

Illinois Emergency and Proposed Local Retail Occupation Tax Sourcing Rules

February 2, 2014

Overview

On January 22, 2014, the Illinois Department of Revenue (“DOR”) issued emergency and proposed local Retail Occupation Tax (“ROT”) sourcing rules in response to the Illinois Supreme Court’s decision in *Hartney Fuel Oil Co. v. Hamer*, 2013 IL 115130 (Nov. 21, 2013).¹ In *Hartney*, the Illinois Supreme Court invalidated the DOR’s regulations that provided guidance regarding proper situs for tax liability under local ROT schemes.² In this Tax Alert we summarize the *Hartney* decision and the emergency sourcing rules. We also provide some taxpayer considerations.

The *Hartney* Decision

In *Hartney*, the Illinois Supreme Court invalidated the DOR’s regulations that had provided guidance for determining which local ROT applied to multi-jurisdictional retailers.³ The court found fault with two aspects of the regulations. First, the regulations did not “amply prescribe the fact-intensive inquiry contemplated by” the statute and as interpreted by previous case law.⁴ Second, the regulations “impermissibly constrict[ed] the scope of” the statute by “allowing for only one potentially minor step in the business of selling to conclusively govern tax situs.”⁵

The Emergency Sourcing Rules

The emergency sourcing rules have three substantive parts. The first part identifies the core principles underlying the ROT:

1. The tax is imposed in the “the retail business of selling and not on specific sales.”⁶
2. The determination of where the occupation of selling takes place is “a fact-specific inquiry into the composite of activities that comprise the retailer’s business.”⁷
3. The underlying purpose of the ROT Act is to allow local jurisdictions to impose taxes on those retailers that take advantage of the public services they provide.⁸

The second substantive part of the emergency rules provides guidance on applying the fact-specific legal standard to common selling operations including: over-the-counter sales, in-state inventory/out-of-state selling activities, long term or blanket contracts, and sales through vending machines, among others.⁹

The emergency rules specifically indicate that order acceptance does not constitute doing business in a jurisdiction if:

1. “The seller has no other selling activity in the jurisdiction except receipt and acceptance of purchase orders;”
2. “All orders for the purchase of tangible personal property are submitted to the seller in the jurisdiction by means of telephone or Internet; and”

¹ The emergency and proposed rules along with press releases are available at on the DOR’s website at:

<http://tax.illinois.gov/News/HartneyDecision.htm>.

² *Hartney Fuel Oil Co. v. Hamer*, 2013 IL 115130, at ¶ 61-67 (Nov. 21, 2013). Note that the ROT Acts “allow home rule county and municipal governments and the Regional Transportation Authority to impose a retail occupation tax ‘upon all persons engaged in the business of selling tangible personal property at retail within the county, municipality, or metropolitan region.’” *Id.* at ¶ 20, citing 55 ILCS 5/5-1006, 65 ILCS 5/8-11-1, and 70 ILCS 3615/4.03.

³ *Hartney*, at ¶ 61-67.

⁴ *Id.*, at ¶ 61.

⁵ *Id.* For additional information on the *Hartney* decision, see our External Tax Alert dated November 26, 2013, accessible at:

http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/Tax/us_tax_multistate_IL_112713.pdf.

⁶ 86 Ill. Admin. Code § 220.115(b)(1) (2014).

⁷ 86 Ill. Admin. Code § 220.115(b)(2) (2014).

⁸ 86 Ill. Admin. Code § 220.115(b)(3) (2014).

⁹ 86 Ill. Admin. Code § 220.115(c) (2014). Note that although long-term or blanket contracts are included in the emergency rules, they are excluded from the proposed rules.

3. “The seller’s employees or agents . . . accept purchase order information relayed by the customer, but do not negotiate or exercise discretion on behalf of the seller.”¹⁰

The third substantive part of the emergency rules provides guidance on applying the fact-specific legal standard to multi-jurisdictional intrastate retailers.¹¹ Under the rules, four primary selling activities generally dictate where a multi-jurisdictional retailer is engaged in the business of selling: offer, acceptance, inventory, and “officers, executives and employees with discretion to negotiate on behalf of, and to bind, the seller.”¹² If the four primary selling activities fail to reveal the location of the business of selling, five additional selling activities may also be considered to determine the correct taxing jurisdiction: the location of the seller’s administrative functions, where solicitation takes place, where contracts are received, where title passes, and where goods are delivered.¹³

In the rare case where a retailer’s selling activities are so dispersed that the seller’s location is uncertain, the DOR will consider both the primary and secondary selling activities “in keeping with the principle that the retailer incurs local retailers’ occupation tax in the jurisdiction where it ‘enjoyed the greater part of governmental protection [and] benefited by . . . [conducting its business] under that protection.’”¹⁴ The DOR may also “‘look through the form of a putatively [multi-jurisdictional] transaction to its substance’ to determine where ‘enough of the business of selling took place’ and thus where the seller is subject to local retailers’ occupation tax.”¹⁵

Considerations

The emergency rules will be in effect for 150 days from the January 22, 2014 date of issuance unless the Joint Committee on Administrative Rules (JCAR) votes by a 3/5th majority to suspend such rules. The proposed permanent rules will replace the emergency rules after the JCAR review process. There is a 45 day 1st Notice period, during which concerned parties may file comments or request a public hearing on the proposed permanent rules. During a 45 day 2nd Notice period, JCAR will review the proposed permanent rules along with any proposed modifications or amendments. At the end of that time, if JCAR takes no further action, the proposed rules will become permanent.¹⁶

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¹⁰ 86 Ill. Admin. Code § 220.115(c)(8)(A) (2014).

¹¹ 86 Ill. Admin. Code § 220.115(d) (2014).

¹² 86 Ill. Admin. Code § 220.115(d)(2)(A)-(d)(2)(D) (2014).

¹³ 86 Ill. Admin. Code § 220.115(d)(3)(A)-(d)(3)(D) (2014).

¹⁴ 86 Ill. Admin. Code § 220.115(d)(4)(A) (2014).

¹⁵ 86 Ill. Admin. Code § 220.115(d)(4)(B) (2014), quoting *Marshall & Huschart Mach. Co. v. Dep’t of Revenue*, 18 Ill. 2d 496, 501 (1960); *Fed. Bryant Mach. Co. v. Dep’t of Revenue*, 41 Ill. 2d 64 67 (1968); *Int’l-Stanley Corp. v. Dep’t of Revenue*, 40 Ill. App. 3d 397, 406 (1st Dist. 1976), *Hartney Fuel Oil Co. v. Hamer*, 2013 IL 115130 ¶ 31.

¹⁶ DOR Press Release – *New Sales Tax Allocation Rules Filed Today, Emergency Rules Effective Immediately*, Released January 22, 2014.