

General Information Letter: Activities described in the request are not protected activities under Public Law 86-272.

July 3, 2008

Dear:

This is in response to your letter dated April 29, 2008 in which you request a letter ruling. The following is in response to your request with respect to Illinois income tax. Your request with respect to sales and excise tax has been referred to the Sales Tax Division and will be addressed by a separate ruling. The nature of your request and the information provided requires 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 2 Ill. Adm. Code § 1200.120(b) and (c), which may be accessed from the Department's web site at www.Iltax.com.

Your letter states as follows:

We are writing this letter on behalf of a client ("TX CLIENT") to determine their responsibility to collect, remit, and file sales, use, income, property, or other state and local tax. Below is a summary of TX CLIENT's business activities and the scope of those activities within ILLINOIS. Furthermore, we have included specific questions on ILLINOIS' nexus requirements and request a preliminary review on the nexus status of TX CLIENT or, if not feasible, any guidance TX CLIENT can use to assess nexus and their responsibility.

General Description of TX CLIENT Business Activity

TX CLIENT manufactures and sells tangible personal property (T.P.P.) as both a retailer and a wholesaler. The T.P.P. is used in, but not limited to, the Commercial Carrier, INDUSTRIES. The T.P.P. is a rotating high pressure nozzle used to clean the inside of tanks, railcars, containers, trailers, and vessels that carry beverages, food, oils, fuels, liquids, polymers, and other chemicals that may be hazardous or regulated. TX CLIENT ships this product throughout the world from their manufacturing plant in CITY, Texas. Their customer base consists of distributors, manufacturers, leasing companies, contractors, service providers, and end users.

The product has a life cycle between 1 month to 2 years depending on the operating conditions and hours of usage. It is usually attached to other T.P.P. that delivers the cleaning agent to the nozzle and attaches the assembled device to the property cleaned. In some cases, the product is combined with other T.P.P. and is permanently attached to real property.

TX CLIENT Business Activity in Illinois

TX CLIENT ships all product into ILLINOIS using a third party common carrier. TX CLIENT does not have any outlets, facilities, related companies, or Passive Investment Companies (P.I.C.) physically located in the state. TX CLIENT does not solicit orders in the state using a salesperson or other representative. Instead, orders are solicited through telephone, email, and/or the company's website. All orders are placed and accepted through telephone, fax, or email at the office address in Texas.

Current Interpretation of Nexus Requirements

Disregarding specific guidance from a state, we recommend that all clients assess nexus using the guidelines developed by the Supreme Court in Quill Corp. v. North Dakota ("Quill") with reference to Complete Auto Transit, Inc. v. Brady, National Bellas Hess, Inc. v. Department of Revenue of Ill., and decisions from other cases upheld in part or full.

Considering the business activities of TX CLIENT, our initial assessment of nexus with ILLINOIS is based on the following:

a. The bright line test of Bellas Hess (further upheld in Quill) which created a safe harbor for vendors "whose only connection with customers in the taxing State is by common carrier or the United States Mail." Under Bellas Hess, such vendors are free from state imposed duties to collect sales and use taxes.

Nexus Questions

1. Considering the business activities of TX CLIENT, do you concur with the conclusion in a.) above that TX CLIENT is not required to collect sales or use tax in ILLINOIS (nexus not established)?

2. Is it possible for an entity without nexus for sales and use tax to establish nexus in one of the other state taxes? If so, which tax is involved? If so, which activities establish nexus?

3. If an entity is not required to collect sales or use tax, can that entity volunteer to collect sales or use tax without exposing it to the associated liability for not collecting the correct amount of tax?

4. Assuming the business activities of TX CLIENT changes, would the solicitation or acceptance of sales within the state by a traveling salesperson establish nexus? If so, is the determination affected by the number of visits or time that a salesperson spends in the state? If so, what is the cutoff for determining nexus?

5. Assuming the business activities of TX CLIENT changes, would the mailing of marketing materials to customers within the state establish nexus? If so, is the determination affected by the quantity of marketing materials shipped or the number of times materials are shipped into the state? If so, what is the cutoff for determining nexus? If so, does it make a difference that marketing materials are only shipped to existing customers and not in connection with a mass mailing solicitation?

6. Assuming the business activities of TX CLIENT changes, would the rental of T.P.P. within the state under an operating lease establish nexus? If so, is the determination affected by the term of the lease? If so, what is the cutoff for determining nexus?

7. Assuming the business activities of TX CLIENT changes, would the rental of T.P.P. within the state under a capital lease (purchase lease) establish nexus? If so, is the determination affected by the term of the lease? If so, what is the cutoff for determining nexus?

Any other guidance you can provide on determining nexus in Illinois would be appreciated.

RULING

The determination whether a taxpayer has nexus with Illinois is extremely fact-specific. Therefore, the Department does not issue rulings regarding whether a taxpayer has nexus with the State. However, the following general information may be provided.

The United States Constitution restricts a state's power to subject to income tax foreign corporations and other nonresidents. The Due Process Clause requires that there exist some minimum connection between a state and the person, property, or transaction the state seeks to tax. (*Quill Corp. v. N. Dakota*, 504 U.S. 298 (1992)) The Commerce Clause requires that a state's tax be applied only to activities with a substantial nexus to the taxing state. (*Id.*) In addition, a state's tax jurisdiction may be limited under Public Law 86-272 (15 U.S.C. § 381). Public Law 86-272 precludes a state from subjecting a nondomiciliary corporation to a net income tax where such corporation's only activities within the state for the taxable year consist of solicitation activities for sales of tangible personal property.

Section 502(a) of the Illinois Income Tax Act ("IITA" ; 35 ILCS 5/502(a)) sets forth the requirements for filing Illinois income tax returns. That section states in pertinent part as follows:

- (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 corporation 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 (regardless of whether it is liable for Illinois tax).

In regards to your particular nexus questions, based on the facts set forth in your letter it appears that TX CLIENT's activities in Illinois fall within the protection afforded under P.L. 86-272. Accordingly, TX CLIENT would not be subject to Illinois income tax, and therefore would not be required to file an Illinois income tax return unless it is a corporation qualified to do business in Illinois. As to the various assumed changes to TX CLIENT's business activities described in your letter, Department Regulations Section 100.9720(c)(2)(A) states:

If a nonresident taxpayer's activities exceed "mere solicitation" as set forth in subsection (a) of PL 86-272 (subsection (c)(1)(A) of this Section), it obtains no immunity under that federal statute. The taxpayer is subject to Illinois income tax and personal property tax replacement income tax for the entire taxable year and its business income is apportioned under IITA Section 304. Whether a nonresident taxpayer's conduct exceeds "mere solicitation" depends upon the facts in each particular case.

Regulations Section 100.9720(c)(4) contains a list of activities that are considered to be beyond "mere solicitation" for purposes of P.L. 86-272. Included in that list of unprotected activities are the

following:

(H) Approving or accepting orders

...

(O) Owning, leasing, or maintaining any of the following facilities or property in-state:

(i) Repair shop.

(ii) Parts department.

(iii) Any kind of office other than an in-home office as described as permitted under subsections (c)(4)(Q) and (c)(5)(B).

(iv) Warehouse.

(v) Meeting place for directors, officers, or employees.

(vi) Stock of goods other than samples for sales personnel or that are used entirely ancillary to solicitation.

(vii) Telephone answering service that is publicly attributed to the nonresident or to an employee or agent of the nonresident in his or her representative status.

(viii) Mobile stores, i.e. vehicles with drivers who are sales personnel making sales from the vehicles.

(ix) Real property or fixtures to real property of any kind.

A taxpayer that engages in unprotected activity within Illinois, unless such activity is de minimus, is not entitled to immunity under the federal statute. Regulations Section 100.9720(c)(2)(D) sets forth the test for determining whether unprotected activities are de minimus.

De minimus activities are those that, when taken together, establish only a trivial additional connection with this State. An activity regularly conducted within this State on a regular or systematic basis or pursuant to a company policy (whether such policy is in writing or not) shall normally not be considered trivial. Whether an activity consists of a trivial or non-trivial additional connection with this State is to be measured on both a qualitative and quantitative basis. If the activity either qualitatively or quantitatively creates a non-trivial connection with this State, then the activity exceeds the protection of PL 86-272. The amount of unprotected activities conducted within this State relative to the amount of protected activities conducted within this State is not determinative of the issue of whether the unprotected activities are de minimus. The determination of whether an unprotected activity creates a non-trivial connection with this State is made on the basis of the taxpayer's entire business activity, not merely its activities conducted within this State. An unprotected activity that would not be de minimus if it were the only business activity of the taxpayer conducted in this State will not be de minimus merely because the taxpayer also conducts a substantial amount of protected activities within this State, nor will an unprotected activity that would be de minimus if conducted in conjunction with a substantial amount of protected activities fail to be de minimus merely because no protected activities are conducted in this State.

Regulations Section 100.9720(c)(5) contains a list of activities that are considered protected activities under P.L. 86-272. Included on that list of protected activities is the following:

A) Soliciting orders for sales by any type of advertising.

...

M) Owning, leasing, using or maintaining personal property for use in the employee's or representative's "in-home" office located within the residence of the employee or other representative that is not publicly attributed to the nonresident or to the employee or other representative of the nonresident in a representative capacity or automobile, when that use is solely limited to the conducting of protected activities. Therefore, the use of personal property such as a cellular telephone, facsimile machine, duplicating equipment, personal computer and computer software, shall not, by itself, remove the protection under this Section, so long as the use of the office is limited to:

(i) soliciting and receiving orders from customers;

(ii) transmitting orders outside the State for acceptance or rejection by the nonresident;

or

(iii) other activities that are protected under PL 86-227 or this Section.

Applying the above provisions to the assumed changed business activities described in your letter, accepting orders within Illinois constitutes an unprotected activity that, unless de minimus, results in loss of immunity under P.L. 86-272. Similarly, the use by a taxpayer of leased tangible personal property within Illinois, unless such use is either de minimus or limited to the solicitation of orders or other protected activities, results in the loss of immunity under P.L. 86-272. On the other hand, the mailing of marketing materials into Illinois is a protected activity that will not result in the loss of immunity under P.L. 86-272.

Finally, note that Regulations Section 100.9720(e) states:

U.S. Constitutional Jurisprudence. If not protected by U.S. or Illinois statute, an income-producing activity may, nonetheless, be protected from State taxation by principles of U.S. Constitutional jurisprudence. Controlling decisions that assert protections afforded by the Interstate Commerce Clause, the Foreign Commerce Clause and the Due Process Clause are accepted by this State as limitations on the reach of its income tax and personal property tax replacement income tax statutes. However, nothing stated in this subsection (e) shall prevent Illinois from challenging taxpayer assertions of U.S. Constitutional protection.

As stated above, this is a GIL. A GIL does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department.

Sincerely,

Brian L. Stocker
Associate Counsel (Income Tax)