

Manufacturer's Purchase Credit may be used to satisfy Use Tax or Service Use Tax liability that is incurred on the purchase of production related tangible personal property that does not qualify for the manufacturing machinery and equipment exemption. See, 86 Ill. Admin. Code 130.331. (This is a GIL.)

October 14, 2008

Dear Xxxxx:

This letter is in response to your letter dated January 28, 2008, in which you request information. We apologize for the delay in responding to your inquiry. 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:

Background

We are a manufacturer of plastic bottles. We use forklifts in our operations primarily to transport finished goods from the production lines to temporary storage and then from storage to shipping areas.

Taxpayer Question

At issue is whether the form of our lease agreement with our forklift vendor affects our ability to use Manufacturer's Purchase Credit (MPC). More specifically, can MPC be used on equipment financed under a conditional sale agreement? (Exhibit A)

Business Hotline Response

Previously, our representative posed this question to the State of Illinois' Business Hotline. The Department's Legal Division issued an internal memo to Taxpayer Services stating, 'If this is an actual conditional sale contract then it would be considered a purchase and the use of MPC may be allowed to satisfy the tax liability. With this in mind the lessor may accept MPC.' (Exhibit B)

Taxpayer Request

Our vendor has refused to accept our initial Form ST-16-C Manufacturers Purchase Credit Certificate on the grounds that the communication from the business hotline is nonbinding. We request a private letter ruling which we intend to attach to the vendor's form ST-16-C.

DEPARTMENT'S RESPONSE:

LEASES

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.

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 the enclosed copy of 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.

MANUFACTURER'S PURCHASE CREDIT

The State of Illinois provides a manufacturer's purchase credit in addition to the exemption for manufacturing machinery and equipment. See 86 Ill. Adm. Code 130.331. Purchasers of manufacturing machinery and equipment that qualifies for the manufacturing machinery and equipment exemption earn a credit in an amount equal to a fixed percentage of the tax which would have been incurred under the Use Tax or Service Use Tax. 35 ILCS 105/3-85; 35 ILCS 110/3-70. The credit may be used to satisfy Use Tax or Service Use Tax liability that is incurred on the purchase of production related tangible personal property. The credit may be used in situations when production related tangible personal property is purchased by means of a conditional sales agreement.

"Production related tangible personal property" includes all tangible personal property used or consumed in a production related process by a manufacturer in a manufacturing facility in which a manufacturing process described in Section 2-45 of the Retailers' Occupation Tax Act takes place, and all tangible personal property used or consumed by a manufacturer or graphic arts producer in

research and development regardless of use within or without a manufacturing or graphic arts production facility. (See 35 ILCS 105/3-85).

The Department's regulation at 86 Ill. Adm. Code 130.331(b)(4)(D) provides that tangible personal property used or consumed in a manufacturing facility for purposes of pre-production and post-production material handling, receiving, quality control, inventory control, storage, staging and packing for shipping or transportation are considered production related. For example, forklift trucks used to move raw materials within a manufacturing area are generally being used in a production related process and may qualify as production related tangible personal property. All tangible personal property used or consumed by a manufacturer in research and development regardless of use within or without a manufacturing facility is considered production related personal property. 86 Ill. Adm. Code 130.331(b)(3)(C).

Office supplies, computers, desks, copiers and equipment which are used for sales, purchasing, accounting, fiscal management, marketing and personnel recruitment or selection activities, even if such use takes place within a manufacturing or graphic arts production facility are not considered production related personal property. 86 Ill. Adm. Code 130.331(b)(5)(B). Tangible personal property used or consumed outside the manufacturing facility, including tangible personal property listed in subsections (b)(4)(D), with the exception of tangible personal property used or consumed for research and development purposes, is not considered production related. 86 Ill. Adm. Code 130.331(b)(5)(D).

In order to accept Manufacturer's Purchase Credit from a manufacturer or graphic arts producer, the supplier or serviceman must obtain a Manufacturer's Purchase Credit certificate from the manufacturer or graphic arts producer unless the manufacturer or graphic arts producer has incorporated its certification into the manufacturer's or graphic arts producer's purchase order. The manufacturer or graphic arts producer may provide the certification on a form provided by the Department or on the manufacturer's or graphic arts producer's own form containing the appropriate information described in subsection (f)(1) of Section 130.331 of the Department's administrative rules. See 86 Ill. Adm. Code 130.331. The certificate must be kept in the supplier's or serviceman's books and records, but need not be submitted to the Department with the supplier's or serviceman's return.

A purchaser who provides an MPC certification and uses Manufacturer's Purchase Credit to satisfy the purchaser's Use Tax or Service Use Tax liability incurred on the purchase of property that is later determined not to qualify as production related tangible personal property may be liable for tax, penalty, and interest on the purchase of that property as of the date of the purchase. See subsection (e)(8) of Section 130.331.

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,

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