

ST 15-0018 GIL 03/18/2015 LEASING

Except as provided in 86 Ill. Adm. Code 130.2011 and 130.2012, lessors incur Use Tax even if the tangible personal property is leased to an exempt entity that has been issued an exemption identification number. See 86 Ill. Adm. Code 130.2011 and 130.2012.
(This is a GIL.)

March 18, 2015

Dear XXXX:

This letter is in response to your letter dated January 29, 2015, 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:

COMPANY (lessor) has entered a FMV lease agreement with Foundation (lessee), a tax exempt charitable organization [exemption letter attached]. It is our understanding, as described in ST 09-0109-GIL, that the Lessee’s charitable organization exemption does not pass through to the Lessor and that the Lessor owes Use Tax on the cost price of the leased assets.

COMPANY understands that under Illinois law, that while lessors may not pass through their tax obligation to the lessees as taxes, 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 lessees agree to reimburse lessors for the amount of the tax paid, then lessees are obligated to fulfill the terms of the private contractual agreements.

The lease agreement between COMPANY and Foundation stipulates that the lessee is to reimburse the lessor for the amount of tax paid. [See section 4. 'Taxes' on the attached the Master Lease Agreement].

The lessee believes that due to their Charitable Organization exemption status they are not liable to reimburse the lessor for the amount of tax paid per the lease agreement.

Please provide a letter ruling on the following:

- a) Whether the Lessee's charitable exemption status passes through to the lessor.
- b) If the Lessee's charitable exemption status precludes the Lessor from pursuing reimbursement by the lessee of tax paid.

Thank you for your time and assistance. If additional information is needed, please contact me at the phone number or email address that is provided below.

DEPARTMENT'S RESPONSE:

Organizations that make application to the Department and are determined to be exclusively religious, educational, or charitable, receive an exemption identification "E" number. See 86 Ill. Adm. Code 130.2007. This number evidences that this State recognizes that the organization qualifies as exempt from incurring Use Tax when purchasing tangible personal property in furtherance of its organizational purpose. An organization must provide a retailer with its "E" number to document the exemption. If an organization or governmental body does not have an "E" number, then its purchases from a company are subject to tax. Only sales to the organization or governmental body holding the "E" number are exempt, not sales to individual members of the organization. The Retailers' Occupation Tax does not apply to receipts from sales to organizations holding a valid "E" number.

For general information purposes please refer to 86 Ill. Adm. Code 130.2010, the Department's regulation that covers the taxation of leases. Under Illinois law, "true leases" and "leases" that are actually conditional sales contracts are treated differently for Retailers' Occupation Tax and Use Tax purposes. Please note that 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 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.

If a purchaser under these transactions had a valid exemption identification “E” number, no tax would be due.

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.

Even though under Illinois law, lessors may not “pass through” their tax obligation to the lessees as taxes, 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 lessees agree to reimburse lessors for the amount of the tax paid, then lessees are obligated to fulfill the terms of the private contractual agreements. The Department, however, is not a party to those agreements, as those are agreements between the lessor and lessee. If the lessee fails to fulfill its obligation under this separate agreement, then the breach of that agreement would be between the lessor and the lessee.

Generally, the tax exempt status of lessees does not affect the tax liability of lessors. However, please note that Illinois does have an exemption for certain purchases of tangible personal property by persons who are leasing that property to exempt hospitals that have been issued an “E” number by the Department. See the Department’s regulation at 86 Ill. Adm. Code 130.2011. This exemption applies to sales of two different types of tangible personal property. The first is computers and communications equipment utilized for any hospital purpose. The second is sales of equipment that are used in the diagnosis, analysis, or treatment of hospital patients.

To qualify for this exemption:

- (1) the qualifying equipment must all be purchased for lease to a tax exempt hospital under a lease that has been executed or is in effect at the time of purchase;
- (2) the lease must be for a period of one year or longer; and
- (3) the lease must be to a hospital that has an active tax exemption identification number issued by the Department under Section 1g of the Retailers' Occupation Tax Act.

The rule does not preclude a lessor from claiming the exemption where the lessor leases the qualifying equipment to a lessee who subleases it to a hospital, as long as all the relevant leases have been executed or are in effect at the time of the purchase and all other criteria in Section 130.2011 have been met. 86 Ill. Adm. Code 130.2011.

Except as provided in the limited exceptions set out in Section 130.2011 and 130.2012, lessors who execute true leases with lessees that have E-numbers owe Use Tax on their cost price of the rental property. The Use Tax liability remains on the lessor notwithstanding the status of the lessee. See Continental Illinois Leasing Corp. v. Department of Revenue, 108 Ill. App. 3d 583 (1st Dist., 1982).

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

DB:kd