



TAX TRENDS

The newsletter of the Illinois State Bar Association's Section on State & Local Taxation

Editor's note

By Stanley R. Kaminski

This issue of *Tax Trends* contains an article by David Dorner on the application of the Illinois Income Tax on persons claiming to be nonresidents. David discusses the rules used to determine whether a person is a nonresident

and some of the facts scrutinized by the Department of Revenue. This Issue of *Tax Trends* also includes the Chicago Department of Revenue's question-and-answer sheet for the new Employers' Expense Tax Relief Ordinance." ■

I'm a nonresident of Illinois—maybe?

By David P. Dorner

Over the last few years, the Illinois Department of Revenue ("Department"), like many other states' tax agencies, has focused considerable attention on high-net-worth former residents now claiming to be residents of another state. The Department has generally limited its audits to prior Illinois residents who accumulated significant wealth while living in Illinois and then moved to another state which does not impose a personal income tax.¹ More often than not, these "nonresidents" of Illinois continue to maintain ties with Illinois, usually through ownership of a home or business in Illinois, or possibly a spouse who continues to reside in Illinois. Therefore, while these persons may believe they are no longer residents of Illinois, they in fact may still be considered residents for Illinois income tax purposes.

Under Illinois law, you are a resident of Illinois for Illinois Income Tax purposes if: (1) you are in Illinois for other than a temporary or transitory purpose, or (2) your domicile is in Illinois but you are absent from Illinois for a temporary or transitory purpose.² A resident of Illinois is usually, but not always, domiciled in Illinois. The term "domicile" commonly means an individual's "permanent home," which is where the individual intends to return to after a period of absence.³ A person has only one domicile and does not acquire a new domicile without first abandoning the prior domicile.⁴ The outcome of residency

cases often depends on whether the person is absent from Illinois for other than a temporary purpose, but is often discussed in terms of domicile. The parties and the courts generally focus on domicile because the mere absence from one's domicile does not generally create residency somewhere else. For instance, if a person maintains two homes—one in Illinois and the second in Florida, and the person spends a substantial amount of time in each home, then the person, for tax purposes, will almost always be a resident of the state in which the person is domiciled since the person's activities in the other state will generally be viewed as transitory or temporary in nature.⁵

Whether a person is "domiciled" in Illinois or present in Illinois only for a "temporary or transitory" purpose depends on the facts and circumstances specific to each situation. There is a presumption, however, that an individual is a resident of Illinois if the individual spends in the aggregate more than nine months of any taxable year in Illinois. Additionally, if an individual is absent from Illinois for one year or more it will be presumed that the individual is a nonresident of Illinois.⁶ A person's residency status is generally a matter of intent—i.e., intent to create a new home in another state (or country), or intent to remain in or be absent from a state for other

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I'm a nonresident of Illinois—maybe?

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than a temporary or transitory purpose. Intent is evidenced by the facts and deeds supporting the person's behavior. Testimonial evidence of a person's intent to become domiciled or to reside outside of Illinois is generally not sufficient to prove a change in domicile or residency.⁷ Rather, documentary evidence must be presented to substantiate a person's claim that he or she is a resident of another state. Such documentary evidence may include: 1) voter registration cards; 2) automobile and driver's license registrations; 3) maintenance of other state licenses (e.g., CPA, broker's, hunting, fishing, boating, etc.); 4) home ownership or long-term rental agreements; 5) club, gym or organizational memberships; 6) religious affiliation with a place of worship; 7) establishment of regular medical and pharmacy providers; 8) if applicable, the filing of income tax returns as a resident in the other state; 9) the opening of bank and investment accounts; 10) burial plots; and 11) safety deposit boxes.⁸ The more factors present in the claimed state of residency, the more likely you will be found to be a nonresident of Illinois.

In addition to the above documents, the Department may request or subpoena other records such as: 1) flight records from a person's airline reward programs; 2) credit card statements; 3) landline telephone and cell phone bills; 4) property tax records; 5) federal and state income tax returns; 6) trust documents and wills; and 7) insurance policies. The Department requests such documents to determine how often the individual is in Illinois during the audit period. Additionally, if the person has Illinois property, the Department will almost always check to see if the person is claiming an Illinois homeowner's exemption on the property, since the homestead exemption for property tax is limited to property used as a primary dwelling place.⁹ Trust documents and wills frequently identify the person's state of residency, and insurance policies may be used to identify the location of other real or personal property. The Department may also inquire as to the domicile of a spouse and/or children, given that a person will generally share a domicile with their immediate family. Ownership interests in a business located in Illinois, particularly if the individual is a director, managing member, partner, or otherwise actively involved in the business, may also draw additional scrutiny

from the Department. The Department may also look into a person's employment, especially employment agreements that outline duties, duration of employment or terms of an out-of-state work assignment.

A particular area of caution and concern is where one spouse remains a resident of Illinois while the other spouse establishes residency outside of Illinois. Although it is not uncommon for married persons to reside in different states, the Department will understandably be more vigilant in their examination of such arrangements. Moreover, resident and nonresident spouses should be very careful as to how they file their Illinois income tax returns. For instance, when one spouse resides outside of Illinois, the State of Illinois requires the married couple to file separate Illinois income tax returns, unless the nonresident spouse elects to be treated as a resident of Illinois for purposes of taxation.¹⁰ By filing a joint Illinois income tax return, the nonresident spouse is electing to be treated as a resident of Illinois.¹¹ It should be noted that it is incorrect and inconsistent to file a joint Illinois income tax return that includes a nonresident schedule (i.e., Illinois Schedule NR) for one spouse.¹² In such instances, the Department requires the nonresident and resident spouses to refile their Illinois income tax return(s) and either file a joint return, without a nonresident schedule, or separate Illinois income tax returns if both spouses have Illinois sourced income.¹³ Historically, due to the inconsistencies of a joint return filed with a resident and nonresident spouse, the Department has not treated the filing of a joint return with a nonresident schedule as an election by the nonresident spouse to be deemed, for tax purposes, as a resident of Illinois. However, an administrative law judge (ALJ) recently ruled, under similar circumstances, that a taxpayer did in fact waive his right to claim that he was a nonresident of Illinois, since he had filed a joint Illinois income tax return with his wife, who was an Illinois resident.¹⁴

As indicated above, a change of residency for state income tax purposes is not as easy as it may seem, particularly for persons who maintain more than one home or reside separately from their spouse or young children. There is nothing wrong with changing one's domicile for the primary purpose of reducing or avoiding taxes; in fact it may be financially

prudent for some people to do so. However, in such instances it becomes even more important to have clear, admissible documents and records reflecting the change in residency and to be cognizant of other records (i.e., credit cards, phone records, frequent flyer programs) that may evidence intent to change residency, including records which demonstrate the amount of time a person spends in their prior state of residency. ■

1. Please note, changing one's domicile for the primary purpose of tax planning is fine, as long as requirements for establishing residency somewhere else are met and can be established by admissible books and records.

2. 35 ILCS 1501(a)(20).

3. 86 ILL. ADMIN. CODE 100.3020(d).

4. *Id.*

5. See the decision in *Dods v. Dep't of Rev.*, Cook County Case No. 07 L 050695 (8/24/2009), currently on appeal.

6. 86 ILL. ADMIN. CODE 100.3020(f).

7. *Mel-Park Drugs, Inc. v. Dep't of Rev.*, 218 Ill. App. 3d 203, 217, 577 N.E.2d 1278, 1287 (1st Dist. 1991).

8. 86 Ill. Admin. Code 100.3020(g); *Dods, supra* note 5, at 5, (citing *Klemp v. Franchise Tax Board*, 45 Cal. App. 3d 870, 873-874 (2d Dist. 1975)).

9. 35 ILCS 200/15-175.

10. 35 ILCS 5/502(c)(3). *Note:* For tax years ending on or after December 31, 2009, if a husband and wife file a joint federal income tax return, then they may elect for the same tax year to file separate Illinois income tax returns. 35 ILCS 5/502(c)(1)(B). The election to file separate Illinois income tax returns must be made on or before the extended due date of the return and, once made, the election is irrevocable. *Id.* For tax years 2008 and earlier, married persons filing a joint federal income tax return are required to file a joint Illinois tax return if both spouses were Illinois residents. 35 ILCS 5/502(c)(1)(A).

11. *Id.*

12. See Form IL-1040-X Instructions, Step 1, Line C (R-12/09) ("If you originally filed a joint return, but did not treat both yourself and your spouse as Illinois residents, you must correct that error by either filing a joint IL-1040-X treating yourselves as Illinois residents or by filing separate IL-1040-X forms, even if the extended due date has passed.")

13. *Id.*

14. ILLINOIS DEPARTMENT OF REVENUE DECISION IT 09-8 (8/3/2009). The ALJ also surprisingly opined that the nonresident spouse, in order to prove that he abandoned his domicile in Illinois, should have transferred his rights in their home in Illinois to his resident spouse. Although a potentially clear indication of intent to abandon one's domicile, this recommendation seems drastic, particularly when there are non-income tax related reasons for not transferring ownership in the home to the resident spouse.

Employer's expense tax relief ordinance FAQs

Drafted by the Chicago Department of Revenue and supplied to the Chicagoland Chamber of Commerce's Tax Liaison Committee with the Department

1) What is the effective date of the ordinance?

The ordinance was effective upon passage and approval by the Chicago City Council, which took place on Wednesday, January 13, 2010.

2) When will tax filers first need to take action on their new employer's expense tax return filing and paying obligations?

Not until they file tax returns covering the annual tax year covering July 1, 2009 through June 30, 2010, which will be distributed in late June 2010 and are due to be filed by August 16, 2010.

3) Does the amendment allow filers to adjust periodic tax payments for covered periods in anticipation of the relief granted under this amendment?

No. None of the municipal code mandated employer's expense tax payment obligations were revised. The relief granted by this amendment is computed and reported on applicable tax returns as they are filed, if applicable. Any amount of tax relieved due to this ordinance that are overpaid as a result of this ordinance, will be refunded or credited to future tax periods as directed by tax filers on applicable tax returns.

4) What specific relief was granted to tax filers in this amendment?

- Employers, located in whole or in part in Chicago throughout the tax year ending June 30, 2009 and who had no obligation to file returns or pay employers expense tax in the tax year ending June 30, 2009 will have no obligation to file returns or pay tax for the tax years ending June 30, 2010 or June 30, 2011
- Employers, located in whole or in part in Chicago throughout 2009 whose liabilities for tax to be computed due for the current tax year ending June 30, 2010, will be limited to the lower amount due for the current year or the prior tax year ending June 30, 2009. Once this lower amount is determined for the tax return period ending June 30, 2010, it will be used in the comparison on the tax return due for the period ending June 30, 2011. In other words, no present tax filers tax liability will increase in the current tax year

ending June 30, 2010, or in the tax year ending June 30, 2011

5) Section 5 of the ordinance discusses the hypothetical prior year liability of entities, that are merged or consolidated in a current tax year. This would be necessary to conduct an apples to apples comparison of annual tax year liabilities and avoid an unintentional loss of revenue to the city. In computing the hypothetical liability for a prior year on what date does a taxpayer assume the hypothetical merger took place?

On the exact same calendar day and month the actual merger took place in the current year.

6) This ordinance includes a repeal date of August 16, 2011. Does that mean relief granted in this ordinance is available to employers for a portion of the tax year ending June 30, 2012? (More specifically the period July 1, 2011 through August 16, 2011).

No. Sections three and four of the ordinance limit relief to the tax years ending June 30, 2010 and June 30, 2011.

7) Is this ordinance an amendment of the Employers Expense Tax in the municipal code?

No, it is a stand alone relief ordinance that will require no further consideration by city council on the August 16, 2011 date of repeal. ■



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Upcoming CLE programs

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June

Friday, 6/18/10- Quincy, Stoney Creek Inn—Legal Writing: Improving What You Do Every Day. Presented by the Illinois State Bar Association. 8:30-12:45.

Monday, 6/21/10- Webinar—Advanced Legal Research on Fastcase. Presented by the Illinois State Bar Association. *An exclusive member benefit provided by ISBA and ISBA Mutual. Register at <https://www1.gotomeeting.com/register/863461769>. 12-1.

Tuesday, 6/22/10- Teleseminar—Buying and Selling Distressed Real Estate, Part 1

Tuesday, 6/22/10- Webcast—Women in the Criminal Justice System. Presented by the ISBA Women in the Law Committee. 12-1.

Wednesday, 6/23/10- Teleseminar—Buying and Selling Distressed Real Estate, Part 2.

Wednesday, 6/23/10- Teleseminar—Health Care Reform 2010- How it Will Impact

Employers, Part 2.

Thursday, 6/24/10- Friday 6/25/10- St. Louis, Hyatt Regency St. Louis at the Arch—CLE Fest Classic St. Louis- 2010. Presented by the Illinois State Bar Association. 11:00-4:40; 8:30-4:10.

Thursday, 6/24/10- Teleseminar—Business Exit and Succession Planning for closely Held Businesses. 12-1.

Tuesday, 6/29/10- Springfield, INB Conference Center, 431 S. 4th St—Legal Writing: Improving What You Do Every Day. Presented by the Illinois State Bar Association. 8:30-12:45.

Tuesday, 6/29/10- Teleseminar—Negligent Hiring. 12-1.

July

Tuesday, 6/6/10- Teleseminar—Like-Kind Exchange of Business and Business Internals.

Thursday, 7/8/10- Webinar—Conducting Legal Research on FastCase. Presented by the Illinois State Bar Association. *An exclusive member benefit provided by ISBA and ISBA Mutual. Register at <https://www1.gotomeeting.com/register/906864752>. 12-1.

Tuesday, 6/13/10- Teleseminar—Business Torts, Part 1.

Wednesday, 6/14/10- Teleseminar—Business Torts, Part 2.

Thursday, 7/22/10- Webinar—Advanced Legal Research on Fastcase. Presented by the Illinois State Bar Association. *An exclusive member benefit provided by ISBA and ISBA Mutual. Register at <https://www1.gotomeeting.com/register/403171688>. 12-1.

Thursday, 7/22/10- Teleseminar—Construction Contracts.

Tuesday, 7/27/10- Teleseminar—Goodwill in Business Transactions. ■



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