

Guidance is provided on allocating certain types of compensation for past services under various scenarios and the related withholding required. (GIL)

January 4, 2024

NAME
ADDRESS

Re: Illinois Income Tax

Dear NAME:

This letter is in response to your correspondence in which you requested 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:

We are writing to request a General Information Letter under 2 Ill. Adm. Code 1200.120 in order to obtain advice on the sourcing of compensation and employer withholding requirements.

Question 1:

Facts:

- Mr. A is a full-time employee of Corp X, a company based in STATE. Mr. A is a full-year resident of STATE from tax years YEAR through YEAR. His base of operations during each of these tax years was STATE. Mr. A is a nonresident of Illinois for each of these tax years. Mr. A's work was not localized in a particular state, as he spent time working in various states during each of these tax years. During each tax year, Mr. A spent "working days" in Illinois.
- As part of his compensation package, in addition to wages, Mr. A received the following three types of incentive compensation:
 1. Cash incentive payment (bonus) - Mr. A will receive a bonus from Corp X in the amount of \$\$\$\$ in MONTH YEAR related to his work performed during YEAR. This compensation will be included in Mr. A's federal adjusted gross income (AGI) for tax year YEAR.
 2. Restricted Stock Units (RSUs) - Mr. A was granted RSUs by Corp X on MONTH DAY, YEAR related to his work performed during YEAR. These RSUs vested on MONTH DAY, YEAR, and the total value attributable to these RSUs was \$\$\$\$\$ at that time. For Federal income tax purposes, the RSU compensation is considered as earned ratably from the grant date (MONTH DAY, YEAR) to vest date (MONTH DAY, YEAR). Mr. A will exercise the RSUs during YEAR, and the total value attributable to these

RSUs will have increased to \$\$\$\$ at that time. Mr. A will include \$\$\$\$ of RSU compensation in his federal AGI for tax year YEAR.

3. Stock options - Mr. A was granted stock options by Corp X on MONTH DAY, YEAR related to his work performed during YEAR. Mr. A will exercise these stock options on MONTH DAY, YEAR, which is the vesting date. For Federal income tax purposes, the compensation from stock options is considered as earned ratably from the grant date (MONTH DAY, YEAR) to vest date (MONTH DAY, YEAR). The related compensation of \$\$\$\$ will be included in Mr. A's federal AGI for tax year YEAR.

Question: Will these three types of compensation (bonus, RSUs, stock options) be sourced to Illinois in each of the following scenarios?

Scenario 1: Mr. A spent the following number of working days in Illinois during each year:

- 2016: 35 days
- 2017: 40 days
- 2018: 45 days
- 2019: 25 days
- 2020: 50 days
- 2021: 20 days

Scenario 2: Mr. A spent the following number of working days in Illinois during each year:

- 2016: 25 days
- 2017: 20 days
- 2018: 15 days
- 2019: 10 days
- 2020: 5 days
- 2021: 40 days

Question 2:

For each type of compensation and for each scenario from Question 1, what is the requirement for the employer, Corp X, to withhold on the compensation of Mr. A if he was a full-year resident of Illinois for YEAR and YEAR but then became a full-year resident of STATE from YEAR through YEAR?

Question 3:

For each type of compensation and for each scenario from Question 1, what is the requirement for the employer, Corp X, to withhold on the compensation of Mr. A if he was a full-year resident of STATE from YEAR through YEAR but then will become a full-year resident of Illinois starting on MONTH DAY, YEAR (i.e., for the tax year during which the compensation is paid)?

Question 4:

Facts:

From Question 1, presume the following changes to the facts for Mr. A:

- Mr. A is instead employed by Corp Y, which is based in Illinois.
- Mr. A was a full-year resident of Illinois from YEAR through YEAR. Mr. A's base of operations was in Illinois during these years.
- Mr. A became a full-year domiciliary resident of STATE on MONTH DAY, YEAR and will remain a STATE resident through the end of YEAR. Mr. A's base of operations has been, and will be, in STATE during YEAR and YEAR.

Mr. A spent the following number of working days in Illinois during each year:

- 2016: 150 days
- 2017: 155 days
- 2018: 160 days
- 2019: 165 days
- 2020: 25 days
- 2021: 35 days

Question: Will these three types of compensation (bonus, RSUs, stock options) be sourced to Illinois?

Question 5:

Ms. B is a full-time employee of Corp Z, a company based in STATE. Ms. B is a full-year resident of STATE for all relevant tax years. During YEAR, as tracked by Corp Z's time and attendance system, Ms. B travelled to Illinois for work and exceeded thirty "working days" in Illinois during MONTH YEAR. Is Corp Z required to compute fourth quarter withholding on Ms. B by using a "working days" ratio that reflects all working days in Illinois (i.e., from days worked in MONTH YEAR and forward)? Or, is Corp Z only required to compute fourth quarter withholding on Ms. B by using a "working days" ratio that reflects working days in Illinois starting in MONTH YEAR through the end of the year (i.e., only including days over the 30 working days threshold)?

RULING

Section 301 of the Illinois Income Tax Act ("IITA"), 35 ILCS 5/301, provides, in pertinent part:

(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.

* * *

(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.

IITA section 302 provides:

(a) In general. All items of compensation paid in this State (as determined under Section 304(a)(2)(B)) to an individual who is a nonresident at the time of such payment and all items of deduction directly allocable thereto, shall be allocated to this State.

IITA section 304(a)(2)(B) provides that, in pertinent part, for employees other than professional athletes:

Compensation is paid in this State if:

(i) The individual's service is performed entirely within this State;

(ii) The individual's service is performed both within and without this State, but the service performed without this State is incidental to the individual's service performed within this State; or

(iii) For tax years ending prior to December 31, 2020, some of the service is performed within this State and either the base of operations, or if there is no base of operations, the place from which the service is directed or controlled is within this State, or the base of operations or the place from which the service is directed or controlled is not in any state in which some part of the service is performed, but the individual's residence is in this State. For tax years ending on or after December 31, 2020, compensation is paid in this State if some of the individual's service is performed within this State, the individual's service performed within this State is nonincidental to the individual's service performed without this State, and the individual's service is performed within this State for more than 30 working days during the tax year. The amount of compensation paid in this State shall include the portion of the individual's total compensation for services performed on behalf of his or her employer during the tax year which the number of working days spent within this State during the tax year bears to the total number of working days spent both within and without this State during the tax year. For purposes of this paragraph:

(a) The term "working day" means all days during the tax year in which the individual performs duties on behalf of his or her employer. All days in which the individual performs no duties on behalf of his or her employer (e.g., weekends, vacation days, sick days, and holidays) are not working days.

(b) A working day is spent within this State if:

(1) the individual performs service on behalf of the employer and a greater amount of time on that day is spent by the individual

performing duties on behalf of the employer within this State, without regard to time spent traveling, than is spent performing duties on behalf of the employer without this State; or

(2) the only service the individual performs on behalf of the employer on that day is traveling to a destination within this State, and the individual arrives on that day.

(c) Working days spent within this State do not include any day in which the employee is performing services in this State during a disaster period solely in response to a request made to his or her employer by the government of this State, by any political subdivision of this State, or by a person conducting business in this State to perform disaster or emergency-related services in this State

IITA section 701 provides, in pertinent part:

(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

(2) payments described in subsection (b) shall deduct and withhold from such compensation for each payroll period (as defined in Section 3401 of the Internal Revenue Code) an amount equal to the amount by which such individual's compensation exceeds the proportionate part of this withholding exemption (computed as provided in Section 702) attributable to the payroll period for which such compensation is payable multiplied by a percentage equal to the percentage tax rate for individuals provided in subsection (b) of Section 201.

(a-5) Withholding from nonresident employees. For taxable years beginning on or after January 1, 2020, for purposes of determining compensation paid in this State under paragraph (B) of item (2) of subsection (a) of Section 304:

(1) If an employer maintains a time and attendance system that tracks where employees perform services on a daily basis, then data from the time and attendance system shall be used. For purposes of this paragraph, time and attendance system means a system:

(A) in which the employee is required, on a contemporaneous basis, to record the work location for every day worked outside of the State where the employment duties are primarily performed; and

(B) that is designed to allow the employer to allocate the employee's wages for income tax purposes among all states in which the employee performs services.

(2) In all other cases, the employer shall obtain a written statement from the employee of the number of days reasonably expected to be spent performing services in this State during the taxable year. Absent the employer's actual knowledge of fraud or gross negligence by the employee in making the determination or collusion between the employer and the employee to evade tax, the certification so made by the employee and maintained in the employer's books and records shall be prima facie evidence and constitute a rebuttable presumption of the number of days spent performing services in this State.

(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.

In Question 1, you state that for Tax years YEAR through YEAR, Mr. A is a full-time employee of Corp X, a company based in STATE, and is a STATE resident with a STATE base of operations. Since Mr. A was a nonresident, pursuant to Section 302(a) of the IITA, only items of compensation paid in Illinois, as determined under Section 304(a)(2)(B), shall be allocated to this State. Under 86 Ill. Adm. Code 100.3120(c)(1), compensation paid for past services is deemed paid ratable over the previous five years, unless clearly attributable to another period. Section 100.3120(c)(1) further provides:

Compensation earned in each past year will be deemed compensation paid in Illinois if the individual's service in that year met the tests set forth in subsection (a) applicable to that year. Compensation paid for past service includes amounts paid under deferred compensation agreements where the amount of compensation is unrelated to the amount of service being currently rendered.

In Scenario 1, the bonus paid in YEAR related to work performed in YEAR. In YEAR, Mr. A spent 50 working days in Illinois, which exceeded the 30-day threshold set forth in IITA section 304(a)(2)(B)(iii). The bonus will be allocated to Illinois in proportion to the 50 working days in Illinois bears to the total number of working days in YEAR. The RSUs related to work performed during YEAR, and the stock options related to work performed during YEAR. For the years ending prior to December 31, 2020,

compensation paid in Illinois was determined using the base of operations test found in IITA section 304(a)(2)(B)(iii). As his base of operations was STATE, none of the compensation paid to Mr. A for services performed in YEAR and YEAR would be allocated to Illinois.

In Scenario 2, Mr. A spent 5 working days in Illinois in YEAR, which did not exceed the 30-day threshold. Because Mr. A was a nonresident, none of the bonus will be allocated to Illinois.

In Question 2, you state that Mr. A was a resident of Illinois in YEAR and YEAR but became a resident of STATE for YEAR through YEAR. Under IITA section 701, income tax must be withheld on compensation paid in the state to an individual. As Mr. A was an Illinois resident, the employer is required to withhold tax on all the compensation paid in YEAR and YEAR to the extent it was not subject to withholding by another state.

In Scenario 1, withholding will not be required on the compensation paid in YEAR and YEAR because the base of operations was STATE. Withholding will be required on compensation paid in YEAR but not YEAR because Mr. A exceeded the 30-day threshold in the former but not the latter. In Scenario 2, withholding will be required on compensation paid in YEAR but not YEAR because Mr. A exceeded the 30-day threshold in the former but not the latter.

In Question 3, you state that Mr. A is a resident of STATE in YEAR through YEAR and became a resident of Illinois in YEAR. The employer will be required to withhold tax on the bonus income in Scenario 1 but not Scenario 2 because the bonus income is attributable to work performed during YEAR and Mr. A exceeded the threshold in Scenario 1 but not in Scenario 2. Withholding will not be required on the RUS and stock option income as those are attributable to work performed during YEAR and YEAR while he was a resident of STATE with his base of operations in STATE.

In Question 4, you state that Mr. A is employed by Corp Y and residing in Illinois with his base of operations in Illinois for YEAR through YEAR. For YEAR and YEAR, he became a resident of STATE. The bonus paid in YEAR will not be allocated to Illinois because it relates to work performed during YEAR while he was a STATE resident and only worked 25 days in Illinois that year. The RSU and stock options income will be sourced to Illinois because they relate to work performed during YEAR and YEAR while he was a resident of Illinois with his base of operations in Illinois.

In Question 5, you state that Ms. B, a STATE resident, exceeded the 30-day threshold in MONTH YEAR. Under 86 Ill. Adm. Code 100.710, the employer will compute fourth quarter withholding using the ratio of total working days in Illinois as compared to total working days everywhere in YEAR.

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 Fliflet
Deputy General Counsel, Income Tax Policy

cc: Daily File
Correspondence file