

Section 304(f) Does Not Authorize Alternative Method of Apportionment under Section 305(a)

March 1, 2017

Re: Petition for Alternative Apportionment

Dear Xxxxx:

This is in response to your letter dated December 2, 2016 in which you requested permission to use an alternative method of allocation or apportionment. Department of Revenue ("Department") regulations require that the Department issue only two types of letter rulings, Private Letter Rulings ("PLRs") and General Information Letters ("GILs"). PLRs are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding against the Department, but only as to the taxpayer issued the ruling and only to the extent the facts recited in the PLR are correct and complete. GILs do not constitute statements of Department policy that apply, interpret or prescribe the tax laws and are not binding against the Department. See 2 Ill. Adm. Code 100.1200(b) and (c). For the reasons discussed below, your petition cannot be granted at this time.

Your letter states as follows:

NAME Real Estate Value Fund, L.P. (the Fund) is submitting this petition under 86 Ill. Adm. Code 100.3390. It is requesting permission to use specific accounting instead of the applicable statutory apportionment formula for filing its 2016 income tax return.

The Fund invests in various companies which own real estate. These investments are long term investments. Currently, two of the investments are single member limited liability companies ("SMLLC"). Each of these SMLLC own property which is only located in one state ("COMPANY, LLC" only has property and operations in Illinois and "COMPANY 1, LLC" only has property and operations in Texas). The third investment owned by the Fund is COMPANY 2, a partnership. COMPANY 2 has property in California, Oregon, Washington, and Nevada.

The Fund is divided into three classes, "A", "B", and "C". The partners of the Fund are not necessarily "partners" for purposes of all the classes within the Fund (see attached schedule) due to various buyouts of partners, etc. that have occurred over the life of the Fund. The allocations and distributions to each partner, for both book and federal purposes, are determined by the funds they have a partnership share in under the Fund agreement. As such, COMPANY 3 and COMPANY 4 have no interests in properties located in California, Oregon, Washington, or Nevada. Similarly, none of their income or distributions for federal income tax or book purposes is derived from operations in these four states. To use the statutory formula provided in Illinois' statutes would result in taxable income being apportioned to these partners when they have no ownership interest in properties within Illinois. In addition, the amount of taxable income in states in which the partners have an interest(s) in properties, and which use the same or similar apportionment schemes, would be disproportionately reduced

The justification for specific accounting is that the typical state apportionment would yield taxable income to each partner which is different from the amount allocable to each partner for federal tax purposes. This is due to the unique structure of this partnership in which properties in specific states are owned by different pass-through or disregarded entities. These entities comprise the funds noted above which have differing ownership; they are almost “partnerships” within a partnership. By using specific accounting, the federal allocable income and state taxable per partner, not to mention the economics of the ownership arrangement, should agree. Using statutory partnership will result in the income “deck” being reshuffled among the partners and not agreeing with federal allocable income.

RULING

Section 304(f) of the Illinois Income Tax Act (“IITA” 35 ILCS 5/304(f)) states:

If the allocation and apportionment provisions of subsections (a) through (e) and of subsection (h) do not, for taxable years ending before December 31, 2008, fairly represent the extent of a person’s business activity in this State, or, for taxable years ending on or after December 31, 2008, fairly represent the market for the person’s goods, services, or other sources of business income, the person may petition for, or the Director may, without a petition, permit or require, in respect of all or any part of the person’s business activity, if reasonable:

- (1) Separate Accounting;
- (2) The exclusion of any one or more factors;
- (3) The inclusion of one or more additional factors which will fairly represent the person’s business activities or market in this State; or
- (4) The employment of any other method to effectuate an equitable allocation and apportionment of the person’s business income.

IITA Section 305(a) provides the method of allocation of partnership business income by nonresident partners. The section states:

The respective shares of partners other than residents in so much of the business income of the partnership as is allocated or apportioned to this State in the possession of the partnership shall be taken into account by such partners pro rata in accordance with their respective distributive shares of such partnership income for the partnership’s taxable year and allocated to this State.

In this case, IITA Section 305(a) governs the apportionment of nonresident partners with respect to their income from the Fund. Your letter indicates that due to the manner in which the partners share the income of the Fund, the apportionment rule under IITA Section 305(a) will result in income to each partner which is different from the amount allocable to each partner for federal tax purposes. IITA Section 304(f) allows the Department to permit or require an alternative apportionment method where the provisions of IITA Section 304(a) through 304(e), and 304(h), do not fairly represent the market for the person’s goods, services, or other sources of business income. Your letter does not indicate that the Fund’s application of IITA Section 304(a) fails to reflect the market for the Fund’s goods, services, or other sources of business income. Section 304(f) does not authorize the Department to permit a

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departure from the apportionment rule for nonresident partners prescribed under IITA Section 305(a). Therefore, your request for an alternative apportionment method cannot be granted.

However, if you have additional information related to this request that was not previously submitted, you may supplement your petition and we will reconsider your request. Please note that 86 Ill. Adm. Code Section 100.3390(e)(1) requires a petition to be filed at least 120 days prior to the due date (including extensions) for the first return for which permission is sought to use the alternative apportionment method.

Sincerely,

Brian Stocker
Associate Counsel (Income Tax)

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