

This letter discusses the application of the sales tax laws to true lease and conditional sale situations. See 86 Ill. Adm. Code 130.220. (This is a GIL.)

February 28, 2008

Dear Xxxxx:

This letter is in response to your letter dated February 7, 2007, 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:

I work for a California software company that tracks banking and taxing information for the automobile industry. Any assistance in acquiring state taxation information regarding automobile leases and purchases will be greatly appreciated. Below is a short questionnaire.

1. Current state sales tax percentage.
2. Is this the same for purchase and lease?
3. Are there any local city or county taxes charged?
4. For a lease, is the sales tax based on the amount of monthly payments or selling price or adjusted selling price? (selling price + negative equity + any inception fees = adjusted selling price)
5. When leasing, is a leased trade-in or a purchased trade-in taxable?
6. In question 5 is there a credit for trade-in allowance?
7. Is this the same for a balloon? (balloon is a hybrid lease/purchase where it is lower payments like lease, but has a large final balloon payment)

8. When purchasing, is a leased trade-in or a purchased trade-in taxable?
9. For lease or purchase, is negative equity added to selling price for sales tax calculation or is it exempt? (\$5000 trade-in allowance - \$7000 loan payoff = \$2000 negative equity)
10. For lease or purchase, is cash or manufacture rebate used as down payment taxable?
11. For lease or purchase, is manufacture rebate used to pay inception fees subject to tax?
12. For lease or purchase, are dealer documentation fees and/or bank acquisition fee taxable?
13. For lease and purchase, are extended warranties taxable?
14. Is there a sales tax on registration fee?
15. Is there a personal property tax on motor vehicles?
16. Are there any other sales tax calculations that apply to leases that has [sic] not been addressed?
17. Are there any other sales tax calculations that apply to purchases that has [sic] not been addressed?
18. Are there any other sales tax calculations that apply to balloons that has [sic] not been addressed?

Thank you for any assistance.

DEPARTMENT'S RESPONSE:

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. The tax is based on the amount of gross receipts received by the retailer on the sale of that property. "Gross receipts" means all the consideration actually received by the seller, except traded-in tangible personal property. See 86 Ill. Adm. Code 130.401.

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. For general information related to conditional sales, please refer to 86 Ill. Adm. Code 130.2010. 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 (6.25%) and local occupation taxes, if any. For items that are required to be titled and registered with an agency of this State's government, the entire amount of tax is due "up-front" before the item can be titled or registered. To determine if a local occupation tax is incurred on a sale

in a county or municipality, please see ST-25 Sales Tax Rate Reference Manuel on the Department's Internet website under the heading "Publications."

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 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 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 a retailer allows a purchaser a discount from the selling price on the basis of a discount coupon for which the retailer receives no reimbursement from any source, the amount of such discount is not subject to Retailers' Occupation Tax liability. See 86 Ill. Adm. Code 130.2125. If a retailer allows a purchaser a discount from the selling price on the basis of a discount coupon for which the retailer will receive full or partial reimbursement (from a manufacturer, distributor or other source), the retailer incurs Retailers' Occupation Tax liability on the receipts received from the purchaser and the amount of any coupon reimbursement.

When an item of tangible personal property such as a car is sold at retail, an express warranty from the manufacturer is often included in the selling price. This express warranty obligates the manufacturer to correct defects in materials and workmanship during a specified timeframe. When repairs are made under the terms of an express warranty, no tax is due and this is true whether the manufacturer makes the repairs or whether the manufacturer pays someone else to make the repairs. This is because the warranty (and any tangible personal property transferred under the warranty) was included as part of the retail selling price of the item and, as such, was subject to Retailers' Occupation Tax and Use Tax when the item was sold at retail. See subsection (b) of 86 Ill. Adm. Code 140.141.

Extended warranties (optional warranties) are contracts to provide repairs for a particular item for a stated period of time after a manufacturer's express warranty has expired. An extended warranty that is not included in the selling price of the item covered by the extended warranty is not subject to Retailers' Occupation Tax and Use Tax liability when the item is sold at retail. However, tangible personal property transferred incident to the completion of an extended warranty or maintenance agreement will result in Use Tax liability by the serviceman based on the cost price of that tangible personal property. See 86 Ill. Adm. Code 140.301(b)(3) and 86 Ill. Adm. Code 140.141(c).

For an explanation of trade-in allowances, see 86 Ill. Adm. Code 130.455. For an explanation of costs of business which are not excludable from gross receipts, see 86 Ill. Adm. Code 130.410.

In January 2008 the Department posted the revised and updated Illinois Aircraft/Watercraft and Vehicle Tax Information Guide, ST-76, on its website. This Guide is very helpful and addresses many of your questions.

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. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Very truly yours,

Richard S. Wolters
Associate Counsel

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