

General Information Letter: Correct computation of income taxed by both Illinois and New Mexico explained.

June 16, 2009

Dear:

This is in response to your letter dated April 28, 2009. 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](http://www.tax.illinois.gov).

In your letter you have stated the following:

I am writing about a taxpayer notification to Mr. & Mrs. Z, XXX-XX-XXXX and XXX-XX-XXXX. The notice is enclosed along with the Illinois Schedule CR Comparison Formulas for Individuals. Mr. Y told me to follow this form and I would arrive at the double taxed income that he arrived at.

After working with the Publication 111 and the New Mexico individual state Illinois CR Comparison formulas of individuals I just could not get my figures to come out to your \$60,079 of double taxed income. I understand how Mr. Y arrived at his figures because he went line by line on his form with me, but that did not match the instruction sheet he told me to use.

I still feel that our number of \$75,741 is the correct figure. This income was totally from New Mexico and had nothing to do with Illinois taxable income. A credit given by New Mexico should only impact New Mexico and the tax paid of \$2,296 was only on New Mexico income. If Illinois is giving a credit for the tax paid to another state, Illinois should also use the correct amount for double-taxed income. I am asking for further consideration on this matter.

Response

First, it appears that you were provided with the New Mexico page from Publication 111 for the wrong taxable year. The correct publication is at <http://www.iltax.com/Publications/Pubs/07-Pub-111-C.pdf>, and a copy of the correct page is enclosed. I apologize for the confusion this must have caused, but using the correct publication shows that the Department's adjustments are correct.

Section 601(b)(3) of the Illinois Income Tax Act (35 ILCS 5/601) provides:

The aggregate amount of tax which is imposed upon or measured by income and which is paid by a resident for a taxable year to another state or states on income which is also subject to the tax imposed by subsections 201(a) and (b) of this Act shall be credited against the tax imposed by subsections 201(a) and (b) otherwise due under this Act for such taxable year. The aggregate credit provided under this paragraph shall not exceed that amount which bears the same ratio to the tax imposed by subsections 201(a) and (b) otherwise due under this Act as the amount of the taxpayer's base income subject to tax both by such other state or states and by this State bears to his

total base income subject to tax by this State for the taxable year.

Illinois income tax regulation 86 Ill. Adm. Code Section 100.2197(b)(4) refers to a taxpayer's "base income subject to tax both by such other state or states and by this State" as "double-taxed income," and provides:

"double-taxed income" means items of income minus items deducted or excluded in computing the tax for which credit is claimed, to the extent such items of income, deduction or exclusion are taken into account in the computation of base income under IITA Section 203 for the person claiming the credit.

As explained in more detail in 86 Ill. Adm. Code Section 100.2197(b)(4), an item of income is included in "double-taxed income" only to the extent it is included in the tax base of the other state and in base income in Illinois, and an expense is deducted in computing "double-taxed income" only to the extent both states allow its deduction. 86 Ill. Adm. Code Section 100.2197(b)(4)(G) provides:

Some states compute the tax liability of a nonresident by first computing the tax on all income of the nonresident from whatever source derived, and then multiplying the resulting amount by a percentage equal to in-state sources of income divided by total sources of income or by allowing a credit based on the percentage of total income from sources outside the state. Other states determine the tax base of a nonresident by computing the tax base as if the person were a resident and multiplying the result by the percentage equal to in-state sources of income divided by total sources of income. The use of either of these methods of computing tax does not mean that income from all sources is included in double-taxed income. See *Comptroller of the Treasury v. Hickey*, 114 Md. App. 388, 689 A.2d 1316 (1997); *Chin v. Director, Division of Taxation*, 14 N.J. Tax 304 (T.C. N.J. 1994). When a state uses either of these methods of computation, double-taxed income shall be the base income of the taxpayer from all sources subject to tax in that state, as computed in accordance with the rest of this subsection (b)(4), multiplied by the percentage of income from sources in that state, as computed under that state's law; provided, however, that no compensation paid in Illinois under IITA Section 304(a)(2)(B) shall be treated as income from sources in that state in computing such percentage in any taxable year beginning prior to January 1, 2006.

New Mexico is one of the states to which this subsection applies.

On the first page of the Zs' New Mexico return, New Mexico taxable income is shown as \$111,733. This amount is the Zs' \$178,539 in federal adjusted gross income, minus their federal itemized deduction, their federal exemption amount, \$36,101 of the net capital gains included in adjusted gross income, and medical expenses. Illinois base income shown on the Form IL-1040 is the Zs' \$178,539 in federal adjusted gross income, minus the \$743 in Illinois income tax refund included in adjusted gross income. Accordingly, all items of income and deductions taken into account in computing the Zs' \$178,539 in adjusted gross income are also taken into account in computing both the New Mexico tax base and Illinois base income, except that \$36,101 of capital gains were not taxed by New Mexico and \$743 in income tax refunds were not taxed by Illinois. The other deductions taken into account on the New Mexico return are ignored, because Illinois does not allow these deductions. As a result, the double-taxed income before application of 86 Ill. Adm. Code Section 100.2197(b)(4)(G) was \$141,695.

Line 13 of Schedule PIT-B reports that 42.4% of their federal adjusted gross income was from New Mexico sources. Multiplying this percentage by \$141,695 yields \$60,078.68, their double-taxed income under 86 Ill. Adm. Code Section 100.2197(b)(4)(G). This is the correct amount, because, under New Mexico's taxing scheme, the Zs were taxed on 42.4% of all items of income, minus deductions, not merely on their income derived from New Mexico sources.

I should also note that this computation is actually more favorable to the Zs than simply computing the limit on the credit by applying the 3% Illinois tax rate to the Zs' taxable income from New Mexico sources, because that income was the \$72,201 in capital gains you used in your computation, minus the \$36,101 exempted from tax by New Mexico, or \$36,100.

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, you may contact me at (217) 782-7055.

Sincerely,

Paul S. Caselton
Deputy General Counsel – Income Tax