

General Information Letter: Application of sales factor statute effective in 2008 to service provider explained.

July 16, 2008

Dear:

This is in response to your letter dated June 1, 2008 in which you request a letter ruling. The nature of your request and the information provided requires that we respond with a General Information Letter (GIL). A GIL 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 accessed from the Department's web site at www.Iltax.com. The following information relates to Illinois income tax. Your request in regard to Illinois sales tax has been forwarded to the Sales and Excise Tax Division and will be addressed by a separate ruling.

Your letter states as follows:

I am writing on behalf of my client and respectfully request a determination as to whether my client would be liable for sales tax and/or income tax in your state in the following situation:

My client (hereinafter referred to as "T" or "Taxpayer") operates a call center located outside of your state to facilitate the completion of maintenance work for a variety of national customers (hereinafter referred to as "R" or "Retailer"). R owns or rents real property in multiple states throughout the country. T accepts phone calls from R for maintenance service requests at the R's location. T then uses a proprietary software product to locate an outside vendor (hereinafter referred to as "V" or "Vendor") in that area that will provide the best service at the most reasonable price. V performs the service and bills T for the work performed including sales tax where applicable. T bills R for the work performed at the price charged by V plus an agreed-upon markup. The mark-up is intended to reimburse T for the work performed in locating V and ensuring that the work was performed to R's satisfaction.

T does not have any physical presence and employees of T do not travel into this state for any reason. All orders for service are handled by T's call center operators located outside of your state.

Please cite the references in the general laws and/or regulations of your state that support your answer. Also, please comment on any de-minimis rules that would limit the application of the above laws based upon the amount of revenue generated from work performed in your state.

RULING

The determination 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 Department of Revenue Regulations Section 100.9720 (accessible from the Department's web site). In addition, the following general information may be provided.

The United States Constitution limits a state's power to subject to income tax foreign corporations and other nonresidents. 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)) The Commerce Clause requires that a state's tax be applied only to activities with a substantial nexus to the taxing state. (Id.) 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 a 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.

Note, however, that aside from the question of nexus is the issue of whether or not there is any income tax liability imposed under the Illinois Income Tax Act ("IITA" ; 35 ILCS 5/101 *et seq.*). A nonresident is liable for Illinois income tax under IITA Section 201 if it derives "net income" as defined under IITA Section 202. IITA Section 202 defines 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. The above provisions may be accessed from the Department's web site.

Base income that constitutes nonbusiness income is allocated to Illinois under IITA Sections 301(c)(2) and 303. Base income that constitutes business income is apportioned to Illinois under IITA Section 304. IITA Section 304(a) provides for taxable years ending on or after December 31, 2000 that the apportionment factor for a nonresident deriving business income from Illinois and one or more other states (other than an insurance company, financial organization, or transportation company) shall be equal to its sales factor. Section 304(a)(3)(A) defines the sales factor as a fraction, the numerator of which is the total sales of the person in Illinois during the taxable year, and the denominator of which is the total sales of the person everywhere. For taxable years ending before December 31, 2008, sales other than sales of tangible personal property are assigned to Illinois for apportionment factor purposes if the income-producing activity that gave rise to the receipts is performed wholly in Illinois, or the income-producing activity is performed in Illinois based on costs of performance. Department regulations define the term "income-producing activity" to mean the transactions and activity directly engaged in by the person in the regular course of its trade or business for the ultimate purpose of obtaining gains or profits. However, such activity does not include transactions and activities performed on behalf of a person, such as those conducted on its behalf by an independent contractor. 86 Ill. Adm. Code 100.3370(c)(3)(A).

In this case, assuming that all of your client's income is business income derived from the activities as described in your letter, none of your client's income would be apportioned to Illinois for taxable years ending prior to December 31, 2008. Since all of the client's income-producing activities are performed outside of Illinois, the client does not derive any Illinois net income and therefore has no Illinois income tax liability.

For taxable years ending on and after December 31, 2008, sales of services are generally assigned to the numerator of the Illinois apportionment factor if the services are received in Illinois. 35 ILCS 5/304(a)(3)(C-5)(iv). However, in the case of services provided to a corporation, partnership, or trust, sales of services may only be attributed to Illinois if the corporation, partnership, or trust has a fixed place of business in Illinois. Id. In addition, if the state where the services are received is not readily determinable or is a state where a recipient corporation, partnership, or trust does not maintain a fixed place of business, the services are deemed received at the location of the office of the customer from which the services were ordered, or if the ordering office cannot be determined, at the office of the customer to which the services are billed. Id. Finally, where a taxpayer is not taxable in a state in which the services are received, the sale must be excluded from both the numerator and denominator

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of the sales factor. Id.

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

Sincerely,

Brian L. Stocker
Associate Counsel (Income Tax)