

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.)

December 10, 2010

Dear Xxxxx:

This letter is in response to your letter dated April 14, 2010, in which you request a Private Letter Ruling. 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:

ABC is requesting a private letter ruling on the below described issues. The parties involved are identified as follows – ABC as Lessor and XYZ as lessee.

Issues

- Is the Lease Intended as Security (LIS) transaction described below considered by the State to be a Conditional Sale, per General Information Letter ST 99-0169-GIL or is it viewed as a debt financing?
- If Lessee (XYZ) has paid sales tax to vendors on their initial purchase, is Lessor (ABC) required to charge and remit tax again on the LIS transaction?
- Alternatively, if the Lessor (ABC) is required to pay tax on the transaction, would the Lessee be entitled to any refund of tax paid to the vendor on the initial purchase?

Statement of Facts

ABC is an equipment financing and leasing company with IL account number #. ABC has a Master Lease Agreement in place with XYZ. ABC entered into a forty-two month (42) Lease Intended as Security (LIS Schedule 003) of computer equipment with XYZ, which purchased the equipment and simultaneously entered into the LIS Schedule 003 transaction with ABC. The Vendor invoices were issued in the name of Lessee, XYZ, and included tax. The equipment is used by XYZ at its CITY, Illinois location.

The lease is referred to as a Lease Intended as Security (LIS) with an end of term **required** purchase for one (\$1) dollar. See the enclosed Schedule Number 003 at ¶8 for specific language to this effect. This is not an optional purchase but rather a 'PUT' or required purchase upon termination. Additionally, any right, title or interest of Lessor in and to the equipment is held for collateral security purposes only, as specified in ¶6 of the same Schedule 003.

Enclosed Documents

- Master Lease Agreement Number #
- Schedule Number 003 (Lease Intended as Security) to Master Lease Agreement

The above issues are not the subject in an audit or being litigated by ABC with the Department. To the best of our knowledge, the Department has not previously ruled on the same or similar issues for ABC or a predecessor nor has ABC previously submitted the same or similar issues to the Department but withdrew it before a letter ruling was issued.

Please consider all exhibits as *trade secret information and/or confidential* material. ABC requests that certain information be deleted prior to dissemination to others. ABC requests that its name, the name of Lessee, address, the location of its facilities and telephone numbers be deleted.

We respectfully request a private letter ruling on our issues. Should you have questions or require additional information, please contact me as shown below. Thank you for your time.

DEPARTMENT'S RESPONSE:

The Department's regulation "Public Information, Rulemaking and Organization" provides that "[w]hether to issue a private letter ruling in response to a letter ruling request is within the discretion of the Department. The Department will respond to all requests for private letter rulings either by issuance of a ruling or by a letter explaining that the request for ruling will not be honored." 2 Ill. Adm. Code 1200.110(a)(4). The Department has decided to respond with a GIL.

Based on the documents attached to your letter, it is unclear whether the situation you describe in your letter amounts to a conditional sale, a sale/leaseback situation, or is simply a financing arrangement that provides for a security interest in the equipment in order to obtain a loan for the equipment. Specifically, the Master Lease Agreement appears to transfer whatever right, title and interest (ownership) the Lessee has in the equipment to the Lessor. The Schedule attached to the Master Lease, however, appears to provide that it is the intent of the parties for the lease to be construed only as a security interest in the personal property in favor of the Lessor. Nonetheless, 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 lessors are 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, thus making all receipts subject to Retailers' Occupation Tax. 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.

In contrast, a true lease generally has no buy out provision at the close of the lease. If a buyout 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.

The above guidelines are applicable to all true leases of tangible personal property in Illinois except for automobiles leased under terms of one year or less, which are subject to the Automobile Renting Occupation and Use Tax found at 35 ILCS 155/1 et seq.

If the contract involved is a true lease, the lessee is not subject to Retailers' Occupation Tax or Use Tax on the lease of a vehicle for more than one year. As a result, the lessee is not subject to sales tax liability for any related lease charges such as late charges, vehicle disposal fees, excess wear and tear fees and excessive mileage fees imposed at the end of the lease are not subject to tax.

If the transaction is a conditional sale, please see 86 Ill. Adm. Code 130.420 and 130.410, the Department's rules regarding finance charges, penalties, discounts, and costs of doing business.

However, if the transaction from the Lessee to the Lessor is a sale, it may involve a sale/leaseback transaction. In a general sale/leaseback transaction, the Lessee would purchase an item for resale and sell it to the Lessor who then leases the item back to the Lessee under a true lease, and the Lessor would not incur Retailers' Occupation Tax on the lease payments. Note, sale/leaseback transactions do not generally involve conditional sales. However, if a sale/leaseback transaction involves a conditional sale, then the Lessee would purchase the item for resale and give the vendor a resale certificate. When the Lessor purchases the item from the Lessee, the Lessor would give the Lessee a retail certificate because at the time of the purchase, the Lessor knows he will be selling the item back to the Lessee and, thus, the Lessor would owe Retailers' Occupation Tax on its gross receipts from the sale of the item back to the Lessee

The resale exemption is applicable when making sales to a purchaser who will in turn sell the tangible personal property. For general information regarding resale certificates, the Department's regulation for resale certificates, "Seller's Responsibility to Obtain Certificates of Resale and Requirements for Certificates of Resale," is found at 86 Ill. Adm. Code 130.1405.

If the transaction is neither a true lease or a conditional sale involving a sale/leaseback situation, but, instead, is simply a transaction involving a debt financing instrument and no ownership transfers from the Lessee to the Lessor, then generally no tax liability exists on that transaction. In those situations, the Lessee normally purchases the equipment from the vendor, pays tax on the purchase price, and obtains title to the property. The Lessor obtains a first priority security interest in the property as a condition of making the lease/loan to the Lessee.

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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