

ILLINOIS REGISTER
DEPARTMENT OF REVENUE
NOTICE OF PROPOSED AMENDMENT

- 1) Heading of the Part: Retailers' Occupation Tax
- 2) Code Citation: 86 Ill. Adm. Code 130
- 3) Section Number: 130.1960 Proposed Action:
Amendment
- 4) Statutory Authority: 35 ILCS 120/12; 20 ILCS 2505/2505-795
- 5) A Complete Description of the Subjects and Issues Involved: This rulemaking amends the Department's regulation at 86 Ill. Adm. Code 130.1960 entitled Finance Companies and Other Lending Agencies – Installment Contracts – Bad Debts. Specifically, this rule is being amended to reflect the changes made to the Retailers' Occupation Tax Act ("ROT") pursuant to P.A. 99-217, effective July 31, 2015. P.A. 99-217 amended the ROT by adding a new Section 6d. Section 6d provides that beginning July 31, 2015, a retailer is relieved from liability for any tax that becomes due and payable if the tax is represented by amounts that are found to be worthless or uncollectible, have been charged off as bad debt on the retailer's books and records in accordance with generally accepted accounting principles, and have been claimed as a deduction pursuant to Section 166 of the Internal Revenue Code. P.A. 99-217 also amended the ROT to provide deductions for bad debts on purchases made through a private-label credit card.
- 6) Published studies or reports, and sources of underlying data, used to compose this rulemaking: None
- 7) Will this rulemaking replace any emergency rulemaking currently in effect? No
- 8) Does this rulemaking contain an automatic repeal date? No
- 9) Does this rulemaking contain incorporations by reference? No
- 10) Are there any other proposed rulemakings pending on this Part? Yes

<u>Section Numbers</u>	<u>Proposed Action</u>	<u>Illinois Register Citation</u>
130.340	Amendment	40 Ill. Reg. 10083, July 29, 2016
130.311	Amendment	41 Ill. Reg. 3168, March 17, 2017
130.320	Amendment	41 Ill. Reg. 3817, March 31, 2017
- 11) Statement of Statewide Policy Objective: This rulemaking does not create a State mandate, nor does it modify any existing State mandates.
- 12) Time, Place and Manner in which interested persons may comment on this proposed rulemaking: Persons who wish to submit comments on this proposed rulemaking may submit them in writing by no later than 45 days after publication of this Notice to:

Debra Boggess

Legal Services Office
Illinois Department of Revenue
101 West Jefferson
Springfield, Illinois 62794

(217) 782-2844

13) Initial Regulatory Flexibility Analysis:

- A) Types of small businesses, small municipalities and not for profit corporations affected: Small businesses that want relief from liability for any tax that becomes due and payable if the tax is represented by amounts that are found to be worthless or uncollectible, have been charged off as bad debt on the retailer's books and records, and claimed on their federal income tax return.
- B) Reporting, bookkeeping or other procedures required for compliance: Basic bookkeeping
- C) Types of professional skills necessary for compliance: Bookkeeping

14) Regulatory Agenda on which this rulemaking was summarized: January 2017

The full text of the Proposed Amendment begins on the next page:

Section 130.1960 Finance Companies and Other Lending Agencies -- Installment Contracts -- Bad Debts

a) Lending Agencies -- When Liable For Tax

Finance companies and other lending agencies are not relieved from liability for tax in cases in which they engage in the business of selling to users or consumers tangible personal property to which they hold or acquire title. Except as provided in subsection (b) of this Section, when a lending agency transfers title to a repossessed car to a user, the lending agency is engaging in the business of selling tangible personal property at retail and incurs Retailers' Occupation Tax liability on its receipts from such sales. It should be registered as a retailer under the Retailers' Occupation Tax Act and should file returns and otherwise comply with that Act.

b) Lending Agencies -- When Not Liable For Tax

- 1) Finance companies and other lending agencies are engaged primarily in the business of financing or acquiring the promissory notes given by purchasers of automobiles, furniture, refrigerators or other items of tangible personal property.
- 2) To guarantee payment of such notes, they sometimes take as security chattel mortgages upon such tangible personal property. In cases where the purchaser of the automobile or other tangible personal property fails to meet his obligation, the lending agency repossesses the property and sells it to satisfy the obligation evidenced by the notes. In connection with such sales, the lending agency acts as agent for the owner of the repossessed property if such owner is known or disclosed to the purchaser, and if the lending agency does not take title to the

property; the lending agency, under such circumstances, is not liable for payment of any Retailers' Occupation Tax with respect to the proceeds from such sales.

3) Even if the lending agency does title a repossessed motor vehicle in its name, if the original buyer, after the expiration of the redemption period provided for in the Retail Installment Sales Act [815 ILCS 405], is granted permission to redeem and to resume possession of the vehicle and to continue performance under his original installment contract without any change in the terms of such contract, and the lending agency re-endorses the repossession title to such original buyer, the transaction is not regarded as a sale and so is not taxable.

c) Installment Sales

- 1) When a retailer of tangible personal property sells an installment contract or "paper" to a third party, the difference between the selling price of the tangible personal property and the selling price of the installment contract or "paper" is a cost of doing business and is therefore not deductible in computing Retailers' Occupation Tax liability. Retailers' Occupation Tax is measured by the total selling price of the tangible personal property purchased from the retailer for use or consumption. Upon sale of the installment contract or "paper" to a third party, Retailers' Occupation Tax becomes due based on the entire selling price to the purchaser of the tangible personal property, with credit allowed for any tax already remitted to the Department based on the receipts from the sale of the tangible personal property. As an illustration, a computer vendor enters into an installment sales contract with a business for a computer system. The selling price of the computer system is \$120,000 and the contract requires monthly installment payments of \$10,000 for one year. After the business makes the first payment, the computer vendor sells the installment contract to a bank for \$90,000. Upon the sale of the installment contract to the bank, the computer vendor incurs Retailers' Occupation Tax on \$120,000 (the entire selling price to the original purchaser), with credit allowed for tax that was remitted on the first \$10,000 payment made by the business.
- 2) For purposes of this Section, "paper" means any instrument of indebtedness which was acquired by the retailer from the purchaser of the tangible personal property. Sales of "paper" to a third party includes the sale of accounts receivable as well as assignments or sales of the actual instruments of indebtedness themselves.

d) Bad Debts

1) Definitions. On and after July 31, 2015, for purposes of this subsection (d):

(A) "Retailer" means a person who holds himself or herself out as being engaged (or who habitually engages) in selling tangible personal property at retail with respect to such sales and includes a retailer's affiliates.

(B) "Lender" means a person, or an affiliate, assignee, or transferee of that person, who owns or has owned a private-label credit card account or an interest in a private-label credit card receivable that the person purchased directly from a retailer who remitted the tax imposed under the Retailers' Occupation Tax Act; originated pursuant to that person's contract with the

retailer who remitted the tax imposed under the Retailers' Occupation Tax Act; or acquired from a third party.

(C) "Private-label credit card" means a charge card or credit card that carries, refers to, or is branded with the name or logo of a retailer and may only be used to make purchases from that retailer or that retailer's affiliates.

(D) "Affiliate" means an entity affiliated under Section 1504 of the Internal Revenue Code, or an entity that would be an affiliate under that Section had the entity been a corporation.

2) Bad debt claimed by retailers through July 30, 2015.

A1) In case a retailer repossesses any tangible personal property and subsequently resells such property to a purchaser for use or consumption, his gross receipts from such sale of the repossessed tangible personal property are subject to Retailers' Occupation Tax. He is entitled to a bad debt credit with respect to the original sale in which the default has occurred to the extent to which he has paid Retailers' Occupation Tax on a portion of the price which he does not collect, or which he is not permitted to retain because of being required to make a repayment thereof to a lending agency under a "with recourse" agreement.

Retailers of tangible personal property other than motor vehicles, watercraft, trailers and aircraft that must be registered with an agency of this State may obtain this bad debt credit by taking a deduction on the returns they file with the Department for the month in which the ~~Federal~~ federal income tax return or amended Federal income tax return on which the receivable is written off is filed, or by filing a claim for credit as provided in subsection (d)(2)(C) ~~(d)(3)~~ of this Section. Because retailers of motor vehicles, watercraft, trailers and aircraft do not pay Retailers' Occupation Tax to the Department on retail sales of motor vehicles, watercraft, trailers, and aircraft with monthly returns, but remit the tax to the Department on a transaction by transaction basis, they are unable to take a deduction on the returns that they file with the Department, but may file a claim for credit with the Department, as provided in subsection (d)(2)(C) ~~(d)(3)~~, on any transaction with respect to which they desire to receive the benefit of the repossession credit.

B2) Retailers who incur bad debt on any tangible personal property that is not repossessed may also obtain bad debt credit as provided in subsections (d)(2)(A) and (C) ~~(d)(1)~~ and ~~(3)~~.

C3) In the case of tax paid on an account receivable that becomes a bad debt, the tax paid becomes a tax paid in error, for which a claim for credit may be filed in accordance with Section 6 of the Retailers' Occupation Tax Act, on the date that the Federal income tax return or amended return on which the receivable is written off is filed.

3) Bad debt claimed by retailers on and after July 31, 2015.

A) On and after July 31, 2015, a retailer is relieved from liability for any tax that becomes due and payable if the tax is represented by amounts that are found to be worthless or uncollectible, have been charged off as bad debt on the retailer's books and records in accordance with generally accepted accounting principles, and have been claimed as a deduction pursuant to Section 166 of the Internal Revenue Code on the income tax return filed by the retailer. A retailer that has previously paid such a tax may, under rules and regulations adopted by the Department, take as a deduction the amount charged off by the retailer. If these accounts are thereafter, in whole or in part, collected by the retailer, the amount collected shall be included in the first return filed after the collection, and the tax shall be paid with the return. [35 ILCS 120/6d(a)]. For purposes of computing the deduction or refund, payments on the accounts or receivables should be prorated against the amounts outstanding on the accounts or receivables (e.g., any penalties, interest and fees).

B) Because retailers of motor vehicles, watercraft, trailers and aircraft do not pay Retailers' Occupation Tax to the Department on retail sales of motor vehicles, watercraft, trailers, and aircraft with monthly returns, but remit the tax to the Department on a transaction-by-transaction basis, they are unable to take a deduction on the returns that they file with the Department, but may file a claim for credit with the Department, as provided in subsection (d)(2)(C), on any eligible transaction.

4) Private-label credit cards – Bad debt on and after July 31, 2015.

A) On and after July 31, 2015, with respect to the payment of taxes on purchases made through a private-label credit card, if consumer accounts or receivables are found to be worthless or uncollectible, the retailer may claim a deduction on a return in an amount equal to, or may obtain a refund of, the tax remitted by the retailer on the unpaid balance due if:

(i) the accounts or receivables have been charged off as bad debt on the lender's books and records on or after January 1, 2016;

(ii) the accounts or receivables have been claimed as a deduction pursuant to Section 166 of the Internal Revenue Code on the federal income tax return filed by the lender; and

(iii) a deduction was not previously claimed and a refund was not previously allowed on that portion of the account receivable.

B) The deduction or refund allowed under subsection (d)(4)(A):

(i) does not apply to credit sale transaction amounts resulting from purchases of titled property;

(ii) includes only those credit sale transaction amounts that represent purchases from the retailer whose name or logo appears on the private-label credit card used to make those purchases;

- (iii) may only be taken by the taxpayer, or its successors, that filed the return and remitted tax on the original sale on which the deduction or refund claim is based; and
- (iv) includes all credit sale transaction amounts eligible under subsection (d)(4)(B)(ii) that are outstanding with respect to the specific private-label credit card account or receivable at the time the account or receivable is charged off, regardless of the date the credit sale transaction actually occurred.

5) Bad debt procedural requirements – record keeping – limitations period on and after July 31, 2015.

- A) The retailer and lender shall maintain adequate books, records, or other documentation supporting the charge off of the accounts or receivables for which a deduction was taken or a refund was claimed under Sections 6 or 6d of the Retailers' Occupation Tax Act, including, but not limited to, a copy of the Federal return on which the deduction or refund was claimed. For purposes of computing the deduction or refund, payments on the accounts or receivables should be prorated against the amounts outstanding on the accounts or receivables.
- B) If a retailer or lender does not charge off an account receivable that is found to be worthless or uncollectible as a bad debt in its books and records and claim a deduction pursuant to Section 166 of the Internal Revenue Code on its Federal income tax return or amended return, the tax paid on that bad debt or receivable will not be considered a tax paid in error and, thus, the retailer will not be able to file a deduction or claim for credit in accordance with Sections 6 or 6d of the Retailers' Occupation Tax Act. Retailers or lenders that file federal returns on a cash basis and cannot claim a deduction pursuant to Section 166 of the Internal Revenue Code are not eligible for the bad debt deduction.
- C) For purposes of the deduction or refund allowable under Section 6d of the Retailers' Occupation Tax Act, the limitations period for claiming the deduction or refund shall be the same as the limitations period set forth in Section 6 of the Retailers' Occupation Tax Act for filing a claim for credit, and shall commence on the date that the accounts or receivables have been claimed as a bad debt deduction pursuant to Section 166 of the Internal Revenue Code on the federal income tax return filed by the lender, regardless of the date on which the sale of the tangible personal property actually occurred.
- D) Section 6d is statutorily exempt from the sunset provisions of Section 2-70 of the Retailers' Occupation Tax Act. [35 ILCS 120/6d]

(Source: Amended at 41 Ill. Reg. _____, effective _____)