

ST 96-32

Tax Type: SALES TAX

Issue: Audit Methodologies and/or Other Computational Issues

STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
SPRINGFIELD, ILLINOIS

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|---------------------------|---|--------------------------|
| THE DEPARTMENT OF REVENUE |) | |
| OF THE STATE OF ILLINOIS |) | Docket # |
| |) | |
| v. |) | IBT # |
| |) | |
| TAXPAYER |) | |
| |) | Karl W. Betz |
| |) | Administrative Law Judge |
| Taxpayer |) | |

RECOMMENDATION FOR DISPOSITION

SYNOPSIS

This cause came on to be heard following an audit performed by the Illinois Department of Revenue (hereinafter the "Department") upon TAXPAYER (hereinafter "taxpayer").

Taxpayer is a leasing company that also sells equipment to end users in Illinois. The Department performed a Retailers' Occupation and Use Tax audit upon the taxpayer for the period of January 1, 1992 through December 31, 1994. Upon completion of the audit, the taxpayer paid the liability on some transactions determined by the auditor to be taxable, and for one other transaction that taxpayer contested, Notice of Tax Liability Number XXXXX was issued for tax of \$1,396.00, plus interest of \$192.00 for a total liability of \$1,588.00.

The transaction at issue herein involves a purchase taxpayer made from a related entity, PURCHASER (hereinafter "PURCHASER"). Taxpayer only self-assessed Use Tax upon the cost that PURCHASER paid to its supplier, not upon the total transaction invoice selling price paid by taxpayer to PURCHASER for the equipment. The question I have to decide concerns the taxability of the markup

portion of the price taxpayer paid for this equipment that it purchased to lease to a lessee in Farmer City, Illinois.

After taxpayer made a timely protest of the NTL, a pre-hearing status conference was scheduled by the Department in this matter. Before the conference, taxpayer submitted a letter dated March 22, 1996, in which it stated it waived its right to a formal hearing and requested a review of its position based upon its submission of certain documents. The convening of a formal hearing having been waived by taxpayer, no witnesses were called to testify and I thus write this recommendation based upon the documents in the record; those submitted by taxpayer and the Department's *prima facie* case consisting of the corrected return, audit file and NTL.

After reviewing this matter, I recommend the issue be resolved in favor of the Department.

FINDINGS OF FACT

1. Taxpayer conducted business operations in Illinois during the audit period by leasing and selling tangible personal property. (Dept. Audit file)
2. The taxpayer purchased computer equipment from PURCHASER on March 24, 1994 with this invoice (#9999/1626) showing \$118,041.00 as the total amount due, to be billed to taxpayer under Sales Contract No. PV01930. (Dept. Audit File)
3. Taxpayer created a check for this \$118,041.00 amount to pay PURCHASER and the auditor saw a copy of that check in the lease file when he was doing his audit work. (Dept. Audit File)
4. Pursuant to statutory authority, the Department auditor did cause to be issued an Audit Correction and/or Determination of Tax Due and this corrected return served as the basis for the Notice of Tax Liability. (Dept. Audit File)

CONCLUSIONS OF LAW

A tax is imposed upon the privilege of using tangible personal property in Illinois. The word "use" is defined in the Use Tax Act as the exercise of ownership power over tangible personal property such as the equipment taxpayer rented to Illinois lessees in the instant case. Use Tax liability is incurred upon the "selling price" when the tangible personal property is purchased in a retail sale. 35 ILCS 105/2 and 3

Taxpayer, as a lessor, was a user of the computer equipment it leased (Philco v. Department of Revenue, 40 Ill.2d 312, 1968), and the U.S. Supreme Court has noted the legality of the Illinois Use Tax. United Air Lines v. Mahin, 410 U.S. 623; 93 S.Ct. 1186, (1973)

Taxpayer argues it is only liable for tax on the \$97,500.00 cost paid by PURCHASER to its supplier, IBM, and in support cites the Departmental Regulation that covers discounts from the selling price, 86 Ill. Adm. Code, ch. I, Sec. 130.420(c).

I do not agree because this is not the type of discount contemplated by Section 130.420(c), which authorizes a reduction from the tax base selling price when a discount is allowed for prompt or cash payment, and the seller does not receive receipts through the buyer's availing himself of that offered discount. Here the record shows the buyer paid seller a check for the full invoice selling price, as was seen by the auditor and also acknowledged by taxpayer in its 12/11/95 letter.

Taxpayer also contends the \$22,341 PURCHASER profit margin was fictitious because the consolidated entity's subsequent accounting entries had the effect of eliminating PURCHASER's profit margin, thus creating a result of no Use Tax due thereon. I do not find this persuasive because the possibility that generally accepted accounting principles may provide for eliminating or reversing entries in the preparation of consolidated financial statements does not change the requirements taxpayers are subject to under the Illinois Retailers' Occupation and Use Tax Acts.

In summary, I find the taxpayer has not overcome the *prima facie* case of the Department and I recommend the NTL stand as issued.

RECOMMENDATION

Based upon my findings and conclusions as stated above, I recommend the Department finalize NTL No. XXXXX and issue a Final Assessment.

Karl W. Betz
Administrative Law Judge