Foreign Investment in Real Estate: Illinois

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WITH PRACTICAL LAW REAL ESTATE

A Q&A guide to foreign investment in commercial real estate in Illinois. This Q&A addresses state laws and customs that impact out-of-state domestic company investors and foreign (non-US) company investors. Federal, local, or municipal law may impose additional or different requirements. Answers to questions can be compared across a number of jurisdictions (see Foreign Investment in Real Estate: State Q&A Tool (*http://us.practicallaw.com/9-517-4024*)).

OUT-OF-STATE DOMESTIC COMPANY INVESTOR

1. Is state permission required for out-of-state domestic company investors to acquire real property?

State permission is not required for out-of-state domestic company investors to acquire or own real property in Illinois. Mere ownership of real property in Illinois does not constitute "transacting business" in the state. (805 Ill. Comp. Stat. 5/13.75.)

However, out-of-state domestic companies must get authority from the Illinois Secretary of State (ILSOS) to transact business in Illinois (805 Ill. Comp. Stat. 5/13.05). A company transacts business when it has regular, systematic, and continuous business contact in Illinois (see *Deluxe Ice Cream Co. v. R.C.H. Tool Corp.*, 726 F.2d 1209, 1212 (7th Cir. 1984)). While there is no statutory definition of "doing business" in Illinois, the Illinois Compiled Statutes provide a nonexclusive list of activities that do **not** constitute transacting business:

- Maintaining, defending, or settling any proceeding.
- Holding meetings of the board of directors or shareholders or carrying on other activities concerning internal corporate affairs.
- Maintaining bank accounts.
- Maintaining offices or agencies for the transfer, exchange, and registration of the corporation's own securities or maintaining trustees or depositaries concerning those securities.
- Selling through independent contractors.
- Soliciting or obtaining orders, whether by mail or through employees or agents or otherwise, if orders require acceptance outside Illinois before they become contracts.
- Owning, without more, real or personal property.
- Conducting an isolated transaction that is:
  - completed within 120 days; and
  - not one in a course of repeated transactions of a like nature.
- Having a corporate officer or director who is a resident of Illinois.

(805 Ill. Comp. Stat. 5/13.75.)

Most practitioners take the position that the leasing of real property as a landlord for any purpose, even occasional use, constitutes transacting business. Therefore, out-of-state owners of commercial property in Illinois typically must get authority to transact business from the ILSOS. To get authority to transact business in Illinois, the out-of-state domestic company must submit the following to the ILSOS:

- Two copies of the application for authority to transact business (Form BCA 13.15).
- A recent certified copy of the articles of incorporation and all amendments and mergers.
- All applicable fees and taxes.

(ILSOS, A Guide for Qualifying Foreign Corporations, p. 1 (July 2014).)

2. Are there any other state restrictions for out-of-state domestic investors purchasing real property or interests in entities which own real property?

Illinois statutes do not impose any special restrictions on out-of-state domestic investors who purchase real property located in Illinois or interests in entities that own real property located in Illinois. However, certain types of businesses with significant investments in real property (for example, mining, gaming, and health care) may be subject to separate and additional restrictions on investment based on their charters or regulatory frameworks.

3. Describe reporting requirements which relate solely to out-of-state domestic (direct and indirect) owners of real property, in relation to:

- Acquisition.
- Ownership.
- Disposition.

There are no special reporting requirements which relate solely to out-of-state domestic owners who acquire, own, or dispose of Illinois real property. The same rules that apply to in-state owners regarding the payment of Illinois transfer and income taxes apply equally to out-of-state owners.

ACQUISITION

Similar to in-state owners, out-of-state owners must:

- File local, county, and state real estate transfer declarations, as applicable.
- Pay local, county, and state transfer taxes, as applicable.

OWNERSHIP

Similar to in-state owners, out-of-state owners must estimate, report, and pay tax on income derived from Illinois real property.

DISPOSITION

Similar to in-state owners, out-of-state owners selling real property must report and pay taxes on their gains from sales of Illinois real property.

4. What are the seller's and purchaser's tax obligations when out-of-state domestic owned real property is transferred?

SELLER'S OBLIGATIONS

A seller's tax obligations when transferring out-of-state domestic-owned real property depend on whether the sale is considered a "bulk sale." The sale of the "major part" of the seller's real property located in Illinois constitutes a bulk sale. (35 Ill. Comp. Stat. 5/902.) (This should not be confused with a bulk sale under Article 6 of the Uniform Commercial Code.)

In a bulk sale, the seller or purchaser must, within ten days after the sale, file the following with the Chicago office of the Illinois Department of Revenue (IDOR):

- The notice of sale, purchase, or transfer of business assets (Form CBS-1).
- A copy of the sales contract.
- The financing agreement.

(35 Ill. Comp. Stat. 5/902(d).)

If the seller is found to owe unpaid taxes, the IDOR will issue a stop order, requiring the purchaser to withhold a portion of the sale consideration from closing to satisfy the tax obligation. If the seller does not owe unpaid taxes, the IDOR issues a clearance certificate. The parties' failure to comply with these requirements creates successor liability for the purchaser for the seller's unpaid taxes described in the stop order (Ill. Admin. Code tit. 86, § 130.1701).

Additionally, there may be similar city or county bulk sales requirements depending on where the real property is located. Out-of-state owners, whether foreign or domestic, should consult local counsel in connection with the sale of Illinois real property.

PURCHASER'S OBLIGATIONS

See Seller's Obligations.

5. What state taxes are levied solely on out-of-state domestic individuals or entities acquiring or transferring real property or ownership interests in entities that own real property?

Illinois levies no taxes solely on out-of-state domestic individuals or entities acquiring or transferring real property or ownership interests in entities that own real property.

Out-of-state domestic individuals and entities are subject to the same taxes, which apply to residents who buy, sell, and own property, for example:

- Transfer tax on the value of the property (35 Ill. Comp. Stat. 200/31-1 to 200/31-70).
- Income tax on the income and gains derived from the real property.

6. Are out-of-state domestic investors required to invest with a local partner? If not, is investment with a local partner advisable?

Out-of-state investors are not required to invest with a local partner. However, for many practical reasons, it is advantageous for an out-of-state investor to partner with a local firm, including knowledge of the local market, customs, and service providers and the ability to be physically present at the property on short notice.

7. Describe what investment vehicles out-of-state domestic investors typically use? For example, are preferred equity structures more common than outright ownership structures?

In Illinois, both out-of-state and in-state investors commonly use a limited liability company (LLC) structure to acquire real property. The choice of the state of formation for the LLC, however, typically depends on the preferences of the sponsor of the investment.

Outright ownership structures are very uncommon. Corporations are not commonly used because of income tax considerations.

FOREIGN (NON-US) COMPANY INVESTOR

8. Is state permission required for foreign investors to acquire real property?

State permission is not required for foreign investors to acquire or own real property in Illinois. While foreign companies "transacting business" in Illinois must get authority from the Illinois Secretary of State, mere ownership of real estate does not constitute transacting business (see Question 1).

In practice, it is extremely rare for investors to acquire Illinois real property through a foreign investment vehicle.

9. Are there any other state restrictions for foreign investors purchasing real property or interests in entities which own real property?

Illinois statutes do not impose any special restrictions on foreign investors purchasing real property located in Illinois or interests in entities owning real property located in Illinois.

10. Describe reporting requirements which relate solely to foreign (direct and indirect) owners of real property in relation to:

- Acquisition.
- Ownership.
- Disposition.

There are no special reporting requirements which relate solely to foreign owners who acquire, own, or dispose of Illinois real property.

ACQUISITION

Foreign owners of real property are subject to the same reporting requirements as out-of-state domestic owners of real property (see Question 3: Acquisition).

OWNERSHIP

Foreign owners of real property are subject to the same reporting requirements as out-of-state domestic owners of real property (see Question 3: Ownership).

DISPOSITION

Foreign owners selling real property are subject to the same reporting requirements as out-of-state domestic owners selling real property (see Question 3: Disposition).

11. What are the seller's and purchaser's tax obligations when foreign-owned real property is transferred?

SELLER'S OBLIGATIONS

The seller's tax obligations are the same for the transfer of foreign-owned real property as out-of-state domestic-owned real property (see Question 4: Seller's Obligations).

PURCHASER'S OBLIGATIONS

The purchaser's tax obligations are the same for the transfer of foreign-owned real property as out-of-state domestic-owned real property (see Question 4: Purchaser's Obligations).

12. What state taxes are levied solely on foreign individuals or entities acquiring or transferring real property or ownership interests in entities that own real property?

Illinois levies no taxes solely on foreign individuals or entities acquiring or transferring real property or ownership interests in entities owning real property.

Foreign individuals and entities are subject to the same taxes that apply to residents who buy, sell, and own real property (see Question 5).

13. Are foreign investors required to invest with a local partner? If not, is investment with a local partner advisable?

Foreign investors are not required to invest with a local partner. However, for many practical reasons, it is advantageous for a foreign investor to partner with a local firm (see Question 6).

14. Describe what investment vehicles foreign investors typically use? For example, are preferred equity structures more common than outright ownership structures?

Foreign investors typically use the same investment vehicles as out-of-state domestic investors (see Question 7).