

General Information Letter: Nexus issues are not generally suitable for resolution by letter ruling.

March 15, 2012

Dear:

This is in response to your letter dated November 15, 2011 in which you state the following:

On behalf of a client, hereafter referred to as AAA (an alias), we are respectfully requesting a general information letter concerning nexus for income tax purposes for the State of Illinois. Specifically we are inquiring if based on the business activities of AAA as described below, would nexus exist for purposes of income taxation to AAA including for registration and reporting purposes.

AAA is organized as a limited liability company under the laws of the State of STATE. All of the members of AAA are residents of STATE. AAA has only one physical location and it is in STATE. All employees work solely in STATE. AAA has agreements with national companies (AAA's customers) to arrange repairs and maintenance to their customer's commercial buildings that are located in various states. For example if a customer's commercial building that is located in Illinois has a water leak, the corporate national office will call directly to AAA to get services of a plumber. The customer's corporate national office may be located in another state or possibly in Illinois. AAA then will locate local contractors (e.g. plumbers in Illinois for this example), and then usually issue a repair order on a not-to exceed basis to a local contractor (e.g. plumber). A not-to exceed order is a work order where the price is set by AAA at a limit that the contractor cannot exceed. The contractor (e.g. plumber) can choose whether to accept such an order or counter with different amount. As an alternative to a not-to-exceed order, on occasion AAA will get bids and then issue a repair order to the contractor (e.g. plumber). The repair order will direct the contractor (e.g. plumber) to contact the building manager to schedule and make the repairs. Upon completion of the repairs AAA will pay the contractor's (e.g. plumber) bill. AAA will then bill their commercial building customer for the cost of the contractor (e.g. plumber) and add on AAA's management fee. Management fees usually run from 14% to 23% of the contractor's bill. AAA has no pre-existing arrangement with the contractors and no continuing one after the job is completed. Repair and maintenance work could include such items as plumbing, electrical, painting and other general building repairs.

Based our review of federal law and Illinois statutes and rules it does not appear AAA's activities would create nexus for income taxation purposes for registration and reporting to Illinois. Nonetheless, we are seeking a general information letter on this matter.

According to the Department of Revenue ("Department") regulations, the Department may issue only two types of letter rulings: Private Letter Rulings ("PLR") and General Information Letters ("GIL"). The regulations explaining these two types of rulings issued by the Department can be found in 2 Ill.Adm.Code §1200, or on the website <http://www.tax.illinois.gov/LegallInformation/regs/part1200>.

Due to the nature of your inquiry and the information presented in your letter, we are required to respond with a GIL. GILs are designed to provide background information on specific topics. GILs, however, are not binding on the Department.

Section 201 of the Illinois Income Tax Act (“IITA,” 35 ILCS 5/101 et seq.) imposes a tax measured by net income on taxpayers for the privilege of earning or receiving income in this State. The Due Process and Commerce Clauses of the Federal Constitution limit the power of Illinois to subject foreign taxpayers to Illinois tax. The Due Process Clause requires that there exist some minimum connection between a state and the person, property, or transaction it seeks to tax (Quill Corp. v. North Dakota, 504 U.S. 298, 112 S.Ct. 1904 (1992)). Similarly, the Commerce Clause requires that the tax be applied to an activity with a substantial nexus with the taxing state. Id.

The citation for the Illinois Department of Revenue regulation clarifying nexus is 86 Ill.Adm.Code Section 100.9720 and can be found on the Department’s website at <http://tax.illinois.gov/LegalInformation/regs/Part100/100-9720.pdf>. Please refer to subsections (c)(4) entitled “Unprotected Activities,” (c)(5) entitled “Protected Activities” and (c)(6) entitled “Independent Contractors.” This will provide you with a helpful guideline in determining whether your client’s activities will subject them to Illinois income taxation.

Your question is whether your client will owe Illinois income taxes as a result of operating a repair and maintenance call center for national companies with multi-site locations. Your client’s business consists of coordinating contracted labor on an as-needed basis for its national customers, some of them located in Illinois. According to the limited facts in your letter, it appears that the “contracted” work is performed by independent contractors. If so, please note the regulation states the use of independent contractors may only afford a nonresident immunity from taxation for “limited activities.” The fact that your client’s business is entirely set up around using independent contractors on a regular basis may jeopardize the protections afforded in 86 Ill.Adm.Code Section 110.9720(c)(6).

The question of nexus is highly fact-dependent. Therefore, the Department does not issue rulings regarding whether a taxpayer has nexus with the State. Such a determination can only be made in the context of an audit where a Department auditor has access to all relevant facts and circumstances. Based on the limited facts presented in your letter, however, it seems likely that contracting sales of services in Illinois on a regular basis will subject your client to Illinois income taxation.

IITA Section 304(a)(3)(C-5) is most applicable to the situation addressed in your letter because your client’s activities are sales *other than* sales of tangible personal property. IITA Section 304(a)(3)(C-5) states as follows:

- (C) Sales, other than sales governed by paragraphs (B), (B-1), (B-2), (B-5) and (B-7), are in this State if:

...

- (iv) Sales of services are in this State if the services are received in this State. For the purposes of this section, gross receipts from the performance of services provided to a corporation, partnership, or trust may only be attributed to a state where that corporation, partnership, or trust has a fixed place of business. If the state where the services are received is not readily determinable or is a state where the corporation, partnership, or trust receiving the service does not have a fixed place of business, the services shall be deemed to be received at the location of the office of the customer

from which the services were ordered in the regular course of the customer's trade or business. If the ordering office cannot be determined, the services shall be deemed to be received at the office of the customer to which the services are billed. If the taxpayer is not taxable in the state in which the services are received, the sale must be excluded from both the numerator and the denominator of the sales factor. The Department shall adopt rules prescribing where specific types of service are received, including, but not limited to, publishing, and utility service.

Section 502(a) of the IITA (35 ILCS 5/502(a)) sets forth the requirements for filing Illinois income tax returns. That section states:

(a) In general. A return with respect to the taxes imposed by this Act shall be made by every person for any taxable year:

- (1) For which such person is liable for a tax imposed by this Act, or
- (2) In the case of a resident or in the case of a corporation which is qualified to do business in this State, for which such person is required to make a federal income tax return, regardless of whether such person is liable for a tax imposed by this Act.

Under this section, a nonresident must file an Illinois income tax return if it incurs a liability for tax imposed under Section 201 of the IITA (or in the case of a corporation qualified to do business in Illinois, if it is required to file a federal return). A nonresident is liable for Illinois income tax under Section 201 if it computes "Illinois net income" as defined under IITA Section 202. IITA Section 202 defines Illinois 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.

As stated above, this is a general information letter which does not constitute a statement of policy that either applies, interprets or prescribes tax law. It is not binding on the Department. Should you have additional questions, please do not hesitate to contact our office.

Sincerely,

Heidi Scott  
Associate Counsel -- Income Tax