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Bulletin

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Leased Motor Vehicle Changes and New Reporting Requirements

**To: Licensed Motor Vehicle Dealers, Leasing
Companies, License and Title Agencies, and
Electronic Registration and Title Program
Vendors**

This bulletin is written to inform you of recent changes; it does not replace statutes, rules and regulations, or court decisions.

This bulletin explains the changes resulting from the passage of Public Act 98-628. This Act changes the basis for determining the “selling price” for certain leased motor vehicles. Also, starting January 1, 2015, all lease transactions will be reported on different returns than those currently used to report motor vehicle transactions.

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Public Act 98-628 amends the Retailers’ Occupation Tax Act and the Use Tax Act to provide for an alternate method of determining the selling price subject to sales and use taxes for certain motor vehicles sold for the purposes of being leased. Per Public Act 98-1080, this change is effective **January 1, 2015**.

You must use this alternate selling price on motor vehicles that qualify, and the following conditions will apply when you use the alternate selling price:

- Trade-in credit is not allowed to reduce the selling price.
- Credit for tax paid on a previously leased motor vehicle cannot be used against the tax liability when it is sold at the end of the lease.
- Additional charges at the end of the lease (*e.g.*, additional charges for excess wear or mileage or for retaining possession of the motor vehicle beyond the term of the lease) must be reported by the leasing company on a new form using the same taxable location and rate as the original return that reported the transaction.

To accommodate these changes, the Department

- created new returns to report *all* lease transactions starting January 1, 2015:
 - Form ST-556-LSE, Transaction Return for Leases,
 - Form RUT-25-LSE, Use Tax Return for Lease Transactions, and
 - Form LSE-1, Tax Return for Vehicle Leasing Companies (used to calculate additional tax due that was not previously reported); and
- revised existing returns to remove their prior applicability for lease transactions:
 - Form ST-556, Sales Tax Transaction Return (now used to report all other (non-lease) vehicle, watercraft, aircraft, trailer, and mobile home transactions), and

- Form RUT-25, Vehicle Use Tax Return (now used to report all other (non-lease) motor vehicle, watercraft, aircraft, trailer, mobile home, snowmobile, or all-terrain vehicle (ATV) transactions).

How is the selling price determined for these motor vehicles?

The selling price for leased motor vehicles is determined in one of two ways:

- the actual selling price, or
- the amount due at lease signing, plus the total amount of payments over the term of the lease.

What lease transactions must use this alternate selling price?

Note: The following provisions regarding the alternate selling price apply only to sales and purchases for lease occurring on or after January 1, 2015. The alternate selling price (*i.e.*, the amount due at lease signing, plus the total amount of payments over the term of the lease) must be used when a qualifying motor vehicle is sold for the purpose of being leased under a fixed-term lease contract for a period of more than one year. Qualifying motor vehicles are

- first division motor vehicles; and
- second division motor vehicles that are
 - self-contained motor vehicles designed or permanently converted to provide living quarters for recreational, camping, or travel use, with direct walk-through access to the living quarters from the driver's seat;
 - motor vehicles of a van configuration designed to transport not less than 7 and not more than 16 passengers; and
 - motor vehicles having a gross vehicle weight rating (GVWR) of 8,000 pounds or less.

Examples of the above listed motor vehicles generally include automobiles, pickup trucks and sport utility vehicles with a GVWR of 8,000 pounds or less, certain vans, motorcycles and motor-driven cycles, and motor homes and recreational vehicles.

For all other leases, you must use the actual selling price to calculate the sales and use taxes due.

Note: The Illinois Vehicle Code defines a first division motor vehicle as one designed to carry not more than 10 persons. The following are second division motor vehicles:

- a motor vehicle designed to carry more than 10

persons;

- a motor vehicle designed or used for living quarters;
- a motor vehicle designed for pulling or carrying freight, cargo, or implements of husbandry; or
- a first division motor vehicle remodeled for use and used as a second division motor vehicle.

Is the alternate selling price used for all lease transactions for qualifying items?

No. Even if the motor vehicle is a qualifying motor vehicle and the lease period exceeds one year, you must use the actual selling price of the item if the term of the lease is not a defined period. This includes leases with a defined initial period with the option to continue the lease on a month-to-month or other basis beyond the defined initial period.

Example: A new vehicle dealer sells a vehicle to a leasing company and acts as a representative of the leasing company and simultaneously enters into a lease contract for the vehicle with the customer at the dealership. If the terms of the lease state that the initial period of the lease is for one year plus one day and that the lease will continue from month to month thereafter until the lessee (customer) terminates the lease, then this lease does not qualify as a lease for a defined period. As a result, the "selling price" of the vehicle for calculating sales tax is the actual price, minus trade-in credit, that the dealership charges to the leasing company to purchase the vehicle.

Note: If, however, a qualifying vehicle is leased for a defined period (*e.g.*, 24, 36, or 48 months) but the contract contains a provision regarding the "Return of the Vehicle" or a similar provision that allows for the lease to continue for a short period (*i.e.*, 1 to 6 months) but only after the lessee (customer) fails to meet the original terms of the lease or only with further agreement by the leasing company, then this provision does not disqualify the sale from being eligible for the new alternative definition of "selling price."

What form will I use to report tax on these items?

Effective January 1, 2015, Form ST-556-LSE will be used for all sales for lease, and Form RUT-25-LSE will be used for all purchases for lease. Whether the tax is calculated using the actual selling price or the value of the lease, all lease transactions must be reported on these new LSE forms, starting January 1, 2015. For all sales that are not for lease, you will continue to use Form ST-556, Sales Tax

Transaction Return. Purchases that are not for lease will continue to be reported by the item's user on Form RUT-25, Vehicle Use Tax Return, at the time the user titles or registers the item in Illinois.

What selling price should I use when calculating additional municipal or county vehicle use tax?

When calculating additional municipal or county vehicle use tax, you should use the selling price you reported on Form ST-556, Form ST-556-LSE, Form RUT-25, or Form RUT-25-LSE.

Are there any other new filing requirements?

Yes. We also are introducing the new Form LSE-1, Tax Return for Vehicle Leasing Companies. Form LSE-1 is only required to be filed for vehicles sold for lease after January 1, 2015, if the selling price reported on either Form RUT-25-LSE or Form ST-556-LSE was the amount due at lease signing, plus the total amount of payments over the term of the lease. Form LSE-1 is used to calculate tax due on any additional taxable amount that was not previously reported on either Form RUT-25-LSE or Form ST-556-LSE. Examples of additional taxable amounts include charges for excess wear and tear, excess mileage charges, and lease payments not reported on the original return. This return must be filed by the leasing company that has been leasing an item that the user has titled or registered in Illinois. Form LSE-1 is filed on a monthly basis and includes the additional taxable amounts from all leases for that month.

Do I need to register to file Form LSE-1?

Yes. If you are a leasing company that has been leasing an item that the user has titled or registered in Illinois you must register with the Department to file Form LSE-1. To register, you can submit Form REG-1, Illinois Business Registration Application, electronically using MyTax Illinois, available on our website at tax.illinois.gov, or you can submit a paper registration application. However, if you have previously registered with the Department for other taxes, you cannot use MyTax Illinois to submit Form REG-1 and must submit your registration application on paper.

Do I need to register to file Form ST-556-LSE if I am already registered to file Form ST-556?

No. Your registration to file Form ST-556 also allows you to file Form ST-556-LSE.

Will there be changes to existing tax forms?

Yes. To implement the new legislation, we have revised Form RUT-25 and Form ST-556, as well as the amended forms of each of those returns.

Who will file Forms RUT-25 and RUT-25-LSE?

Forms RUT-25 and RUT-25-LSE are use tax returns and are filed by the user of the item when it has been purchased or leased from an unregistered out-of-state dealer, lending institution, leasing company selling at retail, or retailer. This situation most often occurs when an item has been purchased or leased outside of Illinois but is subsequently brought into Illinois to be titled or registered.

Who will file Forms ST-556 and ST-556-LSE?

Forms ST-556 and ST-556-LSE are filed by Illinois dealers that sell items that must be titled or registered by an agency of Illinois state government. Form ST-556 also is filed by some leasing companies who are in the business of selling items that must be titled or registered when those items are located in Illinois at the time of the sale. See 86 Ill. Adm. Code Section 130.2013(h).

How do I file Forms ST-556 and ST-556-LSE?

Forms ST-556 and ST-556-LSE can be filed electronically using MyTax Illinois, available on our website at tax.illinois.gov. They also can be filed electronically through a Secretary of State-approved service provider using the Electronic Registration and Title program (ERT).

You can request preprinted returns using MyTax Illinois. You also can request that the Illinois Department of Revenue issue you paper preprinted forms by calling our Central Registration Division at **217 785-3707**. The preprinted forms display information for each of your business locations.

How do I file Forms RUT-25 and RUT-25-LSE?

Forms RUT-25 and RUT-25-LSE can be filed electronically through an approved ERT service provider. They also can be filed on paper. Paper forms are distributed to titling agencies so that they are available when the user titles or registers the item in Illinois.

How do I file Form LSE-1?

Form LSE-1 must be filed electronically and any accompanying tax payment must be paid electronically. MyTax Illinois allows you to file Form LSE-1 and make an electronic payment of any tax due.

Will the correspondence I receive from the Department change for Form ST-556-LSE?

No. The correspondence for Form ST-556-LSE will be incorporated into the correspondence that you currently receive for Form ST-556. Your Taxpayer Statement, Detailed Liability Statement, and Credit Activity Statement will show amounts for each return type, but otherwise the correspondence we send you will remain unchanged.

Can I apply credit resulting from an ST-556 transaction to Form ST-556-LSE?

Yes. If you have available credit resulting from an overpayment on a transaction reported on Form ST-556, you can apply that credit to a transaction reported on Form ST-556-LSE. You also can apply available credit resulting from an overpayment on a transaction reported on Form ST-556-LSE to a transaction reported on Form ST-556.

When can I claim credit for taxes paid on a lease transaction if I sell an item at the end of a lease?

If you are a leasing company leasing an item that must be titled or registered and you sell that item in Illinois at the end of the lease and that sale is subject to Retailers' Occupation Tax, you must report the sale on Form ST-556. If the selling price reported on the return for the original lease transaction was the actual selling price of the item (*i.e.*, method of calculation required prior to January 1, 2015), you can claim credit for tax previously paid on Line 10 of Form ST-556. See 86 Ill. Adm. Code Section 130.2013(h). If the selling price for the original lease transaction was the value of the lease (*i.e.*, method of calculation available on or after January 1, 2015), you cannot claim credit for tax previously paid.

When can I claim trade-in credit on Form ST-556-LSE?

If the selling price for the lease transaction is the actual selling price of the item, you can claim credit for a qualified trade-in on Line 2 on Form ST-556-LSE. If the selling price for the lease transaction is the value of the lease, you cannot claim qualified trade-in credit on Form ST-556-LSE. You can accept a traded-in vehicle from your lease customer as part of the transaction, but you cannot deduct the value of the traded-in vehicle from the selling price of the leased item when calculating the tax due.

Example transaction:

Your customer wants to lease a vehicle with a retail selling price of \$10,000. The leasing company offers a lease contract stating that the customer must pay \$500 at the start of the contract and \$200 per month for 36 months. The customer has a vehicle to trade in that you value at \$500.

If the vehicle to be leased does not qualify for the alternate selling price, the selling price on Form ST-556-LSE would be the actual selling price of \$10,000. Because the selling price is the actual selling price, you could reduce this amount by the \$500 value of the trade-in, and the amount you would use to calculate the tax would be \$9,500.

If the vehicle does qualify for the alternate selling price, the selling price on Form ST-556-LSE would be the value of the lease contract, which in this case is \$7,700 (\$500 down, plus \$200 per month for 36 months). Because the selling price is the value of the lease contract, you cannot reduce this amount by the \$500 value of the trade-in, and the amount you would use to calculate the tax would be \$7,700. However, you are allowed to apply the trade-in credit in other ways that do not affect the tax calculation (*e.g.*, crediting it toward the amount owed on the lease). In this example, assuming the leasing company agrees, the \$500 trade-in credit could be used to pay the amount owed at the start of the lease.

Assume further that the customer owes at the end of the lease an additional \$300 to the leasing company for excess wear and tear. If the original Form ST-556-LSE filed at the start of the lease used the value of the lease as the selling price (in this case, \$7,700), the leasing company must file Form LSE-1 to report the additional tax due on this \$300 for wear and tear. To calculate this additional tax due, Form LSE-1 uses the same tax rate and sales location as that used on the original Form ST-556-LSE or Form RUT-25-LSE, as applicable. If the original Form ST-556-LSE had used the actual selling price of \$10,000 because the vehicle did not qualify for the alternate selling price, the leasing company does not need to file Form LSE-1 for this lease.