

General Information Letter: Wages paid to an employee performing services within and without Illinois are allocable to Illinois if the employee's base of operations is in Illinois or, if the employee has no base of operations, if his services are directed or controlled from a place in Illinois.

January 14, 2009

Dear:

This is in response to your letter dated December 12, 2008 in which you request information regarding the taxation of certain compensation. The nature of your request and the information you have 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 at [www.revenue.state.il.us](http://www.revenue.state.il.us).

In your letter you have stated the following:

I am trying to determine if an employee's wages are subject to Illinois Income Taxes. Following are the facts:

1. The employee is a resident of Washington.
2. The employee performs services in various states.
3. The employer's office is located in Illinois and the employee is instructed from this location of where the services are to be performed.
4. The employee performs no more than 5% of the services in Illinois (it will vary from year to year).
5. The services he performs in Illinois do not have any relationship to the services he performs in the other states.

Does this maximum of 5% of services performed in Illinois qualify as significant and not incidental enough to classify his income as being earned in Illinois? If not, would the 5% be taxable in Illinois?

## **RULING**

Section 302(a) of the Illinois Income Tax Act ("IITA"; 35 ILCS 5/302(a)) states:

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.

IITA Section 304(a)(2)(B) states:

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.

In applying IITA Section 304(a)(2)(B), Department Regulations § 100.7010(a)(3) (86 Ill. Adm. Code 100.7010(a)(3)) states that the rules set forth therein "are to be applied in such manner that, if they were in effect in other states, an item of compensation would constitute 'compensation paid in' only one state. Thus, if an item would, under these rules, constitute compensation paid in a state other than Illinois because the individual's service was localized in such other state under the tests of [section 304(a)(2)(B)], it could not also be compensation paid in Illinois." In addition, Department Regulations § 100.7010(c)(1) states that if compensation is paid in Illinois because the service is localized in Illinois under either Section 304(a)(2)(B)(i) or (ii), the factors set forth in Section 304(a)(2)(B)(iii) are not considered. Therefore, in order to determine whether compensation of a nonresident employee is taxable in Illinois, it must first be determined whether the employee's services are localized in Illinois or another state. Where the services are localized in Illinois the compensation is allocated to Illinois, and where the services are localized in another state the compensation is not allocated to Illinois. If, on the other hand, the employee's services are not localized in any state under the tests set forth in Section 304(a)(2)(B)(i) or (ii), then whether or not the compensation is taxable in Illinois depends upon the location of the employee's base of operations or the place from which the employee is directed or controlled as set forth under Section 304(a)(2)(B)(iii).

In this case, the facts set forth in your letter suggest that the employee's services are not localized in any state. Your letter indicates that the employee performs services in various states, that no more than 5% of the services are performed in Illinois with the exact amount varying from year to year, and that the services performed in Illinois do not bear any relationship to the services performed in other states. Department Regulations § 100.7010(c)(2) states that for purposes of determining whether services performed in one state are incidental to services performed in another, the term "incidental" refers to any service which is necessary to or supportive of the primary service performed by the employee or which is temporary or transitory in nature or consists of isolated transactions. In addition, Regulations § 100.7010(c)(3) states that the amount of time spent or the amount of services performed in a state is not decisive in itself of the question whether services in a state are incidental to services in another state. To this point, the regulations provide the following example:

[A is a resident of State X and a salesman for the B corporation, located in State X.] A's regular territory covers several counties in Illinois and one or two towns in State X. A goes to the State X towns on a regular basis even though more than 95% of his time and sales are with reference to his Illinois territory. The compensation for service which A performs in Illinois and State X is not localized in Illinois within the meaning of subsection (a)(2) because the service performed in State X is regular and permanent in nature and is not necessary to or supportive of sales made in Illinois.

Your letter indicates that the employee performs varying amounts of service in Illinois each year as well as other states, and that the services performed in Illinois do not have any relationship to the

services performed in the other states. Under these facts, it cannot be concluded that the services performed in Illinois are merely incidental to the services performed in other states. As the example illustrates, even assuming that 95% of the employee's services are performed in another state, because the services performed in Illinois are regular and permanent in nature and independent of the services performed outside of Illinois, the Illinois services are not merely incidental to the services performed outside of Illinois. Accordingly, it does not appear from the facts you have provided that the employee's services may be considered localized in any state.

Department Regulations § 100.7010(d)(1) states:

The localization tests are not applicable where an individual's employment normally or continually includes service within this State and also services without the State which are not "incidental" to the services performed within this State. In such case, if the individual's base of operations is within this State, his entire compensation will be [taxable], but if his base of operations is without this State, none of his compensation will be [taxable].

Regarding an employee's base of operations, Regulations § 100.7010(d)(2) states:

The term "base of operations" refers to the place or fixed center from which the individual works. An individual's base of operations may be his business office (which may be maintained in his home), or his contract of employment may specify a place at which the employee is to receive his directions and instructions. In the absence of more controlling factors, an individual's base of operations may be the place to which he has his business mail, supplies, and equipment sent or the place where he maintains his business records.

Regarding the place of direction or control, Regulations § 100.7010(e)(1) states:

The permanent place from which the employee's service is directed or controlled is relevant in determining whether wages are subject to withholding if the localization tests are not applicable and it is impossible to determine the base of operation for such individual. In such a case, if both the place from which the individual's service is directed or controlled is within this State, and some of the service is performed within this State, then his entire compensation will be [taxable], but if not, none of his compensation will be [taxable]. For example, a salesman's territory may be so indefinite and so widespread that he will not retain any fixed business office or address but will receive his orders or instructions by mail or wire wherever he may happen to be. In such case, the location of the permanent place from which direction and control is exercised must be determined.

In this case, you have indicated that the employer's office is located in Illinois and that the employee is instructed from this location. Therefore, unless the employee's base of operations is outside of Illinois, the employee's entire compensation is allocated to Illinois and subject to Illinois income tax.

As stated above, this is a GIL 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 one through eight of 86 Ill. Adm. Code 1200.110(b). If you have additional questions regarding this GIL, you may contact me at (217) 782-7055.

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Sincerely,

Brian L. Stocker  
Staff Attorney (Income Tax)