

Whether taxpayer has nexus with Illinois is extremely fact-specific. Department does not issue rulings regarding nexus with the State

January 9, 2017

Re: Illinois income tax

Dear Xxxxx:

This is in response to your letter received November 22, 2016, in which you request information regarding Illinois income tax. 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.

Your letter states as follows:

I am doing some research regarding private equity funds in the state of Illinois and would like to receive some reference regarding this topic.

1) When members of a private equity fund have ownership in a flow thru investment and then they ultimately decide to sell some of the units (not assets) of the LLC that have operations in the state of Illinois. Do the sellers need to apportion some of the gain/loss and therefore incur withholding in the state of Illinois even if they are not residents of the state of Illinois and their only connection to Illinois is their investment in this flow thru entity.

2) When a private equity fund pays fees to a management company and some of the members of the Limited Partnership are residents of the State of Illinois. Will the management company be subject to Nexus rules since they are only a service organization and have no physical presence in Illinois but will be subject to income tax since the state of Illinois follows market based rules or will they not be subject to income tax in the state of Illinois.

If you can please provide the reference or citations of these laws as well as your ID number that would be much appreciated.

RULING

The determination as to whether a taxpayer has nexus with Illinois is extremely fact-specific. Therefore, the Department does not issue rulings regarding whether a taxpayer has nexus with the State. For information regarding nexus, see Department of Revenue Regulations Section 100.9720 (accessible from the Department's web site). In addition, the following general information may be provided.

A nonresident is liable for Illinois income tax under Section 201 of the Illinois Income Tax Act ("IITA" 35 ILCS 5/201) if it computes "net income" as defined under IITA Section 202. IITA Section 202 defines Illinois net income as that portion of the taxpayer's "base income" as defined in

Section 203, which is allocated or apportioned to Illinois under the provisions of Article 3 of the IITA, less certain deductions.

Under Article 3 of the IITA, business income is apportioned to Illinois based on an apportionment ratio in which the numerator is the amount of the taxpayer's sales in Illinois and the denominator is the amount of the taxpayer's sales everywhere. IITA Section 304(a)(3)(C-5)(iii) allocates income from intangible property (other than patents, copyrights, trademarks, and similar items) to the numerator of the apportionment formula as follows:

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 the 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.

IITA Section 304(a)(3)(C-5)(iv) allocates sales of services to the numerator of the apportionment formula as follows:

Sales of services are in this State if the services are received in this State. For the purposes of this section, gross receipts from the performance of services provided to a corporation, partnership, or trust may only be attributed to a state where that corporation, partnership, or trust has a fixed place of business. If the state where the services are received is not readily determinable or is a state where the corporation, partnership, or trust receiving the service does not have a fixed place of business, the services shall be deemed to be received at the office of the customer from which the services were ordered in the regular course of the customer's trade or business. If the ordering office cannot be determined, the services shall be deemed to be received at the office of the customer to which the services are billed. If the taxpayer is not taxable in the state in which the services are received, the sale must be excluded from both the numerator and denominator of the sales factor. The Department shall adopt rules prescribing where specific types of service are received, including, but not limited to publishing, and utility service.

The nonbusiness income of a nonresident is allocated to Illinois pursuant to the provisions of IITA Sections 301(c)(2) and 303. IITA Section 301(c)(2) provides that any item of income or deduction that is not specifically allocated or apportioned pursuant to IITA Sections 302, 303 or 304, in the case of an individual, trust, or estate, shall not be allocated to Illinois; and in the case of a corporation or partnership, shall be allocated to Illinois only if the taxpayer had its commercial domicile in Illinois. IITA Section 303 provides allocation rules for the specific items of income set forth in that section. In the case of capital gain or loss from the sale or exchange of intangible

personal property, such gain or loss is allocated to Illinois only if the taxpayer's commercial domicile is Illinois.

IITA Section 305 provides special allocation and apportionment rules in the case of a nonresident partner with respect to the partner's distributive share of income of a partnership. Under IITA Section 305(a), a nonresident partner must include in Illinois net income the partner's distributive share of the business income of the partnership that is apportioned to Illinois in the hands of the partnership. Under IITA Section 305(b), a nonresident partner allocates to Illinois the partner's share of the nonbusiness income of the partnership as if such income was received directly by the partner. IITA Section 305(c) states that a partnership shall allocate and apportion its base income to Illinois under Article 3 in the same manner as any other nonresident. IITA Section 305(c-5) provides special rules for the allocation or apportionment of a nonresident partner's distributive share of the income of an investment partnership (as defined in IITA Section 1501(a)(11.5)).

IITA Section 709.5 requires a partnership to withhold partner-level tax with respect to a nonresident partner's distributive share. In general, a partnership must withhold tax on a nonresident partner's distributive share of the business income of the partnership apportioned to Illinois plus the nonresident partner's share of the nonbusiness income of the partnership allocated to Illinois under IITA Section 303 (other than an amount allocated to the commercial domicile of the taxpayer under IITA Section 303).

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 any further questions regarding this letter, you may contact me at (217) 782-2844.

Sincerely,

Brian L. Stocker
Associate Counsel (Income Tax)