



Publication 129

Pass-through Entity Income

August 2018

The information in this publication is current as of the date of the publication. Please visit our website at tax.illinois.gov to verify you have the most current revision.

This publication is written in the plain English style so the tax information is easier to understand. As a result, we do not directly quote Illinois statutes or the Illinois Administrative Code. The contents of this publication are informational only and do not take the place of statutes, rules, and court decisions. For many topics covered in this publication, we have provided a reference to the applicable section or part of the Illinois Administrative Code for further clarification or more detail. All of the sections and parts referenced can be found in Title 86 of the Illinois Administrative Code.

About this publication

Publication 129, Pass-through Entity Income, explains the tax obligations involved with distributions from partnerships, S corporations, and fiduciaries to partners, shareholders, and beneficiaries.

This publication specifically provides assistance to

- pass-through entities (partnerships, S corporations, and fiduciaries) that distribute pass-through income, and
- members (partners, shareholders, and beneficiaries) who receive pass-through income from pass-through entities.

If you need more technical or statutory information, please see [86 Ill. Admin. Code Part 100](#).

Taxpayer Bill of Rights

You have the right to call the Department of Revenue for help in resolving tax problems.

You have the right to privacy and confidentiality under most tax laws.

You have the right to respond, within specified time periods, to Department notices by asking questions, paying the amount due, or providing proof to refute the Department's findings.

You have the right to appeal Department decisions, in many instances, within specified time periods, by asking for Department review, by filing a petition with the Illinois Independent Tax Tribunal, or by filing a complaint in circuit court.

If you have overpaid your taxes, you have the right, within specified time periods, to a credit (or, in some cases, a refund) of that overpayment.

For more information about these rights and other Department procedures, you may write us at the following address:

Problems Resolution Division
Illinois Department of Revenue
PO Box 19014
Springfield, IL 62794-9014

Get forms and other information faster and easier at tax.illinois.gov

Contents

General Information	3
What is a “pass-through entity”?.....	3
What is “pass-through entity income”?	3
What is “pass-through withholding”?	3
Who is a resident?.....	3
Who is a nonresident?.....	3
What is business income?.....	3
When is business income allocable to Illinois?.....	3
What is nonbusiness income?.....	3
When is nonbusiness income allocable to Illinois?.....	4
What is Form IL-1000-E?.....	4
What is Schedule B?	4
What is Schedule D?	4
What is Schedule K-1-P or Schedule K-1-T and what do I do with it?	4
When is pass-through entity income earned by the member?.....	4
What is an “investment partnership”?	4
What is the Personal Property Replacement Income Tax (replacement tax)?	5
What does Illinois do with the pass-through withholding information received from pass-through entities?.....	5
What if a pass-through entity overpays the pass-through withholding?.....	5
Information for Pass-through Entities	6
What is Schedule K-1-P(1) or Schedule K-1-T(1)?	6
What is Schedule K-1-P(3) or Schedule K-1-T(3)?	6
What form(s) must the pass-through entity file?.....	6
Does Form IL-1065, Form IL-1120-ST, or Form IL-1041 satisfy the tax liability for the member?.....	6
Helpful Hints and Reminders for Pass-through Entities	6
Partnerships and S Corporations	6
Fiduciaries.....	6
Information for Members	7
What does the member receive from the pass-through entity?.....	7
What is Schedule K-1-P(2) or Schedule K-1-T(2)?	7
What does the member do with Schedules K-1-P and K-1-P(2) or Schedules K-1-T and K-1-T(2)?.....	7
If a member is filing an Illinois tax return, what form must they use?.....	7
Reciprocal state information	8
What if I have not filed an Illinois tax return?	8
Helpful Hints and Reminders for Members	8
Office Locations	9
For Information or Forms	9

General Information

For purposes of this publication, the term ‘member’ means any partner, shareholder, or beneficiary.

What is a “pass-through entity”?

A pass-through entity is any entity treated as a partnership, S corporation, or fiduciary for federal income tax purposes.

What is “pass-through entity income”?

Pass-through entity income is the income that partnerships, S corporations, or fiduciaries pass through to their members.

What is “pass-through withholding”?

Pass-through withholding is required payments that are to be reported and paid by a pass-through entity on behalf of any **nonresident** members

- who have **not** submitted Form IL-1000-E, Certificate of Exemption for Pass-through Withholding, to the pass-through entity, and
- who receive business and nonbusiness income from the pass-through entity.

Pass-through withholding is

- reported to partners and shareholders on Schedule K-1-P, Partner’s or Shareholder’s Share of Income, Deductions, Credits, and Recapture, **or** reported to beneficiaries on Schedule K-1-T, Beneficiary’s Share of Income and Deductions,
- reported to the Department on Schedule B, Partners’ or Shareholders’ Information, of both Form IL-1065, Partnership Replacement Tax Return and Form IL-1120-ST, Small Business Corporation Replacement Tax Return, **or** reported to the Department on Schedule D, Beneficiary Information, of Form IL-1041, Fiduciary Income and Replacement Tax Return,
- paid using the payment voucher for Form IL-1065, Form IL-1120-ST, or Form IL-1041. For tax years ending before December 31, 2014, pass-through withholding was known as “pass-through entity payments” or “composite return payments” and were reported on Form IL-1000 or Form IL-1023-C respectively.

Who is a resident?

A resident is

- an individual who is present in Illinois for other than a temporary or transitory purpose;
- an individual who is absent from Illinois for a temporary or transitory purpose but who is domiciled in Illinois;
- the estate of a decedent who at his or her death was domiciled in Illinois;

- a trust created by a will of a decedent who at his or her death was domiciled in Illinois; or
- an irrevocable trust, whose grantor was domiciled in Illinois at the time the trust became irrevocable. For purposes of this definition, a trust is irrevocable to the extent that the grantor is not treated as the owner of the trust under Internal Revenue Code (IRC) Sections 671 through 678.

Who is a nonresident?

A nonresident is a person who is not a resident, as previously defined. Corporations, S corporations, and partnerships are considered nonresidents for purposes of pass-through entity income and Illinois Schedule B and Schedule D.

What is business income?

Business income means all income, other than compensation, that may be apportioned by formula among the states in which you are doing business without violating the Constitution of the United States. All income of a partnership or S corporation is business income unless it is clearly attributable to only one state and is earned or received through activities totally unrelated to any business you are conducting in more than one state. Business income is net of all deductions attributable to that income.

When is business income allocable to Illinois?

For a **resident** of Illinois, all income received, regardless of the source, is allocable to Illinois.

For a **nonresident** of Illinois whose business income is derived

- wholly inside Illinois, the entire amount of business income is allocable to Illinois.
- wholly outside Illinois, none of the business income is allocable to Illinois.
- inside and outside Illinois, see the specific instructions for your return and the instructions in Schedule K-1-P(2) or Schedule K-1-T(2).

What is nonbusiness income?

Nonbusiness income is all income other than business income or compensation. It is income you can clearly classify as having no connection to your business. For information about types of nonbusiness income, see the instructions for Illinois Schedule NB, Nonbusiness Income.

When is nonbusiness income allocable to Illinois?

For a **resident** of Illinois, all nonbusiness income is allocable to Illinois.

For a **nonresident**, items of income and deduction that constitute nonbusiness income received through the pass-through entity are treated as if received directly by the member and are allocable to Illinois according to the rules detailed in your return instructions and in the instructions in Schedule K-1-P(2) or Schedule K-1-T(2).

What is Form IL-1000-E?

Any member that is not an individual, that elects to make its own tax payments on income from a pass-through entity may do so by completing Form IL-1000-E and providing a signed copy of the form to the pass-through entity. By completing Form IL-1000-E, the member is certifying it will file all Illinois Income Tax returns and make timely payment of all Illinois income taxes due.

What is Schedule B?

Schedule B is the required schedule for partnerships and S corporations to provide information to the Department about their members, certain items of income and credits the member receives from the pass-through entity, and pass-through withholding made on the members' behalf. If a partnership or S corporation passes any income through to a member, then the pass-through entity must provide the Illinois Department of Revenue with all of the required information on a Department-approved form. Schedule B must be included with Form IL-1065 and Form IL-1120-ST.

What is Schedule D?

Schedule D is the required schedule for fiduciaries to provide information to the Department about their members, certain items of income and credits the members receive from the pass-through entity, and pass-through withholding made on the members' behalf. If a fiduciary passes any income through to a member, then the pass-through entity must provide the Illinois Department of Revenue with all of the required information on a Department-approved form. Schedule D must be included with Form IL-1041.

What is Schedule K-1-P or Schedule K-1-T and what do I do with it?

Similar to the federal Schedule K-1, the purpose of Schedule K-1-P or Schedule K-1-T is for the pass-through entity to supply each individual or entity who was a member at any time during the tax year with the information needed by the member to properly report the pass-through income on the member's Illinois Income Tax return. Every pass-through entity **must** give a completed

- Schedule K-1-P **and** a copy of Schedule K-1-P(2), Partner's and Shareholder's Instructions to each partner or shareholder, or
- Schedule K-1-T **and** Schedule K-1-T(2), Beneficiary's Instructions, to each beneficiary,

by the due date, including any extended due date, of their Form IL-1065, Form IL-1120-ST or Form IL-1041.

The pass-through entity must not submit copies (to the Department) of any Schedule K-1-P or Schedule K-1-T it issues to a member unless requested to do so by the Department. The pass-through entity must maintain copies of any Schedule K-1-P or Schedule K-1-T it issues in its files in the event of an audit or review by Illinois Department of Revenue personnel.

If you are a member in a pass-through entity, that entity is required to send you a Schedule K-1-P or Schedule K-1-T. You must include this pass-through income when completing your Illinois tax return and attach a copy of any Schedule K-1-P or Schedule K-1-T that was issued to you when you file your Illinois income tax return.

If a member does not receive a Schedule K-1-P or Schedule K-1-T, the member should contact the pass-through entity and ask for a copy of the Schedule K-1-P or Schedule K-1-T. The member may wish to take advantage of the six-month automatic filing extension (seven-months for S corporations and corporations with a June 30 tax year end). However, if tax is owed, the member must make any tax payment by the original due date of the tax return or a penalty for late payment of tax due may be imposed.

If a member receives a Schedule K-1-P or Schedule K-1-T after filing an original tax return, the member must file an amended return to include the pass-through income or loss.

When is pass-through entity income earned by the member?

Pass-through entity income is considered earned on the last day of the pass-through entity's taxable year. Pass-through entity income is not considered received equally throughout the year nor is it considered received on the last day of member's tax year. Members need to be aware of how this affects their Illinois Income Tax liability. There are two instances when the timing of the receipt of pass-through entity income is particularly important. First, is when determining estimated payments and the second is if the tax rate changes during the member's tax year.

What is an "investment partnership"?

A partnership is classified as an investment partnership if at least 90 percent of its assets are investments in stocks, bonds, options, and similar intangible assets, and at least 90 percent of its income is derived from those types of assets.

For tax years ending on or after December 31, 2004, an investment partnership is not subject to replacement tax and is not required to file an Illinois tax return.

A partner in an investment partnership is not subject to Illinois tax on the income passed through from the investment partnership, unless the partner's investment in

the partnership was made in connection with a business the partner is conducting at least partially within Illinois. In that case, the partner would include the income from the partnership with the other income of the business as if the partner had received the income directly, rather than through the partnership.

For tax years prior to December 31, 2004, an investment partnership and its partners are subject to the same rules as other partnerships and partners. For those years, any income passed through to a partner from an investment partnership is taxable to Illinois as indicated by the partnership on the Schedule K-1-P that it issued to the partner. See [35 ILCS 5/1501\(a\)\(11.5\)](#) for more information.

What is the Personal Property Replacement Income Tax (replacement tax)?

Replacement taxes are revenues received from businesses and public utilities, collected by the state of Illinois and paid to local governments.

Prior to 1979, business entities were required to pay personal property taxes. Legislation abolished the personal property taxes. To replace the money lost by units of local government and school districts, a new law was enacted that established replacement taxes, assessed at a flat rate based on the income of the business.

Business entities, including corporations, S corporations, partnerships, and trusts pay replacement tax on their annual tax returns. Replacement taxes are different from the standard Illinois income tax. Illinois income tax is paid only by individuals, trusts, estates, and corporations (not including S corporations).

What does Illinois do with the pass-through withholding information received from pass-through entities?

The Illinois Department of Revenue uses the member information obtained from Schedule B or Schedule D to ensure that taxpayers who have received income from Illinois sources have filed the appropriate tax return and paid any required tax liability. Taxpayers who have not filed an Illinois tax return, but who should have, may receive a Nonfiler Notice or a Notice of Proposed Tax Due. Penalties and interest may be assessed according to Illinois law. If taxpayers do not respond to these notices, the tax, penalty, and interest will be deemed assessed, and the taxpayer will be referred for collection activity. Collection activity can result in property liens, frozen assets and accounts, and wage garnishments.

Pass-through entities that have income taxable in Illinois must file an annual tax return with the Illinois Department of Revenue. Partnerships and S corporations do not pay Illinois

Income Tax (the members pay Illinois Income Tax) but they are subject to the Replacement Tax at a rate of 1.5 percent on income taxable to Illinois.

Pass-through entities can **pay** and receive pass-through withholding.

- Pass-through withholding **paid by the pass-through entity** is payments **they pass-through entity made** on behalf of any nonresident member who has not submitted Form IL-1000-E to them.
- Pass-through withholding **reported to the pass-through entity** are is credits for pass-through withholding **they pass-through entity received** on Schedule K-1-P as the partner or shareholder or Schedule K-1-T as the beneficiary in a pass-through entity.

What if a pass-through entity overpays the pass-through withholding?

A pass-through entity cannot request a refund of any pass-through withholding reported to members as paid on their behalf. In the case of any overpayment, the member must file a timely claim for credit or refund of any pass-through amount overwithheld.

Information for Pass-through Entities

What is Schedule K-1-P(1) or Schedule K-1-T(1)?

The purpose of Schedule K-1-P(1) or Schedule K-1-T(1) is to provide you the instructions for how to supply each individual or entity who was a member of your pass-through entity at any time during your tax year with that individual's or entity's share of the amounts you reported on your federal income tax return and your Illinois business income tax return. Use Schedule K-1-P(1) or Schedule K-1-T(1) to assist you in completing Schedule K-1-P or Schedule K-1-T for your members.

What is Schedule K-1-P(3) or Schedule K-1-T(3)?

Use Schedule K-1-P(3) or Schedule K-1-T(3) to calculate the required tax you must report and pay on behalf of your nonresident members that receive business or nonbusiness income from your pass-through entity. See Schedule K-1-P(1) or Schedule K-1-T(1) for instructions on how to complete Schedule K-1-P(3) or Schedule K-1-T(3). Do not send Schedule K-1-P(3) or Schedule K-1-T(3) to your members or submit it to the Illinois Department of Revenue unless we request it from you. Keep Schedule K-1-P(3) or Schedule K-1-T(3) with your income tax records.

What form(s) must the pass-through entity file?

Partnerships file Form IL-1065, including Schedule B.

S corporations file Form IL-1120-ST, including Schedule B.

Fiduciaries (Trusts and Estates) file Form IL-1041, including Schedule D.

Also, all required supporting Illinois schedules must be included with each return. These returns can be

- filed electronically through the IRS Modernized e-File program (MeF) using third-party tax-prep software,
- mailed to the address on the return, or
- filed through MyTax Illinois (IL-1041 only).

Any member that is a pass-through entity itself is required to report and pay pass-through withholding on behalf of the pass-through entity's own nonresident members on the income passed through to them. A member may claim credit on the member's Illinois Income Tax return for pass-through withholding reported and paid on its the member's behalf.

Does Form IL-1065, Form IL-1120-ST or Form IL-1041 satisfy the tax liability for the member?

Maybe. If a member is a nonresident individual and the reported pass-through withholding satisfies the member's Illinois Income Tax liability, then member is not required to file an Illinois Income Tax return. If the member has Illinois income from other sources or the pass-through withholding made on the member's behalf does not cover the member's liability, they member must file a return to report the tax on all of the member's Illinois income and claim a credit for pass-through withholding made on their member's behalf.

Helpful Hints and Reminders for Pass-through Entities

Partnerships and S Corporations

- ◆ File a return with a fully completed Schedule B listing all partners or shareholders.
- ◆ Complete a Schedule K-1-P for each partner or shareholder.
- ◆ Mail the completed Schedule K-1-P to your partners or shareholders in a timely manner and include a copy of Schedule K-1-P(2).
- ◆ If your partners or shareholders contact you with questions that you cannot answer, refer them to the Illinois Department of Revenue or the partner's or shareholder's tax professional. All tax forms are available on our website at tax.illinois.gov.
- ◆ Do not accept Form IL-1000-E from an individual member.

Fiduciaries

- ◆ File a return with a fully completed Schedule D listing all beneficiaries.
- ◆ Complete a Schedule K-1-T for each beneficiary.
- ◆ Mail the completed Schedule K-1-T to your beneficiaries in a timely manner and include a copy of Schedule K-1-T(2).
- ◆ If your beneficiaries contact you with questions that you cannot answer, refer them to the Illinois Department of Revenue or the beneficiary's tax professional. All tax forms are available on our website at tax.illinois.gov.
- ◆ Do not accept Form IL-1000-E from an individual member.

Information for Members

What does the member receive from the pass-through entity?

Each pass-through entity that distributes pass-through entity income and reports pass-through withholding to the Department is also responsible for providing this information to the pass-through entity's members. For Illinois purposes,

- the partnership or S corporation should issue a Schedule K-1-P and Schedule K-1-P(2), showing the partner's or shareholder's share of income and pass-through withholding and
- the fiduciary should issue a Schedule K-1-T and Schedule K-1-T(2), showing the beneficiary's share of income and pass-through withholding.

What is Schedule K-1-P(2) or Schedule K-1-T(2)?

The pass-through entity listed on the front of Schedule K-1-P or Schedule K-1-T has completed and provided you with the schedule to reflect your specific share of the pass-through entity's income, modifications, and credits. Use the completed schedule and Schedule K-1-P(2) or Schedule K-1-T(2) to help you report the items shown on Schedule K-1-P or Schedule K-1-T on your Illinois Income Tax return. **Attach a copy of Schedule K-1-P or Schedule K-1-T to your tax return and keep a copy for your records.**

What does the member do with Schedules K-1-P and K-1-P(2) or Schedules K-1-T and K-1-T(2)?

Based on the information provided by the pass-through entity and any other Illinois-based income, the member must determine its own Illinois tax liability. Use Schedule K-1-P(2)

or Schedule K-1-T(2) to determine where to report the information from Schedule K-1-P or Schedule K-1-T on the member's Illinois Income Tax return.

Any Illinois-sourced income that a member receives is taxable by the State of Illinois. If a member completes its tax return correctly, it should only be taxed on the Illinois-sourced income.

If a member is a nonresident individual and the pass-through withholding reported to the member satisfies the member's Illinois Income Tax liability, then the member is not required to file an Illinois Income Tax return. If a member has Illinois income from other sources or the pass-through withholding made on behalf of the member does not cover the member's liability, then the member must file a return to report the tax on all of the member's Illinois income and claim a credit for the pass-through withholding. A nonresident individual member may be able to take a credit for taxes paid to Illinois on their member's home state's tax return.

All Illinois residents and all pass-through entities must file their own annual Illinois Income Tax returns and claim credit for any pass-through withholding reported to them.

Note Business entities that receive income from a pass-through entity are also responsible for paying replacement tax on the income.

If a member is filing an Illinois tax return, what form must they use?

If the member is a(n)	then the member should file
Individual (married or single)	Form IL-1040, Individual Income Tax Return. Illinois nonresidents must also file IL-1040, Schedule NR, Nonresident and Part-Year Resident Computation of Illinois Tax.
Fiduciary (Trust or Estate)	Form IL-1041, Fiduciary Income and Replacement Tax Return. Illinois nonresidents must also file IL-1041, Schedule NR, Nonresident Computation of Fiduciary Income.
Corporation	Form IL-1120, Corporation Income and Replacement Tax Return.
S corporation	Form IL-1120-ST, Small Business Corporation Replacement Tax Return, including Schedule B.
Partnership	Form IL-1065, Partnership Replacement Tax Return, including Schedule B.
Exempt Organization	Form IL-990-T, Exempt Organization Income and Replacement Tax.
Unitary Group	The appropriate return with Schedule UB, Combined Apportionment for Unitary Business Group, attached.

Additional schedules and information may be required. For more information, see the instructions for the specific tax form you are filing.

Reciprocal state information

If a member lives in a state with which Illinois has a reciprocal agreement (*i.e.*, Wisconsin, Iowa, Michigan, and Kentucky) and receives pass-through income from a pass-through entity then the member has an Illinois Income Tax obligation and must file an Illinois Income Tax return showing the pass-through income as taxable to Illinois. The reciprocal agreement between Illinois and other states is only applicable to employment wages.

What if I have not filed an Illinois tax return?

If a member has not filed an Illinois Income Tax return, but should have filed, then the member should file the necessary tax return and any supporting schedules as soon as possible. If any tax is owed to Illinois, the Department may assess penalties and interest.

There is no statute of limitations for the Department to assess tax on individuals or entities who have not filed a return. However, if a nonfiler participates in our voluntary disclosure program, we will only collect taxes for the last four years. See Form BOA-2, Application for Voluntary Disclosure, for more information.

Helpful Hints and Reminders for Members

- ◆ Any Illinois-sourced income is taxable in Illinois.
- ◆ If you receive one or more Schedules K-1-P or Schedules K-1-T then you may have an Illinois tax liability. You must determine your own Illinois tax liability and filing responsibility.
- ◆ If you did not receive Schedule K-1-P(2) or Schedule K-1-T(2) to help you complete an Illinois Income Tax return, see the Department's website at **tax.illinois.gov** to view these instructions.
- ◆ If you received a Nonfiler Notice or a Notice of Proposed Tax Due from the Illinois Department of Revenue, you should respond within the time frame provided on the notice.
- ◆ If you have a paid tax preparer, complete and submit a Form IL-2848, Power of Attorney, so your preparer may respond to the Department on your behalf.
- ◆ If you did not receive a Schedule K-1-P or Schedule K-1-T from the pass-through entity, then you should contact the pass-through entity directly to obtain the schedule.
- ◆ Individual members and fiduciaries may file using MyTax Illinois, our free online account management program at **mytax.illinois.gov**. Forms are available at **tax.illinois.gov**.
- ◆ Pass-through entity income is deemed earned on the last day of the pass-through entity's taxable year.

Office Locations

Maine North Regional Building
9511 Harrison Street FA 203
Des Plaines, Illinois 60016-1563
847 294-4200

200 South Wyman Street
Rockford, Illinois 61101-1237
815 987-5210

James R. Thompson Center
Concourse Level
100 West Randolph Street
Chicago, Illinois 60601-3274
800 732-8866
217 782-3336

Willard Ice Building
101 West Jefferson
Springfield, Illinois 62702
800 732-8866
217 782-3336

15 Executive Drive
Business Center One, Suite 2
Fairview Heights, Illinois 62208-1331
618 624-6773

2309 W. Main
Suite 114
Marion, Illinois 62959-1196
618 993-7650

For Information or Forms

Visit our website at tax.illinois.gov.

Call us at **1 800 732-8866** or **217 782-3336**.

Call our TDD (telecommunications device for the deaf) at **1 800 544-5304**.

Write us at Illinois Department of Revenue, PO Box 19044, Springfield, IL 62794-9044.

Call our 24-hour Forms Order Line at **1 800 356-6302**.