

This letter responds to a questionnaire. See 86 Ill. Adm. Code, Parts 130, 150, and 270. (This is a GIL.)

January 6, 2012

Dear Xxxxx:

This letter is in response to your e-mail April 24, 2011, 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. Attached to your e-mail was a survey asking several questions as follows:

Your email stated as follows:

As you may know, on September 14, 2010, the U.S. Department of Treasury and the Internal Revenue Service (IRS) issued proposed regulations dealing with ‘series’ entities such as series limited liability companies (Series LLCs), series business or ‘statutory’ trusts, and segregated portfolio companies. The Proposed Series LLC Regulations request comments from interested parties, and the IRS has specifically requested comments from the ASSOCIATION.

Attached, please find a questionnaire that is part of the ASSOCIATION Task Force’s effort to inform the IRS as to whether or to what extent the states plan to conform with its proposed tax classification of series within a Series LLC and also to educate our members and taxpayers generally. We appreciate your assistance and participation in this project – please feel free to forward this survey to the appropriate persons within the Illinois Department of Revenue.

Many thanks,

Your survey states as follows:

QUESTIONS TO STATE DEPARTMENTS OF REVENUE/FINANCE REGARDING THEIR INTENT TO CONFORM WITH THE CLASSIFICATION OF SERIES LLCs AS DISCUSSED IN TREASURY DEPARTMENT/IRS PROPOSED REGULATIONS

ASSOCIATION SECTION OF TAXATION COMMITTEE ON STATE AND LOCAL TAXATION TASK FORCE ON PROPOSED SERIES LLCs REGULATIONS

March 2011

As you may know, on September 14, 2010, the U.S. Department of Treasury and the Internal Revenue Service (IRS) issued proposed regulations dealing with 'series' entities such as series limited liability companies (Series LLCs), series business or 'statutory' trusts, and segregated portfolio companies. A copy of those regulations is attached for your reference (herein called the 'Proposed Series LLC Regulations'). Generally, the Proposed Series LLC Regulations classify each series within a Series LLC as a separate entity, which can then make the same tax elections as a regular LLC itself, e.g., to be classified as a partnership (if it has more than one member), to be disregarded (if it has only one member), or to be taxed as a 'C' or 'S' corporation. Under these Proposed Series LLC Regulations, the Series LLC itself (as opposed to the series within the Series LLC) is considered a separate tax reporting unit independent of the various series within it, but is not required to file a federal income tax return (partnership return) unless it has its own income, deductions or credits (independent of that of the series within it) in any given taxable year.

The Proposed Series LLC Regulations govern only federal income tax issues; they expressly reserve a determination as to the federal (and state) employment tax issues. The Proposed Series LLC Regulations request comments from interested parties, and the IRS has specifically requested comments from the ASSOCIATION. To that end, a joint Task Force was recently formed at the request of the Chair of the Section, and this questionnaire to the states is part of the Task Force's effort to inform the IRS as to whether or to what extent the states plan to conform with its proposed tax classification of series within a Series LLC and also to educate our members and taxpayers generally. For convenience, we have aggregated each form of series entities into the term 'Series LLC' in the questions below. In the event your state differentiates between some of the series forms with respect to one or more of the below taxes, please complete a questionnaire for each differentiated form of series entities.

Each of the following questions are designed to be answered Yes, No, Not Applicable (NA) or Not Yet Determined (ND) by checking the appropriate box. However, we encourage any additional comments or observations you wish to make and therefore encourage you to provide supplemental information referring to the specific question(s) by number.

Questions on Sales/Use Taxes:

16. Does your state levy a 'traditional' sales and use tax on tangible or mixed tangible/intangible personal property? **If not, please skip to Question 19 below.**
Y N NA ND
17. For purposes of its sales and use tax, will your state conform to the Proposed Series LLC Regulations by classifying each series as a separate reporting unit that can make its own sales and use tax elections?

Y N NA ND

- a. If so, will you treat transfers of taxable property between two series or between a series and the Series LLC itself as a potential taxable transaction, unless there is a generally applicable exemption, e.g., wholesale sale or occasional sale?
Y N NA ND
- b. If so, will you treat the nexus-creating activities in your state of one series to be attributed to:
- i. Another series? Y N NA ND
- ii. The Series LLC itself? Y N NA ND
- c. If so, will you treat the nexus-creating activities in your state of the Series LLC itself (independent of activities of any of the series within the Series LLC) to be attributed to each series within the Series LLC?
Y N NA ND
18. For purposes of its sales and use tax, if your state does not conform to the Proposed Series LLC Regulations and treat the Series LLC and each series therein as a single sales and use tax reporting entity, will you treat transfers of taxable property between two series or between a series and the series LLC itself as a potential taxable transaction, unless there is a generally applicable exemption, e.g., wholesale sale or occasional sale? Y N NA ND

Questions Concerning Rental/Lease Taxes:

19. Does your state levy a sales tax or separate rental tax on leases of tangible personal property ('TPP')? **If not, please skip to the conclusion below.**
Y N NA ND
20. Will your state treat each series as a separate reporting entity for purpose of the TPP leasing tax as opposed to the Series LLC itself?
Y N NA ND
- a. If so, will your state impose its sales or rental tax on leases of TPP between two series? Y N NA ND
- b. If so, will the answer differ if the lease is between the Series LLC itself and one of its series? Y N NA ND
- c. If so, will the TPP leasing actions of one series in your state be imputed to the other series of the Series LLC or to the Series LLC itself?
Y N NA ND
- d. If so, will the TPP leasing actions of the Series LLC itself be imputed to each of the series of the Series LLC?
Y N NA ND
- e. If not, will your state disregard rentals between or among the various series of the Series LLC? Y N NA ND

- f. If not, will your state disregard rentals between a series of the Series LLC and the Series LLC itself? Y N NA ND
21. If your state does not treat each series as a separate reporting entity for purposes of the TPP leasing tax, will the Series LLC be the reporting entity even if it has no activity in the state? Y N NA ND
22. If your state treats each series as a separate reporting entity for purposes of the TPP leasing tax, will the Series LLC itself be required to file a return if the Series LLC itself (independent of the series) does not have leasing activity in the state? Y N NA ND

Conclusion:

We thank you for your response to this questionnaire. Is there a specific person to whom should we direct any future questions?

Please send your completed questionnaire and should you have any questions concerning this questionnaire please direct them to:

NAME/ADDRESS

DEPARTMENT'S RESPONSE:

We apologize for the delay in our response. We note that the survey asked questions regarding Income Tax, as well as Sales and Use Taxes, and Rental and Lease Taxes. This response does not address any questions concerning Income Tax; those questions were addressed by the Department's Income Tax Division. The Department does not respond to specific questions in General Information Letters. In any event, though, the questions in the survey cannot be properly answered by checking yes or no without further explanation. Therefore, in lieu of providing you a response to your survey in the format requested, we hope you will find the following general information helpful. Note, there may be some areas where the answers we provide in the Sales and Use Tax area may vary from those provided in the Income Tax area. Under our State Sales and Use Tax laws, we look at transactions between legal entities regardless of how those entities are treated for federal income tax purposes.

Sales Tax

The Illinois Retailers' Occupation Tax Act imposes a tax upon persons engaged in this State in the business of selling tangible personal property to purchasers for use or consumption. See 86 Ill. Adm. Code 130.101. In Illinois, Use Tax is imposed on the privilege of using, in this State, any kind of tangible personal property that is purchased anywhere at retail from a retailer. See 86 Ill. Adm. Code 150.101. These taxes comprise what is commonly known as "sales" tax in Illinois. If the purchases occur in Illinois, the purchasers must pay Use Tax to the retailer at the time of purchase. The retailers are then allowed to retain the amount of Use Tax paid to reimburse themselves for the Retailers' Occupation Tax liability incurred on those sales. Note, generally when one legal entity makes a retail sale to another legal entity, the tax base for Retailers' Occupation Tax purposes is the selling price of the property. See the case of The Superior Coal Company v. The Department of Finance, 377 Ill. 282 (1941). This case held that a sale of coal by a subsidiary coal company to its parent railway corporation was subject to Retailers' Occupation Tax.

Nexus

An “Illinois Retailer” is one who either accepts purchase orders in the State of Illinois or maintains an inventory in Illinois and fills Illinois orders from that inventory. The Illinois Retailer is then liable for Retailers' Occupation Tax on gross receipts from sales and must collect the corresponding Use Tax incurred by the purchasers.

Another type of retailer is the retailer maintaining a place of business in Illinois. The definition of a “retailer maintaining a place of business in Illinois” is described in 86 Ill. Adm. Code 150.201(i). This type of retailer is required to register with the State as an Illinois Use Tax collector. See 86 Ill. Adm. Code 150.801. The retailer must collect and remit Use Tax to the State on behalf of the retailer’s Illinois customers even though the retailer does not incur any Retailers' Occupation Tax liability.

The United States Supreme Court in *Quill Corp. v. North Dakota*, 112 S.Ct. 1904 (1992), set forth the current guidelines for determining what nexus requirements must be met before a person is properly subject to a state's tax laws. The Supreme Court has set out a 2-prong test for nexus. The first prong is whether the Due Process Clause is satisfied. Due process will be satisfied if the person or entity purposely avails itself or himself of the benefits of an economic market in a forum state. *Quill* at 1910. The second prong of the Supreme Court's nexus test requires that, if due process requirements have been satisfied, the person or entity must have physical presence in the forum state to satisfy the Commerce Clause.

A physical presence is not limited to an office or other physical building. Under Illinois law, it also includes the presence of any agent or representative of the seller. The representative need not be a sales representative. Any type of physical presence in the State of Illinois, including the vendor’s delivery and installation of his product on a repetitive basis, will trigger Use Tax collection responsibilities. Please refer to *Brown’s Furniture, Inc. v. Zehnder*, 171 Ill.2d 410 (1996).

The final type of retailer is the out-of-State retailer that does not have sufficient nexus with Illinois to be required to submit to Illinois tax laws. A retailer in this situation does not incur Retailers’ Occupation Tax on sales into Illinois and is not required to collect Use Tax on behalf of its Illinois customers. However, the retailer’s Illinois customers will still incur Use Tax liability on the purchase of the goods and have a duty to self-assess and remit their Use Tax liability directly to the State.

Finally, in general, the imposition of the various local sales taxes in Illinois is triggered when “selling” occurs in a jurisdiction imposing a tax. The Department’s opinion is that the most important element of selling is the seller’s acceptance of the purchase order. Consequently, if a purchase order is accepted in a jurisdiction that imposes a local tax, that tax will be incurred. See 86 Ill. Adm. Code 270.115(b), which can be found on the Department’s website. The tax rate is fixed by the location of the seller, not the delivery location. The fact that the item being sold is shipped from out-of-State or from another Illinois location is immaterial for purposes of local taxes if the sale occurs through order acceptance in an Illinois jurisdiction imposing a local tax. For these transactions, the local tax will be incurred.

Rentals and Leases

The renting of a motor vehicle for a period of one year or less is subject to the Automobile Renting Occupation and Use Tax Act at the rate of 5%. See 35 ILCS 155/1 et seq. If a person rents motor vehicles of the second division that are of the van configuration designed for the transportation

of not less than 7 nor more than 16 passengers, as defined in Section 1-146 of the Illinois Vehicle Code, then that person is subject to the Automobile Renting Occupation and Use Tax Act.

With respect to the rental of items other than motor vehicles for any period of time and the rental of motor vehicles for a period greater than one year, 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.

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

DMB:msk