

General Information Letter: Addresses sourcing of employee compensation in various scenarios, most of which contain insufficient information to allow a conclusion.

July 26, 2012

Dear:

This is in response to your letter dated July 17, 2012, in which you request a letter ruling. 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:

We have a few questions on what should be shown on the W-2 for state wages in the following scenarios. It would be greatly appreciated if you can review the following scenarios and provide guidance on how an employer would populate W-2, Box 16 for the state of Illinois. We are aware of the reciprocity agreement with Iowa, Kentucky, Michigan, and Wisconsin, so the questions below would be directed to other state scenarios:

- 1) Resident of Illinois works 100% in another state (Minnesota) that has withholding, what should show on Illinois resident's W-2, Box 16?
- 2) Resident of Illinois works 50% in another state (Minnesota) that has withholding and 50% within Illinois, what should show on Illinois resident's W-2, Box 16?
- 3) Resident of Illinois works in a state (Tennessee) that does NOT have withholding, what should show on Illinois resident's W-2, Box 16?
- 4) Resident of Illinois works in another state the employee is NOT subject to withholding in the work state for whatever reason, what should show in W-2. Box 16?

We are doing research to determine how to properly populate the Illinois W-2 so we can be in compliance.

Response

Section 302(a) of the Illinois Income Tax Act (35 ILCS 5/302) provides that, with respect to nonresidents:

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.

This provision is also relevant to residents who pay income tax to other states and are allowed a credit for such taxes under Section 601(b)(3) of the Illinois Income Tax Act (35 ILCS 5/601), because that paragraph provides, in part:

the credit provided under this paragraph for tax paid to other states 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 that would be allocated or apportioned to other states if all other states had adopted the provisions in Article 3 of this Act bears to the taxpayer's total base income subject to tax by this State for the taxable year.

Under this provision, employee compensation that is "paid in this State" under Section 304(a)(2)(B) of the Illinois Income Tax Act (35 ILCS 5/304) cannot be included in the numerator of the fraction used to compute the limitation on a resident's credit for taxes paid to another states. In the simplest case, a resident whose only income is employee compensation "paid in this State" would not be entitled to a credit for taxes paid to any other state on that compensation.

Finally, Section 701(a)(1) of the Illinois Income Tax Act (35 ILCS 5/701) requires withholding from employee compensation "paid in this State" under Section 304(a)(2)(B), while Section 701(b) requires withholding from any income, including employee compensation, paid to an Illinois resident if federal income tax withholding is required and no other state income tax is required to be withheld.

Section 304(a)(2)(B) provides that, 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) 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.

Additional guidance on the determination of whether employee compensation is "paid in this State" can be found in 86 Ill. Adm. Code Section 100.3120 and Publication 130, Who Is Required to Withhold Illinois Income Tax?

Pursuant to these provisions, none of the employee compensation paid to an employee who works 100% in Minnesota in your first scenario should be reported as Illinois wages in Box 16 of the Form W-2, because none of the services are performed within Illinois. With respect to the other three scenarios, your letter does not provide sufficient information to determine whether the employee compensation is "paid in this State." However, if the resident employees in the third and fourth scenarios are working 100% in Tennessee or whichever other state imposes no withholding requirement, none of their wages should be reported in Form W-2, Box 16, because their wages are not "paid in this State," even though the wages would be subject to Illinois withholding under Section 701(b) because they are subject to federal income tax withholding and no other state's withholding is required.

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,

IT 12-0019-GIL

July 26, 2012

Page 3

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