

Information regarding sales tax liabilities in lease situations may be found at 86 Ill. Adm. Code 130.220 and 86 Ill. Adm. Code 130.2010. (This is a GIL.)

March 31, 2010

Dear Xxxxx:

This letter is in response to your letter dated January 20, 2010, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

We have been referred to your Department by a taxpayer services representative that we reached by calling the taxpayer services phone number on the State website.

We are researching the sales tax implications of a wholesaler that either rents or leases (via a financing lease) tax exempt manufacturing equipment to customers in Illinois. This wholesaler is a Virginia based company that sells food packaging manufacturing equipment directly to manufacturers in your state. Please advise regarding how renting or leasing of this equipment may impact the tax exempt status. Please provide a copy of the State Regulation that supports your advice or kindly direct us to a web-based source for this information.

DEPARTMENT'S RESPONSE:

Although we cannot give you a specific answer in the form of a General Information Letter, we hope you find the following helpful. The State of Illinois taxes leases differently for Retailers' Occupation Tax and Use Tax purposes than the majority of other states. For Illinois sales tax purposes, there are two types of leasing situations: conditional sales and true leases.

A conditional sale is usually characterized by a nominal or one dollar purchase option at the close of the lease term. Stated otherwise, if a lessor is guaranteed at the time of the lease that the leased property will be sold, this transaction is considered to be a conditional sale at the outset of the transaction. Persons who purchase items for resale under conditional sales contracts can avoid

paying tax to suppliers by providing certificates of resale that contain all the information set forth in 86 Ill. Adm. Code 130.1405. All receipts received by a lessor/retailer under a conditional sales contract are subject to Retailers' Occupation Tax. See 86 Ill. Adm. Code 130.2010.

A true lease generally has no buy out provision at the close of the lease. If a buy-out provision does exist, it must be a fair market value buy-out option in order to maintain the character of the true lease. Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See 86 Ill. Adm. Code 130.220. As end users of tangible personal property located in Illinois, lessors owe Use Tax on their cost price of such property.

The State of Illinois imposes no tax on rental receipts. Consequently, lessees incur no tax liability. As stated above, in the case of a true lease, the lessors of the property being used in Illinois would be the parties with Use Tax obligations. The lessors would either pay their suppliers, if their suppliers were registered to collect Use Tax, or would self-assess and remit the tax to the Department. If the lessors already paid taxes in another state with respect to the acquisition of the tangible personal property, they would be exempt from Use Tax to the extent of the amount of such tax properly due and paid in such other state. See subsection (a)(3) of 86 Ill. Adm. Code 150.310.

Under Illinois law, lessors may not "pass through" their tax obligation to the lessees as taxes. However, lessors and lessees may make private contractual arrangements for a reimbursement of the tax to be paid by the lessees. If lessors and lessees have made private agreements where the lessees agree to reimburse the lessors for the amount of the tax paid, then the lessees are obligated to fulfill the terms of the private contractual agreements.

Under the Retailers' Occupation Tax Act and the Use Tax Act, machinery and equipment that will be used primarily in the process of manufacturing or assembling tangible personal property for wholesale or retail sale or lease is exempt from tax. 35 ILCS 120/2-10(14); 105 ILCS 3-5(1). For this exemption to apply, the purchaser need not itself employ the exempt machinery or equipment in manufacturing. If the purchaser leases that machinery or equipment to a lessee-manufacturer who uses it in an exempt manner, the sale to the purchaser-lessor will be exempt from tax. A supplier may exclude these sales from its taxable gross receipts provided the purchaser-lessor provides to the supplier a properly completed exemption certificate. For the requirements for an exemption certificate, see 86 Ill. Adm. Code at 130.330(g) and the Department's Form ST-587. An exemption certificate is sufficient as long as the information required by the rule is contained in the certificate. Note, however, should the purchaser-lessor lease the machinery or equipment to a lessee who does not use it in a manner that would qualify directly for the exemption, the purchaser-lessor will become liable for the tax from which he was previously exempted. 86 Ill. Adm. Code 130.330(f).

You can find further information on the Department's website listed below along with copies of prior letter rulings and administrative rules.

I hope this information is helpful. If you require additional information, please visit our website at www.tax.illinois.gov or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Debra M. Boggess
Associate Counsel

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