This rulemaking should also repeal Table A and Table B.

Section 100.3370 Sales Factor (IITA Section 304)

a) In general.

1) IITA Section 1501(a)(21) defines the term "sales" to mean all gross receipts of the person not allocated under IITA Sections 301, 302 and 303. Thus, for the purposes of the sales factor of the apportionment formula for each trade or business of the person, the term "sales" means all gross receipts derived by the person from transactions and activity in the regular course of his or her trade or business. The following are rules for determining "sales" in various situations, except in instances in which an alternative method of determining the sales factor is prescribed in Section 100.3380. If the determination prescribed by this section does not clearly reflect the taxpayer's business activities in Illinois (for taxable years ending before December 31, 2008) or the market for the taxpayer's goods, services or other sources of income in Illinois (for taxable years ending on or after December 31, 2008), the taxpayer may request the use of an alternative method of apportionment under Section 100.3390.

A) In the case of a person engaged in manufacturing and selling or purchasing and reselling goods or products, "sales" includes all gross receipts from the sales of those goods or products (or other property of a kind which would properly be included in the inventory of the person if on hand at the close of the tax period) held by the person primarily for sale to customers in the ordinary course of its trade or business. Gross receipts for this purpose means gross sales less returns and allowances, and includes all interest income, service charges, carrying charges, or time-price differential charges attendant to those sales. Federal and state excise taxes (including sales taxes) shall be included as part of the receipts if the taxes are passed on to the buyer or included as part of the selling price of the product.

B) In the case of cost plus fixed fee contracts, such as the operation of a government-owned plant for a fee, "sales" includes the entire reimbursed cost, plus the fee.

C) In the case of a person engaged in providing services, such as the operation of an advertising agency, or the performance of equipment service contracts, or research and development contracts, "sales" includes the gross receipts from the performance of those services, including fees, commissions and similar items.

D) In the case of a person engaged in renting real or tangible property, "sales" includes the gross receipts from the rental, lease or licensing of the use of the property.

E) In the case of a person engaged in the sale, assignment or licensing of intangible personal property such as patents and copyrights, "sales" includes the gross receipts therefrom.

F) If a person derives receipts from the sale of equipment used in its business, those receipts constitute "sales". For example, a truck express company owns a fleet of trucks and sells its trucks under a regular replacement program. The gross receipts from the sales of the trucks are included in the sales factor.

2) The following gross receipts are not included in the sales factor:

A) For taxable years ending on or after December 31, 1995, *dividends; amounts included under 26 USC 78; and Subpart F income* are excluded from the sales factor under IITA Section 304(a)(3)(D).

B) Gross receipts that are excluded from or deducted in the computation of federal taxable income or federal adjusted gross income, and that are not added back in the computation of base income. For example, in years ending prior to December 31, 1995, dividends received from a domestic corporation are excluded from the sales factor to the extent the taxpayer is allowed a deduction under 26 USC 243 with respect to those dividends.

C) Gross receipts that are subtracted from federal taxable income or federal adjusted gross income in the computation of base income or that are eliminated in the computation of taxable income in the case of a unitary business group under Section 100.5270(b)(1). Examples of gross receipts excluded from the sales factor under this provision include:

i) Interest on federal obligations subtracted under IITA Section 203(a)(2)(N), (b)(2)(J), (c)(2)(K) or (d)(2)(G).

ii) For taxable years ending prior to December 31, 1995, dividends included in federal taxable income or federal adjusted gross income are excluded from the sales factor if eliminated in combination or to the extent subtracted under IITA Section 203(a)(2)(J), (a)(2)(K), (b)(2)(K), (b)(2)(L), (b)(2)(O), (c)(2)(M), (c)(2)(O), (d)(2)(K) or (d)(2)(M).

D) Gross receipts that are excluded from or deducted in the computation of federal taxable income or federal adjusted gross income, but are added back in the computation of base income, are included in the sales factor unless subtracted or eliminated in combination. For example:

i) Interest on state obligations excluded from federal taxable income or adjusted gross income under 26 USC 103 and added back in the computation of base income under IITA Section 203(a)(2)(A), (b)(2)(A), (c)(2)(A) or (d)(2)(A) is included in the sales factor except in the case of interest on certain Illinois obligations that is exempt from Illinois Income Tax. (See 86 Ill. Adm. Code 100.2470(f).)

ii) Gross receipts from intercompany transactions between two corporate members of a federal consolidated group, the taxable income on which is deferred under 26 CFR 1.1502-13, will be included in the sales factor of the recipient unless subtracted under a provision of IITA Section 203 or eliminated in combination of the two corporations as members of a unitary business group.

E) In some cases certain gross receipts should be disregarded in determining the sales factor in order that the apportionment formula will operate fairly to apportion to this State the income of the person's trade or business. (See 86 Ill. Adm. Code 100.3380(c).)

F) For taxable years ending on or after December 31, 1999, *gross receipts from the licensing, sale, or other disposition of a patent, copyright, trademark, or similar item of intangible personal property may be included in the sales factor only if gross receipts from licenses, sales, or other dispositions of these items comprise more than 50% of the taxpayer's total gross receipts included in gross income during the tax year and during each of the 2 immediately preceding tax years; provided that, when a taxpayer is a member of a unitary business group, the determination shall be made on the basis of the gross receipts of the entire unitary business group*. (IITA Section 304(a)(3)(B-2) For purposes of this Section:

i) "Gross receipts from the licensing, sale, or other disposition of a patent, copyright, trademark, or similar item of intangible personal property" include amounts received as damages or settlements from claims of infringement.

ii) "Gross receipts from the licensing, sale, or other disposition of a patent" include only amounts received from a person using the patent in the production, fabrication, manufacturing, or other processing of a product or from a person producing, fabricating or manufacturing a product subject to the patent.

iii) "Gross receipts from the licensing, sale, or other disposition of a copyright" include only amounts received by the taxpayer from a person engaged in printing or other publication of the material protected by the copyright, which are governed by Section 100.3373. The term does not include gross receipts from broadcasting within the meaning of IITA Section 304(a)(3)(B-7) or from publishing or advertising within the meaning of IITA Section 304(a)(3)(C-5)(iv).

iv) If a taxpayer has been in existence less than three taxable years, its gross receipts from the licensing, sale, or other disposition of patents, copyrights, trademarks or similar items of intangible personal property will be included in its sales factor if those gross receipts comprise more than 50% of its total gross receipts during each taxable year of its existence.

v) "Patent" means a patent issued under 35 USC 151.

vi) "Copyright" means a copyright registered or eligible for registration under 17 USC 408.

vii) "Trademark" means a trademark registered or eligible for registration under 15 USC 1051.

viii) A "similar item" means an item of intellectual property that is registered or otherwise enforceable under a law equivalent to 35 USC 151, 17 USC 408 or 15 USC 1051 or that is otherwise recognized in the country under whose law the sale or license agreement would be enforced, or under which an infringement claim would be brought.

ix) In the case of a unitary business group, the total gross receipts and gross receipts from the licensing, sale, or other disposition of a patent, copyright, trademark, or similar item of intangible personal property in the two years immediately preceding the tax year include the gross receipts and gross receipts from the licensing, sale, or other disposition of a patent, copyright, trademark, or similar item of intangible personal property of all persons who are members of the unitary business group at some time during the taxable year, whether or not those persons were also members of the unitary business group in a preceding tax year, and only of those persons.

3) In filing returns with this State, if the person departs from or modifies the basis for excluding or including gross receipts in the sales factor used in returns for prior years, the person shall disclose in the return for the current year the nature and extent of the modification. If the returns or reports filed by the person with all states to which the person reports under Article IV of the Multistate Tax Compact or the Uniform Division of Income for Tax Purposes Act are not uniform in the inclusion or exclusion of gross receipts, the person shall disclose in its return to this State the nature and extent of the variance.

4) For taxable years ending prior to December 31, 2008, sales of electricity are sales other than sales of tangible personal property sourced under IITA Section 304(a)(3)(C). For taxable years ending on or after December 31, 2008, and prior to July 16, 2009, sales of electricity are sales of service sourced under IITA Section 304(a)(3)(C-5)(iv). For taxable years ending after July 15, 2009, sales of electricity are sales of tangible personal property sourced under IITA Section 304(a)(3)(B). (See Exelon Corp. v. Department of Revenue, 234 Ill 2d 266 (2009).)

b) Denominator. The denominator of the sales factor shall include the total gross receipts derived by the person from transactions and activity in the regular course of its trade or business, except receipts excluded under 86 Ill. Adm. Code 100.3380(c).

c) Numerator. The numerator of the sales factor shall include the gross receipts attributable to this State and derived by the person from transactions and activity in the regular course of its trade or business. All interest income, service charges, carrying charges, or time-price differential charges incidental to those gross receipts shall be included regardless of the place where the accounting records are maintained or the location of the contract or other evidence of indebtedness.

1) Sales of Tangible Personal Property in this State

A) Gross receipts from the sales of tangible personal property (except sales to the United States Government) (see subsection (c)(2)) are in this State:

i) if the property is delivered or shipped to a purchaser within this State regardless of the f.o.b. (free on board) point or other conditions of sale; or

ii) if the property is shipped from an office, store, warehouse, factory or other place of storage in this State and the taxpayer is not taxable in the state of the purchaser. However, premises owned or leased by a person who has independently contracted with the taxpayer for the printing of newspapers, periodicals or books shall not be deemed to be an office, store, warehouse, factory or other place of storage.

B) Property shall be deemed to be delivered or shipped to a purchaser within this State if the recipient is located in this State, even though the property is ordered from outside this State.

EXAMPLE: A corporation, with inventory in State A, sold $100,000 of its products to a purchaser having branch stores in several states including this State. The order for the purchase was placed by the purchaser's central purchasing department located in State B. $25,000 of the purchase order was shipped directly to purchaser's branch store in this State. The branch store in this State is the "purchaser within this State" with respect to $25,000 of the corporation's sales.

C) Property is delivered or shipped to a purchaser within this State if the shipment terminates in this State, even though the property is subsequently transferred by the purchaser to another state.

EXAMPLE: A corporation makes a sale to a purchaser who maintains a central warehouse in this State at which all merchandise purchases are received. The purchaser reships the goods to its branch stores in other states for sale. All of the corporation's products shipped to the purchaser's warehouse in this State is property "delivered or shipped to a purchaser within this State".

D) The term "purchaser within this State" shall include the ultimate recipient of the property if the person in this State, at the designation of the purchaser, delivers to or has the property shipped to the ultimate recipient within this State.

EXAMPLE: A corporation in this State sold merchandise to a purchaser in State A. The corporation directed the manufacturer or supplier of the merchandise in State B to ship the merchandise to the purchaser's customer in this State pursuant to purchaser's instructions. The sale by the corporation is "in this State".

E) When property being shipped by a seller from the state of origin to a consignee in another state is diverted while en route to a purchaser in this State, the sales are in this State.

EXAMPLE: Corporation X, a produce grower in State A, begins shipment of perishable produce to the purchaser's place of business in State B. While en route the produce is diverted to the purchaser's place of business in this State in which state Corporation X is subject to tax. The sale by the corporation is attributed to this State.

F) If the person is not taxable in the state of the purchaser, the sale is attributed to this State if the property is shipped from an office, store, warehouse, factory, or other place of storage in this State (subject to the exception noted in (c)(1)(A)(ii)).

EXAMPLE: A corporation has its head office and factory in State A. It maintains a branch office and inventory in this State. The corporation's only activity in State B is the solicitation of orders by a resident salesman. All orders by the State B salesman are sent to the branch office in this State for approval and are filled by shipment from the inventory in this State. Since the corporation is immune under Public Law 86-272 from tax in State B, all sales of merchandise to purchasers in State B are attributed to this State, the state from which the merchandise was shipped.

2) Sales of tangible personal property to the United States Government in this State. Gross receipts from the sales of tangible personal property to the United States Government are in this State if the property is shipped from an office, store, warehouse, factory, or other place of storage in this State. For the purposes of this regulation, only sales for which the United States Government makes direct payment to the seller pursuant to the terms of the contract constitute sales to the United States Government. Thus, as a general rule, sales by a subcontractor to the prime contractor, the party to the contract with the United States Government, do not constitute sales to the United States Government.

A) EXAMPLE A: A corporation contracts with General Services Administration to deliver X number of trucks which were paid for by the United States Government. The sale is a sale to the United States Government.

B) EXAMPLE B: A corporation as a subcontractor to a prime contractor with the National Aeronautics and Space Administration contracts to build a component of a rocket for $1,000,000. The sale by the subcontractor to the prime contractor is not a sale to the United States Government.

3) For taxable years ending on or after December 31, 1999, *gross receipts from the licensing, sale, or other disposition of a patent, copyright, trademark, or similar item of intangible personal property* that are not excluded from the sales factor under subsection (a)(2)(F) are included in the numerator of the sales factor *to the extent the item is utilized in this State during the year the gross receipts are included in gross income*. (IITA Section 304(a)(3)(B-1)) For purposes of this subsection (c)(3):

A) *A patent is utilized in a state to the extent that it is employed in production, fabrication, manufacturing, or other processing in the state or to the extent that a patented product is produced in the state. If a patent is utilized in more than one state, the extent to which it is utilized in any one state shall be a fraction equal to the gross receipts of the licensee or purchaser from sales or leases of items produced, fabricated, manufactured, or processed within that state using the patent and of patented items produced within that state, divided by the total of the gross receipts for all states in which the patent is utilized.* (IITA Section 304(a)(3)(B-1)(ii)(I))

B) *A copyright is utilized in a state to the extent that printing or other publication originates in the state*. Printing or other publication originates at the place at which the licensee of the copyright incorporates the copyrighted material into the physical medium by which it will be delivered to the purchaser of the material or, if the copyrighted material is delivered to the purchaser without use of a physical medium, the place at which delivery of the copyrighted material to the person purchasing the material from the licensee originates. *If a copyright is utilized in more than one state, the extent to which it is utilized in any one state shall be a fraction equal to the gross receipts from sales or licenses of materials printed or published in that state divided by the total of the gross receipts for all states in which the copyright is utilized.* (IITA Section 304(a)(3)(B-1)(ii)(II))

C) *Trademarks and other items of intangible personal property governed by this subsection (c)(3) are utilized in the state in which the commercial domicile of the licensee or purchaser is located.* (IITA Section 304(a)(3)(B-1)(ii)(III))

D) If the place of utilization of an item of property under subsection (c)(3)(A), (B) or (C) *cannot be determined from the taxpayer's books and records or from the books and records of any person related to the taxpayer within the meaning of 26 USC 267(b), the gross receipts attributable to that item shall be excluded from both the numerator and the denominator of the sales factor.* (IITA Section 304(a)(3)(B-1)(iii))

4) *For taxable years ending on or after December 31, 2013, gross receipts from winnings under the Illinois Lottery Law* [20 ILCS 1605] *and from the assignment of a prize under Section 13-1 of the Illinois Lottery Law are received in this State.* (IITA Section 304(a)(3)(B-8))

5) For taxable years ending prior to December 31, 2008, gross receipts from transactions not governed by the provisions of subsection (c)(1), (2), (3) or (4) and, for taxable years ending on or after December 31, 2008, from transactions involving intangible personal property when the taxpayer is not a dealer with respect to the intangible personal property, are attributed to this State if the income producing activity that gave rise to the receipts is performed wholly within this State. Also, gross receipts are attributed to this State if, with respect to a particular item of income, the income producing activity is performed in this State, based on costs of performance.

A) Income Producing Activity Defined. The term "income producing activity" applies to each separate item of income and means the transactions and activity directly engaged in by the person in the regular course of its trade or business for the ultimate purpose of obtaining gains or profit. Income producing activity does not include transactions and activities performed on behalf of a person, such as those conducted on its behalf by an independent contractor. The mere holding of intangible personal property is not, of itself, an income producing activity. Accordingly, the income producing activity includes but is not limited to the following:

i) The rendering of personal services by employees or the utilization of tangible and intangible property by the person in performing a service.

ii) The sale, rental, leasing, licensing or other use of real property.

iii) The rental, leasing, licensing or other use of tangible personal property.

iv) The sale, licensing or other use of intangible personal property.

B) Costs of Performance Defined. The term "costs of performance" means direct costs determined in a manner consistent with generally accepted accounting principles and in accordance with accepted conditions or practices in the trade or business of the person.

C) Application. Receipts sourced under this subsection (c)(5) in respect to a particular income producing activity are in this State if:

i) the income producing activity is performed wholly within this State; or

ii) the income producing activity is performed both in and outside this State and, based on costs of performance, a greater proportion of the income producing activity is performed in this State than without this State (for taxable years ending prior to December 31, 2008) or a greater proportion of the income-producing activity of the taxpayer is performed within this State than in any other state (for taxable years ending on or after December 31, 2008).

D) Special Rules. The following are special rules for determining when receipts from the income producing activities described below are in this State.

i) Gross receipts from the sale, lease, rental or licensing of real property are in this State if the real property is located in this State.

ii) Gross receipts from the rental, lease, or licensing of tangible personal property are in this State if the property is located in this State. The principal cost of performance in a rental, leasing or licensing transaction is the depreciation or amortization of the tangible personal property, and the depreciation or amortization expense is incurred in the state in which the tangible personal property is located. The rental, lease, licensing or other use of tangible personal property in this State is a separate income producing activity from the rental, lease, licensing or other use of the same property while located in another state; consequently, if property is within and without this State during the rental, lease or licensing period, gross receipts attributable to this State shall be measured by the ratio which the time the property was physically present or was used in this State bears to the total time or use of the property everywhere during that period.

EXAMPLE: Corporation X is the owner of 10 railroad cars. During the year, the total of the days each railroad car was present in this State was 50 days. The receipts attributable to the use of each of the railroad cars in this State are a separate item of income. Total receipts attributable to this State shall be determined as follows:

(10 x 50)/3650 x Total Receipts

iii) Gross receipts for the performance of personal services are attributable to this State to the extent those services are performed partly within and partly without this State, the gross receipts for the performance of those services shall be attributable to this State only if a greater portion of the services were performed in this State, based on costs of performance. Where services are performed partly within and partly without this State and the services performed in each state constitute a separate income producing activity, the gross receipts for the performance of services attributable to this State shall be measured by the ratio that the time spent in performing the services in this State bears to the total time spent in performing the services everywhere. Time spent in performing services includes the amount of time expended in the performance of a contract or other obligation that gives rise to the gross receipts. Personal service not directly connected with the performance of the contract or other obligation, as for example, time expended in negotiating the contract, is excluded from the computations.

EXAMPLE 1: Corporation X, a road show, gave theatrical performances at various locations in State X and in this State during the tax period. All gross receipts from performances given in this State are attributed to this State.

EXAMPLE 2: A public opinion survey corporation conducted a poll by its employees in State X and in this State for the sum of $9,000. The project required 600 man hours to obtain the basic data and prepare the survey report. Two hundred of the 600 man hours were expended in this State. The receipts attributable to this State are $3,000, calculated as follows:

200/600 x $9,000

6) For taxable years ending on or after December 31, 2008, gross receipts from transactions not governed by the provisions of subsection (c)(1), (2), (3) or (4) *are in this State if any of the following criteria are met*:

A) *Sales from the sale or lease of real property are in this State if the property is located in this State.* (IITA Section 304(a)(3)(C-5)(i))

B) *Sales from the lease or rental of tangible personal property are in this State if the property is located in this State during the rental period. Sales from the lease or rental of tangible personal property that is characteristically moving property, including, but not limited to, motor vehicles, rolling stock, aircraft, vessels, or mobile equipment, are in this State to the extent that the property is used in this State.* (IITA Section 304(a)(3)(C-5)(ii))

C) *In the case of interest, net gains (but not less than zero) and other items of income from intangible personal property, the sale is in this State if:*

i) *in the case of a taxpayer who:*

- *is a dealer in the item of intangible personal property within the meaning of 26 USC 475, the income or gain is received from a customer in this State*. A taxpayer is a dealer with respect to an item of intangible personal property if the taxpayer is a dealer with respect to the item under 26 USC 475(c)(1), or would be a dealer with respect to the item under 26 USC 475(c)(1) if the item were a security as defined under 26 USC 475(c)(2). *For purposes of this subsection (c)(6)(C)(i), a customer is in this State if the customer is an individual, trust or estate who is a resident of this State and, for all other customers, if the customer's commercial domicile is in this State. Unless the dealer has actual knowledge of the residence or commercial domicile of a customer during a taxable year, the customer shall be deemed to be a customer in this State if the billing address of the customer, as shown in the records of the dealer, is in this State.* A dealer shall treat the person with whom it engages in a transaction as the customer, even when that person is acting on behalf of a third party, unless the dealer has actual knowledge of the party on whose behalf the person is acting. If a taxpayer is a dealer with respect to an item of intangible personal property and recognizes gain or loss with respect to that item other than in connection with a transaction with a customer (for example, unrealized gain or loss from marking the item to market under 26 USC 475), that gain or loss shall be excluded from the numerator and denominator of the sales factor (IITA Section 304(a)(3)(C-5)(iii)(a)) or

- is not a dealer with *respect* to the item of *intangible* personal property, *if the income-producing activity of the taxpayer is performed in this State or, if the income-producing activity of the taxpayer is performed both within and without this State, if a greater proportion of the income-producing activity of the taxpayer is performed within this State than in any other state, based on performance costs.* (IITA Section 304(a)(3)(C-5)(iii)(b)) (See subsection (c)(5) of this Section.)

ii) For purposes of this subsection (c)(6)(C), an item of "intangible personal property" includes only an item that can ordinarily be resold or otherwise reconveyed by the person acquiring the item from the taxpayer, and does not include any obligation of the taxpayer to make any payment, perform any act, or otherwise provide anything of value to another person.

EXAMPLE 1. A ticket to attend a sporting event would not be an item of intangible personal property for the owner of the stadium who issues the ticket and is obliged to grant admission to the holder of the ticket. Rather, the sale of the ticket is a prepayment for a service to be provided. However, the ticket would be an item of intangible personal property in the hands of the original purchaser or any subsequent purchaser of the ticket, and a ticket broker engaged in the business of buying and reselling tickets would be a dealer with respect to the ticket.

EXAMPLE 2. A taxpayer selling canned computer software is selling intangible personal property. (First National Bank of Springfield v. Dept. of Revenue, 85 Ill.2d

84 (1981)) If the taxpayer sells software to customers in the ordinary course of its business, it is a dealer with respect to those sales. In contrast, a taxpayer providing programming or maintenance services to its customers is selling services rather than intangible personal property.

EXAMPLE 3. A taxpayer administers a "rewards program" for a group of unrelated businesses. Under the program, a customer of one business can earn discounts or rebates on products and services provided by any of the businesses. As each customer earns rewards, measured in "units", from one of the businesses, that business pays a specified amount per unit to the taxpayer. When a customer uses units earned in the program to purchase products or services at a discount from a participating business, the taxpayer pays that business a specified amount per unit used by the customer. Rebates may be paid to the customer directly by the taxpayer or by one of the businesses, which is then reimbursed by the taxpayer. To the extent payments made to the taxpayer by businesses awarding units exceed the payments the taxpayer must make for discounts and rebates, the excess is payment for operating the program. The units awarded are obligations of the taxpayer to make payments to the business providing products or services at a discount or to pay rebates. Accordingly, payments received by taxpayer from the participating businesses for units awarded are not income from sales of intangible personal property by the taxpayer.

D) *Sales of services are in this State if the services are received in this State.* (IITA Section 304(a)(3)(C-5)(iv))

i) General Rule. Gross receipts from services are assigned to the numerator of the sales factor to the extent that the receipts may be attributed to services received in Illinois.

ii) A contract that involves the provision of a service by the taxpayer and the use of property of the taxpayer by the service recipient shall be treated as a sale of service unless the contract is properly treated as a lease of property under 26 USC 7701(e)(1), taking into account all relevant factors, including whether:

- the service recipient is in physical possession of the property;

- the service recipient controls the property;
- the service recipient has a significant economic or possessory interest in the property;
- the service provider does not bear any risk of substantially diminished receipts or substantially increased expenditures if there is nonperformance under the contract;
- the service provider does not use the property concurrently to provide significant services to entities unrelated to the service recipient; and
- the total contract price does not substantially exceed the rental value of the property for the contract period.

EXAMPLE: A taxpayer selling access to an online database or applications software, and who is required to perform regular update services to the database or software, retains control over the contents of the database or software, and provides access to the same database or software to multiple customers is not selling or licensing an item of intangible personal property to its customers, but rather is providing a service.

iii) Services received in this State include, but are not limited to:

- When the subject matter of the service is an item of tangible personal property, the service is received in this State if possession of the property is restored to the recipient of the service under the principles in subsection (c)(1) for determining whether a sale of that property is in this State.

  EXAMPLE 1. A customer returns a computer to the manufacturer for repair. The manufacturer performs the repairs in Indiana and ships the computer to the customer's Illinois address. The service is received in this State.

  EXAMPLE 2. Individual purchases clothing from Merchant at a store in this State, using a credit card issued by Bank A pursuant to a licensing agreement with Credit Card Company. Credit Card Company is not a financial organization required to apportion its business income under Section 100.3405. Bank A remits the purchase price to Credit Card Company, which deposits the purchase price with Merchant's bank, minus a fee or discount. All fees and discounts earned by Credit Card Company in connection with this purchase are for services received in this State.

- When the subject matter of the service is an item of real property, the service is received in the state in which the real property is located.

  EXAMPLE 3. Individual purchases a parcel of land in Illinois and constructs a house on the parcel. Services performed at an architect's office in Wisconsin regarding the design and construction of the house are received in this State.

- When the service is performed on or with respect to the person of an individual (for example, medical treatment services), the service is received in the state in which the individual is located at the time the service is performed.

- Services performed by a taxpayer that are directly connected to or in support of services received in this State are also services received in this State.

  EXAMPLE 4. Individual purchases automobile repair services from Automobile Dealership at its facility located in this State, using a credit card issued by Bank A pursuant to a licensing agreement with Credit Card Company. Bank A remits the purchase price to Credit Card Company, which deposits the purchase price with Automobile Dealership's bank, minus a fee or discount. All fees and discounts earned by Credit Card Company in connection with this purchase are for services received in this State.

  EXAMPLE 5. Services performed by an investment fund on behalf of an investor are received in this State if the investor resides in this State (in the case of an individual) or has its ordering or billing address in this State (for other investors). In the case of services provided by Taxpayer to or on behalf of the investment fund that are directly connected with services provided separately to the investors, such as preparation of communications and statements to investors, and allocations of earnings and distributions to investors, the service is also received in this State to the extent the investors reside (or have their ordering or billing address) in this State. Accordingly, receipts of Taxpayer for these services are allocated to this State on the basis of the ratio of: the average of the outstanding shares in the fund owned by shareholders, partners or other investors residing (or having their ordering or billing address) within this State at the beginning and end of each taxable year of the taxpayer; and the average of the total number of outstanding shares in the fund at the beginning and end of each year. Residence or ordering or billing address of the shareholder, partner or other investor is determined by the mailing address in the records of the investment fund or the taxpayer. Services provided to an investment fund that are not directly connected to or in support of services provided separately to investors, such as brokerage services or investment advising, are not received by the customer at the location of its investors.

iv) Special Rules

- Under IITA Section 304(a)(3)(C-5)(iv), *if the state where the services are received is not readily determinable, the services shall be deemed to be received at the location of the office of the customer from which the services were ordered in the regular course of the customer's trade or business, or, if the ordering office cannot be determined, at the office of the customer to which the services are billed.* If the service is provided to an individual who provides a residential address as the place from which the services are ordered or to which the services are billed, rather than an office address, the residential address shall be used. For purposes of this provision, the state where services are received is not readily determinable if the facts necessary to make the determination are not contained in the books and records of the taxpayer or any person related to the taxpayer within the meaning of 26 USC 267(b) or if the available facts would allow reasonable persons to reach different determinations of the state in which the services were received.

- Under IITA Section 304(a)(3)(C-5)(iv), *if the services are provided to a corporation, partnership, or trust and the services are received in a state in which the corporation, partnership, or trust does not maintain a fixed place of business* (as defined in Section 100.3405(b)(1)), *the services shall be deemed to be received at the location of the office of the customer from which the services were ordered in the regular course of the customer's trade or business, or, if the ordering office cannot be determined, at the office of the customer to which the services are billed*. For purposes of this provision, in the case of services performed by the taxpayer as a subcontractor or as an agent acting on behalf of a principal, if either the contractor or principal has a fixed place of business in the state in which the services are received or the customer of the contractor or principal either is an individual or has a fixed place of business in the state in which the services are received, the service will be treated as received in a state in which the customer of the taxpayer has a fixed place of business.

- Under IITA Section 304(a)(3)(C-5)(iv), *if the taxpayer is not taxable in the state in which the services are received or deemed to be received, the gross receipts attributed to those services must be excluded from both the numerator and denominator of the sales factor*. (See Section 100.3200 for guidance on determining when a taxpayer is taxable in another state.)

Section 100.3380 Special Rules (IITA Section 304)

a) Determining Business Activity or Market Within Illinois

1) Petition
IITA Section 304(f) provides that *if the allocation and apportionment provisions of subsections (a) through (e) and of subsection (h) do not, for taxable years ending before December 31, 2008, fairly represent the*

extent of a person's business activity in this State, or do not, for taxable years ending on or after December 31, 2008, fairly represent the market for the person's goods, services, or other sources of business income, the person may petition for, or the Director may require, in respect of all or any part of the person's business activity, if reasonable:

A) *Separate accounting;*

B) *The exclusion of any one or more factors;*

C) *The inclusion of one or more additional factors which will fairly represent the person's business activities or market in this State; or*

D) *The employment of any other method to effectuate an equitable allocation and apportionment of the person's business income.*

2) Director's Determination
The Director has determined that, in the instances described in this Section, the apportionment provisions provided in subsections (a) through (e) and (h) of IITA Section 304 do not fairly represent the extent of a person's business activity or market within Illinois. For tax years beginning on or after the effective date of a rulemaking amending this Section to prescribe a specific method of apportioning business income, all nonresident taxpayers are directed to apportion their business income employing that method in order to properly apportion their business income to Illinois. Taxpayers whose business activity or market within Illinois is not fairly represented by a method prescribed in this Section and who ~~do not~~ want to use another ~~that~~ method for a tax year beginning after the effective date of the rulemaking adopting that method may obtain permission to use that other method by filing ~~must file~~ a petition under Section 100.3390 ~~requesting permission to use an alternative method of apportionment~~. For tax years beginning prior to the effective date of the rulemaking adopting a method of apportioning business income, the Department will not require a taxpayer to adopt that method; provided, however, if any taxpayer has used that method for any of those tax years, the taxpayer must continue to use that method for that tax year. Moreover, a taxpayer may file a petition under Section 100.3390 to use a method of apportionment prescribed in this Section for any open tax year beginning prior to the effective date of the rulemaking adopting that method, and that petition shall be granted in the absence of facts showing that that method will not fairly represent the extent of a person's business activity or market in Illinois.

b) Property Factor. The following special rules are established in respect to the property factor in IITA Section 304(a)(1):

1) If the subrents taken into account in determining the net annual rental rate under Section 100.3350(c) produce a negative or clearly inaccurate value for any item of property, another method that will properly reflect the value of rented property may be required by the Director or requested by the person. In no case however may ~~shall~~ the value be less than an amount that bears the same ratio to the annual rental rate paid by the person for the property as the fair market value of that portion of the property used by the person bears to the total fair market value of the rented property.

   EXAMPLE: A corporation rents a 10-story building at an annual rental rate of $1,000,000. The corporation occupies two stories and sublets eight stories for $1,000,000 a year. The net annual rental rate of the taxpayer is at least ~~must not be less than~~ two-tenths of the corporation annual rental rate for the entire year, or $200,000.

2) If property owned by others is used by the person at no charge or rented by the person for a nominal rate, the net annual rental rate for the property is ~~shall be~~ determined on the basis of a reasonable market rental rate for that property.

c) Sales Factor. The following special rules are established in respect to the sales factor in IITA Section 304(a)(3):

1) For taxable years ending ~~on or~~ before December 31, 2008, in the case of sales in which neither the origin nor the destination of the sale is within this State, and the person is taxable in neither the state of origin nor the state of destination, the sale is ~~will be~~ attributed to this State (and included in the numerator of the sales factor) if the person's activities in this State in connection with the sales are not protected by the provisions of P.L. 86-272, 15 USC 381-385. Although P.L. 86-272, by its terms covers only sales of tangible personal property, its rules regarding a state's power to impose a net income tax, for purposes of this special rule, will be applied whether or not the sale is of tangible or intangible property. This subsection (c)(1) does ~~shall~~ not apply in taxable years ending on or after December 31, 2008, because attributing the sale to this State is not required by IITA Section 304(a)(3) and does not *fairly represent the market for the person's goods, services, or other sources of business income* in this State. Notwithstanding the provisions of subsection (a)(2), taxpayers are not required to file a petition under Section 100.3390 requesting permission to file an original or amended return for any tax year ending on or after December 31, 2008 that does not apply the special rule in this subsection (c)(1).

   EXAMPLE: A corporation's salesman operates out of an office in Illinois. He regularly calls on customers both within and without Illinois. Orders are approved by him and transmitted to the corporation's headquarters in

State A. If the property sold by the salesman is shipped from a state in which the corporation is not taxable to a purchaser in a state in which the corporation is not taxable, the sale is attributable to Illinois.

2) When gross receipts arise from an incidental or occasional sale of assets used in the regular course of the person's trade or business, those gross receipts are ~~shall be~~ excluded from the sales factor. For example, gross receipts from the sale of a factory or plant are ~~will be~~ excluded. Gross receipts from an incidental or occasional sale of stock in a subsidiary are ~~will~~ also ~~be~~ excluded. Exclusion of these gross receipts from the sales factor is appropriate for several reasons, more than one of which may apply to a particular sale, including:

A) incidental or occasional sales are not made in the market for the person's goods, services or other ordinary sources of business income;

B) to the extent that gains realized on the sale of assets used in a taxpayer's business are comprised of recapture of depreciation deductions, the economic income of the taxpayer was understated in the years in which those deductions were taken. The recapture gains that reflect a correction of that understatement should be allocated using a method approximating the factors that were used in apportioning the deductions. If the business otherwise remains unchanged, including the gross receipts from the sale in the sales factor numerator of the state in which the assets were located would allocate a disproportionate amount of the recapture gains to that state compared to how the deductions being recaptured were allocated;

C) to the extent the gain on the sale is attributable to goodwill or similar intangibles representing the value of customer relationships, including the gross receipts from the sale in the sales factor does ~~will~~ not reflect the market for the taxpayer's goods, services or other ordinary sources of business income to the extent the sourcing of the receipts from that sale differs from the sales factor computed without regard to that sale; and

D) in the case of sales of assets that are made in connection with a partial or complete withdrawal from the market in the state in which the assets are located, including the gross receipts from those sales in the sales factor would increase the business income apportioned to that state when the taxpayer's market in that state has decreased.

3) When the income producing activity relevant to the sourcing of business

income from intangible personal property can be readily identified, that income is included in the denominator of the sales factor and, if the income producing activity occurs in this State, in the numerator of the sales factor as well. For example, with respect to taxable years ending before December 31, 2008, usually the income producing activity can be readily identified in respect to interest income received on deferred payments on sales of tangible property (see Section 100.3370(a)(1)(A)).

4) When business income from intangible property is sourced according to the income producing activity, and the income cannot readily be attributed to any income producing activity of the person, the income is not ~~cannot be~~ assigned to the numerator of the sales factor for any state and is ~~shall be~~ excluded from the denominator of the sales factor. The following provisions illustrate this concept:

A) Subpart F (26 USC 951-964) income is passive income generated by the mere holding of an intangible. For taxable years ending on or after December 31, 1995, subpart F income is excluded from the sales factor under IITA Section 304(a)(3)(D). For prior taxable years, there is a rebuttable presumption that subpart F income is not includable in either the numerator or the denominator of the sales factor. If a taxpayer wishes to include subpart F income in either the numerator or the denominator of the sales factor, the burden of proof is on the taxpayer to identify the income producing activities and to situs those activities within a particular state, or

B) When business income in the form of dividends received on stock during taxable years ending before December 31, 1995, or interest received on bonds, debentures or government securities results from the mere holding of intangible personal property by the person, those dividends and interest are ~~shall be~~ excluded from the denominator of the sales factor.

5) In the case of sales in the regular course of business of intangibles (including, by means of example, without limitation, patents, copyrights, bonds, stocks and other securities), gross receipts are ~~shall be~~ disregarded and only the net gain (loss) is ~~shall be~~ included in the sales factor, provided that, for taxable years ending on or after December 31, 2008, only net gains may ~~shall~~ be included in the sales factor for sales sourced under IITA Section 304(a)(3)(C-5)(iii).

EXAMPLE: In 1990, Corporation A, a calendar year taxpayer, sells stock with an adjusted basis of $98,000,000 for $100,000,000, realizing a federal net capital gain of $2,000,000. Only the net capital gain of $2,000,000 is reflected in A's sales factor for the taxable year ending December 31, 1990.

6) Hedging Transactions

A) A "hedging transaction" is a transaction entered into by a taxpayer in the normal course of business primarily to manage interest rate risk or the risk of price or currency fluctuations. (See 26 USC 475(c)(3), 1221(b)(2)(A) and 1256(e)(2).) The purpose of the sales factor in IITA Section 304(a) is to apportion the business income of a taxpayer conducting an interstate business to this State based on this State's relative share of the marketplace for the goods and services sold by the taxpayer in the course of its business. Gains and losses on hedging transactions entered into to manage the risks associated with the acquisition of resources by a taxpayer (for example, price fluctuations in commodities consumed in the taxpayer's business) do not reflect the market for the taxpayer's goods and services and, therefore, should be excluded from the sales factor. Gains and losses on hedging transactions entered into to manage risks associated with the gross income the taxpayer expects from its sales of goods and services (for example, the effect of foreign currency fluctuations on the dollar amount of gross income the taxpayer will receive from sales to a particular foreign country) are best accounted for in the sales factor as adjustments to the gross receipts from the transactions whose risks are being hedged. Gains and losses on hedging transactions that manage risks associated with both acquisitions and sales of the taxpayer (for example, electricity futures bought or sold by a taxpayer engaged in the business of buying and selling electrical power), or that otherwise cannot be associated with a particular transaction or class of transactions in the computation of the sales factor, should be excluded from the sales factor. Federal income tax law provides a framework for identifying gains and losses from hedging transactions to the transactions or class of transactions being hedged and for keeping records necessary to support the identifications. The federal practice should be followed for State purposes.

B) General Rule. Except as provided in subsection (c)(6)(C), any income, gain or loss from a transaction properly identified as a hedge under 26 USC 1221(b)(2)(A), 475(c)(3) or 1256(e)(2) is excluded from the numerator and denominator of the sales factor.

C) Special Rule. With respect to any hedging transaction described in subsection (c)(6)(B) as to which identification requirements of subsection (c)(6)(D) are satisfied, any income, gain or loss from the hedging transaction is ~~shall be~~ included in the denominator of the sales factor if the gross receipts from the hedged item are included in the denominator. That income, gain or loss is ~~shall be~~ included in the numerator of the sales factor if the gross receipts from the hedged item are included in the numerator of the sales factor, and are ~~shall be~~ excluded from the numerator of the sales factor if the gross receipts from the hedged item are excluded from the numerator of the sales factor. If the hedging transaction relates to an identified group of hedged items, the income, gain or loss from the hedging transaction is included in the numerator of the sales factor in the same proportion that the gross receipts from the group of hedged items are included in the numerator of the sales factor.

D) Identification Required. The identification requirements of this subsection (c)(6)(D) are met if the taxpayer's books and records clearly identify a hedging transaction as managing risk relating to a particular item or items of gross receipts, including anticipated items of gross receipts, that must be included in the sales factor. The identification requirements are met only if identification is ~~must be~~ made at the time and in the manner required under 26 USC 475(c)(3), 26 CFR 1.1221-2(f) and (g), or 26 CFR 1.1256(e)-1 and the taxpayer's books and records include the information necessary to apply subsection (c)(6)(C).

E) This subsection (c)(6) does not apply to any hedging transaction that, for federal income tax purposes, is integrated with the hedged item, such as under 26 CFR 1.988-5 or 1.1275-6. In addition, for purposes of this subsection (c)(6):

i) a transaction entered into by one member of a federal consolidated group identified as a hedge against a risk of another member of the federal consolidated group under the "single-entity approach" in 26 CFR 1.1221-2(e)(1) is not a hedging transaction if the two members of the federal consolidated group are not members of the same unitary business group, because the transaction is not hedging against a risk faced by the taxpayer entering into the transaction; and

ii) a transaction entered into by one member of a unitary business group with another member of the unitary business group is not a hedging transaction, because the risk remains within the group, except in the case of a transaction identified under 26 CFR 1.1221-2(f) or (g) as a hedging transaction between two member of a unitary business group who are also members of a federal consolidated group that has made the "separate entity election" in 26 CFR 1.1221-2(e)(2) with regard to hedging transactions.

F) EXAMPLES: The provisions of this subsection (c)(6) may be illustrated by the following examples:

i) Taxpayer expects that, during its next production cycle, it will need 10 tons of commodity Y for its interstate manufacturing business. Commodity Y is a raw material used by Taxpayer in the manufacture of its inventory. In order to hedge against exposure to changes in the price of commodity Y, Taxpayer enters into a forward contract to purchase 10 tons of commodity Y. The forward contract is identified as a hedging transaction under IRC section 1221(b)(2)(A). Under subsection (c)(6)(B), any income, gain or loss recognized with respect to the forward contract is excluded from the numerator and denominator of the sales factor.

ii) On January 1, 2008, Taxpayer owns 10 tons of commodity X, which it holds for sale in the ordinary course of business and expects to sell during its taxable year ending December 31, 2008. To hedge against price fluctuations in commodity X, on January 10, 2008, while Taxpayer still owns commodity X, it sells the equivalent of 10 tons of commodity X futures contracts on a futures exchange. Taxpayer expects to sell commodity X to customers in various states, including Illinois. The futures contract is identified as a hedging transaction under IRC section 1221(b)(2)(A), and Taxpayer properly identifies the futures contract as required under subsection (c)(6)(D) as hedging gross receipts from sales of commodity X. Under subsection (c)(6)(C), any gain or loss taken into account by Taxpayer during its taxable year with respect to the futures contract is included in the denominator of the sales factor, and is included in the numerator of the sales factor in the same proportion that gross receipts from actual sales of commodity X during the taxable year are included in the numerator of the sales factor. If a loss is recognized on the futures contract, the loss is treated as a reduction (but not below zero) of the gross receipts from the sale of commodity X in computing the sales factor.

iii) Taxpayer is a corporation on the accrual method of accounting with the U.S. dollar as its functional currency. On January 1, 2008, Taxpayer acquires 1,500 British pounds (£) for \$2,250 (£1 = \$1.50). The acquisition of £1,500 is properly identified by Taxpayer as a hedging transaction under IRC section 1221(b)(2)(A). On February 5, 2008, when the spot rate is £1 = \$1.55, Taxpayer purchases inventory from its supplier by paying £1,500. Accordingly, Taxpayer recognizes \$75 exchange gain for federal income tax purposes upon disposition of the British pounds. The \$75 exchange gain is excluded from both the numerator and denominator of the sales factor under subsection (c)(6)(B).

iv) Taxpayer is a calendar year corporation with the U.S. dollar as its functional currency. Based on past experience, Taxpayer anticipates making 2009 first quarter sales to customers in New Zealand of 100,000 New Zealand dollars (NZD). In order to hedge against currency fluctuations related to the anticipated first quarter sales, on December 31, 2008, Taxpayer enters into a forward contract to sell 100,000 NZD on March 31, 2009 for \$48,000. The forward contract is identified as a hedging transaction under 26 USC 1221(b)(2)(A), and the Taxpayer properly identifies the transaction as hedging its anticipated New Zealand sales in accordance with subsection (c)(6)(D). During the first quarter of its 2009 taxable year, Taxpayer makes sales to its New Zealand customers of 90,000 NZD. Under IITA Section 304(a), gross receipts from its New Zealand sales are included in the denominator of the Taxpayer's sales factor and are excluded from the numerator of the sales factor. Under subsection (c)(6)(C), any gain or loss recognized on the forward contract is included in the denominator of the Taxpayer's sales factor and is excluded from the numerator of the factor. This treatment is appropriate ~~required~~ even though the Taxpayer's sales to New Zealand customers were less than anticipated. Any loss recognized on the forward contract is treated as a reduction (but not below zero) of the gross receipts from sales to New Zealand customers that are included in the denominator of the sales factor.

7) Section 988 Transactions

A) Section 988 Transactions. For sales factor purposes, foreign currency gain or loss that is computed under 26 USC 988, with respect to accrued interest income or expense, gain or loss on a debt instrument, a payable, a receivable or a forward contract payable in a foreign currency described in 26 CFR 1.988-1(a)(2) is treated as an adjustment to the income, expense, gain or loss. Accordingly, the foreign currency gain or loss is included in the numerator and denominator of the sales factor only to the extent that the income to which the foreign currency gain or loss relates is included in the numerator and denominator of the sales factor. Foreign currency gains and losses with respect to expense are excluded from the numerator and denominator of the sales factor.

EXAMPLES: The provisions of this subsection (c)(7)(A) may be illustrated by the following examples:

i) Taxpayer is a corporation on the accrual method of accounting with the U.S. dollar as its functional currency. On January 1, 2008, Taxpayer converts $13,000 to 10,000 British pounds (₤) at the spot rate of ₤1 = $1.30 and loans the ₤10,000 to Y for 3 years. The terms of the loan provide that Y will make interest payments of ₤1,000 on December 31 of 2008, 2009 and 2010 and will repay Taxpayer's ₤10,000 principal on December 31, 2010. Based on average spot rates for 2008, 2009 and 2010 of ₤1 = $1.32, ₤1 = $1.37 and ₤1 = $1.42, respectively, Taxpayer accrues interest income of $1,320 for 2008, $1,370 for 2009, and $1,420 for 2010. Under IITA Section 304(a), the accrued interest income is included in the denominator of Taxpayer's sales factor, but is excluded from the numerator of its sales factor. Based on spot rates on December 31, 2008, December 31, 2009 and December 31, 2010 of ₤1 = $1.35, ₤1 = $1.40 and ₤1 = $1.45, respectively, Taxpayer recognizes for federal income tax purposes exchange gain of $30 upon receipt of the interest on December 31 of 2008, 2009 and 2010. In addition, Taxpayer recognizes, for federal income tax purposes, exchange gain of $1,500 upon repayment of the loan principal on December 31, 2010. Under subsection (c)(7)(A), the $30 of exchange gain recognized with respect to the accrued interest for 2008, 2009 and 2010 is included in the denominator of Taxpayer's sales factor and is excluded from the numerator of its sales factor. The $1,500 of exchange gain with respect to the repayment of principal on December 31, 2010 is excluded from both the numerator and denominator of Taxpayer's sales factor because repayment of principal on a loan is not included in the sales factor.

ii) Taxpayer is a corporation on the accrual method of accounting with the U.S. dollar as its functional currency. On January 15, 2008, Taxpayer sells inventory for 10,000

Canadian dollars (C$). The spot rate on January 15, 2008 is C$1 = U.S. $.55. Under IITA Section 304(a), $5,500 in gross receipts from this sale is included in the denominator of Taxpayer's sales factor, and is excluded from the numerator of the sales factor. On February 23, 2008, when Taxpayer receives payment of the C$10,000, the spot rate is C$1 = U.S. $.50. For federal income tax purposes, Taxpayer recognizes ($500) of exchange loss upon receipt of C$10,000 on February 23, 2008. Under subsection (c)(7)(A), the ($500) exchange loss with respect to the January 15, 2008 sale is included in the denominator of the Taxpayer's sales factor and is excluded from the numerator of the sales factor. The exchange loss is reflected as a reduction of the denominator of the Taxpayer's sales factor.

B) Section 986(c)(1) Foreign Exchange Gain or Loss on Distributions of Previously Taxed Income. Foreign currency gain or loss recognized pursuant to 26 USC 986(c)(1) on distributions of amounts previously taxed to the recipient as subpart F income or as earnings of a qualified electing fund are ~~shall be~~ excluded from both the numerator and denominator of the sales factor because those distributions are excluded from federal gross income and, therefore, from the sales factor.

d) Unitary Partners: Inclusion of shares of partnership unitary business income and factors in combined unitary business income and factors of partners.

1) IITA Section 304(e) provides that whenever *2 or more persons are engaged in a unitary business as described in IITA Section 1501(a)(27), a part of which is conducted in this State by one or more members of the group, the business income attributable to this State by any member or members is ~~shall be~~ apportioned by means of the combined apportionment method.* Because partnerships may be members of a unitary business group within the meaning of IITA Section 1501(a)(27), this provision requires a partnership to use combined apportionment when it is engaged in a unitary business with one or more of its partners. However, partners who are not engaged in a unitary business with the partnership ~~are required to~~ include their shares of the partnership's business income apportioned to Illinois in their Illinois net incomes under IITA Section 305(a), and those partners' business activities or share of the partnership's market in Illinois would not be represented fairly by their shares of partnership income computed by combining the business income and apportionment factors of the partnership with the business income and apportionment factors of its unitary partners.

2) Accordingly, except in a case in which substantially all of the interests in

the partnership (other than a publicly-traded partnership under 26 USC 7704) are owned or controlled by members of the same unitary business group, when the business activities of a partnership and any of its partners' business activities constitute a unitary business:

A) The partner's distributive share of the business income and apportionment factors of the partnership are ~~shall be~~ included in that partner's business income and apportionment factors. Also, for taxable years ending on or after December 31, 2017, the partner's distributive share of the everywhere sales of the partnership is included in the partner's everywhere sales for purposes of applying Section 100.3600. In determining the business income of the partnership, transactions between the unitary partner (or members of its unitary business group) and the partnership are not ~~shall not be~~ eliminated. However, all transactions between the unitary business group and the partnership are ~~shall be~~ eliminated for purposes of computing the apportionment factors of the partner and of any other member of the unitary business group.

EXAMPLE: Partner and Partnership are engaged in a unitary business. Partner owns a 20% interest in Partnership. Partnership has $10,000,000 in sales everywhere, $3,000,000 of which are to Partner, and $4,000,000 in Illinois sales, $1,000,000 of which are to Partner. In computing its apportionment factor, Partner will include $1,400,000 from Partnership in its everywhere sales (20% of Partnership's $10,000,000 in everywhere sales, after eliminating the $3,000,000 in sales to Partner) and $600,000 from Partnership in its Illinois sales (20% of Partnership's $4,000,000 in Illinois sales, after eliminating the $1,000,000 in sales to Partner). Also, Partner must eliminate any sales it made to Partnership.

B) If a partnership and one of its partners are engaged in a unitary business and the partnership is itself a partner in a second partnership:

i) If the partner is not engaged in a unitary business with the second partnership, the partner's share of the first partnership's share of the business income and apportionment factors of the second partnership are not ~~shall not be~~ included in the partner's business income and apportionment factors. Instead, the partner's share of the first partnership's share of the base income apportioned to Illinois by the second partnership are ~~will be~~ included in the partner's Illinois net income.

ii) If the partner is engaged in a unitary business with the second partnership, the partner's share of the first partnership's share of the business income and apportionment factors of the second partnership are ~~shall be~~ included in the partner's business income and apportionment factors.

C) If, for taxable years ending on or after December 31, 2017, a partner and a partnership engaged in a unitary business apportion their business income using different apportionment formulas under IITA Section 304:

i) The apportionment percentage of the partnership is computed under the provisions of Section 100.3600 by treating the partnership as a member of the unitary business group, but using only that partner's distributive share of the partnership's apportionment factors and sales, and that partner's apportionment percentage is equal to that partner's apportionment percentage computed under Section 100.3600 plus the partnership's apportionment percentage computed under Section 100.3600.

ii) If a partnership has more than one partner in the same unitary business group, and the partnership uses a different apportionment formula than one or more of the partners, each partner that uses the same apportionment formula as the partnership will compute its apportionment factor as provided in subparagraph (A) and each partner that uses a different apportionment formula will compute its apportionment factor as provided in (i) of this subparagraph (C).

3) This subsection (d) does ~~shall~~ not apply to a partner's shares of business income and apportionment factors from any partnership that cannot be included in a unitary business group with that partner.

A) This subsection (d) does not apply because:

i) for taxable years ending prior to December 31, 2017, the partner and the partnership ~~are required to~~ apportion their business income using different apportionment formulas under IITA Section 304, and therefore cannot be members of a unitary business group under IITA Section 1501(a)(27); or

ii) the business activities of either the partner or the partnership outside the United States are equal to or greater than 80% of the total worldwide business activities of that partner or partnership, as determined under Section 1502(a)(27) of the IITA. In applying this 80-20 test to a taxpayer, no apportionment factors of any partnership shall be included in the apportionment factors of that taxpayer pursuant to this subsection (d).

B) For taxable years ending prior to December 31, 2017, if ~~If~~ the partnership is itself a partner in a second partnership, and one of its partners is engaged in a unitary business with the second partnership and is not prohibited from being a member of a unitary business group that includes the second partnership under subsection (d)(3)(A)(i) or (ii), that partner includes ~~shall include~~ in its business income and apportionment factors its share of the partnership's share of the second partnership's business income and apportionment factors.

4) If substantially all of the interests in a partnership (other than a publicly-traded partnership under 26 USC 7704) are owned or controlled by members of the same unitary business group as the partnership, the partnership is ~~shall be~~ treated as a member of the unitary business group for all purposes, and, for purposes of applying IITA Section 305(a) to any nonresident partner who is not a member of the same unitary business group, the business income of the partnership apportioned to this State is ~~shall be~~ determined using the combined apportionment method prescribed by IITA Section 304(e). For purposes of this subsection (d), substantially all of the interests in a partnership are owned or controlled by members of the same unitary business group if more than 90% of the federal taxable income of the partnership is allocable to one or more of the following persons:

A) any member of the unitary business group;

B) any person who would be a member of the unitary business group if not for the fact that 80% or more of that person's business activities are conducted outside the United States;

C) any person who would be a member of the unitary business group except for the fact that the person and the partnership apportion their business incomes under different subsections of IITA Section 304 and therefore, for taxable years ending prior to December 31, 2017, would be excluded from a unitary business group in which the partnership is a member; or

D) any person who would be disallowed a deduction for losses by IRC section 267(b), (c) and (f)(1) by virtue of being related to any person described in subsections (d)(4)(A), (B) or (C) of this Section, as well as any partnership in which a person described in subsections (d)(4)(A), (B) or (C) is a partner.

5) EXAMPLES:

A) Corporation A owns a 50% interest in P-1, a partnership. Corporation A and P-1 are engaged in a unitary business within the meaning of IITA Section 1501(a)(27). P-1 itself conducts no business activities in Illinois, and the Illinois numerator of its apportionment factor is zero. P-1 holds a 50% interest in P-2, a partnership doing business exclusively in Illinois. P-1 has $1.4 million of taxable business income, not including any income from P-2. P-2 has base income of $1 million, all of which is business income, and on a separate-entity basis, all of its business income would be apportioned to Illinois.

B) If Corporation A and P-2 are not members of the same unitary business group, Corporation A would compute its business income apportioned to Illinois by including $700,000 (50% of $1.4 million) of P-1's business income in Corporation A's business income, and 50% of P-1's apportionment factors in its apportionment factors. Corporation A also would include in its Illinois net income its 50% share of P-1's 50% share of the base of P-2 apportionable to Illinois, or $250,000 (50% of 50% of $1 million).

C) If Corporation A, P-1 and P-2 are members of the same unitary business group, P-1 will include 50% of P-2's business income and 50% of P-2's apportionment factors in its own business income and apportionment factors. Accordingly, P-1's business income will be $1.9 million (the $1.4 million it earned directly plus its 50% share of P-2's $1 million in business income). Corporation A will then compute its business income apportioned to Illinois by including its 50% share of P-1's business income, or $950,000 (50% of $1.9 million) with its business income and its 50% share of P-1's apportionment factors (which will include P-1's share of P-2's apportionment factors) in its apportionment factors.

D) If Corporation A, P-1 and P-2 are unitary, but P-1 ~~cannot be included in a~~ is excluded from the unitary business group ~~with~~ of Corporation A and P-2 because those entities apportion their business income under IITA Section 304(a) and P-1 is a financial organization that apportions its business income under IITA

Section 304(c) and the taxable year ends prior to December 31, 2017, Corporation A ~~will~~ includes in its business income and apportionment factors its 50% share of P-1's 50% share of the business income and apportionment factors of P-2. Also, Corporation A's Illinois net income ~~will~~ includes 50% of the business income of P-1 apportioned to Illinois by P-1 using its own apportionment factors. Because, in this example, P-1 is not doing business in Illinois, none of its business income is ~~will be~~ included in Corporation A's Illinois net income.

E) In a taxable year ending December 31, 2017, a combined group is comprised of two corporations: Financial Organization (which apportions its business income using the financial organization formula under IITA Section 304(c)) and Insurance Company (which apportions its business income using the premiums factor under IITA Section 304(b)). Financial Organization A is a 20% partner in Partnership, which apportions its business income using the sales factor formula under IITA Section 304(a). Partnership is engaged in a unitary business with the members of the combined group. The apportionment data for the members of the unitary business group are as follows:

Company	Everywhere Sales	Respective Section 304 Formula Numerator	Denominator	Percentage
Insurance Co.	$200	$9	$150	6.000%
Financial Org.	$300	$75	$250	30.000%
Partnership	$500	$100	$500	
Financial Org.'s Partnership Share	$100	$20	$100	20.000%
Grand Total	$600			

The apportionment percentages of each member of the group are computed as follows:

Company	A Section 304 Apportionment Percentage	B Subgroup Everywhere Sales	C A * B	D Group Everywhere Sales	E C ÷ D
Insurance Co.	6.000%	$200	$12.00	$600	2.000%

Financial Org.	30.000%	$300	$90.00	$600	15.000%
Financial Org.'s Partnership Share	20.000%	$100	$20.00	$600	3.333%

Financial Organization's apportionment percentage is 18.333% (the 15.000% computed under Section 100.3600 and its 3.333% share of Partnership's apportionment percentage computed under Section 100.3600) and the apportionment percentage of the group is 20.333%.

e) Apportionment of Business Income by Foreign Taxpayers.

1) Under 26 USCA 882, foreign corporations include only effectively-connected income in their federal taxable income. Foreign taxpayers may exclude other items of income from their federal taxable income if authorized under treaty, as provided in 26 USCA 894. Using a foreign taxpayer's worldwide apportionment factors to determine how much of its domestic business income should be apportioned to Illinois would not fairly represent that taxpayer's business activities or market within Illinois. Accordingly, a foreign taxpayer uses ~~shall use~~ only the apportionment factors related to its domestic business income when apportioning its business income to Illinois. Similarly, in determining whether 80% or more of a foreign taxpayer's total business activity is conducted outside the United States for purposes of IITA Section 1501(a)(27), that taxpayer must use only the apportionment factors related to the business income included in its federal taxable income (plus addition modifications), rather than use all of its worldwide factors.

2) Foreign Sales Corporations. Under 26 USC 921, "exempt foreign trade income" of a foreign sales corporation is treated as foreign source income excluded from gross income. "Exempt foreign trade income" is defined in 26 USC 923 to equal the sum of the amounts of income derived from various categories of transaction, with the income from each category multiplied by specific percentages. As a general rule, there is no systematic relationship between transactions qualifying for this treatment and any particular item of property or payroll of a foreign sales corporation. Accordingly, the provisions of subsection (e)(1) of this Section does ~~shall~~ not apply to a foreign sales corporation and, in apportioning its business income and in determining whether 80% or more of its business activity is conducted outside the United States, a foreign sales corporation uses ~~shall use~~ all of its apportionment factors.

(Source: Amended at 41 Ill. Reg. ______, effective ____________)

Section 100.3600 Combined Apportionment for Taxpayers Using Different Apportionment Formulas (IITA Section1501(a)(27))

a) IITA Section 1501(a)(27) provides that, *in no event, for taxable years ending prior to December 31, 2017, may any unitary business group include members which are ordinarily required to apportion business income under different subsections of IITA Section 304.*

b) For taxable years ending on or after December 31, 2017, the business income of a unitary business group that includes members who apportion their business income under different subsections of IITA Section 304 is apportioned using the average of the apportionment percentages of each subgroup of members using the same apportionment formula (computed as if that subgroup were a separate unitary business group) weighted by the everywhere sales of the members of each subgroup (as determined under Sections 100.3370 and 3380). The apportionment percentage of each member of the unitary business group is the apportionment percentage that member would compute if the subgroup of members using the same apportionment formula of that member were a separate unitary business group. The computation of the apportionment percentage of each member is equal to a fraction in which:

1) the numerator for each member is:

A) the total sales everywhere, as determined under Sections 100.3370 and 3380, for all members of the group that apportion business income under the same subsection of IITA Section 304 as that member,

B) multiplied by a fraction equal to

i) that member's Illinois numerator of the apportionment factor determined under the subsection of IITA Section 304 used by that member to apportion its business income,

ii) divided by the total denominators of that apportionment factor of all members required to apportion business income under the same subsection of IITA Section 304; and

2) the denominator is the sum of the everywhere sales of all members of the unitary business group, as determined under Sections 100.3370 and 3380.

3) EXAMPLE

A) A combined group is composed of 6 members: Corporations A and B (who apportion their business income using the sales factor under IITA Section 304(a), so that the numerator and denominator of the "Respective Section 304 Formula" columns are their Illinois and everywhere sales, respectively), Insurance Companies A and B (who apportion their business income using the premiums factor under IITA Section 304(b), so that the numerator and denominator of the "Respective Section 304 Formula" columns are their Illinois and everywhere premiums, respectively) and Transportation Companies A and B (who apportion their business income using the transportation company formula under IITA Section 304(d), so that the numerator and denominator of the "Respective Section 304 Formula" columns are their Illinois and everywhere transportation receipts and revenue miles, respectively). The apportionment data for the members of the group are as follows:

	Everywhere	Respective Section 304 Formula		
Company	Sales	Numerator	Denominator	Percentage
Corporation A	$100	$10	$100	3.333%
Corporation B	$200	$25	$200	8.333%
Subgroup Total	$300	$35	$300	
Insurance A	$250	$3	$50	2.000%
Insurance B	$450	$6	$100	4.000%
Subgroup Total	$700	$9	$150	
Transportation A	$300	$5	$25	2.500%
Transportation B	$700	$7.5	$175	3.750%
Subgroup Total	$1,000	$12.5	$200	
Grand Total	$2,000			

Note that the everywhere sales of the insurance and transportation companies exceed the denominators of those companies' apportionment formulas because the denominators of insurance and transportation companies include only premiums and income from transportation services, respectively, while the everywhere sales of those companies include all gross business receipts of those companies, except amounts specifically excluded from the sales factor under Sections 100.3370 and 100.3380. For example, interest, gross rental income and net gains or losses on sales of intangibles in the regular course of business are included in the sales factor, but not in the apportionment formulas used by insurance or transportation companies, and so would cause the everywhere sales of an insurance or transportation company to exceed the denominator of its apportionment formula.

The apportionment fraction of each member of the group and for the group is computed as follows:

	A Section 304 Apportionment Percentage	B Subgroup Everywhere Sales	C A * B	D Group Everywhere Sales	E C ÷ D
Corporation A	3.333%	$300	$10.00	$2,000	0.500%
Corporation B	8.333%	$300	$25.00	$2,000	1.250%
Insurance A	2.000%	$700	$14.00	$2,000	0.700%
Insurance B	4.000%	$700	$28.00	$2,000	1.400%
Transportation A	2.500%	$1,000	$25.00	$2,000	1.250%
Transportation B	3.75%	$1,000	$37.50	$2,000	1.875%
Total					6.975%

(Source: Amended at 41 Ill. Reg. ______, effective ____________)

Section 100.5220 Designated Agent for the Members

a) Qualification. The ~~members of a combined group must designate the~~ controlling corporation of a combined group is the designated agent for the group ~~as the agent~~ if the controlling corporation is a member of the combined group. Otherwise, the members of the combined group may ~~must~~ choose ~~which~~ any Illinois taxpayer member of the combined group to ~~will~~ be the designated agent. Designation of the agent is made on Schedule UB. Instances in which a controlling corporation is not ~~will not be~~ a member of the combined group include:

1) The combined group is comprised of corporations which are wholly owned by an individual. In this instance, there is no controlling corporation.

2) A manufacturing corporation that ~~required to~~ apportions its business income under IITA Section 304(a) owns a unitary business group of financial organizations required to apportion their business income under IITA Section 304(c). IITA Section 1502(a)(27) provides that, for taxable years ending prior to December 31, 2017, corporations which use different apportionment formulas under IITA Section 304 are not ~~may not be~~ included in the same unitary business group. Accordingly, the controlling corporation in this example is not a member of the ~~may not be in the same~~ combined group comprised of ~~as~~ its financial organization subsidiaries.

3) The controlling corporation does not have nexus with Illinois, and thus is not an Illinois taxpayer. Only Illinois taxpayers may be members of a combined group.

b) Scope of Agency. The designated agent, for all purposes other than the making of the consent required by Section 100.5210(a)(2) ~~of this Part~~, is ~~shall be~~ the sole agent for each member of the combined group, duly authorized to act in its own name in all matters relating to the tax liability for the combined return year. Except as provided in the preceding sentence, no member has ~~shall have~~ authority to act for or to represent itself in any Illinois income tax ~~such~~ matter. For example, all correspondence between the Department and the combined group is ~~will be~~ carried on directly with the designated agent; the designated agent ~~shall~~ files for all extensions of time; notices of deficiencies are ~~will be~~ mailed only to the designated agent, and the mailing to the designated agent is ~~shall be~~ considered as a mailing to each member in the group; notice and demand for payment of taxes is ~~will be~~ given only to the designated agent and the ~~such~~ notice and demand will be considered as a notice and demand to each member. All taxes, including estimated taxes, are ~~shall be~~ paid in the name of the designated agent. The designated agent ~~shall~~ participates in investigations and hearings on behalf of each member; it ~~shall~~ makes available the information necessary to conduct those proceedings; and it may execute a power of attorney on behalf of itself and the other members of the combined group. The designated agent ~~will~~ files the combined returns and claims for refund or credit of the combined group, and any refund is ~~will be~~ made directly to and in the name of the designated agent and ~~will~~ discharges any liability of the State ~~in respect thereof~~ to any member of the combined group; and the designated agent in its name may ~~will~~ give waivers and execute closing agreements and all other documents, and any waiver so given, or agreement or any other document so executed, is ~~shall be~~ considered as having also been given or executed by each member of the combined group. Notwithstanding ~~Nothwithstanding~~ the preceding provisions, if the Department deals in good faith with a member representing itself to be designated agent for a combined group, any action of such member or of the Department in the course of such dealing has ~~shall have~~ the same effect as if such member were the designated agent.

c) Notices from the Department. Notwithstanding the provisions of subsection (b) above, any Notice of Deficiency, in respect to the tax for a combined return year, will identify each corporation which was a member of the combined group during any part of the period covered by such notice. A failure to properly list all members of the combined group does ~~will~~ not affect the validity of the Notice of Deficiency as to any member. Any notice and demand for payment will be sent to the designated agent and the Department will, if requested by the designated agent, identify each corporation which was a member of the combined group during any part of the period for which the notice and demand is issued. Any levy, any notice of a lien, or any other proceeding to collect the amount of any assessment, after the assessment has been made, will name the corporation from which such collection is to be made.

d) Continuity of Agency. The provisions of subsections (b) and (c) ~~above shall~~ apply to those tax years for which a combined return is required to be made, whether or not a combined return is made for any subsequent year, and whether or not one or more persons have become or have ceased to be members of the combined group at any time.

1) Once a member of a combined group is appointed as the designated agent for that combined group, it ~~shall~~ remains the designated agent for all future years unless:

A) the designated agent ceases to be an eligible member of the combined group, in which case a new designated agent is ~~must be~~ appointed for purposes of common taxable years ending after the date the designated agent ceases to be an eligible member;

B) the controlling corporation of the unitary business group either becomes an eligible member or is replaced as controlling corporation by an eligible member, at which time the controlling corporation ~~shall~~ becomes the designated agent for purposes of common taxable years ending thereafter.

C) a combined group, for its first taxable year ending on or after December 31, 2017, is comprised of two or more combined groups that were not included in the same unitary business group in the previous taxable year because the members of each group used a different apportionment formula under IITA Section 304, and the controlling corporation is not a member of the combined group, the combined group may choose any member of the combined group as the designated agent for that taxable year, whether or not that member was the designated agent of any of the combined groups in the previous taxable year.

2) The designated agent which files a return for a common taxable year ~~must~~ continues to act as designated agent for the combined group for that common taxable year unless:

A) the designated agent is being dissolved or a new designated agent has been appointed for the combined group under subsection (d)(1) ~~above~~, and, in either case, the designated agent notifies the Department in writing that another member of the combined group (or a successor corporation of any member of the combined group) will thereafter act as designated agent for that common taxable year. The member appointed as the substitute designated agent for this purpose need not be the new designated agent appointed under subsection (d)(1) above. The substitute designated agent will succeed to the rights and responsibilities of the former designated agent under subsections (b) and (c) above, and may in turn appoint another substitute designated agent under this subsection (d)(2)(A); or

B) if the designated agent is unable or unwilling to satisfy the tax liability of the combined group or is unresponsive, the Department may, upon notifying the designated agent, deal directly with any member of the combined group in respect to its liability, in which event that ~~such~~ member has ~~shall have~~ full authority to act for itself.

e) Notification of deficiency to corporation which has ceased to be a member of the combined group. If a corporation that joined ~~made the election to file or was required to join~~ in the filing of a combined return has ceased to be a member of the combined group, and if that ~~such~~ corporation files written notice of the ~~such~~ cessation with the Department, then the Department upon request of that ~~such~~ corporation will furnish the corporation with a copy of any Notice of Deficiency in respect of the tax for a combined return year for which it was a member of the combined group and information regarding any notice and demand for payment of that ~~such~~ deficiency. The written notice of cessation should be mailed to the address stated in the instructions to Illinois Schedule UB. The filing of the ~~such~~ written notification and request by a corporation does ~~shall~~ not have the effect of limiting the scope of the agency of the designated agent provided for in subsection (b) above with respect to those tax years during which the corporation was a member of the combined group and a failure by the Department to comply with the corporation's ~~such~~ written request does ~~shall~~ not have the effect of limiting the liability of such corporation provided for in Section 100.5250 ~~of this Part~~.

f) Appointment of designated agent for purposes of resolving disputes over membership in a combined group. If the Department determines that one or more corporations that ~~which~~ did not join in the filing of a combined return are members of a combined group, or that one or more corporations which did join in the filing of a combined return are not members of the combined group that ~~which~~ filed the return, then, for purposes of resolving disputes over the membership of the combined group and any separate company item of any such corporation:

1) If no combined return was filed, the corporations may appoint a member of the combined group that meets the requirements of subsection (a) as the designated agent solely for purposes of contesting the Department's determination. The Department may accept a written representation made by any member of the combined group that it has been appointed the designated agent. The appointment of a designated agent under this

provision is not ~~shall not be construed as~~ a concession by either the corporations or the Department regarding the proper composition of the combined group. The designated agent appointed under this provision has ~~shall have~~ all the rights and responsibilities of a designated agent under this Section. The designated agent appointed under this subsection (f) ~~must meet the qualifications of subsection (a) of this Section and must~~ continues to act as designated agent for the combined group under the provisions of subsection (d) ~~of this Section~~.

2) If a combined return was filed, the designated agent that ~~which~~ filed the return ~~shall~~ represents all corporations which joined in the filing of the combined return and all corporations which the Department asserts are members of the combined group; provided, however, that the Department may allow any corporation which the Department asserts should be added to or eliminated from the combined group included in the return to represent itself after receipt of a written request from such corporation; provided further that, in such case, any such corporation shall be bound by any action taken by the designated agent (including, for example, extensions of the statute of limitations, settlements, stipulations or concessions of fact) before the request of such corporation to represent itself has been accepted by the Department.

(Source: Amended at 41 Ill. Reg. ______, effective ____________)

Section 100.5270 Computation of Combined Net Income and Tax (This draft uses the July 31, 2017 draft version prepared for second notice for the rulemaking updating the regulation provisions dealing with tax rates and exemption amounts, which was published at first notice on July 7, 2017. The amendments from that rulemaking are highlighted in yellow.)

a) Determination of Base Income ~~base income~~. The combined base income is ~~shall be~~ determined by first computing the combined group's combined taxable income and then modifying this amount by the combined group's combined Illinois addition and subtraction modification amounts.

1) Combined Net Income ~~net income~~. ~~The designated agent will determine combined~~ Combined base income is determined by treating all members of the unitary business group (including ineligible members) as if they constituted a federal consolidated group and by applying the federal regulations for determining consolidated taxable income, except that the separate return limitation year provisions and the limitations on consolidation of life and non-life companies in 26 CFR ~~Treasury Reg. Section~~ 1.1502-47 do ~~shall~~ not apply. (See ~~Treasury Reg. Section 1.1502-11,~~ 26 CFR 1.1502-11.) A consolidated net operating loss deduction, as defined in ~~Treasury Reg. Section 1.1502-21,~~ 26 CFR 1.1502-21~~,~~ is ~~shall be~~ added back to taxable income, in whole or in part, in accordance with subsections (a)(2), (4) and (5) ~~below~~. Pursuant to IITA Section

203(e)(2)(E), combined base income is ~~shall be~~ determined as if the election provided by 26 USC ~~Section~~ 243(b)(2) ~~of the Internal Revenue Code~~ had been in effect.

EXAMPLE ~~Example~~ 1. Corporations A and B properly make an election under IITA Section 502(e), or are properly required to file a combined return under IITA Section 502(e). On a separate return basis, A's federal taxable income would be a loss of ($500). This amount does not include an excess capital loss of $75 pursuant to 26 USC ~~Internal Revenue Code Section~~ 1211(a). B's federal taxable income is $1,000 of which $100 is capital gain. As a result of applying 26 CFR ~~Treasury Reg. Section~~ 1.1502-11 and 26 CFR ~~Section~~ 1.1502-22 ~~(26 CFR 1.1502-22)~~, the combined federal taxable income for A and B is $425.

2) Combined Illinois Net Loss ~~net loss~~. The combined group's current year combined taxable income may be less than zero, in which case combined taxable income is ~~it shall be~~ determined by applying the provisions of 26 CFR ~~Treasury Reg.~~ 1.1502-21(f) (consolidated net operating loss) to the unitary business group.

EXAMPLE ~~Example~~ 2. Same facts as Example 1 in subsection (a)(1) ~~above~~ except that Corporation C has also properly joined in the election, or is properly required to join in the combined return filing, and its federal taxable income is a loss of ($800). If there are no addition or subtraction modifications and all of the group's base income is apportioned to Illinois, the group's combined Illinois net loss for the taxable year is ~~will be~~ ($375).

3) Carrybacks and Carryovers ~~carryovers~~. Carrybacks and carryovers, if any, are ~~shall be~~ determined for each member and not for the group. A pro rata share of the loss is attributable to each of the loss members. For Illinois net losses that occurred in taxable years ending on or after December 31, 1986, the amount of any carryback or carryover is ~~shall be~~ determined by applying Sections 100.2340, 100.2350(c)(3) and (c)(4) ~~of this Part~~. For federal net operating losses that occurred in taxable years ending prior to December 31, 1986, the amount of any carryback or carryforward is ~~shall be~~ determined by applying Section 100.2230 ~~of this Part~~.

EXAMPLE ~~Example~~ 3. Same facts as Example 2 in subsection (a)(2) ~~above~~. Assuming the taxable year ends prior to December 31, 1986, the group's combined net operating loss of ($375) is ~~will be~~ divided between A and C as follows for purposes of carryback and carryover:

Corp. A: 500/1,300 x (375) = 144

Corp. C: 800/1,300 x (375) = 231

4) NOL Addition Modification ~~addition modification~~ of Federal Net Operating Loss Deductions ~~federal net operating loss deductions~~ from a Loss Incurred ~~loss incurred~~ in a Taxable Year Ending ~~taxable year ending~~ on or after December 31, 1986. IITA Section 203(b)(2)(D) provides ~~requires~~ that the amount of any federal net operating loss deduction taken in arriving at taxable income for federal tax purposes, other than from a loss in a taxable year ending prior to December 31, 1986, is ~~shall be~~ added back to taxable income in the computation of base income. See Section 100.2320(a) ~~of this Part~~.

5) NOL Addition Modification ~~addition modification~~ of Pre December ~~pre December~~ 31, 1986, Federal Losses ~~federal losses~~. IITA Section 203(b)(2)(E) provides ~~requires~~ an addition modification subject to two limitations for taxable years in which a federal net operating loss carryforward from a taxable year ending prior to December 31, 1986, is an element of taxable income. Consequently, each member allowed to carryback or forward a portion of the group's combined net operating loss from a year in which that combined loss was used to offset a portion of the group's combined excess addition modifications ~~must~~ takes as an addition modification in the carryback or carryover year its respective share of the NOL addition modification provided ~~required~~ by IITA Section 203(b)(2)(E). In accordance with Section 100.2240 ~~of this Part~~, the respective shares are ~~shall be~~ determined in the same manner as the determination of the amount of NOL carryback or carryover.

EXAMPLE ~~Example~~ 4. Same facts as Example 2 in subsection (a)(2) ~~above~~ except that the group had combined excess addition modifications of $100. This amount will be divided among the loss members as follows:

Corp. A: 500/1,300 x 100 = 38

Corp. C: 800/1,300 x 100 = 62

b) Combined Base Income Allocable ~~base income allocable~~ to Illinois. Combined base income allocable to Illinois is the sum of the combined business income or loss apportioned to Illinois plus the combined nonbusiness income or loss allocated to Illinois plus the combined business ~~nonunitary partnership~~ income or loss apportioned ~~allocated~~ to Illinois by partnerships in which the members are partners (other than partnerships that apportion business income under Section 100.3380(d)), less the combined net loss deduction.

1) Combined Business Income Apportionable ~~business income apportionable~~ to Illinois. In the case of a combined group composed solely of members that apportion their business income under the same subsection of IITA Section 304 (that is, insurance companies apportioning business income under IITA Section 304(b), financial organizations apportioning business income under IITA Section 304(c), federally regulated exchanges apportioning business income under IITA Section 304(c-1), transportation companies apportioning business income under IITA Section 304(d), and all other businesses apportioning business income under IITA Section 304(a)), the combined group's combined business income is apportioned using the total Illinois factors of the combined group and total everywhere factors of the unitary business group. In the case of a combined group that includes members that apportion their business income under different subsections of IITA Section 304, the combined group's combined business income is apportioned as provided in Section 100.3600. ~~required to apportion its business income using the three-factor (payroll, property and sales) formula under~~ IITA ~~Section 304(a) of the IITA, the designated agent will apportion the unitary business group's combined business income by using the total Illinois payroll, property and sales of each member of the combined group and the total everywhere payroll, property and sales of each member of the unitary business group (including ineligible members). In the case of groups composed exclusively of one-factor apportionment taxpayers (financial, insurance, or transportation), the unitary business group's combined business income will be apportioned by using the combined group's total Illinois financial, insurance, or transportation factors and total everywhere factors of the unitary business group.~~ Items of income and deduction arising from transactions between members of the unitary business groups are ~~must be~~ eliminated whenever necessary to avoid distortion of the denominators used by the unitary business group in calculating apportionment factors, or of the numerators used by the combined group or by ineligible members of the group in calculating apportionment factors.

A) EXAMPLE ~~Example~~ 1:

i) Corporations A, B, and C constitute a unitary business group. Corporations A and B are eligible to make the election under IITA Section 502(e) for tax years ending before December 31, 1993. However, under Public Law 86-272, Corporation C is not taxable in Illinois.

ii) Based on these facts, if the election to be treated as one taxpayer is made, the combined Illinois sales factor is ~~must be~~ determined by dividing the combined group's total combined Illinois sales (that is, excluding any sales of Corporation C shipped to purchasers in Illinois) by the total combined sales of the unitary business group everywhere. If the same facts are applied to a tax year ending on or after December 31, 1993, the same result will occur in the mandatory combined return situation.

B) EXAMPLE ~~Example~~ 2:

i) Same facts as in Example 1, except these additional facts also exist. Under Public Law 86-272, Corporations B and C are taxable in South Carolina, but corporation A is not.

ii) Based on these facts, if the election to be treated as one taxpayer is made, or the taxpayers are required to be treated as one taxpayer, the combined Illinois sales factor is ~~must be~~ determined by dividing the combined group's total Illinois sales (including any sales of Corporation A shipped to purchasers in South Carolina from any place of storage in Illinois, i.e., throwback sales) by the total sales of the unitary business group everywhere.

2) Combined Nonbusiness Income ~~nonbusiness~~ and Business Income Apportioned ~~nonunitary partnership income allocable~~ to Illinois by Partnerships in which the Members are Partners (other than partnerships that apportion business income under Section 100.3380(d)). The ~~designated agent shall compute the~~ amount of combined nonbusiness income or loss allocable to Illinois is computed by first determining the amount for each member of the combined group and then combining these amounts. Similarly, ~~the designated agent shall compute~~ the amount of combined business ~~nonunitary partnership~~ income or loss apportioned ~~allocable~~ to Illinois by partnerships in which the members are partners (other than partnerships that apportion business income under Section 100.3380(d)) is computed by first determining the amount for each member and then combining these amounts.

3) Combined Illinois Net Loss Deduction ~~net loss deduction~~. The ~~designated agent shall compute the~~ combined Illinois net loss deduction for losses originating in tax years ending on or after December 31, 1986 is computed by determining the amount of deduction available for each member of the combined group in accordance with Sections 100.2330, 100.2340 and 100.2350 ~~of this Part~~ and then by combining these amounts.

c) Combined Exemption ~~exemption~~. Under the election or requirement to be treated as one taxpayer, there is one exemption per combined return. The d~~esignated agent shall compute the~~ combined exemption is computed by multiplying the amount of the exemption allowed under IITA Section 204 and Section 100.2055 ~~$1,000~~ by a fraction, the numerator of which is combined base income allocable to Illinois and the denominator of which is the group's combined base income. The exemption amount for members of unitary groups not making the election, or subject to the requirement, and for members of unitary groups ineligible to make the election, or not subject to the requirement, is computed by multiplying the amount of the exemption allowed under IITA Section 204 and Section 100.2055 ~~$1,000~~ by a fraction, the numerator of which is that member's base income allocable to Illinois, and the denominator of which is the group's combined base income.

d) Combined Credits ~~credits~~

1) Applicability of Credits ~~credits~~. Any ~~The designated agent will compute any~~ credit allowed by the IITA is determined based on the combined activities of the members of the combined group and that ~~such~~ credit is ~~will be~~ applied against the combined liability of the combined group.

2) Credits Based ~~based~~ on Members' Activities ~~members' activities~~. The investment credits provided in IITA Sections 201(e), (f) and (h) and 206(b) are available when certain property is purchased and placed in service by a taxpayer. The combined group is ~~shall be~~ entitled to a combined credit, assuming the other statutory or regulatory requirements applicable to the given credit are satisfied, even if one of the members purchases the qualified property and another member uses the property in a qualified manner.

3) Effective January 1, 1994, the investment credit provided in IITA Section 201(e) is allowed for a taxpayer who is *primarily engaged in manufacturing, or in mining coal or fluorite, or in retailing.* In the case of a combined group, the determination of eligibility is ~~shall be~~ made for the combined group as a whole, rather than for any individual member. The determination of whether a combined group is primarily engaged in a qualifying activity is ~~shall be~~ made by applying the 50% of gross receipts test in Section 100.2101(f) ~~of this Part~~ by taking into account the gross receipts of only the eligible members of the combined group. Gross receipts of corporations which would otherwise be members of the combined group, but which have no taxable presence in Illinois or which cannot be combined for any other reason, are not considered in this determination. In determining whether a combined group is primarily engaged in retailing, gross receipts from transactions between eligible members of the combined group are ~~shall be~~ eliminated from both the numerator and the denominator of the computation. In determining whether a combined group is primarily engaged in manufacturing or in the mining of coal or fluorite, gross receipts from manufacturing or the mining of coal or fluorite ~~shall~~ include:

A) gross receipts from sales of products manufactured or coal or fluorite mined by one eligible member of the combined group to another eligible member of the combined group for use or consumption, and not for resale, provided, however, that the amount of those ~~such~~ gross receipts are ~~shall be~~ subject to adjustment by the Department under the provisions of IITA Section 404 ~~of the IITA~~; and

B) gross receipts from sales to persons outside the combined group by one eligible member of the combined group of items manufactured, or coal or fluorite mined, by another eligible member of the combined group.

4) The additional credit provided in IITA Section 201(e) and the credit provided in IITA Section 201(g) are based on specified increases in employment in Illinois. For purposes of determining entitlement to these credits during a combined-return year, the increase in employment is ~~shall be~~ determined with respect to the employment of all members of the combined group in Illinois and not an individual member's employment. For purposes of determining the increase in employment in Illinois for a common taxable year, the Illinois employment of all taxpayers who are members of the combined group during that common taxable year is ~~shall be~~ used; that is, both prior and current year Illinois employment of current members who were not members of the combined group in the prior year are ~~shall be~~ included in the determination, while prior and current year Illinois employment of taxpayers who ceased to be members of the combined group during the current or prior year are ~~shall be~~ excluded. The application of this subsection (d)(4) is illustrated by the following examples:

EXAMPLE ~~Example~~ 1. Corporations A, B and C were members of a unitary business group which elected to file a combined return for 1989. Corporation D was not a member of the ABC combined group in 1989, but becomes a member of combined group ABCD filing a combined return for 1990. During 1989, Corporations A, B and C employed a total of 150 persons in Illinois and Corporation D employed 50 people in Illinois, for a total of 200.
During 1990, Corporations A, B and C employed 100 persons in Illinois and Corporation D employed 100 persons in Illinois, again for a total of 200.

IITA Section 201(e), which provides for a Replacement Tax Investment Credit for qualified property placed in service by the taxpayer during the year, allows an additional 0.5% credit for that ~~such~~ property to a taxpayer whose Illinois employment has increased by at least 1% over its Illinois employment in the immediately preceding year. Combined group ABCD cannot qualify for the additional 0.5% credit during 1990 because the combined Illinois employment of Corporations A, B, C and D remained unchanged between 1989 and 1990. Because eligibility is determined at the combined group level, no additional credit is ~~can be~~ allowed for qualified property placed in service by Corporation D in 1990, even though Corporation D's Illinois employment doubled between 1989 and 1990.

EXAMPLE ~~Example~~ 2. Corporations P, Q, R and S filed a combined Illinois return for calendar year 1990. On January 1, 1991, Corporation S was sold to an unrelated purchaser. Corporations P, Q and R filed a combined Illinois return for calendar year 1991.

Combined group PQRS employed 400 people in Illinois during 1990, 100 of whom were actually employees of Corporation P and 100 of whom were actually employees of Corporation S. Combined group PQR employed 350 people in Illinois during 1991, 50 of whom were actually employees of Corporation P. Combined group PQR can qualify for the additional 0.5% Replacement Tax Investment Credit allowed under IITA Section 201(e) for qualified property placed in service during 1990 because the Illinois employment of the three members of the combined group increased from 300 in 1989 to 400 in 1990. Because the eligibility is determined at the combined group level, property placed in service by Corporation P during 1990 may qualify for the additional 0.5% credit even though Corporation P's Illinois employment actually decreased.

EXAMPLE ~~Example~~ 3. Prior to its 2013 repeal by Public Act 98-109, IITA Section 201(g) allowed ~~allows~~ a Jobs Tax Credit equal to $500 per eligible employee hired to work in an enterprise zone during a taxable year. The taxpayer must hire 5 or more eligible employees during the taxable year in order to qualify for the credit. The credit is taken in the taxable year following the year the employee is hired. Corporations W, X, Y and Z filed a combined Illinois return for calendar year 1990. Corporation Z was sold to an unrelated purchaser on December 31, 1990. Corporations W, X and Y filed a combined return for 1991.

During 1990, WXYZ hired 5 eligible employees to work in an enterprise zone, 3 of whom were actually hired by Corporation Z. Combined group WXY may claim a Jobs Tax Credit of $2,500 for 1991 because it hired 5 eligible employees during 1990. The fact that Corporation Z, which hired 3 of the employees, left the combined group at the beginning of 1991 does not alter the fact that the combined group earned the Jobs Tax Credit nor entitle Corporation Z to any portion of the credit for its separate company return for 1991.

5) The research and development credit provided in IITA Section 203(j) is based on increasing research activities in this State (see Section 100.2160 ~~of this Part~~). For purposes of determining entitlement to the credit during a combined-return year, the increase in research activities is ~~shall be~~ determined with respect to research activities conducted by all members of the combined group in Illinois and not an individual member's research activities. The following series of examples illustrate the application of the research and development credit in combined return situations involving Corporations A, B and C that incurred the following expenses for qualified research activities in Illinois:

	1990	1991	1992	1993
Corp. A	50,000	50,000	50,000	0
Corp. B	25,000	25,000	100,000	200,000
Corp. C	75,000	125,000	100,000	100,000
	150,000	200,000	250,000	300,000

A) EXAMPLE ~~Example~~ 1. A, B, and C filed combined returns for the years ending December 31, 1990, December 31, 1991, December 31, 1992 and December 31, 1993. The proper amount of the Research and Development Credit for the year ending December 31, 1993 is determined based upon the combined activities on the combined return and is calculated as follows:

Total qualified expenditures for 1993.................. 300,000

Average qualified expenditures for 1990-92......... 200,000

Excess of 1993 expenditures over base period...... 100,000

Research and development credit for 1993.............. 6,500

B) EXAMPLE ~~Example~~ 2. A and B filed a combined return for the year ending December 31, 1990. C filed a separate return for the year ending December 31, 1990. A purchased the common stock of C on January 1, 1991. A, B and C filed combined returns for the years ending December 31, 1991, December 31, 1992 and December 31, 1993. The $75,000 of expenses for qualified research activities in Illinois incurred by C for the year ending December 31, 1990 should be included in the calculation of the average qualified expenditures for the base period. The credit for the combined return is ~~would be~~ calculated as follows:

Total qualified expenditures for 1993.................. 300,000

Average qualified expenditures for 1990-92......... 200,000

Excess of 1993 expenditures over base period...... 100,000

Research & Development Credit for 1993................ 6,500

C) EXAMPLE ~~Example~~ 3. A, B and C filed combined returns for the years ending December 31, 1990, December 31, 1991 and December 31, 1992. On January 1, 1993, A sold the common stock of C to P (an unrelated corporation). For the year ending December 31, 1993, C was included in the combined return filed by P. In determining the proper amount of the Research and Development Credit for the combined return filed by A and B for the year ending December 31, 1993, the expenses for qualified research activities in Illinois incurred by C of $75,000, $125,000 and $100,000 for the years ending December 31, 1990, December 31, 1991 and December 31, 1992, respectively, are not ~~may not be~~ included in the calculation of the average qualified expenditures for the base period for A and B for the year ending December 31, 1993. The credit for the combined return for A and B for the year ending December 31, 1993 is ~~would be~~ calculated as follows:

Total qualified expenditures for 1993.................. 200,000

Average qualified expenditures for 1990-92......... 100,000

Excess of 1993 expenditures over base period...... 100,000

Research & Development Credit for 1993................ 6,500

6) Credit Carryforward ~~carryforward~~. Any combined credit carryforward is ~~shall be~~ available to the combined group for the next combined-return year. For purposes of the credits allowed with respect to certain qualifying property under IITA Sections 201(e), (f), and (h) and 206(b), where a member becomes ineligible to join in the election, or is no longer required to be part of the combined return, the credit carryforward is ~~shall be~~ available to the remaining members if those ~~such~~ members continue to both own and use the property for which the credit was claimed in a qualifying manner for 48 months after the placed-in-service date. The credit carryforward is ~~shall be~~ available to the former member that has become ineligible if that former member both owns and uses the property

for which the credit was claimed in a qualifying manner for the remainder of the 48-month period after the placed-in-service date. If a credit carryforward is available to the former member that has become ineligible, the amount of the carryforward is equal to the combined unused credit multiplied by a fraction, the numerator of which is the credit attributable to the qualified property of that ~~such~~ former member for the combined unused credit year, and the denominator of which is the qualified property of the combined group for the ~~such~~ unused credit year.

EXAMPLE ~~Example~~ 1. In 1985, Corporation A purchased $300,000 of eligible property, $200,000 of which was used by A and $100,000 of which was transferred to and used by Corporation B. A and B filed a combined return for that year which showed an income tax liability of $1,000 and an investment credit of $1,500. The group's unused credit was $500. In 1987, B left the group, and during that year it owned and continued to use the $100,000 of eligible property. Its credit carryforward is ~~would be~~ computed as follows:

$500 x $100,000/$300,000 = $166.67

7) Recapture. For purposes of credits which are recaptured when property ceases to be qualified property or is moved out of Illinois or when property is moved outside of an enterprise zone within 48 months of the placed-in-service date, the members of the combined group are responsible for the recapture of any personal property replacement tax or income tax.

EXAMPLE ~~Example~~ 2. Same facts as in the Example 1 in subsection (d)(6) ~~above~~ except in 1987 Corporation A transferred its eligible property (originally purchased for $200,000, in 1985) to Corporation B. Corporation B was acquired by Corporation C in 1987 and, immediately afterward, B sold all the eligible property (originally purchased for a total of $300,000) to an unrelated third party. B and C file a combined return for that year and ~~they must increase~~ their tax liability is increased by $1,000 due to the credit that was allowed on the combined return filed by A and B in 1985 and is recaptured in 1987.

e) Ineligible Members ~~members~~. If a unitary business group contains one or more ~~an~~ ineligible members (e.g., a partnership that is not required to apply the apportionment method prescribed in Section 100.3380(d), a subchapter ~~i.e., an~~ S Corporation or, for years ending prior to December 31, 1987, a corporation with a different taxable year), the ineligible members shall file ~~a~~ separate unitary returns. In the separate unitary return, the apportionment percentage of that ~~any such~~ ineligible member is ~~shall be~~ determined by dividing the Illinois factor or factors of that member by the combined everywhere factor or factors of all members of the unitary business group. The apportionment percentage is ~~shall~~ then ~~be~~ multiplied by the combined business income of the unitary business group to determine the business income of that ~~such~~ ineligible member apportionable to Illinois. The taxable income of the members is ~~that joined in the election shall be~~ their combined taxable income as determined under subsection (a)(1) ~~of this Section~~. If a corporation is ineligible because it has a different taxable year, ~~it shall use~~ either method of accounting available to part-year members and set forth in subsection (f)(2) may be used to determine the combined taxable income ~~of this Section~~. If two or more corporations are ineligible because they have an accounting period that is different from other members making the election, they may elect to file their own combined return if they have the same taxable year. The foregoing rule also applies in the case of erroneous inclusion of a member in a group otherwise required to file a combined return.

f) Part-year Members ~~members~~

1) General Rule ~~rule~~. If a corporation becomes a member of a unitary business group after the beginning of the combined return year or ceases to be a member of the unitary business group during the combined return year, two tax returns will be affected for that taxable year. The combined return includes ~~shall include~~ the separate company items of that ~~such~~ corporation for the part of the year it was a member of the unitary business group. Separate company items of a part-year member for any portion of its taxable year prior to the date it joins or after the date it leaves the unitary business group are ~~shall either be~~ reported in a short-year separate return filed by that ~~such~~ part-year member (if it is subject to Illinois income tax during that period) or included in any combined return filed on behalf of a unitary business group to which that ~~such~~ part-year member belongs during that portion of the year.

2) Accounting. The part-year member may use ~~shall use~~ either Method 1 or Method 2 (described in Section 100.5265(b) ~~of this Part~~) to determine its separate company items for the portion of the year before it becomes a member and the portion of the year after it becomes a member of the combined group.

(Source: Amended at 41 Ill. Reg. _______, effective __________)

Section 100.9700 Unitary Business Group Defined (IITA Section 1501)

a) Scope
This regulation is designed to clarify the meaning of IITA Section 1501(a)(27), defining "unitary business group", which definition became effective for tax years ending on or after December 31, 1982.

b) Persons Required to Use Combined Apportionment ~~required to use combined apportionment~~

Any person subject to Illinois income taxation may be a member of a unitary business group that ~~and required to~~ uses combined apportionment under IITA Section 304(e). Only corporations ~~Corporations~~ (other than Subchapter S corporations) who are members of a unitary business group ~~are required to~~ file combined returns under IITA Section 502(e). For the treatment of certain partners and partnerships engaged in a unitary business, see Section 100.3380(d) of this Part. Every member of a unitary business group who is neither a corporation that joins ~~required to join~~ in a combined return nor a partnership excluded from combined apportionment under Section 100.3380 determines ~~of this Part shall determine~~ the Illinois portion of its business income pursuant to IITA Section 304(e) by computing the combined business income of the unitary business group in the manner prescribed in Section 100.5270(a) of this Part, and apportioning that ~~such~~ unitary business income to Illinois using the combined "everywhere" apportionment factors of the unitary business group and that person's own "Illinois" apportionment factors. If one or more other members of the unitary business group have taxable years different from the taxable year of the taxpayer filing the return, that taxpayer computes ~~shall compute~~ the combined business income of the group for its taxable year by including the incomes of the members using a different taxable year in the manner prescribed by Section 100.5265 of this Part.

c) The 80-20 U.S. Business Activity Test for Prospective Members of a Unitary Business Group ~~business activity test for prospective members~~

The factors to be used in determining whether 80% or more of a person's business activity is conducted outside the United States are ~~shall be~~ gross figures without eliminations premised on the person's membership in any unitary business group. However, the factors should relate to the common taxable year, as defined in Section 100.5265 of this Part, of the unitary business group of which the person being tested could become a member were the person's business activity found to be less than 80% outside the United States. The factors to be used are as follows:

1) persons who ~~required to~~ apportion business income under IITA Section 304(a) will use property and payroll,

2) persons who ~~required to~~ apportion business income under IITA Sections 304(b), 304(c) or 304(d) will use the respective factors prescribed in those provisions.

A) For taxable years ending prior to December 31, 2017~~In accordance with IITA Section 102 and 26 USC 7701(b)(9)~~, *the phrase "United States" as used in IITA Section 1501(a)(27)* includes ~~shall include~~ *only the fifty states and the District of Columbia, but does not include any territory or possession of the United States or any area* *over which the United States has asserted jurisdiction or claimed exclusive rights with respect to the exploration for or exploitation of natural resources. For taxable years ending on or after December 31, 2017, the phrase "United States", as used in IITA Section 1501(a)(27), means only the 50 states, the District of Columbia, and any area over which the United States has asserted jurisdiction or claimed exclusive rights with respect to the exploration for or exploitation of natural resources, but does not include any territory or possession of the United States*. (IITA Section 1501(a)(27)(B), as amended by P.A. 100-0022) Areas over which the United States has asserted jurisdiction and claimed exclusive rights with respect to the exploration for or exploitation of natural resources include the outer continental shelf. (See 26 USC 638 and 43 USC 1331)

B) Mechanically, the computation of the 80-20 U.S. business activity test involves ~~requires~~ the formation of one or two fractions, as the case may be, and the subsequent averaging of those fractions to arrive at an overall U.S. business activity in relation to world-wide business activity. The numerators of the fraction represents U.S. property, U.S. payroll, U.S. revenue miles or other transportation company factors, insurance premiums on property or risk in the U.S. or financial organization business income from sources within the U.S.; the respective denominators are world-wide figures.

C) In the case of a person who would be a member of a unitary business group for only part of a taxable year if less than 80% of its business activities were conducted outside the United States, the 80-20 U.S. business activity test is ~~shall be~~ applied only to that part of the person's taxable year for which the prospective member otherwise qualifies for membership in the unitary business group. If that person is a corporation and is a prospective member of a unitary business group required to file combined returns under IITA Section 502(f), the 80-20 U.S. business activity test is ~~shall be~~ applied only to that part of the combined group's common taxable year for which that person otherwise qualifies for membership in the combined group.

d) Taxpayers Using Different Apportionment Formulas ~~Entities using different apportionment formulas~~ under IITA Section 304

1) For taxable years ending prior to December 31, 2017, only taxpayers who use the same apportionment formula under IITA Section 304 may be members of the same unitary business group. ~~All members of a unitary business group must be eligible under IITA Section 304 to use the same apportionment formula.~~ As a consequence, a corporation that ~~required to~~

uses the three factor apportionment formula of IITA Section 304(a) ~~cannot be~~ is not a member of the same unitary group as a corporation that ~~required to~~ uses the one factor apportionment formula of IITA Section 304(c), nor is ~~may~~ a corporation that ~~required to~~ uses the one factor apportionment formula of IITA Section 304(c) ~~be~~ a member of the same unitary business group as a corporation that ~~required to~~ uses the one factor apportionment formula of IITA Section 304(b). The proper method for determining unitary business group memberships under IITA Section 1501(a)(27) is first to identify all entities that are related through common ownership and engaged in either horizontally or vertically integrated enterprises with the requisite exercise of strong centralized management and second, to create from the population of entities thus identified one unitary business group composed of entities required to apportion under IITA Section 304(a), one unitary business group composed of entities required to apportion under IITA Section 304(b), one unitary business group composed of entities required to apportion under IITA Section 304(c), one unitary business group composed of entities required to apportion under IITA Section 304(c-1) and one unitary business group composed of entities required to apportion under IITA Section 304(d). For taxable years ending on or after December 31, 2017, all taxpayers may be included in the same unitary business group without regard to the apportionment formula used by any of the taxpayers under IITA Section 304. (IITA Section 1501(a)(27)(B), as amended by P.A. 100-0022)

2) EXAMPLE:

A) FACTS: For the taxable year ending December 31, 2016, Corporation A owns all of the outstanding common stock of Corporations B and C. Corporations B and C each own 30% of the outstanding common stock of Corporation D. Corporation D owns 60% of the outstanding common stock of Corporation E. Corporation A is a mining company operating exclusively in Illinois. Corporation D is a manufacturing company with factories in Illinois and Indiana. Corporation C is an insurance company earning premiums for insuring property and risks located in Illinois and Indiana. Corporation B is an air freight company and Corporation E is a trucking company, both operating nationwide. In their relationships to one another, the five companies: are "steps in a vertically structured enterprise or process" and are "functionally integrated through the exercise of strong centralized management."

B) ANALYSIS AND CONCLUSION: As a result of these facts, Corporations A and D, which would ~~ordinarily be required to~~ apportion business income using the formula in ~~by means of the three factor apportionment formula of~~ IITA Section 304(a), will constitute one unitary business group; Corporations B and E, which would ~~ordinarily be required to~~ apportion business income using the transportation company formula in ~~by means of the one factor transportation formula~~ IITA Section 304(d) will constitute a second unitary business group; and Corporation C will compute its liability on a non-combined apportionment basis using the insurance company formula in ~~under~~ IITA Section 304(b).

e) Common Ownership ~~ownership~~
In the case of a corporation, common ownership means direct or indirect control or ownership of more than 50% of the corporation's outstanding voting stock. In the case of any other entity, common ownership means direct or indirect ownership of an interest sufficient to exercise control over the activities of the entity. For example, ownership of a general partnership interest gives the partner the authority to act on behalf of the partnership and bind the partnership, regardless of actual ownership share. See Section 9 of the Uniform Partnership Act [805 ILCS 205/9]. Accordingly, a general partner in any partnership has an interest in the partnership sufficient to establish common ownership. Insofar as corporations are concerned, a person ~~one~~ has direct ownership of the outstanding voting stock of the corporation ~~another~~ to the extent that the person ~~it~~ owns ~~such~~ the stock and indirect control to the extent that the person ~~it~~ owns the voting stock of a another ~~third~~ corporation that itself owns ~~such~~ stock in the first corporation. Any combination of direct and indirect control or ownership aggregating more than 50% will suffice to qualify the corporation whose stock is owned for membership in the unitary business group if the other tests unrelated to ownership are met.

1) EXAMPLE 1. Corporation A owns 60% of the outstanding voting stock of Corporation B which in turn owns 60% of the outstanding voting stock of Corporation C. There is common ownership of Corporations A, B and C by reason of Corporation A's direct ownership of more than 50% of the outstanding voting stock of Corporation B and indirect control of more than 50% of the outstanding voting stock of Corporation C.

2) EXAMPLE 2. Corporation A owns 60% of the outstanding voting stock of Corporation B and 60% of the outstanding voting stock of Corporation C. Corporations B and C in turn each own 30% of the outstanding voting stock of Corporation D. Corporations A, B, C and D are all under common ownership by reason of Corporation A's direct ownership of more than 50% of the outstanding voting stock of Corporations B and C and by reason of Corporation A's indirect control of more than 50% of the outstanding voting stock of Corporation D.

3) EXAMPLE 3. Corporation A owns 60% of the outstanding voting stock of Corporation B and 40% of the outstanding voting stock of Corporation C. Corporations B and C each in turn own 30% of the outstanding voting

stock of Corporation D. Corporations A and B are under common ownership by reason of Corporation A's direct ownership of more than 50% of the outstanding voting stock of Corporation B, but neither Corporations C or D are under common ownership with Corporations A and B because neither Corporation A nor Corporation B has direct or indirect control or ownership of more than 50% of the outstanding voting stock of Corporations C or D.

4) EXAMPLE 4. Corporation A owns 60% of the outstanding voting stock of Corporation B and 40% of the outstanding voting stock of Corporation C. Corporation B owns 30% of the outstanding voting stock of Corporation D and Corporation C owns 60% of the outstanding voting stock of Corporation D. Corporations A and B are under common ownership by reason of the fact that Corporation A owns more than 50% of the outstanding voting stock of Corporation B, and Corporations C and D are under separate common ownership by reason of the fact that Corporation C owns more than 50% of the outstanding voting stock of Corporation D.

f) Attribution of Stock Ownership Among Certain persons ~~stock ownership among certain persons~~

For the purpose of IITA Section 1501(a)(27), a person is ~~shall be~~ considered to have indirect control over any stock that that person is considered as owning under IRC section 318(a).

EXAMPLE: Strictly as an investment, Mr. X and his wife, Mrs. X, each individually own 30% of the outstanding voting stock of Corporation A and 30% of the outstanding voting stock of Corporation B. Corporations A and B are under common ownership within the meaning of Section 1501(a)(27), and assuming that they meet the other requirements of IITA Section 1501(a)(27), they will be members of the same unitary business group. The common ownership stems from the fact that, under IRC section 318(a)(1), the stock holdings of Mr. X are imputed to his wife and vice versa. Note that it is not necessary in order for Corporations A and B to be members of a unitary business group that the "person" in whom the common ownership is embodied also be a member of the unitary business group.

g) Strong Centralized Management ~~centralized management~~

Under IITA Section 1501(a)(27), no group of persons can be a unitary business group unless they are functionally integrated through the exercise of strong centralized management. It is this exercise of strong centralized management that is the primary indicator of mutual dependency, mutual contribution and mutual integration between persons that is necessary to constitute them members of the same unitary business group. The exercise of strong centralized management is ~~will be~~ deemed to exist where authority over such matters as purchasing, financing, tax compliance, product line, personnel, marketing and capital investment is not left to each member. Thus, some groups of persons may properly be considered as constituting a unitary business group under IITA Section 1501(a)(27) when the executive officers of one of the persons are normally involved in the operations of the other persons in the group and there are centralized units that perform for some or all of the persons functions that truly independent persons would perform for themselves. Note in this connection that neither the existence of central management authority, nor the exercise of that authority over any particular function (through centralized operations), is determinative in itself; the entire operations of the group must be examined in order to determine whether or not strong centralized management exists. A finding of "strong centralized management" is not ~~cannot be~~ supported merely by showing that the requisite ownership percentage exists or that there is some incidental economic benefit accruing to a group because such ownership improves its financial position. Only if both ~~Both~~ elements of strong centralized management, i.e., strong central management authority and the exercise of that authority through centralized operations, are ~~must be~~ present will ~~in order for~~ persons ~~to~~ be a unitary business group under IITA Section 1501(a)(27). Finally, a finding of strong centralized management can be supported even though the authority resides in a person that is not a member of the group, provided that the authority is actually exercised by that ~~such~~ person.

h) General Line of Business and Vertically Structured Enterprises ~~line of business and vertically structured enterprises~~

1) Section 1501(a)(27) of the Act establishes that persons meeting all of the other tests for inclusion in a unitary business group, including common ownership, strong centralized management and comparability of apportionment method, will ordinarily be in one of the following relationships to one another:

A) in the same general line of business, or

B) steps in a vertically structured enterprise or process.

2) IITA Section 1501(a)(27) recites that two persons will ordinarily be considered to be in the same general line of business if they are both involved in one of the following activities:

A) manufacturing

B) wholesaling

C) retailing

D) insurance

E) transportation, or

F) finance

3) IITA Section 1501(a)(27) does not contemplate that the above list be exclusive. For example, two persons that are both involved in rendering services to the public would ordinarily be considered to be in the same general line of business. In this regard, a retailer that renders services that are incidental to its retail business is not ~~will not be~~ in the same general line of business as a person that is primarily a provider of that same type of service ~~dispenser~~.

4) It is not a requirement of IITA Section 1501(a)(27) that the activities of the two persons in whichever category is applicable relate to the same product or product line in order for the two persons to be in the same general line of business.

5) Two persons are steps in a vertically structured enterprise or process under IITA Section 1501(a)(27) even though other persons who are also steps in that enterprise or process are not members of the same unitary business group because of the intervention of: the 80-20 U.S. business activity test or the rules stated in subsection (d) of this Section, relating to the comparability of apportionment formulas of members of a unitary business group.

EXAMPLE 1:

A) FACTS: Corporation A manufactures furniture. Corporation C retails the furniture manufactured by Corporation A. Corporation B is a furniture finisher and wholesaler operating exclusively in Mexico which purchases Corporation A's unfinished furniture, applies the appropriate finishing materials in its Mexican plants, and sells the finished furniture to Corporation C.

B) ANALYSIS AND CONCLUSION: Corporations A and C are steps in a vertically structured enterprise and therefore ~~as such~~ can be members of the same unitary business group. They do not lose their status as steps in a vertically structured enterprise by reason of the fact that they never directly deal with one another, since they both deal with Corporation B which is also a step in the vertically structured enterprise and which would be a member of the unitary business group if the other tests for a unitary business were met ~~were it not for the intervention of the 80/20 U.S. business activity test~~.

6) A person is not ~~will not be~~ a step in a vertically structured enterprise or process unless it is connected to one or more other persons that are steps in the vertically structured enterprise or process by a flow of goods or services, including management services, to itself or from itself. However, if the flow of goods or service is present with respect to a particular person, that person's status as a step in the vertically structured enterprise or process does ~~shall~~ not depend on the relationship between the price at which this flow exists and the fair market price at which this flow would exist in an arm's length transaction.

EXAMPLE 2:

A) FACTS: Same facts as in the previous example, except that Corporation A can establish that it sells its unfinished furniture to Corporation B at a fair market arm's length price and Corporation C can establish that it purchases the finished furniture from Corporation B at a fair market arm's length price.

B) ANALYSIS AND CONCLUSION: Even with their respective showings that the flow of furniture connecting them to Corporation B existed at an arm's length price, Corporations A and C are still steps in a vertically structured enterprise and can still be members of the same unitary business group.

(Source: Amended at 41 Ill. Reg. ______, effective ____________)