

Additional Factual Representations

1. The Taxpayer is a multi-state taxpayer with the right to apportion base income under ILCS 5/304.
2. The Taxpayer will elect to treat all income as "business income" pursuant to ILCS 5/1501(a)(1). As a result, it is represented that the sale of the

COMPANY 1 results in apportionable business income, and as such, the gain on the sale of the partnership interests is not subject to allocation under ILCS 5/303 (nonbusiness income).
3. The Taxpayer is not a dealer for federal income tax purposes because the sale of the COMPANY 1 (non-widely held, non-publicly traded partnerships) is not treated as the sale of a “security” as defined under IRC Section 475(c)(2).
4. The purchase price paid by COMPANY 16 for the COMPANY 1 significantly exceeded the costs paid by the Taxpayer for the development of the projects.
5. The Taxpayer has sold ## partnership interests (in addition to this transaction) since 20XX, in a fact pattern consistent to that described in the below analysis.

RELEVANT AUTHORITY AND ANALYSIS

To determine the sales factor sourcing rule applicable for the sale of the COMPANY 1, we will first review the State’s general allocation and apportionment provisions, and then will specifically analyze the Taxpayer’s status as a dealer in an item of intangible personal property (i.e., partnership interests).
ILCS 5/305(c) states:

Allocation and apportionment of base income by partnerships. Base income of a partnership shall be allocated or apportioned to this State pursuant to Article 3, in the same manner as it is allocated or apportioned for any other nonresident.

ILCS 5/304(a) provides that:

For tax years ending on or after December 31, 1998, and except as otherwise provided by this Section, persons other than residents who derive business income from this State and one or more other states shall compute their apportionment factor by weighting their property, payroll, and sales factors as provided in subsection (h) of this Section.

Subsection (h)(3) of ILCS 5/304 states that for tax years ending on or after December 31, 2000, only the sales factor is used to apportion business income. As such, the Taxpayer is required to apportion its business income in tax year 2015 by use of the sales factor, as calculated under ILCS 5/304.
ILCS 5/304(a)(3)(A) describes the sales factor:

The sales factor is a fraction, the numerator of which is the total sales of the person in this State during the taxable year, and the denominator of which is the total sales of the person everywhere during the taxable year.

ILCS 5/1501(a)(21) defines “sales” as all gross receipts of the taxpayer not allocated under Sections 301 (relating to residents and income not subject to

apportionment under Section 304), 302 (relating to compensation) and 303 (relating to nonbusiness income).
Illinois Administrative Code 100.3370(a)(1) provides additional guidance on what constitutes "sales":

IITA Section 1501(a)(22) defines the term "sales" to mean all gross receipts of the person not allocated under IITA Sections 301, 302, and 303. Thus, for the purposes of the sales factor of the apportionment formula for each trade or business of the person, the term "sales" means all gross receipts derived by the person from transactions and activity in the regular course of such trade or business.

The sale of the Taxpayer's partnership interests in the COMPANY 1 are sales under ILCS 5/1501(a)(21) as the sales are derived by the Taxpayer from transactions and activity in the regular course of its trade or business and are not specifically allocated under IITA Sections 301, 302, or 303. Accordingly, the sale of the partnership interests should receive representation in the Taxpayer's sales factor.
For purposes of determining the sales factor denominator and numerator, Illinois Administrative Code 100.3370(b) and (c) provides for the following:
(b) Denominator. The denominator of the sales factor shall include the total gross receipts derived by the person from transactions and activity in the regular course of its trade or business, except receipts excluded under 86 Ill. Adm. Code 100.3380(b).

(c) Numerator. The numerator of the sales factor shall include the gross receipts attributable to this State and derived by the person from transactions and activity in the regular course of its trade or business. All interest income, service charges, carrying charges, or time-price differential charges incidental to such gross receipts shall be included regardless of the place where the accounting records are maintained or the location of the contract or other evidence of indebtedness.

ILCS 5/304(a)(3)(C-5)(iii) determines how the sale of a partnership interest (an intangible asset) is attributed to Illinois (i.e., when is it included in the numerator of the sales factor):
(C-5) For taxable years ending on or after December 31, 2008, sales, other than sales governed by paragraphs (B) [sales of tangible personal property], (B-1) [patents, copyrights, trademarks, and similar items of intangible personal property], (B-2) [patents, copyrights, trademarks, and similar items of intangible personal property], B-5 [telecommunications services], and (B-7) [broadcasting services], are in this Sate if any of the following criteria are met:

(iii) In the case of interest, net gains (but not less than zero) and other items of income from intangible personal property, the sale is in this State if:

(a) In the case of a taxpayer who is a dealer in the item of intangible personal property within the meaning of Section 475 of the Internal Revenue Code, the income or gain is received from a customer in this State. For purposes of this subparagraph, a customer is in this State if the customer is an individual, trust or estate who is a resident of this State and, for all other customers, if the customer's commercial domicile is in this State. Unless the dealer has actual knowledge of the residence or commercial domicile of a customer during a taxable year, the customer shall be deemed to be a customer in this State if the billing address of the customer, as shown in the records of the dealer, is in this State; or

(b) In all other cases, if the income-producing activity of the taxpayer is performed in this State or, if the income-producing activity of the taxpayer is performed both within and without this State, if a greater proportion of the income-producing activity of the taxpayer is performed within this State than in any other state, based on performance costs.

ILCS 5/304(a)(3)(C-5)(iii) clarifies that only the net gains (not gross receipts) from the sale of intangible personal property (e.g., partnership interests) are to be included in the sales factor, and additionally, provides for two avenues for how to source these types of sales. If the Taxpayer is a "dealer in the item of intangible personal property within the meaning of Section 475 of the Internal Revenue Code", then the Taxpayer sources the sale of the partnership interests based on the location of the customer. If the Taxpayer is not a dealer in the item of intangible personal property within the meaning of Section 475 of the Internal Revenue Code, then the Taxpayer sources the sale of the partnership interests based on where the taxpayer's cost of performance related to the income-producing activity takes place.
IRC Section 475 does not refer to "intangible personal property" but instead applies only to dealers in "securities." IRC Section 475(c)(1) defines the term "dealer in securities" as a taxpayer that:

(A) regularly purchases securities from or sells securities to customers in the ordinary course of a trade or business; or
(B) regularly offers to enter into, assume, offset, assign or otherwise terminate positions in securities with customers in the ordinary course of a trade or business.

IRC Section 475(c)(2) defines "securities" as:

(A) shares of stock in a corporation;
(B) partnership or beneficial ownership interest in a *widely held or publicly traded partnership* or trust; *(emphasis added)*
(C) note, bond, debenture, or other evidence of indebtedness'
(D) interest rate, currency or equity notional principal contract;
(E) evidence of an interest in, or a derivative financial instrument in, any security described in subparagraph (A), (B), (C), or (D), or any currency,

including any option, forward contract, short position, and any similar financial instrument in such a security or currency; and

(F) position which (i) is not a security described in subparagraph (A), (B), (C), (D), or (E), (ii) is a hedge with respect to such a security, and (iii) is clearly identified in the dealer's records as being described in this subparagraph before the close of the day on which it was acquired or entered into (or such other time as the Secretary may by regulations prescribe).

The Taxpayer is not a "dealer in securities" as the COMPANY 1 are not "securities" under IRC Section 475(c)(2) because they are neither widely held nor publicly traded. However, it's important to note that ILCS 5/304(a)(3)(C-5)(iii)(a) does not simply state "dealer in securities", but rather "dealer in the item of intangible personal property within the meaning of Section 475 of the Internal Revenue Code." Based on the plain language of the statute, it appears it was the intent of the Illinois legislature to modify IRC Section 475 for purposes of the State's sourcing statute under ILCS 5/304(a)(3)(C-5)(iii)(a). The modification ("dealer in the item of intangible personal property") provides for a broader definition of the types of intangible sales the State seeks to source, rather than limiting the sourcing provision to the intangible personal property type of "securities" defined under IRC Section 475(c)(2).

Based on the above analysis, if the Taxpayer would be a dealer in the item of intangible personal property under Illinois' modified meaning of IRC Section 475(c)(1), then the Taxpayer sources its sales of intangible personal property based on the location of its customer. Said another way, if the Taxpayer is a dealer within the Illinois modified meaning of IRC Section 475(c)(1) with regards to the sale of partnership interests, then the Taxpayer would source the partnership interest sales based on customer location. This logic and analysis are not inconsistent with the state's guidance in General Information Letter IT 08-0028-GIL, which stated in pertinent part:

For this purpose, a taxpayer is a dealer with respect to an item of intangible personal property if the taxpayer is actually a dealer with respect to the item under IRC Section 475, *or would be a dealer with respect to the item under IRC Section 475 if the item were a security as defined in IRC Section 475(c)(2).* This is consistent with the purpose of IITA Section 304(a)(3)(C-5)(iii) to create a dichotomy between taxpayers that *are in the business of selling the particular item of intangible property and taxpayers not in such business. The purpose of the Section is not to create a customer-based sourcing rule only for dealers in securities, while leaving other taxpayers, including those whose business it is to sell the particular intangible item, to apply the income-producing activity test. Taxpayers in the business of selling a certain intangible item assign gross receipts based on the location of their customers*, while taxpayers not in the business of selling such item assign gross receipts based on the income-producing activity. [*Emphasis added*].

The taxpayer requesting the above general information letter sold online memberships (self-created intangible assets that were not "securities" under IRC

Section 475(c)(2)) in the ordinary course of its trade or business. The Department's ruling concluded that the taxpayer "must assign its gross receipts from sales of membership interests under IITA Section 304(a)(3)(C-5)(iii)(a) because the taxpayer is in the trade or business of selling membership interests". Based on the above, the salient issue for purposes of the sourcing question under ILCS 5/304(a)(3)(C-5)(iii)(a) is to determine whether the taxpayer either:

1. regularly purchases partnership interests from or sells partnership interests to customers in the ordinary course of a trade or business; or
2. regularly offers to enter into, assume, offset, assign or otherwise terminate positions in partnership interests with customers in the ordinary course of a trade or business.

In the context of the GIL cited above and interpreting the conclusion contained therein, if the answer is "yes" to either one of the above, then the Taxpayer is a "dealer in the item of intangible property" and is required to utilize customer based sourcing.

Based on the definition of dealer under IRC Section 475(c)(1) within the context of Illinois' sourcing provisions (i.e., sales of intangible assets, not just those defined within IRC Section 475(c)(2)), the relevant section on which to focus our attention is whether the Taxpayer "regularly" purchases or sells partnership interests to "customers" in the ordinary course of a trade or business. It can be difficult to separate the concepts of "regular" and "customer" for purposes of IRC Section 475. Using a merchant analogy, administrative and judicial precedent have concluded a taxpayer had customers, and was therefore a dealer (under IRC Section 475). The taxpayer's profit margin resulted from purchasing an item in one market, wholesale, and then selling the item in another market, retail, and earning a profit from the difference. In this sense, the taxpayer would be a "market maker". Whether a taxpayer "regularly" does so requires that we look at the taxpayer's business model. The below analysis first focuses on the federal interpretation of "customer" under IRC Section 475, and then focuses on what constitutes "regularly".

COMPANY 16 – the "Customer"

IRC Section 475 does not define the term "customer". In Chief Couns. Adv. 2012-38-025 (Sept. 21, 2012), the Office of Chief Counsel specifically addressed the determination of what constitutes a "customer", stating the following:

Section 475 does not define who is a customer, but we can look at case law prior to the enactment of section 475 to help in making that determination. In determining whether a taxpayer has customers, the courts have looked at how a taxpayer is compensated. The courts in finding dealer status outside of section 475 have looked to whether a taxpayer is paid for its services as an intermediary – as a market-maker…We need to see whether Taxpayer was getting paid for making a market (dealer) and not profiting from a rise in values of the underlying assets during the interval of time between a purchase and resale (investor or trader). Several pre-section 475 cases have used a merchant analogy to distinguish dealers from traders. Dealers, like merchants, sell to customers and purchase the securities with the expectation of selling at a profit. This profit is not

because of a rise in value during the period of time between the purchase and sale, but because they hope to find a market of buyers who will purchase from them at a price in excess of their cost. This excess or mark-up represents remuneration for acting as a middle man, bringing together buyer and seller. See Kemon v. Commissioner, 16 T.C. 1026, 1031-1033.

In the instant case, the Taxpayer sold partnership interests to a Yield Company – COMPANY 12. and its subsidiaries (i.e., COMPANY 16). Per COMPANY 16's 10-K annual report filed with the U.S. Securities and Exchange Commission, the company describes itself as follows:

We are a dividend growth-oriented company formed to own and operate contracted clean power generation assets acquired from COMPANY 17. and its consolidated subsidiaries, or "COMPANY 17," and third parties. Our business objective is to acquire assets with high-quality contracted cash flows, primarily from owning solar and wind generation assets serving utility, commercial and residential customers. Over time, we intend to acquire other clean power generation assets, including natural gas and hydro-electricity facilities, as well as hybrid energy solutions that enable us to provide contracted power on a 24/7 basis. We believe the renewable power generation segment is growing more rapidly than other power generation segments due in part to the emergence in various energy markets of "grid parity," which is the point at which renewable energy sources can generate electricity at a cost equal to or lower than prevailing electricity prices. We expect retail electricity prices to continue to rise due to the increasing cost of producing electricity from fossil fuels caused by required investments in generation facilities and transmission and distribution infrastructure and increasing regulatory costs, among other factors. Our portfolio consists of solar and wind projects located in the CONTINENT, COUNTRY 1, and the COUNTRY 2 and COUNTRY 3 with an aggregate nameplate capacity of 1,507.3 MW as of MONTH 20, 20XX.

Per the above, COMPANY 16 is in the business of owning and operating alternative energy generation assets that produce steady cash flows, in a sector poised for growth. COMPANY 16's business model requires that they find the best possible assets and operations teams in a highly technical and capital intensive space. Suffice it to say, COMPANY 16 is not in the business of building or developing these types of assets, they are in the business of acquiring high quality assets, from highly reputable developers, that secure cash flows for their investors. The above description of COMPANY 16 illustrates that the advent of alternative energy technologies, and the companies that develop them, has created Yield Companies, like COMPANY 16, that have subsequently created a demand for the Taxpayer's product – a high quality product developed and operated by a highly skilled management team and group of engineers, with stable contracted cash flows previously negotiated with regional power authorities. These companies are not in the business to simply purchase wind farm assets (hence why these transactions are not simply structured as asset sales), but rather to purchase the entire platform (an entity that's comprised of assets, negotiated electricity purchase/sale agreements, and operations). It is this relatively recent market

appetite that has created a demand for the Taxpayer's partnership interests over the past six years. Overall, this relationship is not dissimilar to that of airplane manufacturers, who are not in the business of running an airline, but who are in the business of developing, selling, and maintaining aircraft to be used in an airline's (their customers') publicly traded business.

Under the analysis provided in the Chief Counsel Advice Memorandum, the Taxpayer is acting in the capacity of a market-maker in that the Taxpayer is profiting from the value they created from the development of the wind farm projects, creating an effective operating platform, securing long-term negotiated power contracts, and bringing to market (unsolicited) that complete package (a legal entity; a partnership), which is available for sale to COMPANY 16. The Taxpayer's profit was not derived merely from a rise in the underlying value of the partnership interests, as evidenced by the purchase price that was negotiated at a point substantially in excess of the costs of the projects. In addition, the Taxpayer holds itself out to the public as a developer of these types of projects (i.e., seller; a market leader in development and seller of build/transfer projects), and COMPANY 16 (i.e., customer) holds itself out to the public (as evidenced by its Form 10-K) as in the business of acquiring and operating assets produced by the likes of the Taxpayer. Therefore, based on the above analysis and Taxpayer representation that its historical sales of partnership interests were executed within a consistent fact pattern, the Taxpayer sold partnership interests to customers in the ordinary course of its trade or business.

Given that, our next, and final question to address is whether the Taxpayer "regularly" sells partnership interests. In other words, to analyze whether the Taxpayer sells partnership interests pursuant to some practice or order with historical frequency.

Sales of Partnership Interests – "regularly" occurs in ordinary course of Taxpayer's business

IRC Section 475 does not expressly define the term "regularly", and the exact term "regularly" does not appear to be expressly defined elsewhere in the Code. In the absence of a specific definition in the Code or the Regulations, and absent evidence that Congress intended any special or peculiar meaning for the word, it is proper to assume that Congress intended the word to be used "in its generally accepted or 'dictionary' sense." According to Merriam-Webster's online dictionary, "regularly" is an adverb formed from the word "regular", which has the following pertinent meanings: (1) orderly, methodical (regular habit); recurring, attending, or functioning at fixed, uniform, or normal intervals; (2) constituted, conducted, scheduled, or done in conformity with established or prescribed usage, rules, or discipline; normal, standard (including thinking or behaving in an acceptable, normal manner). The term "regularly" has been used to describe a matter of usual practice. Synonyms of the term include routinely, systematically, usually, habitually, ordinarily. Antonyms include uncommonly, unusually, and erratically.

Based on the facts presented, the Taxpayer's recurring activities surrounding the sales of partnership interests may be fairly described as normal, usual, systematic, and a methodical practice whereby the Taxpayer's conduct is pursuant to the normal and ordinary course of its business. The activities surrounding the sales

of the partnership interests is not uncommon, unusual, or consummated erratically, but rather through deliberate action by the Taxpayer to serve market demand (i.e., profit), which allows it to redeploy transaction proceeds for future capital intensive development projects. In other words, the Taxpayer's recurring sales of partnership interests appear to be "regular". In order to determine whether the Taxpayer's partnership interest sales rise to the level of frequency to be described as "regularly" occurring within the meaning of IRC Section 475, requires that one look at the Taxpayer's business model, or how it has historically generated gross/taxable income.

The Taxpayer has consistently generated significant amounts of gross and taxable income from development fees, sales of partnership interests, and build/transfer projects. Each stream of income has historically been core to the Taxpayer's normal course of business. Excluding the sale of partnership interests in question, the Taxpayer has sold, on average, one partnership interest per year since 20XX. Considering the nature of the Taxpayer's business, project cycles, timeline for projects that can take several years to complete, and the number and magnitude of sales over that period of time, it is our understanding that the Taxpayer's recurring partnership interest sales activities occur with such a frequency and continuity that these activities are considered to occur "regularly" in the normal course of its business. Accordingly, we believe the Taxpayer regularly sells partnership interests to customers in the ordinary course of its trade or business, and as such, the related gains should be sourced based on the customer's location pursuant to ILCS 5/304(a)(3)(C-5)(iii)(a).

CONCLUSION

Based on the foregoing facts, representations, and analysis, the Taxpayer's sales of partnership interests is business income subject to apportionment by use of a single sales factor. The sales factor will include the net gains from the sale of the partnership interests, and the net gains should be sourced (i.e., included in the numerator of the sales factor) based on the location of Taxpayer's customer. This determination is based on the foregoing analysis that the Taxpayer is a dealer in the item of intangible personal property (i.e., the partnership interests) within Illinois' modified meaning of Section 475 of the Internal Revenue Code, for sole purposes of Illinois' sales factor sourcing statute under ILCS 5/304(a)(3)(C-5)(iii)(a).

RULING

Section 304(a)(3)(C-5) of the Illinois Income Tax Act ("IITA," 35 ILCS 5/304(a)(3)(C-5)) provides, for purposes of computing the sales factor, in part:

> For taxable years ending on or after December 31, 2008, sales, other than sales governed by paragraphs (B), (B-1), (B-2), (B-5), and (B-7), are in this State if any of the following criteria are met:

…

(iii) In the case of interest, net gains (but not less than zero) and other items of income from intangible personal property, the sale is in this State if

(a) in the case of a taxpayer who is a dealer in the item of intangible personal property within the meaning of Section 475 of the Internal Revenue Code, the income or gain is received from a customer in this State. For purposes of this subparagraph, a customer is in this State if the customer is an individual, trust or estate who is a resident of this State and, for all other customers, if the customer's commercial domicile is in this State. Unless the dealer has actual knowledge of the residence or commercial domicile of a customer during a taxable year, the customer shall be deemed to be a customer in this State if the billing address of the customer, as shown in the records of the dealer, is in this State; or

(b) in all other cases, if the income-producing activity of the taxpayer is performed in this State or, if the income-producing activity of the taxpayer is performed both within and without this State, if a greater proportion of the income-producing activity of the taxpayer is performed within this State than any other state, based on performance costs.

Under this provision, whether gross receipts from sales of intangible personal property are assigned to Illinois for sales factor purposes depends on whether the taxpayer is a dealer in the item of intangible personal property within the meaning of Section 475 of the Internal Revenue Code (IRC). If the taxpayer is a dealer within the meaning of IRC Section 475, the gross receipts are assigned to Illinois if the customer is in Illinois. If the taxpayer is not a dealer within the meaning of IRC Section 475, the gross receipts are assigned to Illinois if the income-producing activity is in Illinois. For purposes of this rule, a taxpayer is a dealer with respect to an item of intangible personal property if the taxpayer is a dealer with respect to the item under IRC Section 475(c)(1), or would be a dealer with respect to the item under IRC Section 475(c)(1) if the item were a security for purposes of IRC Section 475. IRC Section 475(c)(1) defines the term "dealer in securities" as a taxpayer that:

(A) regularly purchases securities from or sells securities to customers in the ordinary course of a trade or business; or

(B) regularly offers to enter into, assume, offset, assign or otherwise terminate positions in securities with customers in the ordinary course of a trade or business.

Under IRC Section 475(a), a dealer in securities must apply the mark-to-market method of accounting with respect to any security that is inventory in the hands of the dealer, and to any security which is not inventory and which is held at the close of the taxable year. Under IRC Section 475(b), the mark-to-market method of accounting does not apply to any security held for investment, certain securities acquired (including originated) by the

taxpayer in the ordinary course of business which are not held for sale, and any security which is a hedge with respect to a security not subject to mark-to-market accounting under IRC Section 475(a). Treasury Regulations §1.475(b)-1(a) states that a security is held for investment, or not held for sale, within the meaning of Section 475(b), if it is "not held by the taxpayer primarily for sale to customers in the ordinary course of the taxpayer's trade or business."

In *Kemon v. C.I.R.*, 16 T.C. 1026 (1951), the Tax Court explained that a "merchant analogy" is generally employed to determine whether a sale of securities is a sale "to customers":

> In determining whether a seller of securities sells to 'customers,' the merchant analogy has been employed. [citations omitted] Those who sell 'to customers' are comparable to a merchant in that they purchase their stock in trade, in this case securities, with the expectation of reselling at a profit, not because of a rise in value during the interval of time between purchase and resale, but merely because they have or hope to find a market of buyers who will purchase from them at a price in excess of their cost. This excess or mark-up represents remuneration for their labors as a middle man bringing together buyer and seller, and performing the usual services of retailer or wholesaler of goods. [citations omitted] Such sellers are known as dealers.

In the instant case, you have represented that the Taxpayer is not a dealer under IRC Section 475 because the partnership interests in the COMPANY 1 are not "securities" as that term is defined in IRC Section 475(c)(2). However, as indicated above, IITA Section 304(a)(3)(C-5)(iii)(a) applies if either the taxpayer is a dealer with respect to the item under IRC Section 475(c)(1), or would be a dealer with respect to the item under IRC Section 475(c)(1) if the item were a security for purposes of IRC Section 475. Therefore, if Taxpayer would be considered a dealer with respect to the COMPANY 1, assuming that the partnership interests is a security under IRC Section 475, then IITA Section 304(a)(3)(C-5)(iii)(a) applies to gain from the sale of those entities. Taxpayer will be considered a dealer with respect to the COMPANY 1 if the partnership interest is held primarily for sale to customers in the ordinary course of the Taxpayer's trade or business.

You represent that the Taxpayer, a STATE limited liability company, has been treated as a partnership for federal income tax purposes since 20XX. You represent that the Taxpayer, along with its affiliated companies, is CONTINENT's largest independent wind power generation company, having fully developed and placed into service XX wind farms across the COUNTRY, COUNTRY 1, and CONTINENT 1. You represent that during the 20XX tax year, the Taxpayer held ## COUNTRY partnership interests, and ## foreign partnership interests, in operational wind project companies. You represent that the Taxpayer has sold ## partnership interests since 20XX, including ## partnership interests following a fact pattern consistent to the sale in the instant case. You represent that substantial amounts of gross and taxable income are derived from development fees related to wind farm projects, and from the sale of partnership interests in wind farm projects. Finally, you represent that, historically, the Taxpayer has sold partnership

interests in wind farm projects before those projects have reached the Flip Point, and that the Taxpayer has yet to reach the Flip Point with regards to any wind farm partnership.

Based on these representations, the Taxpayer is properly considered a dealer with respect to the COMPANY 1. The Taxpayer is in the business of constructing and developing wind farms. The wind farm assets and operations are usually held in LLCs, which are taxed as partnerships. The Taxpayer's business practice is to sell the partnership interests upon the wind farm project becoming operational and as market conditions will allow. Taxpayer does not hold the partnership interests for the purpose of investment or for the purpose of generating distributive share income from the continuing operation of the wind farm. In that regard, the Taxpayer has averaged almost two sales of wind farm partnerships per year since 20XX, without retaining a single partnership past the Flip Point, and using the proceeds from such sales primarily to finance subsequent wind farm development projects, and thereby repeat its business cycle. Taxpayer's profit, namely, gain on the sale of partnership interests, is not attributable to a rise in market value during the period between purchase and sale. Rather, the Taxpayer's profit is attributable to value added through the Taxpayer's efforts to construct and develop wind farm projects. In a sense, the Taxpayer originates partnership interests through its manufacture of wind farms, in order to sell those interests in the wholesale and retail investment markets, such as to Yield Companies. In short, the Taxpayer is performing a merchant function with respect to wind farm partnerships.

Accordingly, the Taxpayer is a dealer with respect to the COMPANY 1. As a dealer, its gain from the sale of partnership interests is sourced for sales factor purposes under the rule at IITA Section 304(a)(3)(C-5)(iii)(a) based on the location of its customers.

This ruling shall bind the Department for the tax year ending MONTH 31, 20XX. 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 and incorporated in this ruling are correct and complete. 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.

Sincerely,

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