

Chicago Personal Property Lease Tax Amendment and Information Bulletin

Overview

As part of the Chicago 2016 Budget Proposal, Mayor Emanuel recently signed the 2016 Revenue Ordinance (SO2015-7403).¹ While SO2015-7403 amended various sections of the Chicago Revenue Ordinance, this Tax Alert addresses the following changes made specifically to Chicago Revenue Ordinance Article I, titled the “Personal Property Lease Transaction Tax” (Lease Tax), as applied to cloud computing (i.e., nonpossessory computer leases):

- The amendment of the Lease Tax to codify the specific application of the Illinois Mobile Telecommunication sourcing rules for determining which customers and charges are subject to the tax where a user accesses the provider’s computer from a mobile device.²
- A reduction in the tax rate from 9 percent to 5.25 percent for cloud-based services where customers access their own data or information.³
- The addition of a “small new business” exemption from the Lease Tax.⁴

The small new business exemption and tax rate reduction are both effective January 1, 2016, while the sourcing amendment was effective upon passage and publication of SO2015-7403.⁵

The City of Chicago (City) Department of Finance (Department) also recently issued an Information Bulletin providing further guidance on the application of the Lease Tax.⁶ The Information Bulletin addresses the SO2015-7403 amendments to the Lease Tax and provides a response to questions the Department received after it issued Lease Tax Ruling #12 (Ruling #12) on June 9, 2015.⁷ Also, the Information Bulletin discusses a limited-scope voluntary disclosure offer through January 1, 2016, for taxpayers with potential exposure related to certain nonpossessory computer lease transactions.

In this Tax Alert we summarize the SO2015-7403 amendments and pertinent elements of the Information Bulletin, and provide some taxpayer considerations.

Codification of the applicability of the Illinois Mobile Telecommunication sourcing rules

In the case of a nonpossessory computer lease⁸ where the user accesses the provider’s computer from a mobile device, SO2015-7403 amends the Lease Tax to codify that the rules set forth in the Illinois Mobile Telecommunications Sourcing Conformity Act, 35 ILCS 638, “may be utilized for the purpose of determining which customers and charges are subject to the tax imposed by this chapter.”⁹ Generally these rules result in tax applying to Chicago residents and companies with primary or residential street addresses in the city as evidenced by their credit card billing information.¹⁰ If the rules indicate that the tax applies, it shall be presumed that the tax applies unless the contrary is established by books, records, or other documentary evidence.¹¹

¹ Chicago, Ill., SO2015-7403 (2015), available [here](#) (signed by Mayor Emanuel on Nov. 2, 2015).

² Chicago, Ill., SO2015-7403 (2015), Art. I, § 1, amending Chicago, Ill. Code § 3-32-020(I).

³ Chicago, Ill., SO2015-7403 (2015), Art. I, § 1, amending Chicago, Ill. Code § 3-32-030(B).

⁴ Chicago, Ill., SO2015-7403 (2015), Art. I, § 1, adding Chicago, Ill. Code § 3-32-050(13).

⁵ Chicago, Ill., SO2015-7403 (2015), Art. XIV, § 1. Note that SO2015-7403 was passed by the City Council on Oct. 28, 2015, and, as noted above, was signed by the Mayor on Nov. 2, 2015.

⁶ Transaction Tax Information Bulletin, City of Chicago Dept. of Fin. (Nov. 19, 2015), available [here](#).

⁷ The background and implications of Letter Ruling #12 were summarized in our August 14, 2015 Tax Alert: [Chicago update-Personal Property Lease Transaction Tax and Amusement Tax rulings](#).

⁸ The term “nonpossessory computer lease” means a nonpossessory lease in which the customer obtains access to the provider’s computer and uses the computer and its software to input, modify, or retrieve data or information, in each case without the intervention (other than de minimis intervention) of personnel acting on behalf of the provider. The term “nonpossessory computer lease” includes, but is not limited to, time sharing or time or other use of a computer with other users. In the case of a nonpossessory computer lease, the location of the terminal or other device by which a user accesses the computer shall be deemed to be the place of lease or rental and the place of use of the computer for purposes of the tax imposed by this chapter. Chicago, Ill. Code § 3-32-020(I).

⁹ SO2015-7403 (2015), Art. I, § 1, amending Chicago, Ill. Code § 3-32-020(I).

¹⁰ Transaction Tax Information Bulletin, FAQ No. 2 at 7.

¹¹ SO2015-7403 (2015), Art. I, § 1, amending Chicago, Ill. Code § 3-32-020(I).

If a provider has no information to indicate any of its customer's use will take place in Chicago, then the provider will not be required to collect the Lease Tax from its customer.¹² Where the provider has information that indicates only some of the customer's use will take place in Chicago, but does not have sufficient information to determine a reasonable apportionment between Chicago and non-Chicago use, the provider may rely on actual information or estimates provided by the customer.¹³

Tax rate reduction for cloud-based services where the customer accesses its own data

Effective January 1, 2016, the levied tax rate will be reduced to 5.25 percent (from 9 percent) "in the case of a nonpossessory lease of a computer primarily for the purpose of allowing a customer to use the provider's computer and software to input, modify, or retrieve data or information that is supplied by the customer."¹⁴

The Information Bulletin provides that the lower rate will apply to "cloud" products such as PaaS, IaaS, and SaaS, but not to "database" products. In the Information Bulletin, the Department states that a "cloud" product "is a nonpossessory lease primarily for the purpose of allowing the customer to use the provider's computer and software to input, modify or retrieve data or information that is supplied by the customer." By contrast, a "database" product "is a nonpossessory lease for the purpose of allowing the customer to use the provider's computer and software to input, modify or retrieve data or information that is supplied by the provider."¹⁵

"Small new business" exemption

Effective January 1, 2016, SO2015-7403 amends the Lease Tax to provide that the "nonpossessory lease of a computer, where the lessee or lessor is a small new business" will be exempt from the tax.¹⁶ The term "small new business" is defined as a business that:

1. [H]olds a valid and current Chicago license issued by the City or another jurisdiction,
2. During the most recent full calendar year prior to the annual tax year for which the exemption ... is sought has under \$25 million in gross receipts or sales, as the term 'gross receipts' is defined for federal income tax purposes,¹⁷ and
3. Has been in operation for fewer than 60 months.¹⁸

For purposes of calculating the 60-month limit, the time in operation begins during the first calendar month in which the business seeking the exemption first received any gross receipts or sales.¹⁹ A small new business that is the lessor of a nonpossessory computer lease will not be required to collect the Lease Tax on its charges for such nonpossessory lease charge. Similarly, a small business that is the lessee of a nonpossessory computer lease will not be required to pay Lease Tax on its charges for the nonpossessory computer lease.

In the Information Bulletin, the Department notes that it is preparing exemption certificate forms that will be available on its website for purposes of proper documentation of the small new business exemption.²⁰

Information Bulletin highlights

In addition to addressing the recent amendments to the Lease Tax provided by SO2015-7403, the Information Bulletin issued by the Department on November 19 discusses other considerations relevant to the application of the Lease Tax to nonpossessory computer leases, notably questions that had arisen subsequent to the Department's issuance of Ruling #12 on June 9, 2015. The Department previously issued Ruling #12 so that taxpayers that had not been aware of the scope and application of the Lease Tax, particularly around nonpossessory computer lease

¹² Transaction Tax Information Bulletin, FAQ No. 2 at 7.

¹³ *Id.*

¹⁴ SO2015-7403 (2015), Art. I, § 1, adding Chicago, Ill. Code § 3-32-030(B)(1).

¹⁵ Transaction Tax Information Bulletin at 5.

¹⁶ SO2015-7403 (2015), Art. I, § 1, adding Chicago, Ill. Code § 3-32-050(13).

¹⁷ For the purpose of calculating the \$25 million limit, gross receipts or sales will be combined if they are received by members of a single unitary business group. For purposes of this subsection, the term "unitary business group" is as defined for Illinois income tax purposes. SO2015-7403 (2015), Art 1, § 1, adding Chicago, Ill. Code § 3-32-050(13)(a).

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ Transaction Tax Information Bulletin at 5.

transactions, could be brought into compliance. In the Information Bulletin, the Department acknowledges that Ruling #12 affected a change in interpretation of Exemption 11²¹ by the Department:

In the past, the Department had generally interpreted the reference to “fleeting and transitory” information as exempting certain products that provide financial market data. Ruling #12 clarified that such uses are exempt only if the receipt (and any usage) is simply the passive receipt of information [T]his means that a subscription to an interactive website will be subject to the lease tax, and will not be exempt, even if most or all of the information available on the web site is fleeting or transitory. This would include, for example, a web site that provides financial research, information, and analytical tools.²²

As a result of this change in interpretation and questions raised as to the effective date of Ruling #12, the Information Bulletin outlines a voluntary disclosure offer for any provider or customer that comes into compliance with the Lease Tax and Ruling #12 by January 1, 2016.²³

- Eligible providers and customers that have charges for nonpossessory computer leases that no longer qualify as fleeting and transitory as a result of the change in interpretation described in Ruling #12 can file a voluntary disclosure application by January 1, 2016. Those coming forward and coming into compliance with the Chicago Lease Tax Ordinance and Ruling #12 by the January 1, 2016, deadline will not be liable for tax, interest, or penalties based on those charges for any periods ending before January 1, 2016.
- Eligible providers and customers that have charges for other nonpossessory computer leases not impacted by the Department’s clarification to Exemption 11 can also file a voluntary disclosure application by January 1, 2016. Such providers and customers will be required to make payment of taxes for the period of January 1, 2015 through December 31, 2015 (one year), with no liability for interest or penalties.²⁴

The Information Bulletin also includes an FAQ section addressing a number of topics, including, but not limited to, who pays the Lease Tax, how a business determines a Chicago customer, allocation of Chicago usage, nexus, types of digital uses that are taxable, taxability of storage charges, bundled charges, and the lease for re-lease exemption.²⁵

Additional considerations

This Tax Alert only covers the updates in the budgetary ordinance concerning the Lease Tax. The Tax Alert does not address any of the other changes contained in the City’s 2016 Budget Proposal, including those with respect to liquid nicotine products, amusement tax, parking tax, overweight truck permit fees, uninsured motorists, building permit/construction fees, refuse collection, capital improvement tax levy, and taxi rate airport surcharges.

Businesses that may benefit from the Lease Tax voluntary disclosure program as outlined in the Information Bulletin should keep in mind the applicable deadline and the requirement to come into compliance with the Lease Tax and Ruling #12 by January 1, 2016.

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If you have questions regarding the Lease Tax or other Chicago or Illinois tax matters, please contact any of the following Deloitte Tax professionals:

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²¹ Chicago, Ill. Code § 3-32-050(A)(11) exempts “the nonpossessory lease of a computer in which the customer’s use or control of the provider’s computer is de minimis and the related charge is predominantly for information transferred to the customer rather than for the customer’s use or control of the computer, such as the nonpossessory lease of a computer to receive either current price quotations or other information having a fleeting or transitory character.”

²² Transaction Tax Information Bulletin at 3.

²³ *Id.* at 6-7.

²⁴ With respect to other Lease Taxes owed on leases other than nonpossessory computer leases, or taxes other than Lease Tax, the terms of the City’s standard voluntary disclosure program will apply, whereby the business agrees to pay no more than four years of tax and interest, and receives a waiver of penalties. Transaction Tax Information Bulletin at 7.

²⁵ *Id.* at 7-11.

The authors of this alert would like to acknowledge the contributions of Eric A. Miller to the drafting process. Eric is a Staff member working in the Chicago Multistate practice of Deloitte Tax LLP.

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