Chapter 18: Illinois Update

Please note. Corrections for all of the chapters are available at **www.TaxSchool.uiuc.edu.** For clarification about acronyms used throughout this chapter, see the Acronym Glossary at the end of the Index.

The Illinois Department of Revenue (IDOR) instituted several changes this year — some legislative, some administrative. This chapter begins with information on the implementation of IDOR's new computer system and how it will affect taxpayers and practitioners.

Next, in-depth coverage is provided on recent changes to rules affecting Illinois payroll tax withholding and a new requirement for pass-through organizations to submit annual tax payments on behalf of nonresident partners, shareholders, and beneficiaries.[1] The preparation of composite state tax returns is also covered, as are the tax implications of the recently enacted Illinois Employee Classification Act.[2]

The rest of this chapter addresses limited liability companies (LLCs), including a review of the Illinois Limited Liability Company Act[3] and the Illinois series LLC which was enacted in 2005.[4]

IDOR IMPLEMENTS NEW COMPUTER SYSTEM

In December 2007, IDOR began the monumental task of consolidating the administration of more than 200 state tax and fee programs into a single, integrated computer management system.[5] The department plans to phase in this system migration over a 4-year period at a cost of $45 million.[6]

By merging and updating the state's multiple computer systems, some of which are 30 years old, IDOR hopes to improve taxpayer service. The new system will enhance the department's processing of tax returns and its ability to provide information to taxpayers and practitioners. It will also improve IDOR's billing and collection procedures, as well as the department's ability to enforce Illinois tax laws. With this increased efficiency, the state projects revenue collections will increase by $250 million.[7]

1. 35 Illinois Compiled Statutes (ILCS) 5/709.5
2. Illinois Employee Classification Act, Public Act 95-0026 (HB 1795), effective January 1, 2008
3. Limited Liability Company Act, 805 ILCS 180 et seq.
4. Series LLCs, 805 ILCS 180/37-40
5. *Illinois Begins Implementation of New Tax Computer System*, IDOR Informational Bulletin FY 2008-10 (Dec. 2007)
6. IDOR/Governor Rod Blagojevich Press Release, *State to launch modernization project that will improve services for taxpayers* (Sept. 1, 2006)
7. Ibid

PHASE ONE IMPLEMENTATION

The first phase of improvements, which began at the end of 2007, includes the following taxes and forms:

- Sales tax (ST-1, *Sales and Use Tax Return*, only)
- Income tax withholding (IL-941, *Illinois Quarterly Withholding Income Tax Return*)
- Business income and replacement taxes, including:
  - IL-1120, *Corporation Income and Replacement Tax Return*,
  - IL-1120-ST, *Small Business Corporation Replacement Tax Return*,
  - IL-1065, *Partnership Replacement Tax Return*,
  - IL-1041, *Illinois Fiduciary and Replacement Tax Return*,
  - IL-1023-C, *Composite Income and Replacement Tax Return*, and
  - IL-990-T, *Exempt Organization Income and Replacement Tax Return*.

EFFECT ON ILLINOIS TAXPAYERS

Taxpayers and practitioners affected by the first phase implementation of the new computer system will see changes in the appearance of IDOR communications. Notices and bills will have an updated look, including an **account ID** for each type of tax and a section titled "Taxpayer Statement."

The Taxpayer Statement section is new for business income tax and withholding-tax filers and replaces the "Statement of Account" for sales-tax filers. This portion of the notice details amounts owed and available credits, as well as whether the taxpayer has any nonfiled returns.

Taxpayers will continue to receive separate notices and billings under their current tax identification numbers for taxes and fees that have not yet been rolled into the new system. However, account IDs will gradually replace the use of Illinois business tax (IBT) numbers. At the end of the 4-year transition period, **IBT numbers will be obsolete**.

Changes for ST-1 Filers

Sales and use tax return filers have already received statements under the new format. These updated forms reference the taxpayer's account ID instead of IBT number. Taxpayers filing related sales tax returns, such as County Motor Fuel Tax returns, will receive separate notices until these taxes are migrated to the new system.

Outstanding sales-tax balances will automatically be offset by any credit memoranda on the taxpayer's account. This information will be shown in the Taxpayer Statement section. IDOR will apply any accelerated payments to the oldest accelerated payment due (quarter-monthly). Taxpayers must report any corrections on Form ST-1-X, *Amended Sales and Use Tax Return*.

Form Changes for Business Income and Replacement Tax Filers

In 2007, IDOR extensively revised Forms IL-1041, IL-1023-C, and IL-990-T to make these forms more consistent with other Illinois business income tax returns. For tax years ending on or after December 31, 2007, taxpayers should use the following forms in lieu of Form IL-843, *Illinois Amended Return or Notice of Change in Income*:

- IL-1041-X, *Amended Fiduciary Income and Replacement Tax Return*
- IL-1023-C-X, *Amended Composite Income and Replacement Tax Return*
- IL-990-T-X, *Amended Exempt Organization Income and Replacement Tax Return*

SCHEDULED IMPLEMENTATION CHANGES FOR 2008

IDOR projects the second wave of system changes will be completed by the end of 2008. These changes will expand the new system to include individual income tax returns and motor fuel use taxes.

PAYROLL TAX WITHHOLDING CHANGES[8]

Effective January 1, 2008, Illinois made significant changes in the way withholding taxes are remitted to the state.[9] These changes include new payment due dates, new filing due dates, and the elimination of Form IL-W-3, *Illinois Annual Withholding Income Tax Return*.

In place of withholding coupon booklets, IDOR will now send annual return filers a single Form IL-941-A, *Illinois Yearly Withholding Income Tax Return*, as shown below.

IL-941-A **Illinois Department of Revenue**
Illinois Yearly Withholding Income Tax Return

We encourage you to use TaxNet or FSET. Visit tax.illinois.gov

Complete all lines.

___ ___ ___ ___
Tax year

___ ___ - ___ ___ ___ ___ ___ ___ ___ ___ ___ ___
Federal employer identification number Seq. number

Business name

Number and street address

City State ZIP

(______)
Daytime phone

IL-941-A (N-12/07) IL-492-4538

Complete Lines 1 through 5, reporting the totals for the year.

1 Total compensation and gambling winnings subject to withholding. **1** ___________

2 Illinois Income Tax required to be withheld. **2** ___________

3 Withholding payments (electronic and IL-501 payment coupons) plus any overpayment from the previous Form IL-941. **3** ___________

4 If Line 2 is greater than Line 3, subtract Line 3 from Line 2. This is your balance due. Make your remittance payable to "**Illinois Department of Revenue.**" **4** ___________

5 If Line 2 is less than Line 3, subtract Line 2 from Line 3. This is your overpayment. Claim it on your next Form IL-941-A. **5** ___________

Check this box if you have **permanently** stopped withholding. ☐

Under penalties of perjury, I state that, to the best of my knowledge, this return is true, correct, and complete.

Signature Daytime telephone number Date

Mail to **ILLINOIS DEPARTMENT OF REVENUE, PO BOX 19447, SPRINGFIELD IL 62794-9447**

NEW FILING AND PAYMENT REQUIREMENTS

Beginning January 1, 2008, and each subsequent year, IDOR will inform employers when their Illinois income tax withholding payments are due and when to file their withholding tax returns. Employers will be **assigned to one of three due-date schedules** on a mandatory basis: semi-weekly, monthly, or annually. These dates are intended to align more closely with federal dates.

Look-Back Period

IDOR determines the frequency with which employers must remit payments and file withholding tax returns by the total tax withheld during a "look-back" period. This look-back covers a 1-year period ending June 30 of the immediately-preceding calendar year. For calendar year 2008, the look-back period extended from July 1, 2006 through June 30, 2007.

---

8. 35 ILCS 5/701 et seq.

9. Illinois Public Act 095-0008 (SB 1395), enacted June 29, 2007

Payment Frequency

Employers are assigned to semi-weekly, monthly, or annual payment schedules based on the total amount of tax withholding they reported during the look-back period. The following table shows how these amounts are used to determine payment schedules:

Amount of Tax Reported During Look-Back	Payment Frequency Schedule
$1,000 or less	Annual
$1,001–12,000	Monthly
$12,001 and over	Semi-Weekly
Newly-registered employers	Monthly

Exception. Employers who qualify for the annual payment schedule, but who are **not in good standing** with IDOR, must file monthly.

As noted in the table above, newly-registered employers or those without sufficient look-back data are also assigned to the monthly schedule.

Changes in Frequency

Employers assigned to semi-weekly payments cannot change their payment or filing frequency schedule. However, any employers who are assigned to monthly or annual frequencies **must change** to the semi-weekly schedule if their withholding exceeds $12,000 during any quarter.[10] This change takes effect in the following quarter and applies to the remainder of the year and the subsequent year.

Employers assigned to the annual schedule must file a return by the last day of the month following the end of the quarter in which their withholding exceeded $12,000. These employers must report and pay all amounts that have been withheld through the end of that quarter.

Note. Employers bear the responsibility of notifying IDOR of any changes to their payment-frequency schedule. Taxpayers may use EFTPS, TaxNet, FSET, or EFT to report changes. They also may call IDOR to request a new withholding coupon booklet.

IDOR changed the payment and return due dates to reflect the new filing-frequency assignments.

10. Pub. 131, *Withholding Income Tax Filing and Payment Requirements*

NEW PAYMENT DUE DATES

The following table describes payment and filing methods and due dates by assigned frequency schedule.

Frequency Assigned	Payment Methods	Payment Due Dates	Filing Methods	Filing
Semi-weekly	EFTPS, TaxNet, FSET, EFT, or IL-501 (coupon)	Wednesday for amounts withheld on the preceding Wednesday, Thursday, or Friday; Friday for amounts withheld on the preceding Saturday, Sunday, Monday, or Tuesday	TaxNet, FSET, or Form IL-941	The last day of April, July, October, and January
Monthly	EFTPS, TaxNet, FSET, EFT, or IL-501 (coupon)	15th day of each month for amounts withheld the preceding month	TaxNet, FSET, or Form IL-941	The last day of April, July, October, and January
Annually	EFTPS, TaxNet, FSET, EFT, or Form IL-941-A	January 31 of the following year for amounts withheld the entire preceding year	EFTPS, TaxNet, FSET, EFT, or Form IL-941-A	January 31 of the following year for amounts withheld the entire preceding year

Employers assigned to the semi-weekly frequency plan may follow the federal rule that allows payments to be made up to three business days after the tax is withheld. Tax is not considered withheld until the employees' pay date.

Payments Withheld from Different Quarters

When the amount of tax withheld straddles two different quarters, the employer must remit two separate payments. The amount of each payment should clearly identify the quarter to which the payment applies. IDOR will apply payments that are not clearly identified to one quarter only.

PAYMENT AND FILING METHODS

IDOR encourages the use of electronic filing and payment methods. In an April 1, 2008, press release, Governor Rod Blagojevich's office claimed **electronic filers saved the state $2.4 million** in paper processing and postage costs during the first three months of the 2008 tax season.[11] Additionally, the press release states that electronic filing reduces the amount of trash in landfills, saves energy, and decreases pollution.

11. *Governor Blagojevich encourages Illinoisans to Go Green, file taxes electronically*, Office of the Governor's Press Release (Apr. 1, 2008)

Electronic Methods

To stimulate the use of electronic filing, IDOR offers employers a variety of electronic filing and payment options, including:

- **Electronic Federal Tax Payment System (EFTPS)** — allows employers to make Illinois withholding and federal employment tax payments in one transaction;
- **TaxNet** — allows employers to file and pay Illinois withholding tax and/or Illinois Unemployment Insurance and Wage Reports (UI-3-40);
- **Federal/State Employment Taxes Program (FSET)** — allows employers to **file and pay Illinois withholding and federal employment taxes through software or third-party payroll service providers;** and
- **Electronic Funds Transfer (EFT)** — provides employers with two payment options: ACH credit or ACH debit. **ACH credit** allows an employer to instruct its financial institution to transfer funds to IDOR; **ACH debit** allows an employer to instruct IDOR to withdraw a payment from the employer's account. Before making EFT payments, employers must complete Form EFT-1, *Authorization Agreement for Electronic Funds Transfer.*

Note. Employers with annual tax liability in excess of $200,000 must use an electronic payment option.

Observation. Many software companies now offer eFile and ePay options for their payroll programs.

Nonelectronic Methods

Employers assigned to monthly or semi-weekly schedules, whose annual tax liability is less than $200,000, may opt to submit payments and file paper returns by mail. IDOR issues payment coupon booklets to these employers.

Employers on an annual schedule should file and pay using Form IL-941-A. Employers on monthly and semi-weekly payment schedules should file quarterly using Form IL-941, *Illinois Quarterly Withholding Income Tax Return*, and pay using Form IL-501, *Payment Coupon*.

Payments may be remitted electronically, regardless of whether a return is filed electronically or by mail. Payment coupons are not required for electronic payments, annually-filed payments, qualified payments remitted for household employees, and payments showing zero due.

PENALTIES

IDOR may impose penalties for late payments or underpayments of withholding tax. The department also will assess a $25 bad-check penalty for payments that do not clear the employer's financial institution. Further information on penalties is found in IL Pub. 103, *Uniform Penalties and Interest*.

Note. IDOR may request to inspect an employer's payroll records to ensure that payments are made on the proper due dates.

ILLINOIS WITHHOLDING TAX INFORMATION SOURCES

The following IDOR publications provide additional information on Illinois withholding tax law:

- IL Pub. 130, *Who is Required to Withhold Illinois Income Tax* (December 2007)
- IL Pub. 131, *Withholding Income Tax Filing and Payment Requirements* (December 2007)
- IL Pub. 121, *Illinois Income Tax Withholding for Household Employees* (January 2006)

NEW WITHHOLDING REQUIREMENT FOR PASS-THROUGH ENTITIES

As part of the Budget Implementation Act for fiscal year 2008, Illinois enacted a new law requiring certain pass-through entities to remit "withholding" tax on Illinois-apportioned distributions allocated to nonresident partners, shareholders, and beneficiaries.[12] This withholding requirement is **effective for tax years ending on or after December 31, 2008.**

By collecting the tax due on behalf of nonresidents in advance, Illinois reduces the risk of noncompliance by out-of-state taxpayers. This practice will not only increase revenue coming into the state, it will also reduce IDOR's collection costs and administrative overhead.

Nonresident taxpayers will receive an Illinois income tax credit for any amount remitted on their behalf.[13] However, if the amount of the tax remitted on behalf of the partner, shareholder, or beneficiary is sufficient to cover their tax liability, the nonresident taxpayer does not have to file an Illinois tax return.[14]

ENTITIES REQUIRED TO WITHHOLD

The following pass-through entities are affected by the withholding requirement:

- Partnerships, other than publicly-traded partnerships under IRC §7704 and investment partnerships[15]
- S corporations
- Trusts

COMPLIANCE REQUIREMENTS

Affected entities are required to remit an annual payment equal to the distributable share of the entity's Illinois-apportioned business income for each nonresident partner, shareholder, or beneficiary **multiplied by the taxpayers' applicable Illinois tax rate.**[16] Exceptions are made for partners, shareholders, or beneficiaries that are exempt from tax under IRC §501(a)[17] or Illinois Income Tax Act (IITA) §205 and for those partners and shareholders included in composite returns under IITA §502(f).

Although the new law refers to "withholding" amounts, the term is misleading. Since the applicable tax must be remitted to the state whether or not the distribution was actually made to the partner, shareholder, or beneficiary, the tax technically is not withheld from taxpayers.

> **Note.** For the affected entities, the new requirements induce a **mandatory, or forced distribution** of at least the amount of Illinois tax that is required to be paid. This amount paid to the State of Illinois is **treated as a distribution for tax purposes.** The applicable tax must be remitted to the state whether or not any cash distribution was actually made to the partner, shareholder, or beneficiary.

---

12. 35 ILCS 5/709.5 as enacted by P.A. 95-0233 (SB1544), effective August 16, 2007; and P.A. 95-0707 (SB 783), effective January 11, 2008.
13. 35 ILCS 5/709.5(b)
14. 35 ILCS 5/502(a)(2)
15. For taxable years ending on or after December 31, 2004, an "investment partnership" is exempt from Illinois income taxation. (35 ILCS 5/205(b))
16. 35 ILCS 5/ 201(a)-(d) determine the taxpayer's tax rate.
17. Qualified pension, profit-sharing, and stock bonus plans

Payment Due Date

Pass-through entities must make payments to the state on behalf of their nonresident taxpayers based on the portion of the taxpayers' income that is taxable to Illinois for that year, multiplied by the individual taxpayer's applicable tax rate. These payments must be remitted no later than the unextended due date for the return of the partnership, S corporation, or trust.[18]

> **Note.** At the time of this writing, IDOR has not yet promulgated rules or regulations to guide taxpayers and practitioners on how to comply with this pass-through withholding requirement. Department guidance is expected to be issued before the first withholding payments are due on March 15, 2009.

> **Observation.** The requirement for pass-through entities to remit Illinois tax payments on behalf of nonresident partners, shareholders, and beneficiaries may complicate preparation of the entity's federal tax returns, especially when the partner's, shareholder's, or beneficiary's allocated taxable distribution is not actually distributed during the tax year.
>
> An S corporation with a distribution to a nonresident shareholder should consider making a similar payment to other shareholders, so that all shareholders **are treated equally,** in proportion to their stock ownership.

> **Caution.** Disproportionate S corporation distributions could jeopardize existing Subchapter S elections. Resident and exempt entities that do not share in the Illinois tax distribution could create risks for S corporations.

Reporting Requirement

Each entity affected by the pass-through withholding requirement is responsible for notifying nonresident taxpayers of any amounts withheld on their behalf. These information statements must show the amount of the taxpayer's Illinois-apportioned income, the amount withheld, and any other information the department may require.[19] IDOR is developing new forms for this purpose.

WITHHOLDING EXEMPTIONS

The legislature provided an exemption from the withholding requirement for entities with nonresident partners, shareholders, or beneficiaries who agree to voluntarily comply with Illinois tax law.

Pass-through entities are not required to remit withholding for nonresident partners, shareholders, or beneficiaries who certify that they will comply with requirements to:[20]

- File all Illinois tax returns required under IITA §502;[21]
- Make timely payments of all Illinois income taxes; and
- Be subject to personal jurisdiction in Illinois for the collection of taxes, penalties, and interest with respect to income originating from the partnership, S corporation, or trust.

---

18. 35 ILCS 5/711(a-5)

19. 35 ILCS 5/711(b)

20. 35 ILCS 5/709.5(c)

21. 35 ILCS 5/502(a)(2) exempts a nonresident from filing an Illinois income tax return if the taxpayer's pass-through withholding credit satisfies the taxpayer's Illinois tax liability.

Certificates must be completed in a manner prescribed by IDOR and must be kept on file by the partnership, S corporation, or trust. IDOR may request a copy of the certification for review and may require certificates to be maintained electronically.[22]

IDOR may revoke a taxpayer's certification for noncompliance. If a certification is revoked, IDOR notifies the entity of the revocation, and the entity is then required to remit withholding on behalf of the taxpayer. However, the entity is not required to remit payment within the first 60 days after notice of revocation.[23]

IL-1023-C, *COMPOSITE INCOME AND REPLACEMENT TAX RETURN*

Illinois-based partnerships and S corporations can have nonresident owners. When these entities show distributions of Illinois income, it follows that their nonresident partners and shareholders are required to file Illinois income tax returns and pay their respective shares of Illinois tax.

However, this requirement creates compliance problems for both the partners/shareholders and the State of Illinois. Many nonresident taxpayers may be unaware of their need to file Illinois returns. Others may be aware of their obligation, but fail to comply due to the time and expense necessary to prepare an out-of-state return. The state is then burdened with searching for noncompliant out-of-state taxpayers. Because the amounts owed by each taxpayer may be small, the costs of ensuring compliance may outweigh the benefits of collecting these taxes.

Even compliant taxpayers can stress the system. Processing large quantities of nonresident partner and shareholder returns strains IDOR's administrative resources. To ease the compliance concerns and administrative burdens that arise from nonresident member distributions, Illinois authorizes partnerships and S corporations to file "composite" tax returns and pay Illinois income tax on behalf of certain partners and shareholders.

ELIGIBILITY FOR COMPOSITE RETURNS

Illinois allows only authorized agents to file Form IL-1023-C, *Composite Income and Replacement Tax Return*. These authorized agents may file only on behalf of certain members.

Authorized Agents

The following Illinois-based entities are authorized to file composite tax returns:

- Partnerships
- S corporations
- Insurance businesses organized under a Lloyd's plan of operation.[24]

> **Note.** A Lloyd's plan of operation refers to an insurance contract in which members of an unincorporated association agree to indemnify each other or a third party against loss. Lloyd's plans are subject to many different rules and regulations when filing composite returns. These rules are not included in this section. For more information on filing a composite return for a Lloyd's plan, please refer to the Form IL-1023-C instructions and Ill. Admin. Code Title 20, Part 100.5130(b).

22. 35 ILCS 5/709.5(c)(4)
23. 35 ILCS 5/709.5(c)(3)
24. "Lloyd's Plan of Operation" is defined in Ill. Admin. Code Title 20, Part 100.5170

Authorized agents who file Form IL-1023-C are responsible for:

- Filing any required petitions;
- Paying estimated tax;
- Paying any assessed tax, penalty, or interest;
- Responding to IDOR notices;
- Filing any required amended returns; and
- Participating in any audits.

Eligible Members

Generally, authorized agents may file composite returns only **on behalf of nonresident members who have no other Illinois income.** Eligibility is also restricted to the following types of taxpayers, who are members of the same authorized partnership or S corporation:

- Individuals
- Estates
- Trusts

It is not mandatory for all eligible members to be included on a composite return. The decision on whether or not to be included is made by the member and the authorized agent for each year that the member is eligible to be included. Certain members who are not otherwise eligible may **become eligible for inclusion by petition.**

Petition for Inclusion. Authorized agents may petition IDOR to include the following members in composite returns:

- Members who are Illinois residents
- Members with indeterminable residency
- Nonresident members with other sources of Illinois income who wish to:
  - File a separate Illinois return, and
  - Claim a credit for their share of tax paid on a composite return.

Petitions must be mailed to the following address before the end of the authorized entity's tax year:

Business Processing Division
Illinois Department of Revenue
PO Box 19014
Springfield, IL 61794-9014

IDOR must approve the petition prior to the **original** due date of the return before petitioned members may be included on a composite return.

IDOR will approve petitions when the authorized agent clearly shows that filing a composite return will achieve the greatest degree of compliance and administrative ease. It will also approve petitions that prove a member's state of residency is not readily determinable.

Members' Requirement to File Individual Illinois Income Tax Returns. Nonresident members that do not have any Illinois income outside of income reported on composite returns generally are not required to file Illinois income tax returns, unless they wish to request a refund of any estimated tax payments they personally made to Illinois.

Nonresident members with Illinois income in addition to income included on composite returns must file separate Illinois income tax returns. All resident members are also required to file individually. Resident and nonresident taxpayers should include their share of income from any entities filing composite returns on their behalf.

Nonresidents may claim a credit for any composite tax paid for them, but residents may claim a credit only if IDOR approved a petition authorizing their inclusion on the composite return.

Note. Eligible taxpayers may be included on more than one composite tax return.

Note. For taxable years ending on or after December 31, 2008, every nonresident member included on a composite return may claim a credit for tax paid by the partnership or corporation on the member's behalf. Prior to this time, nonresident members with other Illinois income had to petition and receive IDOR's approval before claiming a credit for any tax paid on their behalf on a composite return. Residents included on composite returns still must seek and receive IDOR's permission before claiming a credit for composite taxes paid.

Example 1. The Macon Money Partnership was formed to manage an apartment building in Macon, Illinois. There are five equal partners: brothers Abe Jones, Ben Jones, and Carl Jones, the Missouri-based Dean Jones Trust, and the Edgar Jones Investment Corp., an S corporation formed in Kentucky and owned by the heirs of their deceased brother Edgar.

Abe, who lives in Decatur, Illinois, and works at Caterpillar, is paid $100 a month by the partnership to manage the building if the building is fully rented. He received $1,200 in 2007. Ben lives in Indiana; Carl retired early and spends half his time in Florida and half in Illinois. Since neither Ben nor Carl have any other Illinois income, they don't want the hassle of filing an Illinois return on their share of the partnership's profits. The partners instruct the tax matters partner to file a composite Illinois tax return.

Question 1. Which partners are eligible for inclusion in Macon Money's composite Illinois return?

Answer 1. Only individuals, trusts, and estates are eligible members. Consequently, the **Edgar Jones Investment Corp.** cannot be included on a composite return filed by Macon Money.

Although the other partners are all members of an eligible taxpayer group, they must also satisfy the "nonresidency" and "no other Illinois income" tests to be automatically included on the partnership's composite return. Each remaining partner's eligibility is discussed below:

Abe. As an Illinois resident, Abe is required to petition for inclusion on the composite return. However, it is doubtful that IDOR would grant this petition. Abe is not perceived as a compliance risk because he receives wages subject to Illinois withholding.

Ben. As a nonresident with no other taxable Illinois income, Ben's share of the partnership income and tax may be included on the partnership's composite tax return. This relieves Ben of the necessity to file an Illinois tax return.

Carl. Carl is an individual of questionable residency. The partnership is required to petition IDOR for Carl's inclusion on the composite return. If the petition demonstrates reasonable doubt as to the status of Carl's residency, the petition to include Carl is likely to be approved.

Dean Jones Trust. As a nonresident entity, the Dean Jones Trust may be eligible for inclusion on the partnership's composite return. However, if the trust has any other Illinois income, the partnership must file a petition and receive IDOR approval before including the trust in the composite return.

GENERAL INFORMATION ON FILING A COMPOSITE RETURN

The filing of a composite return is elective each year. Partnerships and S corporations that elect to file composite returns must submit their Forms IL-1023-C to IDOR separately from their respective Forms IL-1065, *Partnership Replacement Tax Return*, or IL-1120-ST, *Small Business Corporation Replacement Tax Return*. Composite returns must be signed by a general partner or an officer of an S corporation.

Estimated Tax Payments

Authorized agents who expect to file composite returns must submit composite estimated tax payments to Illinois. One-fourth of any expected annual tax liability for the composite return should be remitted to the state on a quarterly basis along with Form IL-1023-CES, *Composite Estimated Tax Payments for Partners and Shareholders*. The Form IL-1023-CES instructions include a worksheet to determine the proper amount of each estimated tax payment.

Filing Deadline

Authorized agents must file Form IL-1023-C on or before the **15th day of the 4th month** following the close of their tax year.

IDOR will grant an automatic 6-month extension of time to file, regardless of whether the agent requested an extension. Authorized agents who require an extension and expect to owe a composite tax should file Form IL-505-B, *Automatic Extension Payment*, and remit any tentative tax due by the original return due date in order to avoid penalty and interest.

> **Note.** Authorized agents may not use Form IL-505-I, *Automatic Extension Payment (for Individuals)*, to remit tentative composite payments.

Penalties and Interest

Authorized agents filing composite returns may be subject to late-filing penalties, late-payment penalties, and bad-check penalties. If the composite tax liability is not paid within 30 days of the date printed on an IDOR bill, the agent is also responsible for a collection fee. Interest on any unpaid liability is calculated from the return's original due date.

Amended Composite Return

After Form IL-1023-C is filed, it can be corrected or changed only by filing Form IL-1023-C-X, *Amended Composite Income and Replacement Tax Return*. Forms IL-1023-C-X **filed before the extended due date** of the authorized agent's Form IL-1023-C should be marked **"CORRECTED"** at the top. It will be treated as an originally-filed return for all purposes.

Composite returns cannot be amended to transfer tax payments or overpayments from or to any other type of Illinois return or to claim a net operating loss carryforward or carryback.

Reportable Transactions

Entities participating in listed transactions that are reportable to the IRS also must disclose this information to IDOR. Members whose reportable transactions are included on a composite tax return are relieved from the obligation to disclose the **same** transactions individually.

Authorized agents must send IDOR two copies of the form used to disclose any listed transactions to the IRS. One copy should be attached to the composite tax return. The other copy should be mailed to:

Illinois Department of Revenue
PO Box 19029
Springfield, IL 62794-9029

PREPARING FORM IL-1023-C

All forms and schedules used to file Illinois composite returns must be IDOR provided or approved. Computer-generated printouts, other than those from IDOR-approved software developers, are not accepted. Failure to submit the required forms delays processing of the composite return, and noncompliance may result in a referral to IDOR's Audit Bureau.

Calculating Composite Income (Form IL-1023-C, Lines 1a and 2a)

The calculation of composite income begins with the partnership or S corporation's **modified base income.** Modified **base income** is computed by eliminating certain additions and subtractions from Steps 4 and 5 of the authorized agent's income computed on either Form IL-1065 or Form IL-1120-ST.

Partnership Modifications. To arrive at modified **base income,** the partnership's base is **recomputed without** regard to the following:

- The addition modification for guaranteed payments to partners,[25] other than those partners included in the composite return
- The subtraction modification for personal-service income or for a reasonable allowance for compensation paid or accrued to partners[26]
- The subtraction or addition modification for the share of income (or loss) distributable to a partner subject to Personal Property Tax Replacement Income Tax[27]

Shorthand Method. Taxpayers may quickly calculate a **partnership's modified base** income using this shorthand method. Starting with a blank second page of Form IL-1065, recompute Steps 4 through 6 with the following modifications (see page IL-17 for page 2 of Form IL-1065):

1. Copy the amount of the partnership's unmodified base income onto line 14.
2. Write the amount of any guaranteed payments to a partner **included in the composite return** on line 20**.**
3. Enter zeros on line 21 (the amount of loss distributable to a partner subject to replacement tax), line 26 (personal-service income or reasonable allowance for compensation of partners, and line 27 (share of income distributable to a partner subject to replacement tax).
4. Include on line 34 any amount of the federal domestic production activity or oil and gas depletion deductions that the partnership is not allowed to claim on its Form IL-1065, but may pass through to eligible shareholders.
5. Complete the remaining line entries in Steps 4 through 6 using information from the partnership's tax return and recalculate totals when required.
6. Transfer the recalculated amounts as follows (see page IL-21 for Form IL-1023-C):
   - Transfer the amount from IL Form 1065, Step 5, line 36 to **Form IL-1023-C, Step 2, line 1a,** and if **all** of the partnership's income is allocated to Illinois, also transfer this amount to **Form IL-1023-C, Step 2, line 2a.**
   - If some of the partnership's income is derived outside of Illinois, transfer the amount from Form IL-1065, Step 6, line 47 to **Form IL-1023-C, Step 2, line 2a.**

---

25. 35 ILCS 5/ 203(d)(2)(C)
26. 35 ILCS 5/ 203(d)(2)(H)
27. 35 ILCS 5/ 203(d)(2)(I)

S Corporation Modifications. To arrive at modified **base income,** the S corporation's modified base income is recomputed **without regard** to subtraction modifications for the following:

- Amounts included in federal taxable income under IRC §78 (dividends received from certain foreign corporations by domestic corporations choosing foreign tax credit)[28]
- Interest income recognized by certain financial institutions from loans secured by property eligible for the Enterprise Zone Investment Credit[29]
- Interest income recognized by certain financial institutions from loans secured by property eligible for the High Impact Business Investment Credit[30]
- Contributions to eligible Enterprise Zone projects[31]
- Dividends received from foreign corporations[32]
- Contributions to job-training projects[33]
- The share of income or loss attributable to a shareholder subject to the Personal Property Tax Replacement Income Tax[34]

Shorthand Method. Taxpayers may quickly calculate an **S corporation's modified base** income using this shorthand method. Starting with a blank second page of Form IL-1120-ST, recompute Steps 4 through 6 with the following modifications:

1. Copy the amount of the S corporation's unmodified base income onto line 14.
2. Enter zeros on line 20 (the amount of loss distributable to a shareholder subject to replacement tax), line 24 (share of income distributable to a shareholder subject to replacement tax), line 27 (Enterprise Zone or River Edge Redevelopment Zone interest subtraction), line 29 (High Impact Business interest subtraction), and line 30 (contribution subtraction).
3. Make the following line 34 (other subtractions) adjustments:
   - Do not include any subtractions allowed for foreign dividend gross-up, Subpart F income, or foreign dividends received.
   - Include any amount of the federal domestic production activity or oil and gas depletion deductions that the corporation is not allowed to claim on Form IL-1120-ST, but may pass through to eligible shareholders.
4. Complete the remaining line entries in Steps 4 through 6 using information from the corporation's tax return and recalculating totals when required.
5. Transfer the recalculated amounts as follows (see page IL-21 for Form IL-1023-C):
   - Transfer the amount from IL Form-1120-ST, Step 5, line 36 to **Form IL-1023-C, Step 2, line 1a,** and if **all** of the corporation's income is allocated to Illinois, also transfer this amount to **Form IL-1023-C, Step 2, line 2a.**
   - If some of the corporation's income is derived outside of Illinois, transfer the amount from IL Form-1120-ST, Step 6, line 47 to **Form IL-1023-C, Step 2, line 2a.**

---

28. 35 ILCS 5/203(b)(2)(G)
29. 35 ILCS 5/203(b)(2)(M)
30. 35 ILCS 5/203(b)(2)(M-1)
31. 35 ILCS 5/203(b)(2)(N)
32. 35 ILCS 5/203(b)(2)(O)
33. 35 ILCS 5/203(b)(2)(P)
34. 35 ILCS 5/203(b)(2)(S)

> **Note.** Composite income cannot be reduced by any type of NOL deduction. Also, Form IL-1023-C contains no provision for standard exemption amounts or tax credits.

Other Line Instructions

Take note of the following special instructions when completing Form IL-1023-C:

1. **Line 1b.** Write in the total percentage of ownership for resident members included in the composite return on Form IL-1023-C, Step 2, line 1b. **Do not include any Illinois residents unless IDOR approved them for inclusion.**
2. **Line 2b.** Write in the total percentage of ownership for nonresident members included in the composite return.
3. **Line 3.** If a partnership agreement calls for the specific allocation of certain items that differs from the partner's percentage allocation of income or loss, such as guaranteed payments, compute line 3 based on this allocation. A statement must be attached to the return detailing the special items and percentage allocations. In the event the specific allocations cause some partners to have income and others to have losses, the loss of one partner cannot be used to offset the income of another partner.
4. **Lines 5 and 6.** Composite returns that include members that are trusts must compute and remit the trust member's Illinois replacement tax liability. Form IL-1023-C, Step 3, lines 5 and 6 may be skipped if the composite return includes only individuals and estate members.

Schedule BC

IL Schedule BC, *Composite Return Membership*, must be attached to every Form IL-1023-C. Schedule BC requires identification of each member included in the composite return by name, address, taxpayer identification number, and type ("I" for individual, "T" for trust, "M" for estate). Each member's percentage share of the authorized entity's income or loss also is required to be identified. A checkbox indicates whether a resident member petitioned and received approval for inclusion.

Example 2. Use the same facts as **Example 1,** except IDOR timely approved petitions for Carl Jones and the Dean Jones Trust to be included in a 2007 composite return filed by the Macon Money Partnership. Carl is considered an Illinois resident for 2007 and Dean Jones Trust had other Illinois income in 2007.

Abe Jones projected the partnership would net $15,000 in Illinois income for tax year 2007. Anticipating that IDOR would approve petitions to include Carl and the trust, Abe based the partnership's quarterly estimated composite tax payments on the liabilities of these members and submitted three payments of $79 each, totaling $237 for the year. Due to unforeseen expenses at yearend, the partnership's total income was far below Abe's projection, so he skipped the last quarterly payment.

Macon Money Partnership's 4-page 2007 Illinois Form IL-1065 return, including Schedule B, is presented on the following pages. The partnership's modified base income recalculation is shown next. Finally, the partnership's completed 2007 Form IL-1023-C composite return with Schedule BC is included.

For Example 2

Illinois Department of Revenue

2007 Form IL-1065

Partnership Replacement Tax Return

Due on or before the 15th day of the 4th month following the close of the tax year.

If this return is not for calendar year 2007, write your fiscal tax year here.

Tax year beginning _____/_____, 2007, ending _____/_____/ 20__ __

Write the amount you are paying. $ 58.00

Step 1: Identify your partnership

A Write your business name and mailing address. If you have an address change, check this box. ☐

Macon Money Partnership
Name

Abe Jones
C/O

1234 West Main St.
Mailing address

Decatur | IL | 62522
City | State | ZIP

B Check the box if one of the following apply.
☐ first return ☐ final return (If final, write the date ___/___/___)

C If this is a final return because you sold this business, write the date sold ___/___/___ , and the new owner's FEIN.
__ __ - __ __ __ __ __ __ __

D **Special Apportionment Formulas**. If you use a special apportionment formula, check the appropriate box and see Special Apportionment Formula instructions.
☐ Financial organizations ☐ Transportation companies

E Check if you are classified as an investment partnership. ☐

F Write your federal employer identification no. (FEIN).
3 7 - 1 2 3 4 5 6 7

G Write your Illinois Business Tax number (IBT).
1 2 3 4 - 5 6 7 8

H ☐ Check the box if you are a member of a unitary business group, and write the FEIN of the member filing the Schedule UB, Combined Apportionment for Unitary Business Groups.
__ __ - __ __ __ __ __ __ __

I Write the state and zip code where your accounting records are kept. (Use the two-letter postal abbreviation. E.g., IL, GA, etc.)
IL 62522
State Zip

J If you are making the business income election, to treat all nonbusiness income as business income, check here and write "0" on Lines 37 and 45. ☐

K Check if you are making an IRC § 761 election. ☐

L If you have completed the following federal forms, check the box and **attach** them to this return.
☐ Federal Form 8886 ☐ Federal Sch. M-3

Step 2: Figure your ordinary income or loss

Attach your payment here.

1	Ordinary income or loss or equivalent from federal Schedule K.	1	
2	Net income or loss from all rental real estate activities.	2	10,000
3	Net income or loss from other rental activities.	3	
4	Portfolio income or loss.	4	
5	Net IRC Section 1231 gain or loss from involuntary conversions due to casualty and theft.	5	
6	All other items of income or loss that were not included in the computation of income or loss on Page 1 of U.S Form 1065 or 1065-B. See instructions. Identify:__________	6	
7	Add Lines 1 through 6. This is your ordinary income or loss.	7	10,000

Step 3: Figure your unmodified base income or loss

8	Charitable contributions.	8	
9	Expense deduction under IRC Section 179.	9	
10	Interest on investment indebtedness.	10	
11	All other items of expense that were not deducted in the computation of ordinary income or loss on Page 1 of U.S. Form 1065 or 1065-B. See instructions. Identify: __________	11	
12	Add Lines 8 through 11.	12	0
13	Subtract Line 12 from Line 7. This amount is your total unmodified base income or loss.	13	10,000

NS DR_______

IL-1065 (R-12/07) Page 1

For Example 2

14 Write your unmodified base income from Line 13.	14	10,000

Step 4: Figure your income or loss

15 State, municipal, and other interest income excluded from Line 14.	15	
16 Illinois replacement tax deducted in arriving at Line 14.	16	150
17 Illinois Bonus Depreciation addition. **Attach** Form IL-4562.	17	
18 Related-Party Expenses addition. **Attach** Schedule 80/20.	18	
19 Distributive share of additions. **Attach** Schedule K-1-P or K-1-T.	19	
20 Guaranteed payments to partners from U.S. Form 1065.	20	
21 The amount of loss distributable to a partner subject to replacement tax. **Attach** Schedule B.	21	
22 Other additions. **Attach** Illinois Schedule M (for businesses).	22	
23 Add Lines 14 through 22. This amount is your income or loss.	23	10,150

Step 5: Figure your Illinois base income or net loss

24 Interest income from U.S. Treasury obligations or other exempt federal obligations.	24	
25 August 1, 1969 valuation limitation amount. **Attach** Schedule F.	25	
26 Personal service income or reasonable allowance for compensation of partners.	26	1,200
27 Share of income distributable to a partner subject to replacement tax. **Attach** Schedule B.	27	4,060
28 Expenses incurred in producing certain federally tax-exempt income or federal credits.	28	
29 Enterprise Zone or River Edge Redevelopment Zone dividend subtraction. **Attach** Schedule 1299-A.	29	
30 High Impact Business dividend subtraction. **Attach** Schedule 1299-A.	30	
31 Illinois Bonus Depreciation subtraction. **Attach** Form IL-4562.	31	
32 Related-Party Expenses subtraction. **Attach** Schedule 80/20.	32	
33 Distributive share of subtractions. **Attach** Schedule K-1-P or K-1-T.	33	
34 Other subtractions. **Attach** Schedule M (for businesses).	34	
35 Total subtractions. Add Lines 24 through 34.	35	5,260
36 Base income or net loss. Subtract Line 35 from Line 23.	36	4,890

STOP **If the amount on Line 36 is derived inside and outside Illinois, complete Step 6; otherwise go to Step 7.**

Step 6: Figure your income allocable to Illinois

37 Nonbusiness income or loss. **Attach** Schedule NB.			37	
38 Non-unitary partnership business income or loss included in Line 36.			38	
39 Add Lines 37 and 38.			39	
40 Business income or loss. Subtract Line 39 from Line 36.			40	
41 Total sales everywhere. This amount cannot be negative.	41			
42 Total sales inside Illinois. This amount cannot be negative.	42			
43 Apportionment factor. Divide Line 42 by Line 41 (carry to six decimal places).	43	.		
44 Business income or loss apportionable to Illinois. Multiply Line 40 by Line 43.			44	
45 Nonbusiness income or loss allocable to Illinois. **Attach** Schedule NB.			45	
46 Non-unitary partnership business income or loss apportionable to Illinois.			46	
47 Base income or net loss allocable to Illinois. Add Lines 44 through 46.			47	

Step 7: Figure your net income

48 Base income or net loss from Step 5, Line 36, or Step 6, Line 47.	48	4,890
49 Illinois net loss deduction. **Attach** Schedule NLD. If Line 48 is zero or a negative amount, write "0."	49	
50 Income after NLD. Subtract Line 49 from Line 48.	50	4,890
51 Write the amount from Step 5, Line 36.	51	4,890
52 Divide Line 48 by Line 51. (This figure cannot be greater than "1.")	52	1 .
53 Exemption allowance. Multiply Line 52 by $1,000. (Short-year filers, see instructions.)	53	1,000
54 **Net income**. Subtract Line 53 from Line 50.	54	3,890

Page 2 of 4 IL-1065 (R-12/07)

For Example 2

55	Write the amount from Line 54.	55	3,890

Step 8: Figure your net replacement tax

56	Replacement tax. Multiply Line 55 by 1.5% (.015).	56	58
57	Recapture of investment credits. **Attach** Schedule 4255.	57	
58	Replacement tax before investment credits. Add Lines 56 and 57.	58	
59	Investment credits. **Attach** Form IL-477.	59	
60	Net replacement tax. Subtract Line 59 from Line 58. Write "0" if this is a negative amount.	60	

Step 9: Figure your refund or balance due

61	Payments		
	a Credit from 2006 overpayment.	a	
	b Form IL-505-B (extension) payment.	b	
62	Total payments. Add Lines 61a and 61b.	62	0
63	Overpayment. If Line 62 is greater than Line 60, subtract Line 60 from Line 62.	63	
64	Amount to be **credited to 2008.**	64	
65	Refund. Subtract Line 64 from Line 63. This is the amount to be refunded.	65	
66	Tax Due. If Line 60 is greater than Line 62, subtract Line 62 from Line 60.	66	58

▶ Make your check payable to "Illinois Department of Revenue" and attach to the front of this form. ◀

Special Note → Write the amount of your payment on the top of Page 1 in the space provided.

Step 10: Sign here

Under penalties of perjury, I state that I have examined this return and, to the best of my knowledge, it is true, correct, and complete.

Signature of partner ___ Date __/__/__ Title ___ Phone (___)___

Signature of preparer ___ Date __/__/__ Preparer's Social Security number or firm's FEIN ___

Preparer firm's name (or yours, if self-employed) ___ Address ___ Phone (___)___

▶ Mail this return to: Illinois Department of Revenue, P.O. Box 19031, Springfield, IL 62794-9031 ◀

IL-1065 (R-12/07)

This form is authorized as outlined by the Illinois Income Tax Act. Disclosure of this information is REQUIRED. Failure to provide information could result in a penalty. This form has been approved by the Forms Management Center. IL-492-0073

Page 3

For Example 2

Illinois Department of Revenue

Schedule B Partners' or Shareholders' Identification

Attach to your Form IL-1065 or Form IL-1120-ST

Year ending 12 (Month) 07 (Year)

IL Attachment no. 1

Write your name as shown on your Form IL-1065 or Form IL-1120-ST.

Macon Money Partnership

Write your federal employer identification number (FEIN).

37-1234567

Step 1: Provide the following information

1 Write the amount of base income or net loss from your Form IL-1065 or Form IL-1120-ST, Line 48. 1 **4,890.00**

2 Write the apportionment factor from your Form IL-1065 or Form IL-1120-ST, Line 43. 2 **1 .**

Step 2: Identify your partners or shareholders. Attach additional sheets if necessary.

	A Name and Address	B Social Security number or FEIN	C Partner or Shareholder type (See instructions.)	D Total amount of base income (loss) distributable (See instructions.)	E Check if the partner or shareholder is subject to Illinois replacement tax (See instructions.)	F Check if partner or shareholder's income is included on a Composite return (Form IL-1023-C).
1	**Abe Jones** **1234 West Main Street** **Decatur, IL 62522**	**311-12-1314**	**I**	**830.00**	☐	☐
2	**Ben Jones** **456 North Race Street** **Indianapolis, IN 46201**	**333-44-5555**	**I**	**2,030.00**	☐	☒
3	**Carl Jones** **RR #1 Box 201** **Macon, IL 62544**	**322-33-4444**	**I**	**2,030.00**	☐	☒
4	**Dean Jones Trust** **c/o Sally Jones-Smith** **1234 Clydesdale Drive** **St. Louis, MO 63101**	**43-4567890**	**T**	**2,030.00**	☒	☒
5	**Edgar Jones Investment Corp.** **c/o Edgar Jones, Jr.** **456 Derby Avenue** **Louisville, KY 40202**	**61-6789123**	**S**	**2,030.00**	☒	☐
6					☐	☐
7					☐	☐

8 Add the amounts shown in Column D for partners or shareholders for which you have entered a check in Column E. Write the total here. (See instructions.) 8 **4,060.00**

Page 4 of 4

Schedule B (R-12/07)

For Example 2

14	Write your unmodified base income from Line 13.	14	10,000

Step 4: Figure your income or loss

15	State, municipal, and other interest income excluded from Line 14.	15	
16	Illinois replacement tax deducted in arriving at Line 14.	16	150
17	Illinois Bonus Depreciation addition. **Attach** Form IL-4562.	17	
18	Related-Party Expenses addition. **Attach** Schedule 80/20.	18	
19	Distributive share of additions. **Attach** Schedule K-1-P or K-1-T.	19	
20	Guaranteed payments to partners from U.S. Form 1065.	20	0
21	The amount of loss distributable to a partner subject to replacement tax. **Attach** Schedule B.	21	0
22	Other additions. **Attach** Illinois Schedule M (for businesses).	22	
23	Add Lines 14 through 22. This amount is your income or loss.	23	10,150

Step 5: Figure your Illinois base income or net loss

24	Interest income from U.S. Treasury obligations or other exempt federal obligations.	24	
25	August 1, 1969 valuation limitation amount. **Attach** Schedule F.	25	
26	Personal service income or reasonable allowance for compensation of partners.	26	0
27	Share of income distributable to a partner subject to replacement tax. **Attach** Schedule B.	27	0
28	Expenses incurred in producing certain federally tax-exempt income or federal credits.	28	
29	Enterprise Zone or River Edge Redevelopment Zone dividend subtraction. **Attach** Schedule 1299-A.	29	
30	High Impact Business dividend subtraction. **Attach** Schedule 1299-A.	30	
31	Illinois Bonus Depreciation subtraction. **Attach** Form IL-4562.	31	
32	Related-Party Expenses subtraction. **Attach** Schedule 80/20.	32	
33	Distributive share of subtractions. **Attach** Schedule K-1-P or K-1-T.	33	
34	Other subtractions. **Attach** Schedule M (for businesses).	34	
35	Total subtractions. Add Lines 24 through 34.	35	0
36	Base income or net loss. Subtract Line 35 from Line 23.	36	10,150

STOP **If the amount on Line 36 is derived inside and outside Illinois, complete Step 6; otherwise go to Step 7.**

Beginning with the unmodified base income from Macon Money Partnership's 2007 Form IL-1065, line 14, the following steps are used to "shorthand" calculate the partnership's modified base income for its composite tax return:

- Line 20 was zeroed out because there were no guaranteed payments made to any partner included in the composite return.
- Zeros were entered on lines 21, 26, and 27.
- Nothing was entered on line 34, because the partnership claimed no domestic production activity deduction and no oil or gas well depletion deductions.
- Line 16 was transferred from the partnership's Form IL-1065 and all worksheet totals were recalculated.
- Because all of the partnership's 2007 income was derived in Illinois, the amount from line 36 of the worksheet was transferred to the partnership's Form IL-1023-C lines 1a and 2a.

For Example 2

Illinois Department of Revenue

2007 Form IL-1023-C

Composite Income and Replacement Tax Return

Due on or before the 15th day of the 4th month following the close of the tax year.

If this return is not for calendar year 2007, write your fiscal tax year here.
Tax year beginning _____/_____, 2007, ending _____/_____/ 20__ __

Write the amount you are paying. $ **0.00**

Step 1: Provide the following information

If you have an address change, check this box. ☐

A **Macon Money Partnership**
Name of partnership or subchapter S corporation

Abe Jones
In care of

1234 West Main Street
Mailing address

City	State	ZIP
Decatur	**IL**	**62522**

B Check the box if one of the following apply. ☐ first return ☐ final return

C Write your federal employer identification no. (FEIN).
3 7 - 1 2 3 4 5 6 7   666 Seq. code

D Write your Illinois Business Tax number (IBT).
1 2 3 4 - 5 6 7 8

E Check the box that identifies the return you filed.
☒ Form IL-1065 ☐ Form IL-1120-ST

F ☒ Check if the partners or shareholders included are trust members.

G ☐ Check if the partners or shareholders included are individuals and/or estate members only.

Step 2: Figure your income and net income tax

1	**a** Modified base income of the partnership or subchapter S corporation.	1a 10,150		
	b Total percentage of ownership for resident members. (**Stop** - see instructions.)	1b 20.00 %		
	c Multiply Line 1a by Line 1b.		1c	2,030
2	**a** Modified base income allocable to Illinois.	2a 10,150		
	b Total percentage of ownership for nonresident members.	2b 40.00 %		
	c Multiply Line 2a by Line 2b.		2c	4,060
3	Add Lines 1c and 2c. This amount is your income.		3	6,090
4	**Net income tax.** Multiply Line 3 by 3% (.03).		4	183

Step 3: Figure your net replacement tax (Complete only if this return includes any trust members.)

5	Income included in Line 3 that is subject to replacement tax.	5 2,030		
6	**Net replacement tax.** Multiply Line 5 by 1.5% (.015).		6	30

Step 4: Figure your refund or balance due

7	**Total net income and replacement taxes.** Add Lines 4 and 6.		7	213
8	Payments.			
	a Credit from 2006 overpayment.	8a		
	b Form IL-1023-CES payments.	8b 237		
	c Form IL-505-B (extension) payment.	8c		
9	Total payments. Add Lines 8a through 8c.		9	237
10	**Overpayment.** If Line 9 is greater than Line 7, subtract Line 7 from Line 9.		10	24
11	Amount to be **credited to 2008**.		11	24
12	**Refund.** Subtract Line 11 from Line 10. This is the amount to be refunded.		12	0
13	**Tax due.** If Line 7 is greater than Line 9, subtract Line 9 from Line 7. This is the amount you owe.		13	0

▶ **Make your check payable to "Illinois Department of Revenue."** ◀

Note **Write the amount of your payment on the top of this page in the space provided.**

Step 5: Sign here

Under penalties of perjury, I state that I have examined this return and, to the best of my knowledge, it is true, correct, and complete and that each of the qualifying partners or shareholders is aware of, and complies with, the rules and regulations set forth and made binding by this composite return.

Signature of authorized agent ___/___/_____ Date ________ Title (____)________ Phone

Signature of preparer ___/___/_____ Date ________ Preparer's Social Security number or firm's FEIN

Preparer firm's name (or yours, if self-employed) ________ Address (____)________ Phone

▶ **Mail this return to: Illinois Department of Revenue, P.O. Box 19009, Springfield, IL 62794-9009** ◀

NS DR________
IL-1023-C (R-12/07)

For Example 2

Illinois Department of Revenue

Schedule BC Composite Return Membership

Attach to your Form IL-1023-C

Year ending 12 (Month) 2007 (Year)

IL Attachment no. 1

Write your name as shown on your Form IL-1023-C.

Macon Money Partnership

Write your federal employer identification number (FEIN).

3 7 - 1 2 3 4 5 6 7

Identify the members included in your composite return.

	A Name and Address	B Social Security number or FEIN	C Partner or Shareholder type (See instructions.)	D Share of income or loss (%)	E Check the box if the member is an Illinois resident and is included based on department-approved petition.
1	Ben Jones 456 North Race Street Indianapolis, IN 46201	333-44-5555	I	20.00	☐
2	Carl Jones RR #1 PO Box 201 Macon, IL 62544	322-33-4444	I	20.00	☒
3	Dean Jones Trust c/o Sally Jones-Smith 1234 Clydesdale Drive St. Louis, MO 63101	43-4567890	T	20.00	☐
4					☐
5					☐
6					☐
7					☐
8					☐
9					☐

Schedule BC (N-12/06)

Abe and the Edgar Jones Investment Corp. must include their share of the partnership's taxable income on separately-filed Illinois income tax returns. Because Ben had no other Illinois income during the tax year, he is not required to file a 2007 Illinois income tax return. Carl is considered an Illinois resident and received IDOR approval to be included on the partnership's composite return. Therefore, he may claim a $61 ($2,030 × 3%) credit on his individual Illinois income tax return for tax paid by the partnership on his behalf.

The Dean Jones Trust must file a 2007 Form IL-1041, *Illinois Fiduciary and Replacement Tax Return* if it has other Illinois income. The trust must include all Illinois income received in 2007, including its share of income from the Macon Money Partnership. The trust may claim a credit of $91, representing $61 ($2,030 × 3%) of income tax and $30 ($2,030 × 1.5%) of replacement tax paid by the partnership on its behalf.

EMPLOYEE CLASSIFICATION ACT

In 2007, Illinois passed the Employee Classification Act which legislatively addresses the practice of misclassifying construction workers as independent contractors.[35] This Act is administered by the Illinois Department of Labor (IDOL), not by IDOR. A written summary of the January 2008 IDOR Practitioners' Meeting states "...the Act **does not change the classification** of individuals as employees versus independent contractors **for Illinois income tax purposes.**"[36]

The law's main purpose is to ensure that construction workers retain the protections of labor laws, such as minimum wage and overtime guarantees, workers' compensation, unemployment insurance, pensions, and health and welfare benefits. Because these benefits apply only to employees, workers who are improperly categorized as independent contractors do not benefit from these protections.

Illinois employers are under increased scrutiny to properly classify contract workers as either employees or independent contractors. Because 22% of independent contractors work in the construction industry, **employers in construction and construction-related fields bear the brunt of increased examinations** into worker misclassifications. The Act takes a broad view of construction workers, including auxiliary workers such as landscapers, maintenance providers, painters, remodelers, demolishers, and construction material haulers.[37]

ECONOMIC ASPECTS OF WORKER MISCLASSIFICATION

In addition to lost benefits for workers, misclassification decreases revenue coming into both federal and state coffers. An IRS study found that misclassified workers who received nonemployee compensation, such as income reported on Form 1099-MISC, reported only 77% of that income on their tax returns. However, workers who did not receive Form 1099-MISC voluntarily reported only 29% of their nonemployee compensation.[38]

A study released in December 2006 by the University of Missouri–Kansas City's Department of Economics calls attention to problems stemming from the improper classification of workers.[39] The study's authors claim misclassification cost Illinois up to $248.4 million in lost income tax revenue in 2005 alone. And misclassification is increasing; there was a 21% increase in misclassification violations from 2001 to 2005.

The study analyzed Illinois Department of Employment Security (IDES) audit data over a 5-year period from 2001–2005 and found that the majority of the audits were random, although nearly 25% were triggered by suspected noncompliance.

In comparing the study's findings to other states, the authors found that Illinois had the highest suspected rate of misclassification. Illinois' misclassification rate for 2005 was 19.5%. Because the "underground economy" (i.e., cash economy) was not included in the study, this rate is considered an underestimation.

---

35. The Employee Classification Act (820 ILCS 185/1-999) was authorized by Public Act 95-26, effective January 1, 2008.

36. *January 2008 IDOR Practitioners Meetings, Questions Submitted From Practitioners*, accessed online at http://www.revenue.state.il.us/LegalInformation/Practqna/2008qna.pdf

37. 820 ILCS 185/5

38. *Tax Administration. Issues in Classifying Workers as Employees or Independent Contractors.* United States General Accounting Office. GAO/T-GGD-96-130 (June 20, 1996)

39. Kelsay, M.P., Sturgeon, J. I., Pinkham, K. D. (Dec. 6, 2006) *The Economic Costs of Employee Misclassification in the State of Illinois*

Misclassification and Illinois Unemployment Insurance

Illinois allows an employee who was misclassified as an independent contractor to file for state unemployment benefits if the misclassified worker completes a waiver when applying. This action triggers an IDES audit to determine the worker's eligibility. If the IDES deems the worker is an employee, the employer must pay back taxes to the state.

The University of Missouri study estimates that from 2001–2005, the IDES lost an average of $39.2 million **per year** in uncollected unemployment insurance taxes caused by the misclassification of employees as independent contractors. Illinois lost $53.7 million in unemployment taxes for 2005 alone, according to the study's estimates.

Other Costs Related to Misclassification

Misclassification creates problems throughout society. Not only does it prevent workers from receiving employment benefits and reduce federal and state tax collections, it also indirectly affects the general public.

Health Care. Independent contractors often cannot afford health insurance. This not only jeopardizes the health and safety of the affected worker and his family, it also increases health risks for the general public when untreated illnesses and diseases are allowed to spread.

In 2001, health care providers supplied $34.5 billion in uncompensated medical services to the uninsured. The costs of treating uninsured patients are often borne by the insured population or the government, thereby increasing costs for all.

Competitive Advantage. Employers who improperly classify employees as independent contractors gain an advantage over competitors who abide by the law. By avoiding payroll costs and the cost of workers' compensation premiums, noncompliant companies can underbid compliant competitors.

MECHANICS OF THE ACT

Under the Act, a construction worker is deemed to be an employee **unless** the worker meets one of the two following statutory exceptions.

Exception 1. An individual must satisfy all the following conditions to be classified as an independent contractor:

1. The individual's performance of service must be free from the control or direction of the contractor, both under the individual's contract of service and in fact.
2. The service performed by the individual must be outside of the contractor's usual course of services.
3. The individual must be engaged in an independently-established trade, occupation, profession, or business.

Exception 2. An individual is deemed to be a legitimate sole proprietor or partnership if he meets the following tests:

1. Is free from control or direction over the means and manner of providing the service, subject to the contractor's right to specify the desired result;
2. Is not subject to cancellation or destruction upon severance of the relationship with the contractor;
3. Has a substantial investment of capital in the sole proprietorship or partnership beyond ordinary tools and equipment and a personal vehicle;
4. Owns the capital goods, gains from the profits, and bears the losses of the sole proprietorship or partnership;
5. Makes services available to the general public or the business community on a continuing basis;
6. Claims the income as SE income on a federal income tax return;
7. Performs services under the name of the sole proprietorship or partnership;
8. Obtains and pays for any required licenses or permits in the name of the sole proprietorship or partnership;

9. Furnishes any tools or equipment necessary to perform the job;
10. Hires employees if necessary without contractor approval, pays the employees without contractor reimbursement, and reports the employees' income to the IRS;
11. Refrains from representing the sole proprietorship or partnership as an employee of the contractor to customers; and
12. Retains the right to perform similar services for others on a whatever/whenever basis.

If a sole proprietor or partnership fails to meet **all** of the above 12 conditions, the sole proprietorship or partnership is deemed to be an individual. An individual must satisfy the three tests under **Exception 1** to be considered an independent contractor.

> **Observation.** The above exceptions imply that a worker who is incorporated cannot be considered an employee. This rationale has led some contractors to require subcontractors to become incorporated before they hire them. Many central-Illinois carpet layers have had to incorporate in order to retain business. If this trend continues, tax practitioners should be prepared to complete significantly more corporate returns.

Interagency Cooperation

The Act authorizes the IDOL, IDES, IDOR, and the Illinois Workers' Compensation Commission to share information concerning any suspected misclassification of an employee as an independent contractor.

The Act mandates that the IDOL notify the IDES, IDOR, the Office of the State Comptroller, and the Illinois Workers' Compensation Commission of any violations of the Act. These agencies and offices are then required to utilize their own definitions, standards, and procedures to determine whether the employer is in compliance with their laws.[40]

Sophisticated data-mining tools now allow IDOR to target employers for worker-classification compliance audits. For example, criteria can be set to find taxpayers who receive only one Form 1099-MISC per year that reports a large sum of money.

> **Note.** IDOR utilizes the IRC to determine if a worker is an employee or independent contractor.

Penalties for Violators

The IDOL is authorized to impose the following penalties and sanctions on employers who violate the Act:[41]

- First audit — up to $1,500 per violation
- Subsequent audits within five years — up to $2,500 per repeat violation, and barred from receiving state contracts for four years

Willful violators are subject to penalties that are up to double the statutory penalties under the Act and are liable to pay the employee for punitive damages. The first willful violation is considered a **Class C misdemeanor;** subsequent willful violations within a 5-year period are classified as **Class 4 felonies.**[42]

40. 820 ILCS 185/75
41. 820 ILCS 185/40, 185/42
42. 820 ILCS 185/45

FEDERAL LEGISLATION

Several federal legislators are jumping on the bandwagon to prevent the misclassification of workers. In September 2007, Illinois Senators Barack Obama (D) and Dick Durbin (D), in cooperation with Senator Edward M. Kennedy (D-MA) and Patty Murray (D-WA), introduced the Independent Contractor Proper Classification Act of 2007. This bill is intended to close a perceived tax loophole in the Revenue Act of 1978, Section 530 that allows employers to classify workers as independent contractors.

> **Note.** See Chapter 1, "Employment Taxation," for additional information on classification of employees and Section 530 relief.

LIMITED LIABILITY COMPANIES

A limited liability company (LLC) is a state-created business entity. Every state in the United States and the District of Columbia statutorily provides for the creation of LLCs.

> **Note.** See Chapter 4, "Limited Liability Companies," for information pertaining to federal taxation laws related to LLCs. The following content only describes aspects specific to LLCs formed or operating in Illinois.

ILLINOIS LIMITED LIABILITY COMPANY ACT

Illinois initiated its Limited Liability Company Act (LLCA) on January 1, 1994.[43] The Illinois Secretary of State's (SOS) office governs LLCs in Illinois. The SOS has two locations to serve business clients — one in Springfield and one in Chicago. The agency's website at **www.cyberdriveillinois.com** provides information regarding the requirements for establishing an Illinois LLC as well as the documents necessary to register and maintain both domestic (Illinois) and foreign (non-Illinois) LLCs.

The SOS's office does not provide any legal, financial, or business advice. Prospective businesses that wish to form an Illinois LLC are advised to seek competent advice from an attorney and accountant.

Naming an Illinois LLC

Before filing to organize an Illinois LLC, a name must be established. The LLC's name must be unique and original so it may be easily distinguished from the name of any other LLC or corporation, domestic or foreign, actual or assumed, including any name reserved or registered with the Illinois SOS under either the LLCA or the Business Corporation Act.

Before filing the paperwork to form an LLC, an organizer may contact the SOS's Department of Business Services to determine if the chosen name is available. Preliminary checks can be made through the SOS website at **www.cyberdriveillinois.com,** or by calling the Springfield office at 217-524-8008.

Several backup names should be selected because preliminary checks do not guarantee the name will be available when the LLC's organizer registers the name. Names are approved only after a Form LLC-1.15, *Application to Reserve a Name*, Form LLC-5.5, *Articles of Organization*, or Form LLC-1.20, *Application to Adopt an Assumed Name*, is filed.

LLC Designator. An Illinois LLC must contain the words "Limited Liability Company," or the abbreviation "L.L.C." or "LLC." The name must contain only letters in the English alphabet or Roman or Arabic numerals. The Department of Business Services must be able to reproduce any symbol used in the name.

---

43. 805 ILCS 180 et seq.

Prohibited Words. The name of an Illinois LLC cannot contain any of the following terms: Corporation, Corp., Incorporated, Inc., Ltd., Co., Limited Partnership, or L.P. The name cannot be offensive or in poor taste.

The name also cannot contain any word or phrase that implies that the LLC is engaged in insurance, assurance, or banking. However, the words "bank," "banker," and "banking" may be used as provided under the Illinois Banking Act.[44] Special rules apply to LLCs acting as corporate fiduciaries and those organized as trusts.[45]

Articles of Organization

To form an LLC in Illinois, Articles of Organization must be filed in duplicate (one original and one true copy) with the SOS's Department of Business Services. If the standard Form LLC-5.5, *Articles of Organization*, is used, it must be typed or completed in black ink. With the exception of Article 7, which is optional, Form LLC-5.5 must be fully completed.

Contents. Articles of Organization must contain the name of the LLC, the address for the LLC's principal place of business, the effective date for the Articles of Organization, the name of the LLC's registered agent and the address of the LLC's registered office in Illinois, the LLC's purpose and terms of existence, and a statement regarding whether the LLC will be member-managed or manager-managed. Additionally, the Articles of Organization should include the names and addresses of the initial managers or members.

Effective Date and Duration. An Illinois LLC comes into existence when the SOS's Department of Business Services "files" the Articles of Organization. An alternate date, not to exceed 60 days from the filing date, can be specified in Form LLC-5.5, Article 3. Illinois LLCs may be perpetual if so stated in Article 6. If a dissolution date is specified, the LLC must file Form LLC-5.25, *Articles of Amendment*, to alter the specified date.

Purpose. The Articles of Organization must state the LLC's business objective in the "purpose clause" of Form LLC-5.5, Article 5. A general purpose is acceptable. In fact, the following "general purpose clause" is preprinted on this form:

> *The transaction of any or all lawful business for which Limited Liability Companies may be organized under this Act.*

An Illinois LLC is prohibited from organizing for the purposes of banking or insurance. If an LLC is organized for the purposes of practicing dentistry or medicine, all members and managers (if any) must be licensed under either the respective Illinois Dental Practice Act or the Medical Practice Act of 1987. Other businesses and professions may impose restrictions as to permissible LLC purposes or require the LLC's purpose to be stated in a precise language.

Powers. Because the Illinois LLCA §1-30[46] sets forth the powers of an LLC, the Articles of Organization do not need to specifically enumerate the LLC's powers. However, the Articles of Organization cannot state that the LLC has the powers of a natural person.

Membership and Management. An LLC's owners and/or investors are called members. Members may be individuals or business entities such as corporations, partnerships, or LLCs. An LLC must have at least one member, but there is no maximum member limit.

Illinois LLCs may be either member-managed or manager-managed. In a member-managed LLC, each member has equal rights and equal say in the way the LLC conducts its business. In a manager-managed LLC, one or more members are designated to manage the company. Each manager has equal rights in the operation and conduct of the LLC.

An LLC may have one or more **organizers.** Organizers may be a business entity, such as a corporation, partnership, limited partnership, or LLC, or a natural person age 18 or older. Organizers of LLCs practicing medicine must be licensed in Illinois as either doctors or attorneys.

---

44. 205 ILCS 5/46

45. Corporate Fiduciary Act, 205 ILCS 620/1-9

46. 05 ILCS 180/1-30

Fees

Illinois charges a fee for many different services, including reserving an LLC name ($300), filing the Articles of Organization ($500), annual report fee ($250), and dissolution of the LLC ($100). Following is a listing of the various fees charged by the State of Illinois for LLCs.[47]

Limited Liability Company Forms and Fees

All form numbers correspond to the relevant Section of the Limited Liability Company Act. Note that the **expedited service fee** only applies if the document is **delivered in person** to the appropriate office of the Department of Business Services for filing within a 24-hour period, and does not apply to documents submitted by the mail. While expedited service is available for all forms at the Springfield office, only those denoted with an asterisk (*) can be processed on an expedited basis in the Chicago office.

Form #	Type of Form	Filing Fee	Expedited Fee
LLC-1.15	Application to Reserve a Name*	$ 300	$ 50 *
LLC-1.15	Cancellation or Transfer of a Reserved Name*	100	50 *
LLC-1.20	Application to Adopt an Assumed Name*	**	50 *
LLC-1.20	Application to Change or Cancel an Assumed Name*	100	50 *
LLC-1.20	Application to Renew an Assumed Name*	150	50 *
LLC-1.35	Resignation of Registered Agent	100	50
LLC-1.36/1.37	Statement of Change of Registered Agent and/or Registered Office*	25	50 *
LLC-1.50	Affidavit of Compliance	100	50
LLC-5.5	Articles of Organization*	500****	100 *
LLC-5.5(S)	Articles of Organization (Series)*	750****	100 *
LLC-5.25	Articles of Amendment*	150	100 *
LLC-5.30	Restated Articles of Organization	500	200
LLC-5.40	Application for Withdrawal-Domestic	100	50
LLC-5.47	Statement of Correction	25	50
LLC-5.48	Petition for Refund	15	50
LLC-35.15	Articles of Dissolution	100	50
LLC-35.40/45.65	Application for Reinstatement following Administrative Dissolution or Revocation*	500	100 *
LLC-37.10	Requirements for Partnership Conversion (no form)	100	200
LLC-37.25	Articles of Merger	50 per entity	200
LLC-37.40	Certificate of Designation*	50	50 *
LLC-45.5	Application for Admission to Transact Business	500	100
LLC-45.5(S)	Application for Admission to Transact Business (Series)	750	100
LLC-45.20	Application for Registration of Name	300	50
LLC-45.20	Renewal or Cancellation of a Registered Name	100	50
LLC-45.25	Amended Application for Admission	150	100
LLC-45.40	Application for Withdrawal-Foreign*	100	50 *
LLC-50.1	Annual Report*	250	50 *
LLC-50.15	Penalty-Return to Good Standing	300***	N/A
LLC-50.25	LLC Fax Transmittal Request Form for Certificates of Good Standing and/or Certified Copies of Documents:		
	- Abstract or Certificate of Good Standing*	25	50 *
	- Photocopy or Certified Copy*	25	20 *

** Based upon the years evenly divisible by 5, the fee to adopt an assumed name varies as follows: $150 for each year or part thereof ending in 0 or 5; $120 for each year or part thereof ending in 1 or 6; $90 for each year or part thereof ending in 2 or 7; $60 for each year or part thereof ending in 3 or 8; $30 for each year or part thereof ending in 4 or 9.

*** Plus $100 for each year or fraction thereof beginning with the second year of delinquency until the company is returned to good standing.

**** Also applies to online filings.

47. Illinois Secretary of State, *A Guide for Organizing Domestic Limited Liability Companies* (February 2008).

Tax Treatment of LLCs

There is no statutory equivalent to an LLC in the IRC. Therefore, for federal tax purposes, an LLC must file as a sole proprietorship, partnership, or corporation, including an S corporation.

Illinois follows the federal income tax treatment of LLCs, as shown below:

- **Single-Member LLCs (SMLLCs) —** An LLC with only one member can elect to be treated as a corporation for federal tax purposes by filing IRS Form 8832, *Entity Classification Election*. Absent this election, the IRS considers an SMLLC as a "disregarded entity" that must file as a sole proprietorship.
- **Multi-Member LLCs —** An LLC with more than one member can elect to be treated as a corporation for federal tax purposes by filing IRS Form 8832. Absent this election, the IRS treats a multi-member LLC as a partnership.

> **Note.** The disregarded entity status applies for tax purposes only; it does not affect the member's liability protection under the LLC.

CHARGING ORDERS

LLC members are basically equal partners that can exert significant control over an LLC's operations. This makes LLCs especially vulnerable to the influence of outside creditors, i.e., those to whom individual members owe debts from transactions that have arisen outside the LLC.

States have legislatively protected partnerships from becoming forced partners with outside creditors by means of a device called a "charging order." Charging orders allow creditors to garnish a partner's right to receive income from the partnership, while allowing the partner to retain the right to operate the partnership per the terms of the partnership agreement.

Illinois bases its LLCA on the Revised Uniform Limited Partnership Act (RULPA). A provision of RULPA prevents the forced liquidation of an owner's interest to satisfy the owner's personal debts. This means an Illinois LLC member's **outside creditors cannot assume management of the LLC** or exercise any of the debtor member's voting rights. The outside creditor cannot force liquidation or foreclosure of the LLC.

> **Note.** State law to the contrary, federal bankruptcy courts may appoint a trustee with the power to exercise control over an LLC member's interests. Because there is no provision in the bankruptcy code to address LLCs, the interpretation of this provision is handled differently across the country.

ILLINOIS SERIES LLCs

The latest statutorily-created business model, a series LLC, is a single legal entity that can be segregated into several separate entities called "cells" or "series." Each series has its own interests, liabilities, and membership. Separating business interests into a series of business interests segregates the liabilities of each interest and allows the parent LLC to separate potentially-dangerous ventures from safer enterprises.

Pros and Cons of Series LLCs

To visualize the series LLC concept, think of a mall. The building represents a single entity (LLC) composed of a series of separate stores (cells/series). Each store/cell is contained within the mall, but each store/cell is unique and can be distinguished from the others. Each store has its own interests, assets/liabilities, and investor/owners (i.e., members).

Example 3. Linkin Mall is a strip mall owned by Linkin Mall LLC, an Illinois company. Linkin Mall LLC owns the building and all 10 stores within the mall. The LLC members are considering adding a go-kart track to the property. However, many of the members are worried that liabilities arising from the go-kart track could wipe out their investment in the rest of the mall.

The members decide to segregate the go-kart operation from the rest of their investment by forming a series LLC to operate the track.

Ostensibly, by adding a series LLC to the parent LLC instead of forming another company, the parent company would save the time, effort, and expense of establishing a second LLC. However, the savings may not always be significant.

Time and Effort Savings. Creating a subsidiary series may seem less daunting than creating a whole new company. However, to support individual liability protection, Illinois requires each cell in a series LLC to maintain separate and distinct records and account for assets separately from the assets of the parent company.[48]

Cost Savings. Although an Illinois series LLC pays just one filing fee, the fees are higher than for a single LLC. To establish an Illinois series LLC, organizers must file Form LLC-5.5(S), *Articles of Organization (Series)*, and complete Article 7 to designate the LLC as one authorized to establish subsidiary series.

Form LLC-5.5(S) currently costs $750 to file, as opposed to $500 for Form LLC-5.5. After filing the Form LLC-5.5(S), the company may form one or more series LLCs by filing Form LLC-37.40, *Certificate of Designation*, for each series. Each certificate costs $50 to file.

Example 4. Use the facts from **Example 3.** Instead of forming a separate LLC to manage the go-kart track, the Linkin Mall LLC forms a subsidiary series LLC called the Linkin Mall LLC Go-Karts. The cost of filing two separate Forms LLC-5.5 is $1,000 ($500 × 2). The cost of filing Form LLC-5.5(S) and a Certificate of Designation for the go-kart subsidiary is $800 ($750 + $50). This $200 cost savings may not be significant enough to warrant establishment of a series LLC.

Other expenses to take into consideration include the legal fees necessary to draft the LLC operating agreement and the individual series agreements, as well as fees associated with preparing and filing annual reports and any necessary amendments to the articles of organization and/or certificates.

One potential advantage to establishing a series LLC over establishing two or more separate LLCs is the ease by which assets may be transferred among subsidiaries without triggering capital gains or real-estate transfer taxes. However, for reasons to be discussed later in this section, this advantage may not be material for LLCs established under Illinois law.

Liability Protection. Because the series LLC is a relatively new business model, it has not been adequately tested in the courts. For this reason, the liability protection of series LLCs may be uncertain, especially when a subsidiary becomes involved in a bankruptcy or when lax business practices persuade the court to pierce the corporate veil.[49]

Also uncertain is how series LLCs are treated when the liability arises in a state that does not statutorily authorize series LLCs. For example, if an Illinois tire manufacturer sells tires to a Michigan car manufacturer and the tires are suspected as the cause of a rollover accident in Pennsylvania, it is uncertain if the Michigan or Pennsylvania courts will honor the limited liability protection of the Illinois series LLC.

48. 805 ILCS 180/37-40(b)

49. Goforth, Carol R., *The Series LLC, and a Series of Difficult Questions*, 60 Ark. L. Rev. 385 (2007).

Distinctions between State Series LLCs

Delaware initiated the series LLC concept in 1996. Illinois authorized the formation of series LLCs in 2005.[50] The following seven states now offer series LLCs:

- Delaware
- Illinois
- Iowa
- Nevada
- Oklahoma
- Tennessee
- Utah

Although Delaware set the precedent for series LLCs, Illinois did not follow this model. Delaware segregates the business purpose and "debts, liabilities and obligations and expenses" for each series in the LLC but does not provide for each subsidiary to be autonomous.

Illinois, on the other hand, explicitly provides that **each series is separate and distinct** to the extent set forth in its articles of organization. Illinois allows each limited liability series, in its own name, to "contract, hold title to assets, grant security interests, sue and be sued and otherwise conduct business and exercise the powers of a limited liability company." [51]

Illinois also provides that a series LLC may elect to consolidate the operations of the parent company and any of its subsidiaries into a single taxpayer "to the extent permitted under applicable law."[52]

Illinois LLCs also may individually elect to work cooperatively, to contract jointly, or "to be treated a single business for purposes of qualification to do business in [Illinois] or any other state." These elections do not impede the limitation of liability except when the election is made to accept joint liability by contract.[53]

Administering an Illinois Series LLC

To establish an Illinois series LLC, organizers must file Form LLC-5.5(S) and a Certificate of Designation for each series established. (See Cost Savings under Pros and Cons of Series LLCs in this section.) The Certificate of Designation must list the names of the series LLC members if the series is member-managed or the names of the managers if the series is manager-managed.[54]

Series Name. The name of each series must contain the entire name of the LLC and be distinguishable from the names of the other series specified in the series LLC Articles of Organization.[55]

Changes. A new Certificate of Designation must be filed if the name of the series changes or if the members of a member-managed series or the manager(s) of a manager-managed series are different from those set forth in the LLC's Articles of Organization.[56]

---

50. 805 ILCS 180/37-40
51. 805 ILCS 180/37-40(b)
52. Ibid
53. Ibid
54. 805 ILCS 180/37-40(d)
55. 805 ILCS 180/37-40(c)
56. 805 ILCS 180/37-40(d)

Dissolution. An individual series within a series LLC may be dissolved by filing a Certificate of Designation with the Illinois SOS. A series is automatically dissolved if the parent LLC dissolves.[57]

Tax Treatment of Illinois LLCs

Illinois law authorizes each subsidiary in an Illinois series LLC to have a separate and distinct business purpose from the parent LLC and for each series to conduct business and exercise the powers of an LLC.[58] Based on these facts and others, University of Illinois College of Law Professor Charles T. Terry concludes that "each Illinois series organization may clearly be treated as a stand-alone business entity for federal tax purposes."[59]

As further support for the legislative intent of the statute to treat series LLCs as separate taxable entities, Terry cites provisions of the Illinois Series Limited Liability Act that state that each series may register to do business under its own name in Illinois or any foreign jurisdiction[60] and that the parent LLC and any of its subsidiary series may **elect** to consolidate as a single taxpayer to the extent permitted by law.[61]

> **Note.** In its Questions and Answers for 2006/2007 IDOR Practitioners' Meetings notes, IDOR stated that the state income tax treatment of Illinois series LLCs would follow the federal income tax treatment.

Because each Illinois series LLC may be considered a separate taxable entity unless an election is made to consolidate, Illinois series LLCs generally cannot benefit from the ability to transfer assets between series without incurring tax consequences.

FILING REQUIREMENTS FOR FOREIGN LLCs

According to the Illinois SOS's website, "Through fees and taxes, the department [of Business Services] generates approximately 69% of the money deposited into the General Revenue Fund by the Secretary of State's office."[62]

Because LLC filing fees represent a portion of this revenue, it is understandable that Illinois would not let foreign LLCs — or foreign series LLCs — escape paying their fair share of fees if the foreign LLCs or series LLCs conduct any business in Illinois.

To conduct business in Illinois, a foreign LLC must file the following forms with the Illinois SOS's Department of Business Services:

- Form LLC-45.5, *Application for Admission to Transact Business* ($500), or Form LLC-45.5(S), *Application for Admission to Transact Business (Series)* ($750)
- A Certificate of Good Standing or Existence from the LLC's "home" state
- A copy of the LLC's Articles of Organization, as amended, duly authenticated within 60 days of filing by an officer of the state or county where the LLC was formed
- A copy of the page from the LLC's operating agreement that states the LLC's duration period, if the period of duration is a date certain and is not stated in the Articles of Organization (if the date is listed as perpetual, this requirement is waived)

---

57. 805 ILCS 180/37-40(d), (m)
58. 805 ILCS 180/37-40(b)
59. Terry, C. T. and Samz, D. (Mar. 6, 2006) *An Initial Inquiry into the Federal Tax Classification of Series Limited Liability Companies*, 110 Tax Notes 1093. Professor Terry helped draft the Illinois Series Limited Liability Company Act (ISLLCA) when he served on the Illinois Secretary of State Business Acts Advisory Committee.
60. 805 ILCS 180/37-40(n)
61. 805 ILCS 180/37-40(b)
62. www.cyberdriveillinois.com/departments/business_services/home.html

If a foreign-based LLC operates in Illinois, it must file Form LLC-50.1, *Annual Report* ($250), every June 1. Failure to file this annual report within 60 days of June 1 results in a $300 penalty. If not paid within five months, the state revokes the foreign LLC's admission to transact business in Illinois.

If an LLC forms in another state but transacts business in Illinois without filing the appropriate forms, the Illinois SOS imposes a $2,000 penalty plus an additional $100 per month until the LLC files the proper forms and pays the associated fees. This includes filing back-dated copies of the LLC's annual report.

> **Observation.** If you combine the fees and potential fines associated with doing business as an LLC in Illinois, there is little incentive to form an LLC out of state where the initial filing fees may be less expensive.
>
> For instance, if an Illinois business chose to form an LLC in Missouri, where the minimum filing fee is $116 and the annual report fee is $45, it would still be required to file as a foreign LLC in Illinois as well as a domestic LLC in Missouri.

Rejected Foreign Applications

According to the Illinois SOS's Department of Business Services, applications for foreign LLCs to transact business in Illinois are rejected most often for the following reasons:

- Certified copies required on Form LLC-45.5, item 12, are missing
- The LLC's name is not available or Form LLC-1.20, *Application to Adopt an Assumed Name*, is not attached (Form LLC-45.5, item 2)
- The names and addresses of managers or members required on Form LLC-45.5, item 10 are missing
- The signatures are out of compliance with Illinois LLCA §5-45
- The documentation required for the period of duration is missing
- The date on which the company first conducted business in Illinois is missing from Form LLC-45.5, item 8