

**Illinois Department of Revenue  
Regulations**

**Title 86 Part 100 Section 100.2101 Replacement Tax Investment Credit (IITA 201(e))**

**TITLE 86: REVENUE**

**PART 100  
INCOME TAX**

**Section 100.2101 Replacement Tax Investment Credit (IITA 201(e))**

- a) A taxpayer shall be allowed a credit against the Personal Property Replacement Income Tax for investment in qualified property ("the investment credit"). The qualified property must be used in Illinois by a taxpayer who is primarily engaged in manufacturing, retailing, coal mining or fluorite mining.
- b) *A taxpayer shall be allowed a credit equal to .5% of the basis of qualified property placed in service during the taxable year, provided such property is placed in service on or after July 1, 1984 (IITA Section 201(e)(1)). However, the basis of qualified property shall not include costs incurred after December 31, 2013, except for costs incurred pursuant to a binding contract entered into on or before December 31, 2013 (IITA Section 201(e)(8)).*
- c) *There shall be allowed an additional credit equal to .5% of the basis of qualified property placed in service during the taxable year, provided such property is placed in service on or after July 1, 1986, and the taxpayer's base employment in Illinois has increased by at least 1% over the preceding year. If, in any year, the increase in base employment within Illinois over the preceding year is less than 1%, the additional credit shall be limited to that percentage times a fraction, the numerator of which is .5% and denominator of which is 1%, but shall not exceed .5% (IITA Section 201(e)(1)).*
  - 1) Base employment. For purposes of calculating the additional investment credit, base employment in Illinois is defined as the average monthly total of individuals employed in Illinois by a taxpayer during the taxable year. To calculate base employment for a particular taxable year, the taxpayer need only total the number of individuals he employed in Illinois during each month of the taxable year as reported to the Illinois Department of Employment Security on Line 1 of Form UC-3/40 or Form UI-3/40M and divide this total by the number of months in the taxable year.
  - 2) Example of the Additional Investment Credit Computation. During the calendar year 1994, Corporation A reported 500 employees each month on Line 1 of Form UC-3/40. Therefore, Corporation A's base employment in Illinois for 1994 was 500 ((500 x 12) divided by 12 = 500). In 1995, Corporation A reported 500 employees for each of the first six months, and 505 employees for each of the remaining six months of the taxable year. Therefore, Corporation A's base employment for 1995 was 502.5 ((500 x 6) + (505 x 6) divided by 12 = 502.5). Corporation A's percentage of increase in 1995 base employment over 1994 base employment is .5%. This figure is computed by subtracting the 1994 base

employment from the 1995 base employment and dividing the remainder by the 1994 base employment  $((502.5 - 500) \text{ divided by } 500 = .005 \text{ or } .5\%)$ . Corporation A will be allowed an additional investment credit for 1995 of .25% (one-half of the percentage of increase) times the adjusted basis of qualified property placed in service in Illinois during the taxable year and on or after July 1, 1986.

- d) The investment credit is not allowed to the extent it would decrease the taxpayer's replacement tax liability for the taxable year to less than zero, nor may any credit for qualified property be allowed for any year other than the year in which the property was placed in service in Illinois. No carryback or carryforward of unused credit is allowed for tax years ending prior to December 31, 1985. For tax years ending after December 31, 1988, the credit shall be allowed for the tax year in which the property is placed in service, or, if the amount of the credit exceeds the tax liability for that year, whether it exceeds the original liability or the liability as later amended, such excess may be carried forward and applied to the tax liability of the 5 taxable years following the excess credit year. The credit shall be applied to the earliest year for which there is a liability. If there is credit from more than one tax year that is available to offset a liability, earlier credit shall be applied first.
  
- e) Qualified property. In order to qualify for the investment credit, property must be tangible; depreciable pursuant to Internal Revenue Code Section 167, except that "3-year property" as defined in IRC section 168(c)(2)(A) is not eligible; and acquired by purchase as defined in Internal Revenue Code section 179(d). IRC section 168(c)(2)(A), as in effect at the time the credit was enacted, defined "3-year property" to mean "section 1245 property: with a present class life of 4 years or less; or used in connection with research and experimentation". In addition to the above requirements, property must be used in Illinois by the taxpayer who is engaged primarily in manufacturing, retailing, coal mining or fluorite mining, in order to qualify for the IITA Section 201(e) credit against the replacement tax. Qualified property can be new or used, but cannot have been previously used in Illinois, in such a manner and by such a person as would qualify for the investment credit, or for the Section 201(f) Enterprise Zone Investment Credit, and includes buildings and structural components of buildings.
  - 1) Tangible property, whether new or used, can consist of personalty or realty and includes, but is not limited to, buildings and structural components of buildings, signs that are real property, machinery, equipment, and vehicles. Certain property, though tangible in nature, does not qualify as investment credit property because it is not depreciable.
  
  - 2) Depreciable. In order to qualify for the investment credit, property must also be depreciable pursuant to IRC section 167. IRC section 167 provides that depreciable property is property used in the taxpayer's trade or business or held for the production of income which is subject to wear and tear, exhaustion, or obsolescence.
    - A) Property that is depreciated under the Modified Accelerated Cost Recovery System (MACRS), as provided by IRC section 168, is considered depreciable pursuant to IRC section 167 for purposes of the investment credit. Property assigned to a MACRS class of less than 4 years does not qualify for the investment credit.

- B) Examples of tangible property that is not depreciable are land, inventories or stock in trade, natural resources, and coin or currency.
  - C) The provisions of Treasury Reg. section 1.167(a)-4 shall govern in determining whether leasehold improvements are depreciable.
  - D) IRC section 179 allows taxpayers, under certain circumstances, to expense up to \$25,000 of equipment purchased in a single tax year. Based on this provision, if the total cost of the property was \$25,000 or less, the taxpayer has the option of expensing the cost all in one year as a depreciation expense. While the property does have a useful life of four or more years, since the election was made to completely expense the cost of the property in one year, the property has no federal depreciable basis and does not have a basis upon which to compute the Illinois investment tax credit. Property not fully expensed under section 179 would qualify for the credit based on the cost of the depreciable property reduced by the section 179 deduction.
- 3) Placed in service. For purposes of the Illinois investment credit, "placed in service" has the same meaning as under IRC section 46. Property will be considered to have been placed in service in the same taxable year in which it is taken into account in determining the federal investment tax credit. See Treasury Reg. section 1.46-3(d).
- A) Even though property is placed in service in the same taxable year in which it is taken into account in determining the Federal investment tax credit, only property placed in service in Illinois after June 30, 1984 and before January 1, 1997 can qualify for consideration in determining the credit against the replacement tax. Qualifying property shall be considered placed in service in Illinois on the date on which the property is placed in a condition or state of readiness and available for a specifically assigned function. See Treasury Reg. section 1.46-3(d)(2).
  - B) Property that is disposed of, moved out of Illinois or which ceases to qualify for any other reason during the same taxable year it was placed in service in Illinois will not be considered in computing the investment credit for the taxable year.
- 4) Adjusted basis. The basis of qualified property for purposes of the investment credit is the property's basis used to compute the depreciation deduction for federal income tax purposes. Accordingly, the basis for the credit is determined without regard to any bonus depreciation under IRC section 168(k), but after taking into account any amount treated as an expense not chargeable to capital under IRC section 179.
- A) In computing the amount of investment credit available for a taxable year, the proper investment credit rate will be applied to the total basis of all qualified property placed in service in Illinois during the taxable year, provided the property continues to qualify on the last day of the taxable year.
  - B) If the basis of property placed in service during a taxable year is increased

or decreased during the same taxable year, the increased or decreased basis will be used to compute the investment credit for the taxable year.

- 5) Acquired by purchase. In order to qualify for the investment credit, the property must have been acquired by purchase as defined in IRC section 179(d). For purposes of determining whether property is acquired by purchase as defined by IRC section 179(d), the family of an individual includes only his spouse, ancestors and lineal descendants. Also, for these purposes only, a controlled group has the same meaning as in IRC section 1563(a), except stock ownership of only 50% or more is required. See Treasury Reg. section 1.179-4 under the Internal Revenue Code. Property which the taxpayer constructs, reconstructs or erects itself is generally considered acquired by purchase. IRC section 179 defines purchase as any acquisition of property except:
  - A) an acquisition from a person whose relationship to the acquiring person is such that a resulting loss would be disallowed under IRC section 267 or 707(b);
  - B) an acquisition by one component member of a controlled group from another component member of the group; an acquisition of property, if the basis of the property in the hands of the person acquiring it is determined in whole or in part by its adjusted basis in the hands of the person from whom the property was acquired; or
  - C) an acquisition of property, the basis of which is determined under IRC section 1014(a). IRC section 1014(a) covers property acquired from a decedent. Property acquired by bequest or demise is not acquired by purchase.
- 6) Used in Illinois. Mobile property such as vehicles must be used predominantly in Illinois. Removal of such property from Illinois for a temporary and transitory purpose will not disqualify the property so long as it continues to be used predominantly in the Illinois operation of the taxpayer. For purposes of this Section, mobile property is considered to be predominantly used in Illinois if usage in Illinois exceeds usage outside of Illinois. Example: A retailer sometimes uses its trucks based in Illinois to deliver goods both in Illinois and to out-of-State buyers. Temporary absence of its trucks from Illinois does not disqualify them.
- 7) A lessor of otherwise qualifying property that is used by the lessee in manufacturing, retailing, or coal or fluorite mining operations, would not qualify for the credit because the property is not used "by the taxpayer".
- 8) "Manufacturing" is defined in IITA Section 201(e)(3) as *the material staging and production of tangible personal property by procedures commonly regarded as manufacturing, processing, fabrication or assembling which changes some existing material into new shapes, new qualities, or new combinations*. It is not necessary that these procedures result in a finished consumer product. Procedures commonly regarded as manufacturing, processing, fabrication or assembling are those so regarded by the general public. If a taxpayer primarily engages in the following operations, the taxpayer will not qualify for the investment credit on the basis of engaging primarily in manufacturing. The activities described are generally not considered manufacturing operations:

- A) Agricultural activities such as cultivating the soil, raising or harvesting crops, the production of seed or seedlings, and the development of hybrid seeds, plants or shoots are not manufacturing operations. The raising or breeding of livestock, poultry, fish or any other animals, as well as commercial fishing or beekeeping, is not manufacturing.
  - B) Manufacturing operations do not include mining, quarrying, logging, drilling for oil, gas or water, or any other operations that result in the extraction or procurement of a natural resource. However, the refining or processing of natural resources into a product of a different form or a product that has different qualities is manufacturing.
  - C) Persons engaged in the construction, reconstruction, alteration, remodeling or improvement of real estate are not considered engaged in manufacturing operations.
  - D) Manufacturing operations do not include research and development of new products or production techniques.
  - E) Manufacturing operations do not include the use of machinery or equipment in managerial or other non-production, non-operational activities including disposal of waste, scrap or residue, inventory control, production scheduling, work routing, purchasing, receiving, accounting, fiscal management, general communications, plant security, or personnel recruitment, selection or training.
- 9) Retailing. Retailing is defined as *the sale of tangible personal property for use or consumption and not for resale, or services rendered in conjunction with the sale of tangible personal property for use or consumption and not for resale. For purposes of this Section, the term "tangible personal property" has the same meaning as when used in the Retailers' Occupation Tax Act, and does not include the generation, transmission, or distribution of electricity* (IITA Section 201(e)(3)). It is required that the tangible personal property be finished consumer goods, and the property be sold to its ultimate consumer. For example, sales of tangible personal property for resale are not included in the definition of retailing. The following activities are not considered retailing operations:
- A) The construction, reconstruction, alteration, remodeling or improvement of real estate;
  - B) The operation of a hotel or motel or other institution providing only lodging facilities;
  - C) Other service professions that do not involve the transfer of tangible personal property other than as an incident to the service performed. For guidance in distinguishing service professions from retailing professions, the Department will rely on rules promulgated under the Service Occupation Tax Act at 86 Ill. Adm. Code 140;
  - D) Farming operations related to crop and livestock production do not constitute retailing. However, the marketing of these products would

constitute a retailing operation.

- 10) Mining of coal or fluorite. *Mining has the same meaning as in section 613(c) of the Internal Revenue Code*, but shall be limited to the mining of coal and fluorite (IITA Section 201(e)(3)). Mining as defined in IRC Section 613(c) includes not only extraction, but also treatment processes such as cleaning, breaking, sorting, sizing, dust allaying, and loading for shipment.
- 11) New or used. Qualifying property can be new or used; however, used property does not qualify if it was previously used in Illinois in such a manner and by such a person as would qualify for the Illinois investment credit.
  - A) Example: Corporation A purchases a used pick-up truck, for use in its manufacturing business in Illinois, from an Illinois resident who used the truck for personal purposes in Illinois. If the truck meets all the other requirements for the investment credit, it will not be disqualified merely because it was previously used in Illinois for a purpose that did not qualify for the credit. However, had Corporation A purchased the used truck from an Illinois taxpayer in whose hands the truck qualified for the investment credit, the truck would not be qualified property to Corporation A, even though the party from whom the truck was acquired had never received an investment credit for it.
  - B) Property that would otherwise qualify for the credit will not be disqualified because it was previously used in such a manner and by such a person as would have qualified for the investment credit before the credit came into effect. Example: In August of 1983, Corporation A purchased a drill press for use in its manufacturing operation in an Illinois Enterprise Zone from Corporation B. Corporation B originally placed the drill press into service in its Illinois manufacturing operation in January of 1980, before IITA Section 201(e) came into effect. Even though Corporation B would have qualified for the Illinois investment credit had there been a credit in 1980, this will not disqualify Corporation A from claiming a credit for this property, provided the property is otherwise qualified. However, should Corporation A sell the property to Corporation C for use in its Illinois manufacturing operation, the property would not qualify for the credit, even though it would otherwise qualify, because the property was used in such a manner and by such a person as would have qualified for the investment credit under Section 201(e) or 201(f) at a time when at least one of the credits was in effect. The fact that the Section 201(e) credit was not yet effective when Corporation A placed the property in service will not cause the property to qualify for the Section 201(e) credit in the hands of Corporation C because IITA Section 201(e) specifically provides that the property is disqualified if it previously qualified under either IITA Section 201(e) or 201(f).
- f) To qualify for the credit, property must be used in Illinois by a taxpayer who is primarily engaged in manufacturing, or in mining coal or fluorite, or in retailing. It is not required that the property be used exclusively in manufacturing, mining of coal or fluorite or in retailing. So long as the taxpayer is primarily, more than 50%, engaged in one of these operations, all qualified property is eligible for the credit, even if the property is not actually used in an exempt manufacturing, coal or fluorite mining or retailing process.

The taxpayer must engage primarily in one or more of the operations. In other words, a taxpayer that is engaged 30% of the time in retailing and 40% of the time in manufacturing will qualify for the credit, because the taxpayer is engaged primarily in one or more of the operations. In determining whether a taxpayer is primarily engaged in an activity the Department will look to the gross receipts of the taxpayer received in the ordinary course of business by that taxpayer. For example, if more than 50% of the taxpayer's gross receipts are from manufacturing, the taxpayer is primarily engaged in manufacturing, or if more than 50% of the gross receipts are from retailing, the taxpayer is primarily engaged in retailing. The taxpayer (and the Department) will look to the gross receipts received by the taxpayer in the ordinary course of business. Therefore, if, for example, the taxpayer suffers a casualty loss and that is compensated for by an insurance payment, the amount of money so received will not be deemed gross receipts received in the ordinary course of business, and disqualify the taxpayer from eligibility and perhaps result in the recapture of credits granted in prior years.

EXAMPLE 1: Corporation A manufactures CD ROM Units for personal computers, which are sold to others for resale. Corporation A also engages in the retail sale of canned computer software. Finally, Corporation A develops and sells custom computer software to various clients. Corporation A receives 20% of its gross receipts from the manufacturing of CD ROM Units, 40% of its gross receipts from retail sales of canned software, and 40% of its gross receipts from its custom computer software development and sales operations. Corporation A is eligible for the credit. Corporation A is engaged primarily in manufacturing and retailing, because the total of its manufacturing and retailing operations is 80% of its gross receipts. Therefore, the Corporation is eligible for the credit.

EXAMPLE 2: Corporation B operates a hotel. 80% of the gross receipts of Corporation B are from the renting of rooms, 5% of the gross receipts are from the operation of a gift shop in the hotel and the remaining 15% of the gross receipts are from the operation of a restaurant and lounge in the hotel. The renting of rooms is not retailing. Therefore, Corporation B is ineligible for the credit because it is not engaged primarily in retailing, even though it does, through the operation of the gift shop, restaurant and lounge, engage in some retailing activities.

g) *Recapture. If, within 48 months after being placed in service, any property ceases to be qualified property in the hands of the taxpayer or the situs of any qualified property is moved outside of Illinois, or outside of the enterprise zone, for other than a temporary or transitory purpose, then the personal property tax replacement income for the taxable year in which such event occurred will be increased (IITA Section 201(e)(7)). If, during the 48 month period, the taxpayer ceased to be primarily engaged in retailing, manufacturing, coal or fluorite mining, the property ceases to be qualified property. Therefore, previously granted credits must be recaptured.*

- 1) Any property disposed of by the taxpayer within 48 months after being placed in service ceases to qualify.
- 2) A taxpayer disposes of property when he sells the property, exchanges or trades in worn-out property for new property, abandons the property or retires it from use. Property destroyed by casualty, stolen, or transferred as a gift is treated as having been disposed of. Property which is mortgaged or used as security for a loan does not cease to qualify provided the taxpayer continues to use the property within Illinois. Property transferred to a trustee in bankruptcy is

considered disposed of in the year the property is transferred to the trustee. A transfer of property by foreclosure is treated as a disposition.

- 3) The reduction of the basis of qualified property resulting from the redetermination of the purchase price is a disposition of qualified property to the extent of such reduction in the taxable year the reduction takes place. This occurs, for example, when property is purchased and placed in service in one year, and in a later year the taxpayer receives a refund of part of the original purchase price. See 26 CFR 1.47-2(c) (2010).
- 4) In order to determine the amount by which the personal property tax replacement income tax must be increased in the taxable year in which the property ceased to qualify or was moved outside of Illinois or the enterprise zone, the taxpayer must recompute the investment credit for the taxable year in which the property was placed in service by eliminating from his calculations any such property. This recomputed investment credit is subtracted from the amount of credit actually used in the year in which the disqualified property was placed in service. The difference between the recomputed credit and the credit actually used is added to the personal property tax replacement income tax or the income tax for the year in which the property ceased to qualify or was moved outside of Illinois. If the recomputed credit is greater than the credit actually used in the year the property was placed in service, no addition to the current taxable year's personal property tax replacement income tax or income tax is required.

EXAMPLE: In 1985, Corporation A places qualifying property with a basis of \$55,000 into service in an enterprise zone located in Illinois and computes a Section 201(e) investment credit for the year of \$275 ( $\$55,000 \times .5\%$ ) and a Section 201(h) investment credit of \$275 ( $\$55,000 \times .5\%$ ). Corporation A's 1985 personal property tax replacement income tax is \$260 and its income tax liability for the year is \$420. After application of the credit, Corporation A has no remaining replacement tax liability and its remaining income tax liability is \$145. In the following year Corporation A moved a qualifying asset having a basis in 1985 of \$5,000 from Illinois and is therefore required to recapture a portion of the investment credit applied against its replacement tax. In order to determine its additional income tax for 1986, Corporation A must recompute its 1985 investment credit by eliminating the disqualified property ( $\$55,000 - \$5,000 \times .5\% = \$250$ ). This recomputed credit is subtracted from the investment credit actually used in 1985 against the income tax ( $\$260 - \$250 = \$10$ ) and the difference is added to Corporation A's 1986 income tax after application of the 1986 investment credit.

h) Partnerships and Subchapter S Corporations.

- 1) *For each taxable year ending before December 31, 2000, a partnership may elect to pass through to its partners the credits to which the partnership is entitled under IITA Section 201(e) for the taxable year. The election to pass through the credits shall be irrevocable. [IITA Section 201(e)(9)]*
  - A) This subsection (h)(1) applies only to partnerships. Subchapter S corporations may not pass credits through to their stockholders under this provision.

- B) Subject to the statute of limitations, the election under this subsection (h)(1) may be made retroactively. See *Borden Chemicals and Plastics, L.P. v. Zehnder*, 312 IllApp3d 35 (1<sup>st</sup> Dist. 2000). A retroactive election shall be made by filing an amended return by the partnership making the election for the tax year of the election and for any subsequent year affected by the election, and including a schedule of the credits to be passed through. An example of a subsequent year affected by an election would be a year in which a credit carried forward from a year prior to the election was used by the partnership or was passed through to the partners by an election for that subsequent year.
  - C) All credits to which the partnership is entitled under IITA Section 201(e) in the year an election is made are passed through to the partners, including credits passed through to the partnership from another partnership, credits carried forward from prior years and the share attributable to partners who are not subject to Personal Property Tax Replacement Income Tax and exempt organizations not subject to tax under IITA Section 205(a).
  - D) Any credit passed through to a partner must be used within the 5-year carryforward period allowed to the partnership. Thus, a credit earned by a partnership in the year the election is made may be used by the partner to whom it is passed in that partner's taxable year in which the taxable year of the partnership for which the election was made ends, and any unused amount may be carried forward to the 5 succeeding taxable years of the partner. If a partnership elects to pass through to its partners a credit earned in its immediately preceding taxable year, a partner may use that credit in its taxable year in which the taxable year of the partnership for which the election was made ends, and any unused amount may be carried forward to the 4 succeeding taxable years of the partner.
- 2) *For taxable years ending on or after December 31, 2000, a partner that qualifies its partnership for a subtraction under Section 203(d)(2)(I) of IITA or a shareholder that qualifies a subchapter S corporation for a subtraction under Section 203(b)(2)(S) shall be allowed a credit under IITA Section 201(e) equal to its share of the credit earned under IITA Section 201(e) during the taxable year by the partnership or subchapter S corporation, determined in accordance with the determination of income and distributive share of income under sections 702 and 704 and subchapter S of the Internal Revenue Code. [35 ILCS 5/201(e)(9)]* Under this subsection (h)(2):
- A) The provisions of this subsection (h)(2) apply to both partnerships and subchapter S corporations.
  - B) Credits are passed through only in the year earned. Any amount carried forward from a prior year cannot flow through to the partners or shareholders of the entity.
  - C) The share of credits allocable to a partner or shareholder who is not subject to Personal Property Tax Replacement Income Tax and who is not exempt from taxation under IRC section 501(a) do not pass through to that partner or shareholder. Those amounts may be used by the partnership or subchapter S corporation against the Personal Property Tax

Replacement Income Tax liability it incurs on the share of its income attributable to such partners or shareholders.

- D) Any credit passed through to a partner or shareholder under this subsection (h)(2) may be used in the taxable year of the partner or shareholder in which the taxable year of the entity that passes the credit through ends, and may be carried forward to the 5 succeeding taxable years of the partner or shareholder until used.
- E) Any credit passed through to a partnership or subchapter S corporation under this subsection (h)(2) shall pass through to its partners or shareholders in the same manner as a credit earned by the partnership or subchapter S corporation.

(Source: Amended at 35 Ill. Reg. 15092, effective August 24, 2011)