ST 17-0001-GIL 1/10/2017 PENALTIES:

This letter discusses application of the $100 Uniform Penalty and Interest Act penalty for failure to file zero liability transaction reporting returns (e.g. ST-556 and ST-556-LSE). See 35 ILCS 735/3-3(a-15) and 35 ILCS 120/3. (This is a GIL.)

January 10, 2017

Re: General Information Letter

Dear Xxxxx:

This letter is in response to your letter dated January 3, 2017, in which you requested 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:

> As counsel for and on behalf of a certain unnamed Taxpayer, we hereby submit this General Information Letter pursuant to 2 Ill. Admin. Code §1200.110 requesting confirmation from the Illinois Department of Revenue ("Department") that neither an original motor vehicle manufacturer, a captive finance company for an original motor vehicle manufacturer, nor a vehicle leasing trust are a "retailer" of motor vehicles because all of their sales of motor vehicles are for resale and, as a result, they are not required to file Illinois ST-556 tax returns.
>
> **FACTS**
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> The taxpayer has three distinct legal entities that are relevant to this request: 1) a manufacturer of motor vehicles ("Manufacturer"); 2) a captive finance company ("Finance Company"); and 3) a vehicle leasing trust ("Trust").
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> **Manufacturer**

Manufacturer is in the business of manufacturing various styles of passenger motor vehicles. Manufacturer is registered for both Illinois Retailers' Occupation Tax ("ROT") and Illinois Automobile Renting and Occupation Tax (35 ILCS 155/1, et seq.) ("AROT").

Manufacturer sells brand new motor vehicles to Illinois dealers for resale or re-lease. Manufacturer does not sell motor vehicles at retail to any consumers and it is therefore not registered as an Illinois motor vehicle dealer. In certain limited circumstances, Manufacturer leases motor vehicles to company employees. In such instances, Manufacturer remits applicable AROT. Additionally, Manufacturer publishes and sells informational bulletins and pamphlets providing details of its vehicles. Manufacturer sells such materials directly to Illinois dealers for use in showrooms ("Bulletins"). Manufacturer also sells handheld tools to Illinois dealers for use in servicing Taxpayer branded motor vehicles. In both instances where Manufacturer makes retail sales of tangible personal property other than motor vehicles, Manufacturer files ROT returns (ST-1) and remits applicable ROT. Manufacturer's sales of Bulletins and handheld tools make up less than 0.5% of its total Illinois sales.

Finance Company

Finance Company is a captive finance company and a part of Taxpayer's financial services branch, which provides vehicle financing options for the purchase and lease of motor vehicles by end users. Finance Company has Illinois employees and it also owns real property in the form of dealer signs that it leases to Taxpayer dealerships located in Illinois. The signs are treated as real property under Illinois law.

In a typical vehicle lease transaction, a customer leases a Taxpayer branded motor vehicle from an authorized dealership. The lease terms are generally three to five years. The lease agreement is entered into between the customer and the dealership. The dealership then assigns the lease to Finance Company who becomes the owner and lessor of the motor vehicle. Finance Company also leases forklifts to end users in Illinois. Finance Company offers both operating leases and finance leases to Illinois customers.

Finance Company never sells a vehicle to an end user for final use or consumption and it is therefore not registered as an Illinois motor vehicle dealer. Finance Company is registered for both ROT and AROT but it has no ROT or AROT tax liability and therefore files zero returns.

Trust

Trust, another part of Taxpayer's financial services branch, is a titling trust that owns leased vehicles for purposes of asset backed transactions. Trust has no employees in Illinois or anywhere. Like Finance Company, Trust never sells a motor vehicle to an end user. It strictly leases to a consumer, and in instances where it does sell a motor vehicle, it sells to dealerships or auctioneers for subsequent resale.

Trust owns the vehicles that are leased through Taxpayer's rental car program and courtesy car program to dealers for re-lease to the dealers' customers. Trust is registered for ROT and AROT and it files ROT and AROT returns but because it has no ROT or AROT tax liability, it files zero returns.

At the conclusion of a lease, Finance Company and Trust dispose of their motor vehicles in one of four ways:

1) Off-lease Sale to Dealership for resale to Lessee

Every time Finance Company or Trust make a sale of an off-lease motor vehicle, the vehicle is always sold to a party for a subsequent resale. Neither Finance company nor Trust ever sell a vehicle to an end user. For example, if a customer would like to purchase his or her vehicle at the end of the lease term, he or she would notify the dealer of the intention to do so. The dealership then purchases the vehicle in "RPM"[1] on behalf of the customer from Trust or Finance Company for subsequent resale to the customer. The respective entity, Finance Company or Trust, sends the title directly to the purchasing customer. However, the actual retail sale is from the dealership to the customer. Finance Company and Trust obtain a valid resale certificate from the purchasing dealership.

2) Off-lease sale to Dealership for Placement in Used Car Inventory

At the conclusion of a customer lease, if the lessee does not purchase the off-lease vehicle, the dealership that originated the lease has the option to purchase the vehicle from Finance Company or Trust for placement in its used car inventory for resale. In this scenario, the dealership purchases the vehicle directly from the Finance Company or Trust. Finance Company or Trust obtains a for [sic] valid resale certificate from the purchasing dealership.

3) Off-lease sale to Dealer Lot

At the conclusion of a customer lease, if neither the customer nor the dealership that originated the lease purchases the off-lease vehicle, the vehicle will be placed in "RPM" where other dealerships have the option to purchase the vehicle for a limited time. If a dealership chooses to purchase the vehicle, Finance Company/Trust will sell the vehicle to the dealership for subsequent resale. Finance Company or Trust obtains a valid resale certificate from the purchasing dealership.

4) Off-lease sale to Auction House

If neither the customer nor the dealership that originated the lease nor any other dealership chooses to purchase the off-lease vehicle, then the vehicle will be sent to

[1] Additional information provided to the Department indicates that this is the name of the Taxpayer's internal system in which they list motor vehicles that have been turned in from a lease. Dealers have the opportunity to purchase these vehicles before they go to auction.

auction for resale. The auction house has a POA on behalf of Finance Company or Trust. All vehicles sold at auction are for subsequent resale.

In short, under the four scenarios identified above, all motor vehicles sold by Manufacturer, Finance Company and Trust are nontaxable sales for subsequent resale. Neither Manufacturer, Finance Company nor Trust ever sell a motor vehicle to an end user for consumption or use. The three entities sell approximately ## – ## motor vehicles for resale in Illinois per year.

ILLINOIS LAW

Section 3 of the Illinois ROT Act (35 ILCS 120/3) provides that, "with respect to motor vehicles… that are required to be registered with an agency in this State, every *retailer* selling this kind of tangible personal property shall file, with the Department, upon a form to be prescribed by the Department, a separate return for each such item of tangible personal property which the retailer sells…." (emphasis added). The prescribed Department "transaction reporting" form requests the following information: the name and address of the seller, the name and address of the purchaser; the amount of the selling price, including the amount allowed by the retailer for traded-in property, if any; the amount allowed by the retailer for the traded-in tangible personal property, if any, to the extent to which an exemption for the traded-in-property is allowed; the balance payable after allowing such trade-ins; the amount of tax due from the retailer with respect to such transaction; the amount of tax collected from the purchaser by the retailer (or satisfactory evidence that such tax is not due in that particular instance); the place and date of the sale; sufficient identification of the vehicle sold; and any other such information required by the Illinois Vehicle Code. *Id.*

In Illinois, a sale at retail means any transfer of the ownership of or title to tangible personal property to a buyer for use or consumption, and not for resale, for a valuable consideration. 35 ILCS 120/1; 86 Ill. Admin. Code § 130.201(a). Thus, an entity which sells tangible personal property exclusively for resale is not a retailer under Illinois law. *Dearborn Wholesale Grocers v Whitler*, 82 Ill. 2d 471, 413 N.E.2d 370 (1980).

Effective August 10, 2015, Illinois enacted Public Act 99-335, which imposes a penalty of $100 for failure to file a transaction reporting return required by section 3 of the ROT Act on or before the date a return is required to be filed but only if the return, when properly prepared and filed, would not result in the imposition of tax. 35 ILCS 735/3-3(a-15). This law, in other words, imposes a $100 penalty for the failure to file a "zero return". In November, 2016, the Department issued a Compliance alert entitled "Penalty for *Dealers* who Fail to File Form ST-556 or Form ST-556-LSE When Making sales for Which No Tax Is Due" (emphasis added). In this Alert, the Department stated, "[t]his provision requires the Department to impose this $100 penalty for each instance in which a *dealer* makes a sale for which no tax is due but fails to properly report that sale to the Department using Form ST-556 or Form ST-556-LSE, Transaction Return for Leases (with regard to sales for lease.)"

The term “dealer” is not defined by nor even found in the Illinois ROT Act. However, the Illinois Vehicle Code defines “dealer” as “every person engaged in the business of acquiring or disposing of vehicles or their essential parts and who has an established place of business for such purpose.” 625 ILCS § 5/1-115.

In addition, Illinois provides retailers with a discount in order to reimburse the retailers for the expenses incurred for keeping ROT records and supplying the information and tax to the Department. 35 ILCS 120/3. Retailers are to pay the tax collected minus a 1.7% [sic] discount, or $5 per calendar year, whichever is greater. *Id.*

Here, the Manufacturer, Finance Company, and Trust make tens of thousands of sales of motor vehicles to dealers for resale every year. None of these sales, though, are retail sales to an end user for use or consumption. Thus, while these entities might be registered for ROT and AROT and while the Manufacturer might actually pay ROT on its sales of Bulletins and service tools, none of the entities are “retailers” of motor vehicles because all of their motor vehicle sales are for resale. Moreover, the entities are clearly not dealers under the Illinois Motor Vehicle code because they do not have an established place of business for selling motor vehicles. Indeed, the Department’s recently issued Compliance Alert suggests that only “dealers” are subject to the penalty for failing to file ST-556 returns that report no tax liability. Moreover, the retailers’ discount of $5 annually (as a result of all returns reporting zero tax liability) for filing ## - ## returns is not a fair trade off for the entities keeping records and supplying the information to the Department.

If required to file Illinois ST-556 returns for all sales for resale, the administrative burden for each of the entities will be substantial and will require the entities to employ additional personnel for the sole purpose of filing zero returns. Additionally, this administrative burden to process the returns will carry over to the Department, especially considering that the model outlined above is used for all or most other major car manufacturers and their respective captive financial units.

REQUEST FOR RULING

Pursuant to 2 Ill. Admin. Code Section 1200.110, the Taxpayer respectfully requests that the Department of Revenue issue a General Information Letter declaring that: (i) if a company such as Finance Company or Trust sells motor vehicles for resale purposes only, and its sells no other tangible personal property, then it is not required to file an Illinois ST-556 return; and (ii) if a company, such as Manufacturer, sells to dealers or another end user tangible personal property other than motor vehicles, in addition to motor vehicles that are sold exclusively for resale, such seller is not considered a “retailer” of motor vehicles and it is not required to file an Illinois ST-556 for each sale for resale of motor vehicles.

If you agree, please issue your favorable ruling to the undersigned. If you do not agree, please advise so that we may discuss your reasoning before an adverse ruling is issued.

DEPARTMENT'S RESPONSE:

The Uniform Penalty and Interest Act, as amended by P.A. 98-425 (effective August 16, 2013), imposed a $100 penalty for failure to file a transaction reporting return on or before the due date as required by Section 3 of the Retailers' Occupation Tax Act (35 ILCS 120/3) and Section 9 of the Use Tax Act (35 ILCS 105/9). This penalty was imposed regardless of whether the return reported any tax due. P.A. 99-335 (effective August 10, 2015) amended the provisions of P.A. 98-425 to impose the $100 penalty for failure to file a transaction reporting return on or before the due date as required by Section 3 of the Retailers' Occupation Tax Act and Section 9 of the Use Tax Act only if there is no tax due. 35 ILCS 735/3-3(a-15). After amendment by P.A. 99-335, the provision reads:

> (a-15) A penalty of $100 shall be imposed for failure to file a transaction reporting return required by Section 3 of the Retailers' Occupation Tax Act and Section 9 of the Use Tax Act on or before the date a return is required to be filed; provided, however, that this penalty shall be imposed only if the return when properly prepared and filed would not result in the imposition of a tax. 35 ILCS 735/3-3(a-15)

This provision requires the Department to impose this $100 penalty for each instance in which a retailer makes a sale for which no tax is due but fails to properly report that sale to the Department using Form ST-556, Sales Tax Transaction Return or Form ST-556-LSE, Transaction Return for Leases (with regard to sales for lease).

The Uniform Penalty and Interest Act's $100 penalty provision is triggered by a failure to file a transaction reporting return "required by Section 3 of the Retailers' Occupation Tax Act." Section 3 of the Retailers' Occupation Tax Act provides that "... with respect to motor vehicles … that are required to be registered with an agency of this State, every retailer selling this kind of tangible personal property shall file, with the Department, upon a form to be prescribed and supplied by the Department, a separate return for each such item of tangible personal property which the retailer sells…." 35 ILCS 120/3. For purposes of this $100 penalty for failure to file zero liability transaction reporting returns, it is the Department's position that a "retailer selling this kind of tangible personal property" means a person registered with the Illinois Department of Revenue as a retailer of titled and registered property who is required to report and pay tax using transaction reporting returns (e.g., ST-556 and ST-556-LSE). A person who sells only titled and registered property exclusively for resale is not considered to be a retailer required to report and pay tax using transaction reporting returns. See *Dearborn Wholesale Grocers, Inc. v. Whitler,* 82 Ill.2d 471 (1980). In addition, it is the Department's position that a person who sells merchandise at retail other than titled and registered property (i.e., a person required to file Form ST-1, Sales and Use Tax and E911 Surcharge Returns) and who also sells titled and registered property exclusively for resale is not considered to be a retailer required to report and pay tax using transaction reporting returns.

This means that, if, for example, a company sells motor vehicles exclusively for resale and not at retail and it sells no other tangible personal property, then the sales of motor vehicles for resale are not required to be reported on transaction reporting returns and no penalty is imposed under the Uniform Penalty and Interest Act for failure to file transaction reporting returns. This also means that, if, for example, a company sells merchandise at retail other than titled and registered property (i.e., a company that is registered to and does file Form ST-1, Sales and Use Tax and E911 Surcharge Returns) and also sells titled and registered property exclusively for resale (i.e., no retail sales of titled and registered property), then the sales of motor vehicles for resale are not required to be reported on

transaction reporting returns and no penalty is imposed under the Uniform Penalty and Interest Act for failure to file transaction reporting returns.

It is important to note, however, that if a company makes any retail sales of titled and registered property in Illinois, then all sales of titled and registered property in Illinois must be reported on transaction reporting returns, including sales for resale. This results from the requirement in the Retailers' Occupation Tax Act that "… retailers selling this kind of tangible personal property shall file, with the Department, upon a form to be prescribed and supplied by the Department, a separate return for each such item of tangible personal property which the retailer sells…." (35 ILCS 120/3). Failure of these retailers to file returns reporting sales for resale is subject to the $100 penalty imposed under subsection (a-15) of Section 3 of the Uniform Penalty and Interest Act.

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,

Samuel J. Moore
Associate Counsel

SJM:bkl