

Private Letter Ruling: The commercial domicile of a qualified settlement fund is at the location of the court creating and administering the fund.

July 10, 2008

Dear:

This is in response to your letter dated April 4, 2007, in which you request a Private Letter Ruling on behalf of the qualified settlement fund formed in connection with CASE – Case No. X-XX-XX-XXXXX, TIN XX-XXXXXXX (the “Qualified Settlement Fund”). Review of your request for a Private Letter Ruling disclosed that all information described in paragraphs 1 through 8 of subsection (b) of 2 Ill. Adm. Code Section 1200.110 appears to be contained in your request. The Private Letter Ruling will bind the Department only with respect to the Qualified Settlement Fund for the issue or issues presented in this ruling. Issuance of this ruling is conditioned upon the understanding that neither the Qualified Settlement Fund nor a party related to the Qualified Settlement Fund is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request.

The facts and analysis as you have presented them are as follows:

CASE – Case No. X-XX-XX-XXXXX (“Taxpayer”) is a qualified settlement fund (“QSF”), as that term is defined in Internal Revenue Code (“IRC”) section 468B(g) and the Treasury Regulations (“Reg.”) promulgated thereunder, section 1.468B-1 *et seq.*

The QSF Taxpayer was established after the United States Securities and Exchange Commission (“SEC”) litigated an enforcement action against Mr. Z, *et al.*, in the United States District court for the northern District of Illinois (CASE, *et al.*, Case No. XX X XXXX). Pursuant to an order of the aforementioned court (“Court”) entering Final Judgment as to Defendant Mr. Y (attached for your reference as Exhibit A), the defendant, Mr. Y, paid a total of \$809,159 in disgorgement, prejudgment interest and civil penalties. The funds were deposited into an interest-bearing account with the Court Registry Investment System (“CRIS”) of the Court. For Federal income tax purposes, the earned interest is taxable pursuant to IRC section 468B(g) and the aforementioned Treasury Regulations. Accordingly, Taxpayer has filed IRS Form 1120-SF reporting such income.

On MONTH DAY, 2005, the Court entered an Order (attached for your reference as Exhibit B) in which the Court approved the appointment of ACCOUNTING FIRM, a certified public accounting firm in CITY, California, to provide tax administrator services to the fund, including, but not limited to, filing applicable estate tax returns and paying taxes reported thereon out of the Settlement Fund.

### **RULINGS REQUESTED**

The Taxpayer requests the following rulings:

1. The QSF Taxpayer is an entity subject to Illinois Corporate Income Tax.
2. The domicile of the QSF Taxpayer is determined by reference to the location of the fund administrator; therefore, Taxpayer is not subject to Illinois tax because the fund administrator is located in California.

## **STATEMENT OF LAW**

Pursuant to General Information Letters IT 99-0051-GIL and IT 03-0011-GIL (attached for your reference as Exhibit C), obtained in response to an inquiry submitted by the Tax Administrator, qualified settlement funds are subject to Illinois Corporate Income Tax and their domicile is determined, generally, by reference to the location of the fund administrator.<sup>1</sup>

## **ANALYSIS**

### **Ruling Request #1**

Pursuant to General Information Letters ("GIL") IT 99-0051-GIL and IT 03-0011-GIL, the Taxpayer believes, assuming it is domiciled in Illinois (see Ruling request #2, below), it is an entity subject to Illinois Corporate Income Tax.

### **Ruling Request #2**

GIL IT 99-0051-GIL provides:

For purposes of domicile, the QSF would have its domicile wherever someone was managing it. Most likely, this would be location of the fund administrator who would be keeping the books for the QSF. This, in general would be the main criteria for domicile.

Because the Taxpayer believes that the above-referenced language in GIL IT 99-0051-GIL is vague with respect to Illinois' criteria for determining the domicile of a QSF, Taxpayer seeks guidance from the Department.

If Taxpayer mechanically applies the criteria set forth in GIL IT 99-0051-GIL to determine its domicile, the Taxpayer believes that it is not domiciled in Illinois because the Tax Administrator is located in CITY, California. Consequently, under such analysis, Taxpayer believes it would not be subject to Illinois taxation.

However, pursuant to Treasury Regulation Section 1.468B-1(c)(1), a QSF is established by order or approval of the court that has continuing jurisdiction over the QSF. Consequently, although an "administrator" of a QSF (here, the Tax Administrator) is responsible for discharging the tax related obligations of the QSF (see Treasury Regulation § 1.468B-2(k)), a QSF, by definition, is subject to the jurisdiction, or "management," of the court that established it.

Indeed, in order to carry out its duties, the Tax Administrator, upon determining the Taxpayer's tax liability, must notify the SEC attorney who litigated the case of such liability. In turn, the SEC attorney must motion the Court requesting that the Court enter an order approving disbursement of funds by the Clerk of Court to pay the tax liability. Only if and when the Court enters such order does the Tax Administrator have the ability to discharge its duties. Furthermore, the Tax Administrator was appointed, and may be removed, by the Court. The Taxpayer, accordingly, believes that it is "managed" by the above-referenced Court and that the location of the court is the

appropriate criterion to reference to determine the domicile of a QSF.<sup>2</sup>

### **PROCEDURAL REQUIREMENTS**

Pursuant to Regulation § 1200.110(b)(4), to the best knowledge of the Taxpayer and the Taxpayer's representatives, the Department has not previously ruled on the same or a similar issue for the Taxpayer or a predecessor, nor has the Taxpayer or the Taxpayer's representatives previously submitted the same or a similar issue to the Department but withdrew it before a letter ruling was issued.

Pursuant to Regulation § 1200.110(b)(6), The Taxpayer has determined that there are no authorities contrary to its views, or Taxpayer is unable to locate such authority.

### **Ruling of the Department**

Section 1501(a)(4) of the Illinois Income Tax Act (35 ILCS 5/1501) provides:

The term "corporation" includes associations, joint-stock companies, insurance companies and cooperatives. Any entity, including a limited liability company formed under the Illinois Limited Liability Company Act, shall be treated as a corporation if it is so classified for federal income tax purposes.

Section 468B(b)(5) of the Internal Revenue Code provides:

For purposes of subtitle F [Procedure and Administration] -

(A) a designated settlement fund shall be treated as a corporation, and

(B) any tax imposed by this subsection shall be treated as a tax imposed by section 11 [imposing tax on corporations].

Accordingly, the Qualified Settlement Fund is treated as a corporation for Illinois income tax purposes.

Section 301(c)(2) of the Illinois Income Tax Act (35 ILCS 5/301) provides:

Any item of income or deduction which was taken into account in the computation of base income for the taxable year by any person other than a resident and which is not otherwise specifically allocated or apportioned pursuant to Section 302, 303 or 304 (including, without limitation, interest, dividends, items of income taken into account under the provisions of Sections 401 through 425 of the Internal Revenue Code, and benefit payments received by a beneficiary of a supplemental unemployment benefit trust which is referred to in Section 501(c)(17) of the Internal Revenue Code):

(A) in the case of an individual, trust or estate, shall not be allocated to this State; and

(B) in the case of a corporation or a partnership, shall be allocated to this State if the taxpayer had its commercial domicile in this State at the time such item was paid, incurred or accrued.

Section 302 of the Illinois Income Tax Act (35 ILCS 5/302) allocates employee compensation. Section 303 of the Illinois Income Tax Act (35 ILCS 5/303) allocates nonbusiness income, but has no provisions for interest income. Section 304(a) of the Illinois Income Tax Act (35 ILCS 5/304) provides, in part:

The business income of a person other than a resident shall be allocated to this State if such person's business income is derived solely from this State.

Section 1501(a)(2) of the Illinois Income Tax Act provides:

The term "commercial domicile" means the principal place from which the trade or business of the taxpayer is directed or managed.

The MONTH DAY, 2004, order of the United States District Court for the Northern District of Illinois states that the funds comprising the Qualified Settlement Fund shall be deposited by the clerk of the court "into an interest bearing account with the Court Registry Investment System." The clerk is also directed to collect a fee equal to 10% of the income earned on the funds. Pursuant to the order, disbursements may be made from the Qualified Settlement Fund only upon a motion by the Securities and Exchange Commission that has been approved by the court.

Based on these facts, the principal place from which the trade or business of the Qualified Settlement Fund is directed or managed is the United States District Court for the Northern District of Illinois. No source of income outside Illinois is identified. Accordingly, any interest income earned from the Court Registry Investment System will be allocated to Illinois under Section 301(c)(2) of the Illinois Income Tax Act if it is nonbusiness income or under Section 304(a) of the Illinois Income Tax Act if it is business income.

The factual representations upon which this ruling is based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the factual representations recited in this ruling are correct and complete. This Private Letter Ruling is revoked and will cease to bind the Department 10 years after the date of this letter under the provisions of 2 Ill. Adm. Code 1200.110(e) or earlier if there is a pertinent change in statutory law, case law, rules or in the factual representations recited in this ruling.

If you have questions concerning this Private Letter Ruling, you may contact me at (217) 782-2844. If you have further questions related to the Illinois sales tax laws, please visit our website at [www.tax.illinois.gov](http://www.tax.illinois.gov) or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Terry D. Charlton  
Chairman, Private Letter Ruling Committee

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<sup>1</sup> This inquiry was not related to a specific taxpayer, including the instant Taxpayer. Taxpayer seeks the instant Private Letter Ruling because it understands that GILs do *not* constitute statements of agency policy that apply, interpret or prescribe the tax laws and are not binding on the Department.

<sup>2</sup> Although some courts may not be as active in the “management” of a QSF, a QSF (as previously discussed) is *a/ways* subject to the continuing jurisdiction of the court that established it. Therefore, Taxpayer believes that the location of the court is *a/ways* the appropriate criterion to reference to determine a Use’s domicile for purposes of Illinois Taxation.