



TAXPAYERS'
FEDERATION
— OF ILLINOIS —

Re-Leveling or Tearing Up the Playing Field in Illinois

October 17, 2024

The information herein is to be used for general guidance and should not be relied on for compliance purposes.

The information provided herein is educational in nature and is based on authorities that are subject to change. You should contact your tax adviser regarding application of the information provided to your specific facts and circumstances.

History

Illinois Tax Types

- Retailers' Occupation Tax (ROT): Imposed on persons engaged in the business of selling at retail tangible personal property (TPP).
- Use Tax: A privilege tax imposed on the purchaser for the privilege of using TPP in the state of Illinois purchased from a retailer anywhere.



Pre-Hartney

- Prior to the *Hartney Fuel Oil Co. v. Hamer* case, Illinois sourced sales for local sales tax purposes based on the location of sales order acceptance.



Hartney Fuel Oil Co. v. Hamer

- The Illinois Supreme Court affirmed an appellate court’s ruling that a company was not liable for local sales taxes imposed at the location of the company’s home office because it accepted purchase orders at a sales office located in a county and city that did not impose local sales taxes.
- The Court ruled that the “business of selling” requires a fact-intensive test to determine the proper situs based on a composite of all the activities related to making a sale.
- Therefore, the “Jurisdictional Questions” embodied in the Department’s Regulation 86 Ill. Adm. Code 220.115, 270.115, and 320.115 are too inconsistent with the statutes and case law and are held invalid.
- (*Hartney Fuel Oil Co. v. Hamer*, Illinois Supreme Court, No. 2013 IL 115130, November 21, 2013)
- As a result of the *Hartney* ruling, the state issued new sourcing rules in 2014.



New Sourcing Rules – 11-Prong Test

- 5 Primary Selling Activities
 - Location of sales personnel exercising discretion and authority to solicit customers on behalf of a seller and to bind the seller to the sale;
 - Location where the seller takes action that binds it to the sale, which may be acceptance of purchase orders, submission of offers subject to unilateral acceptance by the buyer, or other actions that bind the seller to that sale;
 - The location where payment is tendered and received, or from which invoices are issued with respect to each sale;
 - Location of inventory if tangible personal property that is sold is in the retailer's inventory at the time of its sale or delivery; and
 - The location of the retailer's headquarters, which is the principal place from which the business of selling tangible personal property is directed or managed. In general, this is the place at which the offices of the principal executives are located. When executive authority is located in multiple jurisdictions, the place of daily operational decision making is the headquarters.



New Sourcing Rules – 11-Prong Test (Cont.)

- 6 Secondary Activities
 - Location where marketing and solicitation occur;
 - Location where the seller engages in activities necessary to procure goods for sale;
 - Location of the retailer’s officers, executives or employees with authority to set prices or determine other terms of sale if determinations are made in a location different than that identified in subsection (c)(1)(A);
 - Location where purchase orders or other contractual documents are received when purchase orders are accepted, processed or fulfilled in a location or locations different from where they are received;
 - Location where title passes; and
 - Location where the retailer displays goods to prospective customers, such as a showroom.



Exceptions to the Sourcing Rules

- Sales over the Internet – The Department will presume that the retailer's predominant selling activities take place outside of IL. Therefore, such a sale will be subject to Illinois Use Tax.
- In-State-Inventory/Out of State Selling Activity - The jurisdiction where the property is located at the time of the sale or when it is subsequently produced by the retailer will determine where the retailer is engaged in business.
- Sales of Coal or Other Minerals - A retail sale by a producer of coal or other mineral mined in Illinois is a sale at retail in the jurisdiction where the coal or other mineral mined in Illinois is extracted from the earth.



Leveling the Playing Field

- Effective January 1, 2021, Illinois amended the Retailers Occupation Tax and enacted the Leveling the Playing Field for Illinois Retail Act to require remote retailers and marketplace facilitators to collect and remit state and local retailers' occupation tax based on destination sourcing.
- Primary Selling Activity tests and default use tax on sales over the internet no longer apply



Re-Leveling the Playing Field

- Effective January 1, 2025, legislation goes into effect which makes certain Illinois retailers responsible for destination-based sourcing for sales tax purposes.
- Illinois retailers who maintain a place of business in Illinois and sell tangible personal property from a location (or locations) outside Illinois will be required to collect all applicable state and local taxes at the location to where it is shipped or delivered (or the location where the purchaser takes possession).
- This provision attempts to create more consistency in tax collection and promotes more fair tax collection and allocation
 - But does it? Or is this also unconstitutional?



Compliance Challenges

Compliance Challenges in Illinois

- Understanding sourcing and charging correct rates
- Setting up all the locations on the return
- Inputting sales and tax by location on each return
- Managing and reporting credits/returns by location
- Tax engines – What changes will need to be made to software set up and when will that guidance be released?
 - Large number of audits after Leveling the Playing Field solely to assess local taxes.



Example

- Company B has only one location in Indianapolis, IN. However, they have salespeople who regularly travel into Illinois to solicit sales. The majority of the “primary selling activities” still occur in Indiana.
 - Under Leveling the Playing Field Company B would charge 6.25% on all Illinois sales.
 - Under Re-Leveling the Playing Field Company B would need to begin charging tax at the destination rate – the location of its Illinois customers. Indiana has one rate and Company B had previously been charging only one rate in Illinois. They now have to charge a large number of rates.
 - Do they have the systems/ability to charge all these rates on invoices?
 - Do they have the expertise and people resources to file these returns or the funds to outsource?



Example

- Company A has 2 locations in Rolling Meadows, IL and Davenport, IA. The Rolling Meadows location sells in northern Illinois, Indiana and Wisconsin and the Davenport location sells in central/southern Illinois, Iowa and Missouri.
 - Under Leveling the Playing Field, the Rolling Meadows location would charge 10.25% on all Illinois sales and the Davenport location would charge 6.25% on all Illinois sales.
 - Under Re-Leveling the Playing Field, the Rolling Meadows location would continue to charge 10.25% but the Davenport location would need to begin charging tax at the destination rate.
 - Do they have the systems/ability to charge all these rates on invoices?
 - Where or how is ship from location noted?
 - Do they have the expertise and personnel/resources to file these returns or the funds to outsource?



Use Tax Implications

- When does Sellers Use Tax still apply?
 - Serviceman Use Tax
 - Voluntary filers (do not meet nexus requirements)
 - Direct wine shippers
- Consumers Use Tax Applies
 - Items removed from inventory
 - Items purchased from vendors without nexus
- Exemptions lost when ROT applies instead of UT.
 - Temporary Storage



Legal Challenges

PetMed Express, Inc. v. Illinois Department of Revenue

- Operates as a pet pharmacy in the United States.
- Sells prescription and non-prescription medications, foods, supplements, treats, tangible personal property, and certain veterinary services.
- Markets and sells directly to consumers throughout the United States including Illinois, through its website, television advertising, direct mail, toll-free number and mobile app.



PetMed Express, Inc. v. Illinois Department of Revenue (Cont.)

- Count I – The assessment violates the commerce clause of the U.S. Constitution as it discriminates against interstate commerce and creates an undue burden on out-of-state retailers.
 - Leveling the Playing Field Violates the Commerce Clause Because it Discriminates Against Interstate Commerce.
 - Leveling the Playing Field Violates the Commerce Clause By Imposing an Undue Burden on Remote Sellers.
- Count II – The Department’s assessment of tax on PetMed’s sales erroneously contravenes the uniformity requirements of the Illinois Constitution.
- Count III – The Department’s delay in completing and processing the audit contravenes the Taxpayer Bill of Rights and an additional interest accrued as a result of such delay must be abated.



PetMed Express, Inc. v. Illinois Department of Revenue (Cont.)

- Case dismissed with prejudice on October 1 because parties reached a settlement
- With no decision, taxpayers are left without guidance regarding constitutionality of the law



Coast to Coast Computer Products, Inc. v. The Illinois Department of Revenue

- Telemarketing company that primarily sells toner, computers, printers, software and other computer-related supplies.
- Based in California and also maintained an office in Nevada.
- No location, property, or offices in Illinois and has no Illinois-based employees, representatives, or agents.
- Never advertised locally in Illinois through media such as local television stations, local radio stations, local newspapers, or local billboards.



Coast to Coast Computer Products, Inc. v. The Illinois Department of Revenue (Cont.)

- Count I –The Department improperly taxed sales for resale.
- Count II – The Department improperly taxed sales to exempt purchasers.
- Count III – Requiring the Petitioner to collect Illinois use tax less than four months after Wayfair decision creates an unconstitutional undue burden.



Coast to Coast Computer Products, Inc. v. The Illinois Department of Revenue (Cont.)

- Count IV – Illinois' economic nexus statute violates the commerce clause as applied to petitioner because the petitioner does not have extensive virtual contacts with Illinois
- Count V – Illinois' Leveling the Playing Field Act violates the Commerce Clause because it discriminates against interstate commerce and remote retailers such.



Norton Company v. Department of Revenue of Illinois

- Massachusetts corporation, manufacturers and sells abrasive machines and supplies.
- Operated a branch office and warehouse in Chicago from which it makes sales at retail.
- Carries inventory of about 3,000 most frequently purchased items.
- Serves cash customers and those who credit the home office has approved.
- For those with no established credit, those who order items not from local stock, and those who want special equipment it receives orders and forwards to home office.
- Chicago office and reconsigns the separate orders in their original package to customers.



Norton Company v. Department of Revenue of Illinois (Cont.)

- The Supreme Court of Illinois found that the presence of petitioner's local retailer outlet, in the circumstances of this case, was sufficient to attribute all income derived from Illinois sales to that outlet and render it taxable.
- The US Supreme Court decided that the tax is sustained on all sales to Illinois customers, except on orders sent directly by customers to the head office and shipped directly to the customers from the head office.

“Corporation has gone into the State to do local business by state permission and has submitted itself to the taxing power of the State, it can avoid taxation on some Illinois sales only by showing that particular transactions are dissociated from the local business and interstate in nature. The general rule, applicable here, is that a taxpayer claiming immunity from a tax has the burden of establishing his exemption.”



Questions?

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