

Nexus issues are not generally suitable for resolution by letter ruling. (This is a GIL.)

June 14, 2022

NAME
ADDRESS

Re: Out-of-State Corporate Filing Requirements Form IL-1120

Dear NAME:

This is in response to your letter dated May 12, 2022, in which you request information regarding out-of-state corporate filing requirements for Form IL-1120. 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 Section 1200.120(b) and (c), which may be found on the Department's website at www.tax.illinois.gov.

Your letter states as follows:

I, as a Certified Public Accountant, request a private ruling letter to determine if the out-of-state corporations need to file Form IL-1120 when the corporations have sales in the state of Illinois.

Company A has started sales to IL in 2021. A warehouse was leased in IL but without employees in the state. Due to the sales tax exemption because of industry use, the company A doesn't collect sales taxes from the customer in the past. The company is in the process of registering the sales permit. The company is filing federal and state tax returns for 2021 now. My question is whether the company is required to file corporate income tax returns in IL for 2021? Should the company file the initial IL income tax return for 2022 as the registration is done in 2022?

Company B has sales in IL without warehouse or salesperson in the state. The company conducts sales through internet and delivers the products to the customers in IL. The company had registered sales permit in the state and has complied sales tax filing properly each period. My question is whether the company needs to file corporate income tax returns with sales in IL but no presence?

Company C has sales via internet in IL. The total annual sales are below \$100,000. The company has not registered to do business in IL. The questions is whether the company needs to file corporate income tax returns with merely online sales?

Public Law 86-272 (15 USC Section 381) holds that States can't impose a tax based on net income, such as the corporate income tax or franchise tax to out-of-state business entities. Both companies are selling tangible goods to the state in which case should be protected from income taxes under the Public Law 86-272.

In the meantime, the instructions of the Form IL-1120, Corporation Income and Replacement Tax Return, requires for filing returns when a corporation that:

has net income or loss as defined under the Illinois Income Tax Act (IITA); or is qualified to do business in the state of Illinois and is required to file a federal income tax return (regardless of net income or loss).

The instructions seem the tax returns are needed for the two companies because both of them have taxable income (losses) in the state. However, the interpretation is not consistent with the Public Law 86-272. Please advise.

Feel free to reach me at my email E-MAIL or mail to address ADDRESS.

Your help is highly appreciated!

RULING

Section 502(a) of the Illinois Income Tax Act ("IITA", 35 ILCS 5/101 et seq.) describes when an Illinois income tax return is required. Pursuant to Section 502(a), an Illinois income tax return is required in two situations: when a taxpayer is liable for Illinois income tax (Section 502(a)(1)) or, in the case of a corporation qualified to do business in Illinois, when the taxpayer is required to file a federal income tax return, regardless of whether such person is liable for Illinois income tax (Section 502(a)(2)).

Section 201(a) of the IITA imposes a tax measured by net income on corporations on the privilege of earning or receiving income in or as a resident of Illinois. In addition, Section 201(c) of the IITA imposes a second tax (the personal property tax replacement income tax) measured by net income on corporations on the privilege of earning or receiving income in or as a resident of Illinois.

86 Ill. Adm. Code Section 100.9720(a) provides in pertinent part:

In general, a resident of this State will always be subject to these taxes. Activity conducted in interstate commerce may establish sufficient nexus with Illinois to permit imposition of these taxes on a non-resident taxpayer, as well, when the non-resident earns or receives income in this State within the meaning of the IITA. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 97 S. Ct. 1076 (1977); *Quill v. North Dakota*, 504 U.S. 298, 112 S. Ct. 1904 (1992). However, the fact that Article 3 of the IITA requires a non-resident taxpayer to allocate or apportion income to this State does not create a presumption that the taxpayer has nexus.

Further, 86 Ill. Adm. Code Section 100.9720(e) provides:

U.S. Constitutional Jurisprudence. If not protected by U.S. or Illinois statute, an income-producing activity may, nonetheless, be protected from State taxation by principles of U.S. Constitutional jurisprudence. Controlling decisions that assert protections afforded by the Interstate Commerce Clause, the Foreign Commerce Clause and the Due Process Clause are accepted by this State as limitations on the reach of its income tax and personal property tax replacement income tax statutes. However, nothing stated in this subsection (e) shall prevent Illinois from challenging taxpayer assertions of U.S. Constitutional protection.

The Due Process Clause and the Commerce Clause of the United States Constitution limit the power of states to subject foreign corporations and other nonresidents to income tax. The Due Process Clause requires that there exist some minimum connection between a state and the person, property, or transaction the state seeks to tax. (*Quill Corp. v. N. Dakota*, 504 U.S. 298 (1992)) Similarly, the Commerce Clause requires that a state's tax be applied only to activities with a substantial nexus to the taxing state. (*Id.*)

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 86 Ill. Adm. Code Section 100.9720 (accessible from the Department's website). In addition, the following general information may be provided.

In the case of foreign corporations, Illinois may assert nexus to tax unless the corporation falls under the protection conferred by Public Law 86-272. (15 U.S.C. § 381) Public Law 86-272 precludes any state from subjecting a nondomiciliary corporation to a net income tax where such corporation's only activities within the state for the taxable year consist of solicitation activities for sales of tangible personal property.

86 Ill. Adm. Code Section 100.9720(c) provides:

- c) The scope of federal statutes limiting nexus for imposition of Illinois income and replacement taxes are described in this subsection (c):
- 1) Public Law 86-272. In 1959, Congress enacted PL 86-272 (15 USC 381-384), which prohibits states and their political subdivisions from imposing a net income tax on nonresident taxpayers who operate primarily in interstate commerce and whose activity within a state is limited. PL 86-272 provides in pertinent part:
 - A) No state or political subdivision thereof shall have the power to impose . . . a net income tax on the income derived within such state by any person from interstate commerce if the only business activities within such state by or on behalf of such person during such taxable year are either, or both of the following:
 - i) the solicitation of orders by such person, or his representative, in such state for sales of tangible personal property, which orders are sent outside the state for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the state; and
 - ii) the solicitation of orders by such person, or his representative, in such state in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in subsection (c)(1)(A)(i).
 - B) The provisions of subsection (c)(1)(A) of this Section shall not apply to the imposition of a net income tax by any State or political subdivision thereof, with respect to –
 - i) Any corporation which is incorporated under the laws of such state; or
 - ii) any individual who, under the laws of such state, is domiciled in, or a resident of, such state.

- C) For the purposes of subsection (c)(1)(A) of this Section, a person shall not be considered to have engaged in business activities within a state during any taxable year merely by reason of sales in such state, or the solicitation of orders for sales in such state, of tangible personal property on behalf of such person by one or more independent contractors whose activities on behalf of such person in such state consist solely of making sales, or soliciting orders for sales, of tangible personal property.
- D) For purposes of this subsection (c)(1) –
 - i) The term "independent contractor" means a commission agent, broker, or other independent contractor who is engaged in selling, or soliciting orders for the sale of tangible personal property for more than one principal and who holds himself out as such in the regular course of his business activities; and
 - ii) the term "representative" does not include an independent contractor.

If a nonresident taxpayer's activities exceed "mere solicitation" as set forth in subsection (c)(1)(A) of 86 Ill. Adm. Code Section 100.9720, the taxpayer obtains no immunity under Public Law 86-272 and is subject to Illinois income tax and personal property tax replacement income tax for the entire taxable year and its business income is apportioned under Section 304 of the IITA. Solicitation of orders is defined in 86 Ill. Adm. Code Section 100.9720(c)(2)(C) as speech or conduct that explicitly or implicitly invites an order and activity ancillary to invitations for an order.

Whether a corporation's conduct exceeds the "mere solicitation" standard depends upon the facts of each particular case. Specific activities that go beyond "mere solicitation" and are unprotected by Public Law 86-272 are listed within 86 Ill. Adm. Code Section 100.9720(c)(4). Additionally, 86 Ill. Adm. Code Section 100.9720(c)(5) lists specific activities that are considered to be protected activities in Illinois. As provided in 86 Ill. Adm. Code Section 100.9720(c)(3)(B), the inclusion of an activity on the listing of "protected activities" is neither a declaration nor an admission by this State that the activity must be afforded protection under Public Law 86-272.

De minimis activities, as outlined in 86 Ill. Adm. Code Section 100.9720(c)(2)(D), are those activities that when taken together, establish only a trivial additional

connection with this State. Activities that are regularly conducted within Illinois on a regular or systematic basis or pursuant to a company policy are normally not considered to be trivial. An unprotected activity that would not be de minimis if it were the only business activity of the taxpayer conducted in this State will not be de minimis merely because the taxpayer also conducts a substantial amount of protected activities within this State, nor will an unprotected activity that would be de minimis if conducted in conjunction with a substantial amount of protected activities fail to be de minimis merely because no protected activities are conducted in this State.

A nonresident is liable for Illinois income tax under Section 201 of the IITA 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, 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. Section 304(a)(3)(B) of the IITA allocates sales of tangible personal property to the numerator of the apportionment formula:

Sales of tangible personal property are in this State if:

- i) The property is delivered or shipped to a purchaser, other than the United States government, within this State regardless of the f.o.b. point or other conditions of the sale; or
- ii) The property is shipped from an office, store, warehouse, factory or other place of storage in this State and either the purchaser is the United States government or the person is not taxable in the state of the purchaser; provided, however, that premises owned or leased by a person who has independently contracted with the seller for the printing of newspapers, periodicals or books shall not be deemed to be an office, store, warehouse, factory or other place of storage for purposes of this Section. Sales of tangible personal property are not in this State if the seller and purchaser would be members of the same unitary business group but for the fact that either the seller or purchaser is a person with 80% or more of total business activity outside of the United States and the property is purchased for resale.

If the taxpayer has no sales in Illinois, then their numerator would be zero resulting in no business income and no net Illinois income. If a foreign corporation has no Illinois net income under Section 202, there is no liability for

tax under Section 201. Therefore, the requirement to file an Illinois income tax return as provided in Section 502(a)(1) of the IITA would not apply. However, this does not necessarily mean that the taxpayer will not have to file a Corporate Income Tax return.

If the taxpayer is registered to conduct business in Illinois and is required to file a federal income tax return, then under Section 502(a)(2) of the IITA, the taxpayer would be required to file an Illinois income tax return. If the taxpayer has no Illinois income tax liability and is not registered to do business in Illinois, then most likely the taxpayer would not be required to file an Illinois income tax return.

In *South Dakota v. Wayfair, Inc.* (138 S. Ct. 2080 (2018)), the United States Supreme Court ruled that states may tax remote sales based on economic as well as physical presence. For sales tax purposes, Illinois requires remote sellers to collect sales tax from Illinois customers if their amount of sales into Illinois exceed \$100,000 or 200 transactions. Illinois has not adopted a similar threshold for income tax nexus but asserts jurisdiction to tax business income to the full extent allowed under the U.S. Constitution. For sales of tangible personal property, Illinois income tax nexus is still determined in accordance with the Commerce Clause, the Due Process Clause, and Public Law 86-272.

Your letter indicates “both companies are selling tangible goods to the state” but your letter requests corporate filing guidance about the activities of three companies (Company A, Company B, and Company C).

Regarding Company A, your letter indicates that company started sales to Illinois in 2021 and leases a warehouse in this State. If the sales of Company A are sales of tangible personal property, then Section 304(a)(3)(B) of the IITA provides when those sales are to be allocated to this State. In addition, pursuant to 86 Ill. Adm. Code Section 100.9720(c)(4)(O)(iv), leasing a warehouse in Illinois, assuming the activity is not de minimis, does not constitute neither “mere solicitation” of orders nor an ancillary activity, and is not otherwise protected under Public Law 86-272. Therefore, an otherwise protected nonresident taxpayer would not be protected from Illinois income taxation under Public Law 86-272.

In regard to Company B and Company C, your letter indicates that Company B has sales in Illinois, conducted through the internet, without a warehouse or salesperson in the State, and Company C has sales in Illinois via the internet with the total annual sales below \$100,000. As indicated above, the dollar amount of sales into this State will only trigger an Illinois sales tax nexus analysis. For Illinois income tax, if the sales of Company B and Company C are sales of tangible personal property, then Section 304(a)(3)(B) of the IITA provides when those sales are to be allocated to this State. Company B and Company C would be protected from Illinois income taxation if the activities in Illinois have not exceeded those permitted under Public Law 86-272.

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)