

Addresses sourcing of employee compensation for resident who performs services in a state with no state withholding requirements. (This is a GIL).

June 6, 2023

NAME/ADDRESS

Re: Illinois income tax

Dear NAME:

This is in response to your letter dated July 15, 2020, in which you request additional 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 seeking clarification of the Illinois W-2 wage reporting requirement for an Illinois resident working in another state that does not have income tax. **I am seeking this clarification because the Illinois Department of Revenue has issued two different publications that directly contradict one another on this issue.**

To illustrate the tax situation in question, here is an example: An employee lives in Illinois but works full-time in Tennessee. **Should we report the wages on the W-2 as Illinois wages, or should we report 0.00?**

Here are the two contradictory publications from the Illinois Department of Revenue:

The current Illinois Pub.130 has the following relevant information:

*For Illinois purposes when completing Form W-2, Box 16, **enter the amount of wages paid in Illinois** or paid to an Illinois resident employed in a reciprocal state (Iowa, Kentucky, Michigan, or Wisconsin), under the rules in the section "When is compensation paid in Illinois?" even if you withheld other states' tax on some of those wages or withheld Illinois tax on a different amount. If none of the employee's wages were paid in Illinois or for an Illinois resident's employment in a non-reciprocal state, report zero in Box 16 even if you withheld Illinois income tax from those wages. Illinois residents who pay income tax to other states need this information*

in order to correctly compute the credit allowed for those taxes. Make sure that the sum of the state wages in Box 16 are equal to Box 1.

On page 4, the section, "*When is compensation paid in Illinois?*", includes:

If the employee is an Illinois resident and

- neither of the rules above apply and*
- no other state's taxes are withheld,*

then compensation is considered paid in Illinois and is subject to Illinois income tax withholding.

My understanding after reviewing these sections of Pub. 130 (and the credit formula for taxes paid to another state) is: **for compensation paid to a resident of Illinois working in a state that does not require withholding, Illinois withholding is required and wages should be considered compensation paid in Illinois and reported as Illinois W-2 wages.** When the employee calculates credit for other state taxes on the Schedule CR, the wages would be excluded from "non-Illinois" wages to determine the ratio for tax credit.

However, here is the second Illinois Department of Revenue Publication: General Information Letter IT 12-0019-GIL. **It directly contradicts Pub. 130.** The letter states 'if the resident employees ... are working 100% in Tennessee or whichever state imposes no withholding requirement, none of their wages should be reported in Form W-2, Box 16, because their wages are not "paid in this State," even though the wages would be subject to Illinois withholding'.

As you can see, we clearly need clarification from the Department of Revenue on this issue. May we rely on Pub. 130 and report the Tennessee wages as paid in Illinois, or should we disregard the publication and rely on the old information letter, IT 12-0019-GIL?

(emphasis in original).

RULING

Section 301 of the Illinois Income Tax Act ("IITA", 35 ILCS 5/301) states that 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 Illinois.

In the case of individuals, Section 203 of the IITA, 35 ILCS 5/203, defines "base income" as "an amount equal to the taxpayer's adjusted gross income for

the taxable year as modified by certain statutory addition and subtraction modifications.

Section 701 of the IITA, 35 ILCS 5/701, provides, in pertinent part, as follows:

(a) In General. Every employer maintaining an office or transacting business within this State and required under the provisions of the Internal Revenue Code to withhold a tax on:

(1) compensation paid in this State (as determined under Section 304(a)(2)(B)) to an individual; or

* * *

(b) Payment to Residents. Any payment (including compensation, but not including a payment from which withholding is required under Section 710 of this Act) to a resident by a payor maintaining an office or transacting business within this State (including any agency, officer, or employee of this State or of any political subdivision of this State) and on which withholding of tax is required under the provisions of the Internal Revenue Code shall be deemed to be compensation paid in this State by an employer to an employee for the purposes of Article 7 and Section 601(b)(1) to the extent such payment is included in the recipient's base income and not subjected to withholding by another state. Notwithstanding any other provision to the contrary, no amount shall be withheld from unemployment insurance benefit payments made to an individual pursuant to the Unemployment Insurance Act unless the individual has voluntarily elected the withholding pursuant to rules promulgated by the Director of Employment Security.

As cited in your letter, the most recent version of the Department's *Publication 130: Who is Required to Withhold Illinois Income Tax*, accurately reflects the requirements of the IITA and should be applied as written. In the example you provided, the taxpayer is an Illinois resident who works fulltime, performing services entirely within the state of Tennessee, which as of the date of this letter does not collect an income tax or tax normal wage income and therefore does not require withholding of any state income tax. In that situation, the taxpayer would fall under the requirements of Section 701(b) of the IITA, which are reflected in the guidance found on page 4 of *Publication 130*. The taxpayer is a resident of Illinois and none of their service is performed in Illinois. The taxpayer's income is not subject to withholding in Tennessee or any other state. Accordingly, pursuant to Section 701(b), those wages are deemed "compensation paid in Illinois" upon which withholding is required pursuant to Section 701(a) of the IITA, assuming the party paying the wages maintains an office or transacts business within Illinois.

If the wages are deemed compensation paid in Illinois, and are not allocated to any other state, then they should be recorded in the "State wages, tips, etc." box

on the U.S. Form W-2 Wage and Tax Statement, which for Tax Years 2020 and 2021 is designated Box 16.

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,

Michael D. Mankowski
Associate Counsel - Income Tax

cc: Daily File
Correspondence file: