

Blog Post

Illinois DOR Proposes to Change Income Tax Liability for Businesses That Make Sales to Foreign Countries

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By [David C. Blum](#) and [Lauren A. Ferrante](#)

The Illinois Department of Revenue (“IDOR” or “Department”) recently issued a Notice of Proposed Amendment to amend its Regulation (86 Ill. Admin. Code § 100.3200) governing the “throwback” and “throwout” apportionment provisions (the “Amendments”). [46 Ill. Reg. ____ \(Apr. 15, 2022\), at 5856](#). If adopted, the Amendments would change the Illinois income tax burden imposed on a business by altering the business’ apportionment with respect to sales made into certain foreign countries.

If a business is subject to Illinois income tax, the business must both: (1) throwback to (i.e., include in its apportionment factor numerator)[1] its sales of tangible personal property delivered to a state where the business is not taxable; and (2) throwout of (i.e., exclude from) its entire apportionment factor (both numerator and denominator) sales of services that were received in a state where the business is not taxable. 35 ILCS 5/304(a)(3)(B)(ii), (a)(3)(C-5)(iv); *see also* 86 Ill. Admin. Code § 100.3370(c)(1)(A)(ii), (c)(1)(F), (c)(7)(D)(iv).

Currently, IDOR regulations interpret the statute to require taxpayers to throwback and throwout sales made into foreign countries where the taxpayer is not taxable as a result of a treaty provision. 86 Ill. Admin. Code § 100.3200(a)(2)(C). For taxpayers,

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depending on their facts and sales volume, this rule can have the effect of increasing or decreasing their Illinois tax liability.

The Amendments propose to amend the rules so that for tax years beginning on or after January 1, 2021, taxpayers are not required to throwback and throwout sales made into treaty protected countries, so long as the taxpayer otherwise is taxable in that country. In the Amendments, the Department states that it is proposing this change to align its rule with the Multistate Tax Commission Model Sourcing Rule, which likewise carves out from its throwback and throwout rules (*see* Reg. IV.16.(a)(1)(B), IV.17.(a)(6)(D)) sales made into treaty protected countries (Reg. IV.3.(c))

Throwback and throwout rules are generally bad tax policy, because they tax income that should not be attributed to the taxing state and are incongruous with market-based sourcing regimes enacted in many states and inconsistent with the tax determination of the destination state. While IDOR should be commended for narrowing the scope of these rules, the Amendments arguably do not go far enough as other states have repealed throwback and throwout entirely. Taxpayers affected by the Amendments should confirm the effect on their Illinois tax liability. Written comments to the proposed Amendments were due to IDOR by May 30th.

[1] Illinois uses a single sales factor only.

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