

Illinois – Local sales tax sourcing emergency regulations adopted in response to Hartney decision

January 24, 2014

Update (03/10/2014): Due to an inadvertent error, the proposed rules related to local sales tax sourcing are being withdrawn and new rules are being proposed. The Department filed the new proposed rules (as well as a Notice of Withdrawal for the current proposed rules) on March 10, 2014 with the Secretary of State. These items are expected to be published in the Illinois Register on Friday, March 21, 2014. The previously scheduled public hearing will be held on March 21, 2014, as originally announced. Please note that this does not affect the emergency regulations, which will continue until expiration of the 150-day period.

The new proposed rules differ in one important respect from the current emergency rules. The new proposed rules do not contain the subsection titled “Long Term or Blanket Contracts,” which is currently found in the emergency rules. In other respects, the new proposed rules are substantively identical to the emergency rules.

In brief

The Illinois Department of Revenue (Department) filed emergency regulations on January 22, 2014, with the Joint Committee on Administrative Rules. The regulations reflect guidance provided in the Illinois Supreme Court’s decision in *Hartney Fuel Oil Co v. Hamer* ([click here](#) for our summary of the decision) and provide direction to Illinois taxpayers as to how sales should be sourced for local sales tax purposes.

As drafted, the regulations are to be effective immediately. Impacted taxpayers should review the implications of the state’s interpretation regarding how to source retail sales. The fact-intensive inquiry may alter the local sourcing of sales for certain taxpayers. [Illinois Department of Revenue, [Hartney Decision Regarding Sales Tax Sourcing Regulations/Emergency and Proposed Rules](#) (1/22/14 update)]

In detail

The emergency regulations note that Illinois local Retailers’ Occupation Taxes are imposed on those engaged in the business of selling tangible personal property at retail within the locality. Determining the location of a business’s

selling activities is critical for situsing transactions. Hartney followed existing Department guidance that allowed businesses to use the single element of purchase order acceptance as the bright-line factor for determining location

of selling and, therefore, the local taxing jurisdiction.

The Illinois Supreme Court in *Hartney Fuel Oil* found that while Hartney had followed regulatory guidance, the regulation improperly narrowed the scope and intent of the

statute. The court struck down the regulation. The Department hosted hearings and solicited feedback from Illinois businesses concerned with the outcome of the anticipated guidance changes.

Fact-intensive inquiry for sourcing

Following the court's analysis, the newly released regulations remove the sole emphasis on purchase order acceptance and support a fact-specific inquiry. The emergency regulations provide factors that should be examined to determine where the business of selling occurs. The emergency guidance provides four 'Primary Factors' and five 'Secondary Factors' to be employed in the determination of where the business of selling takes place.

The Primary Factors are:

- location of officers, executives, and employees with the ability to negotiate and bind the seller
- location where offers are prepared and made
- location where purchase orders are accepted
- location of tangible personal property sold - if such property is in inventory at the time of sale or delivery.

If these factors fail to provide a clear outcome of where the business of selling occurs, the Department has identified the following Secondary Factors to consider:

- location where marketing and solicitation occur
- location where purchase orders are received when purchase orders are accepted, processed, or fulfilled in a location different from where they are received
- location of the delivery of the property to the purchaser
- location where title passes
- location of the retailer's ordering, billing, accounts receivable, and other administrative functions.

Common selling operations

Prior to analyzing Primary and Secondary Factors, a seller may fit into a category that the Department has identified as 'Common Selling Operations.' If a taxpayer falls into one of these categories, the Department has set out the guidance for situsing sales, with no further need to analyze additional selling activities. The common selling operations are:

- over-the-counter sales
- in-state inventory/out-of-state selling activity

- long term blanket contracts
- sales through vending machines
- sales from vehicles carrying uncommitted goods
- sales of coal or other minerals.

The takeaway

Although there is no longer a bright-line test for taxpayers to follow, the Department establishes the requirement for an objective review of the 'activities of selling.' The emergency regulations provide that the Department has the right to look beyond the form of a transaction to its substance to determine where "enough of the business of selling took place."

Impacted taxpayers should review the implications of the state's interpretation of selling activities. The fact-intensive inquiry may alter the local sourcing of sales for certain taxpayers.

The emergency regulations will be effective for a maximum of 150 days. In addition to the emergency rules, the Department also filed proposed permanent rules that are intended to replace the emergency rules.

Let's talk

If you have any questions regarding how the emergency regulations impact your business, please contact:

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