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June 5, 2026

Sent Via Email (REV.GCO@illinois.gov)

Brian Stocker
Illinois Department of Revenue
Legal Services Office
101 W. Jefferson Street
Springfield Illinois 62706

Re: Comments - Amendments to 86 Ill. Adm. Code 100.2430.

Dear Mr. Stocker:

On behalf of the Council On State Taxation (COST), I appreciate the opportunity to provide comments on the proposed amendments to Regulation 86 Ill. Adm. Code 100.2430 which were published in the Illinois Register on April 24, 2026. While the amendments aim to align the regulation with statutory changes under Public Act 104-6, as outlined in this letter COST is concerned with several issues that arise from the revised regulatory language and its practical application.

About COST

COST is a nonprofit trade association based in Washington, DC. COST was formed in 1969 and today has a membership of approximately 450 major corporations engaged in interstate and international business. The organization's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities. Numerous COST members have operations in Illinois and are impacted by the amended regulations.

Draft Regulatory Amendments

The proposed amendments to 86 Ill. Adm. Code 100.2430 are in response to provisions of the fiscal 2025 tax and revenue budget bill, Public Act 104-6 (Budget Bill). The Budget Bill amended 35 ILCS 5/203 by significantly limiting the deductions for interest expense and intangible expense when paid to an entity that conducts at least 80 percent of its business outside the United States. Although the proposed amendments attempt to clarify when a deduction will be permitted, the amendments provide limited guidance and more importantly would significantly limit the application of the remaining safe-harbor provisions found in §§203((b)(E-12) and (E-13) by imposing evidentiary restraints not reflected in the statute.

The amendments to §203 repealed three safe-harbor exceptions that allowed taxpayers deductions for interest and intangible expenses if the foreign affiliate was 1) subject to a foreign income tax, 2) if the transaction was at arm's length, or 3) if the principal purpose of the transaction was not the avoidance of Illinois tax. As a result, for tax years ending on or after December 31, 2026, taxpayers, absent a showing of unreasonableness or an agreement to use an alternative apportionment method, are required to add back expenses related to bona fide cross-border transactions with no tax avoidance motive. The regulation would require taxpayers to establish by "clear and convincing evidence" that an adjustment would be unreasonable but also specifies that the presence of any or all of the enumerated factors (the foreign person is subject to a net income tax, the transaction is at arm's length, or that the principal purpose was not tax avoidance) is not sufficient to establish unreasonableness. These regulatory limitations exceed the scope of the statutory framework by narrowing the meaning of "unreasonableness". The lack of guidance regarding unreasonableness creates uncertainty about what additional evidence is required to support a deduction, invites inconsistent application on audit, and significantly increases litigation risks.

The suggestion that a taxpayer should obtain a Private Letter Ruling to establish that an adjustment is unreasonable fails to adequately resolve the lack of guidance regarding the additional evidence needed to sustain the deduction. Additionally, seeking a Private Letter Ruling is not a practical solution due to both the time and cost constraints for taxpayers and would likely strain Department resources.

Although the Budget Bill repealed three safe harbor provisions, it did not authorize the Department to exclude or discount otherwise relevant probative evidence in establishing "unreasonableness". The statute does not preclude taxpayers from establishing by clear and convincing evidence that the transaction was an arm's-length transaction, the income was previously taxed, or that the motivation for the transaction was not tax avoidance. The language in subsection (c)(1)(D) and (c)(2)(C) of the proposed regulation is beyond the intent of the statute and the stated purpose of the modification: to prevent interest expense or intangible expense arising from intercompany arrangements between persons who would be members of the same unitary group but for the 80/20 rule, from **improperly reducing** (emphasis added) the base income of the persons or groups subject to the Illinois income tax. As drafted, the regulatory language makes it extremely difficult, if not impossible, for a taxpayer to establish that the addition modification is unreasonable. The diminished relevance or exclusion of key factors such as an advance pricing agreement establishing a bona fide business transaction[1] is contrary to the stated purpose of the adjustments. Expenses related to legitimate cross-border business transactions do not **improperly** reduce the base income of an Illinois unitary group and in many instances are subject to tax in the foreign jurisdiction. The restrictions placed on the determination of an unreasonable adjustment by the proposed

[1]An Advance Pricing Agreement (APA) is a binding agreement between a taxpayer and the Internal Revenue Service that determines in advance the appropriate transfer pricing methodology for intercompany transactions. Rev. Proc. 2015-41 governs the process, which includes a detailed factual and economic analysis of the transactions. The result is an agreement with a term of typically 5 years that will specify the transfer pricing methodology, covered transactions, critical assumptions, and compliance requirements. APAs may be unilateral (IRS only), bilateral (IRS and one foreign tax authority), or multilateral (IRS and multiple foreign authorities).

regulations fail to adequately take into consideration the existence of bona fide cross-border transactions, the potential for double taxation, and heighten the risk of protracted and costly litigation.

Proposed Changes to Draft Regulations

COST respectfully requests the Department to add language to Sections 100.2340(c)(1)(D) and (c)(2)(C) that provides greater clarity regarding the relevant factors in determining unreasonableness, including a statement that no single factor is dispositive and taxpayers may rely on probative evidence that demonstrates unreasonableness under the clear and convincing evidentiary standard. Such probative evidence should include items such as (1) arm's-length transactions evidenced by contracts or agreements; (2) interest payments that meet the arm's-length standards set forth in 26 C.F.R. § 1.482-2(a)(2); (3) Internal Revenue Service advance pricing agreements; (4) documentation that the adjustment results in an improper matching of income and expenses; and (5) evidence of double taxation. Additionally, language should be added specifying that the examples set forth in subsection (4) are illustrative and not exhaustive of what will be considered an unreasonable adjustment.

COST also requests that the Department consider adding the following example (addressing the operations of financial institutions) which we believe clearly establishes an unreasonable adjustment:

> Example: Bank A is a domestic bank and operates branches in numerous foreign jurisdictions and takes deposits in the normal course of its banking business from domestic and foreign customers, the majority of which are unrelated. Assume member B, who would be a member of the same unitary business group but for the 80/20 rule, and FC have deposits with affiliated bank A. The deposits did not have as a principal purpose the avoidance of Illinois income tax. The interest on the deposits meets the arm's-length standard set forth in 26 C.F.R. 1.482-2(a)(2) and is compliant with regulation 12 CFR Part 223 and Federal Reserve regulation implementing Sections 23A and 23B of the Federal Reserve Act. Based on these facts, an addback adjustment would be considered unreasonable.

Conclusion

COST appreciates the Department's efforts to implement the statutory changes enacted under Public Act 104-6 and to provide guidance to taxpayers impacted by those changes. However, the proposed amendments to 86 Ill. Adm. Code 100.2430 impose limitations that extend beyond the statutory framework and create significant uncertainty regarding the circumstances under which taxpayers may demonstrate that an addback modification is unreasonable. In particular, the restrictive treatment of relevant evidentiary factors and the lack of clear standards for satisfying the "clear and convincing" evidentiary burden risk inconsistent administration, heightened litigation risks, and increase risk of double taxation on legitimate cross-border transactions.

By incorporating the recommended revisions, clarifying that no single factor is dispositive, recognizing a broader range of probative evidence, and confirming that the regulatory examples are illustrative rather than exhaustive, the regulations would better align with the intent of the statute while preserving its core objective of preventing improper base erosion.

These changes would provide taxpayers with meaningful guidance, reduce litigation risks, and promote fair, consistent, and predictable application of the law.

COST offers to work with the Department to revise the proposed regulations to ensure the regulations achieve the intended purpose without unduly burdening compliant taxpayers engaged in bona fide cross-border business activities.

Thank you for your consideration of this matter.

Respectfully,

Marilyn Wethekam

cc: Director Harris, Illinois Department of Revenue
Bridget DiBattista, General Counsel Illinois Department of Revenue
Kim Schultz Executive Director, Joint. Committee on Admin Rules
COST Board of Directors
Patrick J. Reynolds, COST President & Executive Director