

General Information Letter: Application of 80-20 test to corporation governed by federal income tax treaty.

August 11, 1998

Dear:

This is in response to your letter dated July 23, 1998, in which you request a General Information Letter. 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 on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. GILs do not constitute statements of agency policy that apply, interpret or prescribe the tax laws and are not binding on the Department. For your general information we have enclosed a copy of 2 Ill. Adm. Code Part 1200 regarding rulings and other information issued by the Department.

Although you have not specifically requested either type of ruling, the information you have provided requires that we respond with a general information letter.

In your request you stated:

I represent two entities with corporate income tax nexus in the state of Illinois. Both entities are controlled by the same German corporation.

Entity A is a New York State Corporation. Its parent company is in Germany and it is a wholly owned (100%) subsidiary of this German parent company. Entity A has nexus in the state of Illinois because it has an employee and office rent in Illinois. Entity A will have a three factor Illinois allocation of about 3.25%. Entity A files Form 1120 for purposes of the Internal Revenue Service and is not part of any consolidated tax return or federal affiliated group.

Entity B is a German Corporation registered to do business in the state of Illinois. Entity B files Form 1120F with a 6114 Disclosure Statement for Federal purposes stating that is immune from IRS tax because it has an office and three employees in Illinois. This German corporation doing business in Illinois is a subsidiary of the parent company located in Germany of Entity A. Entity B has an Illinois allocation of 0.01%.

Thus, Entity A and Entity B have the same German Parent company. Entity A and Entity B share an office in Illinois. Entity A and Entity B have no intercompany sales. The president of Entity A is located at the corporation headquarters of Entity A in New York State. The president of Entity B is located in Germany.

The question is if Entity A and Entity B form an Illinois unitary group. If so, is an Illinois combined report needed? Keep in mind that Entity B is not a United States taxpayer and has over 99% of its activity outside the United States.

#### Department Analysis

For Illinois income tax purposes, combined reporting is required when two or more persons [i.e. businesses] are engaged in a unitary business as described in section 1527(a)(27) of the Illinois Income Tax Act ("IITA"). Section 1527(a)(27) defines a unitary business as:

a group of persons related through common ownership whose business activities are integrated with, dependent upon and contribute to each other. The group will not include those members whose business activity outside the United States is 80% or more of any such member's total business activity; for purposes of this paragraph and clause (a) (3) (B) (ii) of Section 304, business activity within the United States shall be measured by means of the factors ordinarily applicable under subsections (a), (b), (c), and (d) of Section 304 except that, in the case of members ordinarily required to apportion business income by means of the 3 factor formula of property, payroll and sales specified in subsection (a) of Section 304, such members shall not use the sales factor in the computation and the results of the property and payroll factor computations shall be divided by 2 (by one if either the property or payroll factor has a denominator of zero).

35 ILCS §1527(a)(27) (full text enclosed)

In your letter you stated that Entity B has over 99% of its activity outside of the United States. If this is true for IITA purposes then Entity B would not be counted towards the establishment of a unitary business in Illinois. The determination of how to compute the 80% figure for total business activity out of the country is spelled out in 86 Illinois Administrative Code §100.9700 (copy enclosed). Therefore, assuming no other entities besides Entity A exist in Illinois, a unitary business would not exist and no consolidated return would be needed.

I hope that this has been helpful to you. If you have additional questions please feel free to contact me at the above address.

Sincerely,

Charles E. Matoesian  
Associate Attorney (Income Tax)