

Sourcing self-employment income (This is a GIL.)

December 27, 2017

Re: Sourcing self-employment income

Dear Xxxxx:

This is in response to your letter received December 18, 2017, in which you requested information regarding sourcing of Illinois individual 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 ask your guidance with respect to a question concerning the 2016 Illinois income tax return that was prepared for the above captioned individuals and the proper allocation of income to the State of Illinois for compensation earned by a non-resident, self-employed individual for consulting services performed for an Illinois based company.

I have reviewed the Illinois regulations regarding sourcing of revenue (Title 86, Part 100, Section 100.3370, Section 5(iii)) and have spoken with two of your department's customer service representatives but am still not clear on the proper allocation of income to be taxed in Illinois.

The 2016 Illinois return that we prepared for the above clients included 100% of the income earned by the taxpayer for consulting services under a contract for a company headquartered in Illinois. Both customer service representatives with your agency with whom I spoke indicated that 100% of the income from that contract is taxable in Illinois for the sole reason that the headquarters of the company was in Illinois, despite the fact that my client was physically present in Illinois for only 12 days in 2016 and the and the majority of the work on the contract was done outside of Illinois.

Here are the facts of the case:

- The taxpayer is a domiciliary resident of Virginia who performs consulting services for various clients throughout the country and who receives self-employment income for those services. In most cases, the client receives a monthly retainer for services so there is not direct payment for a direct service, no hourly payment and no "per job" payment. There may be times where the taxpayer enters a state to give a speech or to make a presentation for which he is paid a specific amount but no such event occurred in 2016 in Illinois.
- The taxpayer's base of operations is his home office in Virginia. His work product consists of written documents, communicated electronically, or participation in teleconferences or other digital communications.
- In 2016, the taxpayer was physically present in Illinois for 12 days (non-consecutive) at the request of his client. The taxpayer's physical presence in Illinois for those 12 days was *de*

minimis to the overall work that he performed for the client in 2016 and incidental to the volume of his work for this client.

I ask your guidance regarding the following situations:

1. Is the entire amount of the retainer paid by an Illinois company (a company that is headquartered in Illinois) taxable as Illinois source income regardless of the number of days of physical presence in the state?
2. If the entire amount of the retainer paid by an Illinois company (a company that is headquartered in Illinois) is not fully taxable in Illinois, what is the appropriate method of allocation? E.g. Taxpayer is in Illinois 12 days for his client X during the 2016 tax year. Is the allocation of the retainer earned from this client based on 12 days/240 working days during the year? Or some other method?
3. The taxpayer has a contract with ABC Company, which is not headquartered in Illinois. As part of the contract, for which he receives a retainer, he is physically present in 10 different states during the tax year, for 2 days at a time, one of which is Illinois. How would the income from that contract be allocated—10%? Because 10% of his time was physically present in Illinois or 2 days/240 working days during the year? Or none at all?

Illinois Code Section 304(a)(2) indicates that “gross receipts for the performance of personal services performed partly within and partly without this State . . . shall be attributable to this State only if a greater portion of the services were performed in this State, based on costs of performance.” Another indicates that the “throwout” rule applies.

The taxpayer maintains that his physical presence in Illinois was incidental to the overall performance of his services as his availability to his clients at all times (via electronic means) represents the very reason for which he has the contract.

I would appreciate your guidance on these issues.

RULING

The factors you reference would be pertinent if the income constituted wages. (See IITA section 304(a)(2)(B) and Publication 130 for information on when compensation is considered received in Illinois by non-residents.) Given that the nature of the income in question constitutes business income, we look to the allocation and apportionment rules in Article 3 of the Illinois Income Tax Act.

IITA section 304(a)(3)(C-5)(iv) provides:

Sales of services are in this State if the services are received in this State. For 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.

35 ILCS 5/304(a)(3)(C-5)(iv). Based on the information provided in your letter, the services appear to be received in Illinois by a corporation, partnership or trust with a fixed place of business in Illinois. Therefore, the income from that contract would be sourced 100% to Illinois.

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 (312) 814-1722.

Sincerely,

Brian E. Fliflet
Deputy General Counsel, Income Tax