

Subtraction Not Applicable to Retirement Plan of a Private Employer in Foreign Country
(This is a GIL.)

March 1, 2017

Re: Illinois income tax

Dear Xxxxx:

This is in response to your letter dated January 6, 2016, in which you request a private letter ruling. The nature of your letter and the information provided require that we respond with a General Information Letter (GIL). A GIL 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 accessed from the Department's web site at www.tax.illinois.gov.

Your letter states as follows:

I have been working for the Illinois – based publicly traded COMPANY, including several of its subsidiaries as an expatriate employee in several jurisdictions since April 1, 1985. My initial employment started in Germany. As of September 1st, 2016 I have retired from my employment with the German subsidiary of COMPANY and transferred to a U.S. employment with COMPANY 1, a U.S. subsidiary of COMPANY.

As a resident of Illinois, I am subject to paying taxes in the State of Illinois and have complied with this obligation ever since I was a resident in this State.

With my retirement from my German employment, I am entitled to a monthly pension from my former German employer at the amount of \$\$\$\$.

This letter requests a private ruling concerning the taxability for Illinois tax purposes of the pension paid by my former German employer, specifically for the exclusion of this income for Illinois State Tax purposes. The pension is includable – and will be included in my federal tax return.

The Illinois Income Tax Act provides for an individual to subtract certain amounts from the adjusted gross income that is subject to taxation in the State of Illinois, including pensions, i.e. essentially those which are included in Sections 401(a), 402(c), 403(b), 406(a), 407(a) or 408 of the Internal Revenue Code. It appears that none of these provisions apply directly to a pension received from a foreign employer.

However, according to the "PROTOCOL, AMENDING THE CONVENTION BETWEEN THE UNITED STATES OF AMERICA AND THE FEDERAL REPUBLIC OF GERMANY FOR THE AVOIDANCE OF DOUBLE TAXATION AND THE PREVENTION OF FISCAL EVASION WITH RESPECT TO TAXES ON INCOME AND CAPITAL AND TO CERTAIN OTHER TAXES, SIGNED ON AUGUST 29, 1989 (the "U.S. – Germany Income Tax Treaty")

Article VIII of the U.S.-Germany Income Tax Treaty added under (b) a new paragraph as follows: "Social security benefits paid under the social security legislation of a Contracting State ...paid ... to a resident of another Contracting State shall be taxable only in that other Contracting State. In applying the precedent sentence, that other Contracting State shall treat such ...or pension as though it were a social security benefit paid under the social security legislation of that other Contracting State." Illinois follows that bi-lateral treaty.

The German pension I receive is based on an arrangement under Section 1 of the German law on employment-related pensions (Betriebsrentengesetz), i.e. a social security benefit paid under the social security legislation of Germany and therefore qualifies for being treated equal to U.S. pension plans arranged under the Sections of the Internal Revenue Code cited earlier. Plans under the German "Betriebsrentengesetz" are 'generally corresponding' to social security benefits paid under U.S. laws that are eligible for a deduction for Illinois tax purposes. As such, with the pension payments treated equal to a U.S. pension payments, they should qualify as subtractable from my Illinois Tax Return.

This result is also in line with the spirit of the U.S.-Germany Income Tax Treaty which bi-laterally addresses the issue that there should be no discrimination between tax payers in either country and provides for social security benefits paid under the social security legislation of either country to be treated as if it were a social security benefit of that other country/contracting state.

I kindly ask you for a private letter ruling on that matter that supports the deductibility of this pension income for Illinois tax purposes.

RULING

Section 203(a)(2)(F) provides the following deduction in the computation of an individual's Illinois base income:

An amount equal to all amounts included in such total pursuant to the provisions of Sections 402(a), 402(c), 403(a), 403(b), 406(a), 407(a), and 408 of the Internal Revenue Code, or included in such total as distributions under the provisions of any retirement or disability plan for employees of any governmental agency or unit, or retirement payments to retired partners, which payments are excluded in computing net earnings from self employment by Section 1402 of the Internal Revenue Code and regulations adopted pursuant thereto. (Emphasis added)

Section 402 of the Internal Revenue Code deals with distributions from employee trusts exempt under Section 401(a) of the Internal Revenue Code, which provides an exemption for certain employee trusts "created or organized in the United States."

Section 403(a) of the Internal Revenue Code deals with annuities described in Section 402(a)(2) of the Internal Revenue Code, which describes certain annuities purchased by employee trusts exempt under Section 401(a) of the Internal Revenue Code.

Section 403(b) of the Internal Revenue Code deals with annuities for employees of exempt organizations.

Sections 406 and 407 of the Internal Revenue Code deal with employee benefit plans under Section 401 that cover overseas employees of affiliates of the employer that created the plan.

Section 408 of the Internal Revenue Code deals with individual retirement accounts.

None of these provisions appear to apply to a retirement plan of a private employer in Germany, and the pension income would therefore not qualify for subtraction under IITA Section 203(a)(2)(F).

Your letter indicates that your pension income is covered under Article VIII of the Protocol Amending the Convention between the United States of America and the Federal Republic of Germany. Article VIII of the Protocol amends Article 18 of the Convention as described in your letter. However, it appears that your pension income is actually governed under Article IX of the Protocol, which added new Article 18A to the Convention. The Department of the Treasury Technical Explanation of the Protocol Signed at Berlin on June 1, 2006 Amending the Convention between United States of America and the Federal Republic of Germany, states, in part:

Paragraph 4 defines the term “pension plan” for purposes of Article 18A to mean an arrangement established in a Contracting State which is operated principally to administer or provide pension or retirement benefits or to earn income for the benefit of one or more such arrangements. ... In the case of the Federal Republic of Germany, clause (a)(bb) of paragraph 16 of Article XVI of the Protocol provides that the term “pension plan” shall include arrangements under section 1 of the German law on employment related pensions (*Betriebsrentengesetz*) and any identical or substantially similar plans established pursuant to legislation enacted after the date of signature of this Protocol.

Pension plans under *Betriebsrentengesetz* are subject to Section 18A of the Convention. Paragraph 1 of Section 18A of the Convention states that if a resident of a Contracting State participates in a pension plan established in the other Contracting State, the State of residence will not tax the income of the pension plan with respect to that resident until a distribution is made from the pension plan. Assuming, *arguendo*, that treaty language may determine application of the subtraction modification under IITA Sections 203(a)(2)(F) or 203(a)(2)(L), the Convention does not treat your pension income as included in gross income under Internal Revenue Code Sections 402(a), 402(c), 403(a), 403(b), 406(a), 407(a), or 408, or under Internal Revenue Code Section 86.

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 regarding this letter, you may contact me at (217) 782-2844.

Sincerely,

Brian L. Stocker
Associate Counsel (Income Tax)