

IT-22-0006 04/15/2022 ALLOCATION - GUARANTEED PAYMENTS FROM PARTNERSHIP TO RESIDENT

Resident partners include guaranteed payments in Illinois base income.
(This is a GIL.)

April 15, 2022

Re: Illinois income tax

Dear NAME:

This is in response to your letter received March 2, 2022, 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 ("GIL"), which is designed to provide general information, is not a statement of Department policy, and is not binding on the Department. See 2 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:

Please advise regarding state tax apportionment of guaranteed payments for commission on sale of real estate.

We have partners earning a guaranteed payment (commission) for sale of real estate in various states. Does the state of Illinois handle these payments as allocable to the state the commission was earned in or apportioned based on total sales of partnership?

We have an Illinois partner who has never even been to other states we operate in who earned all his guaranteed payments by selling Illinois property and we are questioning if this should be by apportionment based on the partnership activity in various states or directly allocated to Illinois.

Thank you for your guidance.

RULING

Section 707(c) of the Internal Revenue Code ("IRC") provides for the definition of guaranteed payments:

To the extent determined without regard to the income of the partnership, payments to a partner for services or the use of capital shall be considered as made to one who is not a member of the partnership, but only for the purposes of section 61(a) (relating to gross income) and, subject to section 263, for purposes of section 162(a) (relating to trade or business expenses).

Treasury Regulation Section 1.707-1(c) further provides that:

Guaranteed payments are considered as made to one who is not a member of the partnership only for the purposes of section 61(a)(relating to gross income) and section 162(a)(relating to trade or business expenses) . . . For the purposes of other provisions of the internal revenue laws, guaranteed payments are regarded as a partner's distributive share of ordinary income. Thus, a partner who receives guaranteed payments for a period during which he is absent from work because of personal injuries or sickness is not entitled to exclude such payments from his gross income under section 105(d). Similarly, a partner who receives guaranteed payments is not regarded as an employee of the partnership for the purposes of withholding of tax at source, deferred compensation plans, etc.

The "ordinary income" of a partnership referred to in this regulation is the partnership's income excluding amounts required to be separately taken into account by the partners, such as capital gains and losses, dividends, charitable deductions, etc. See Sections 702(a) and Section 703(a) of the IRC.

Section 301 of the Illinois Income Tax Act ("IITA", 35 ILCS 5/101 et seq.) provides the general rule for allocation and apportionment of base income:

(a) Residents. All items of income or deduction which were taken into account in the computation of base income for the taxable year by a resident shall be allocated to this State.

(b) Part-year residents. All items of income or deduction which were taken into account in the computation of base income for the taxable year by a part-year resident shall, for that part of the year the part-year resident was a resident of this State, be allocated to this State and, for the remaining part of the year, be allocated to this State only to the extent provided by Section 302, 303 or 304 (relating to compensation, nonbusiness income and business income, respectively).

(c) Other persons.

(1) In general. Any item of income or deduction which was taken into account in the computation of base income for the taxable year by any person other than a resident and which is referred to in Section 302, 303 or 304 (relating to compensation, nonbusiness income and business income, respectively) shall be allocated to this State only to the extent provided by such section.

(2) Unspecified items. Any item of income or deduction which was taken into account in the computation of base income for the taxable year by any person other than a resident and which is not otherwise specifically allocated or apportioned pursuant to Section 302, 303 or 304 (including, without limitation, interest, dividends, items of income taken into account under the provisions of Sections 401 through 425 of the Internal Revenue Code, and benefit payments received by a beneficiary of a supplemental unemployment benefit trust which is referred to in Section 501(c)(17) of the Internal Revenue Code):

(A) in the case of an individual, trust, or estate, shall not be allocated to this State; and

(B) in the case of a corporation or a partnership, shall be allocated to this State if the taxpayer had its commercial domicile in this State at the time such item was paid, incurred or accrued.

Section 1501(a)(20) of the IITA defines “resident” as:

- A. An individual (i) who is in this State for other than a temporary or transitory purpose during the taxable year; or (ii) who is domiciled in this State but is absent from the State for a temporary or transitory purpose during the taxable year;
- B. The estate of a decedent who at his or her death was domiciled in this State;
- C. A trust created by the will of a decedent who at his death was domiciled in this State; and
- D. An irrevocable trust, the grantor of which was domiciled in this State at the time such trust became irrevocable. For purpose of this subparagraph, a trust shall be considered irrevocable to the extent that the grantor is not treated as the owner thereof under Sections 671 through 678 of the Internal Revenue Code.

86 Ill. Admin. Code 100.3020 provides further guidance on the IITA definition of resident.

Section 1501(a)(14) of the IITA defines “nonresident” as a person who is not a resident.

Section 305 of the IITA in relevant part provides:

(a) Allocation of partnership business income by partners other than residents. The respective shares of partners other than residents in so much of the business income of the partnership as is allocated or apportioned to this State in the possession of the partnership shall be taken into account by such partners pro rata in accordance with their respective distributive shares of such partnership income for the partnership's taxable year and allocated to this State.

(b) Allocation of partnership nonbusiness income by partners other than residents. The respective shares of partners other than residents in the items of partnership income and deduction not taken into account in computing the business income of a partnership shall be taken into account by such partners pro rata in accordance with their respective distributive shares of such partnership income for the partnership's taxable year, and allocated as if such items had been paid, incurred or accrued directly to such partners in their separate capacities.

(c) Allocation or apportionment of base income by partnership. 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.

The allocation and apportionment of base income by nonresident partners is further outlined in 86 Ill. Admin. Code 100.3500. Section 100.3500(a)(4) provides:

Except as provided in this subsection (a), all items of base income of a partner that are derived from the partnership shall be allocated or apportioned pursuant to this Section, including all items required to be separately stated to the partner under IRC section 703(a)(1), all guaranteed payments under IRC section 707(c), and all addition and subtraction modifications, but excluding items described in IRC section 707(a).

Therefore, nonresident partners apportion guaranteed payments to Illinois based on the apportionment factor of the partnership. Resident partners include the guaranteed payments in Illinois base income. You represent in your ruling request the partner in question is an Illinois resident. If you determine that the partner meets the IITA definition of "resident", then the partner would allocate the guaranteed payments to Illinois. To claim credit for any taxes paid to other states, a resident should complete and attach Schedule CR, Credit for Tax Paid to Other States, to their Form IL-1040, Individual Income Tax Return.

As stated above, this is a GIL. A GIL does not constitute a statement of Department policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department.

Sincerely,

Jennifer Uhles
Associate Counsel (Income Tax)