

Compensation paid in Illinois under IITA Section 304(a)(2)(B) does not qualify for the credit for taxes paid to other states.

May 7, 2015

Re: TAXPAYER – Credit for Taxes Paid to Other States

Dear Mr. XXXX:

This is in response to your letter to NAME of the Illinois Department of Revenue's Problems Resolution Division, dated May 4, 2015. 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 submitting the enclosed paperwork under power of attorney for above-named taxpayer to enable you to accept the 2011 IL tax return as originally. This case is similar to the other cases my firm has submitted for other BUSINESS employees, in that the taxpayers are Illinois residents who have had credit for taxes paid to other states disallowed.

The State has already denied the credit from other states in letters dated X-XX-XX and XX-XX-XX. As a result of the history of correspondence that is ultimately denying the tax credit, we believe that this case is eligible for consideration by your office.

We believe this is a case of double taxation and it would be unfair to not allow a credit for taxes paid to the other states on the same income. To support my position, I am enclosing an excerpt from IDOR Regulations which addresses the issue. I have underlined the applicable lines on the third page. In general, it states that compensation paid in Illinois that is taxed in other states may be included in double-taxed income in taxable years beginning on or after January 1, 2006.

The Form W-2 provided by TAXPAYER's employer indicates in Box 16 that 100% of her INCOME in compensation for 2011 was sourced to Illinois. In the letter from the employer, dated XX-XX-XX, which you enclosed with your letter, the employer states that only ALLOCATED AMOUNT of her compensation was sourced to Illinois, "based on where the

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associated work has been performed for the client. That allocation is calculated based on timesheet hours.”

Response

The credit for taxes paid to other states is allowed by Section 601(b)(3) of the Illinois Income Tax Act (35 ILCS 5/601), which also provides:

For taxable years ending on or after December 31, 2009, 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.

In other words, a resident is entitled to a credit for any taxes paid to other states on income taxed by Illinois, but the total credit cannot exceed a limit. The limit equals the amount of Illinois income tax attributable to the income that is sourced outside Illinois using Illinois' allocation and apportionment provisions, determined by taking the taxpayer's Illinois tax before credits, and multiplying it by a fraction equal to the base income that would be allocated or apportioned to other states if they all used Illinois allocation and apportionment rules, divided by the taxpayer's total base income.

In the allocation and apportionment provisions of Article 3 of the Illinois Income Tax Act, Section 302(a) (35 ILCS 5/302) provides:

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.

Section 304(a)(2)(B) of the Illinois Income Tax Act (35 ILCS 5/304) 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.

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Publication 130, Who is Required to Withhold Illinois Income Tax, provides guidance on determining when compensation is sourced to Illinois and instructs employers:

When completing the W-2, enter only the amount of wages paid in Illinois or paid to an Illinois resident employed in Iowa, Kentucky, Michigan or Wisconsin in Box 16. If none of the employee's wages were paid in Illinois or for an Illinois resident's employment in a non-reciprocal state, report zero in Box 16 even if you withheld Illinois income tax from those wages. Illinois residents who pay income tax to other states need this information in order to compute the credit allowed for those taxes.

As noted above, the W-2 provided by TAXPAYER's employer indicates that all of her compensation is sourced to Illinois. This would indicate that none of her compensation would be sourced to other states if they all followed Illinois' rule for sourcing compensation. Because the Schedule CR, Credit for Tax Paid to Other States, she attached to her return shows no other income that would be sourced to other states under Illinois' allocation and apportionment rules, the limit on her credit should be zero.

The letter from the employer you provided states that the allocation of employee compensation that it shows is based on the hours worked in each state, which is not relevant for this purpose. Also, the copy of the 86 Ill. Adm. Code Section 100.2197 you provided is out of date. It does not reflect the changes to Section 601(b)(3) of the Illinois Income Tax Act that apply to taxable years ending on or after December 31, 2009, quoted above, and has since been amended to apply the new statute. Accordingly, you have not provided us with any information that would show that our determination of TAXPAYER's credit is incorrect.

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