

SALES & USE TAX ALERT

Vol. XV, No. 1, January 15, 2005

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CALIFORNIA TAX GUIDE

CCH's *California Taxes, Guidebook to (2005)* covers all taxes levied by the state. The 2005 Guidebook reflects significant new legislation, regulations, court decisions, State Board of Equalization decisions and a new bonus CPE course supplement. Pages: 816. Price: \$59.50. Call (800) 248-3248.

COMING SOON

- Arizona incentives
- Ohio issues guidance on exempt Internet equipment
- South Carolina tells grocers how to refund sales tax to customers

■ GETTING STARTED

New Year checklist: Six actions to take now to prevent trouble later

As sales tax managers face a new year, the workload already mounts. If your company's fiscal year ended Dec. 31, you are busy with year-end closing activities. And financial auditors may be pressing you for figures estimating upcoming sales tax liabilities. Though finding time may be difficult, completing certain proactive measures at the front side could greatly enhance sales and use tax compliance throughout the year. Plus, a little preventative work now can go a long way in halting mistakes before they show up in an assessment, experts say.

"It's the first of the year, and people are busy," says **Ned A. Lenhart**, president of **Sales Tax Advisors of Georgia P.C.** in Atlanta. "But if you take a little time and get your arms around it early, you save yourself pain later."

1. Update tax rates and tax matrices

Review and update tax rates and tax matrices for rate and law changes that became effective Jan. 1, 2005.

Often, tax rates become effective at the beginning of the year, as well as exemptions. Some exemptions may have expired as of last year.

For example, Georgia for the past five years has been phasing in an exemption for repair parts for machinery and equipment, Lenhart says. This year, such repair parts are fully exempt as opposed to 80% exempt in 2004.

"You really can't assume that every tax rule is going to be the same from Dec. 31 to Jan. 1," he adds. "Unfortunately, some companies aren't aware of the changes until they're well into the year—they've either overcharged or undercharged."

Look back in your tickler file, says **Diane Yetter**, president of **Yetter Consulting Services Inc.** in Chicago. Pay attention to the many changes legislated by states to conform with the Streamlined Sales Tax Project. Check for local rate changes.

2. Update sales tax calendar

Update your sales and use tax calendar for changes in filing frequency that are effective Jan. 1, 2005.

Check all the states where you conduct business to see if a change in filing frequency has occurred. While you are at it, see if your com-

pany should be changing frequency for other reasons. Perhaps your company was required to file only quarterly when you first registered. Since then, your company has grown, sales have increased and now you should now be filing monthly, Lenhart notes.

What about changes in the amount of sales tax deposits for those jurisdictions that require sales taxpayers to pay a monthly deposit, then reconcile the amount when the return is later filed? Even if a law change has not occurred, have you calculated the amount of your deposit to see if it has changed because of a change in average monthly sales in 2004 compared to 2003?

Also, many states have reduced their thresholds for electronic funds transfer and e-filing. Your company may now be required to change its remittance from paper check to EFT. Many of these thresholds are very low, Yetter warns.

3. Compare tax types

Compare state and local sales tax filings with state income tax and franchise filings and property tax filings and then evaluate any discrepancies.

At the beginning of the year, property taxes may be due. Perhaps state corporate income tax extensions must be filed. It's a time of a high concentration of filings, so take a moment to compare. See if you should be collecting sales or use tax in the jurisdictions where you are filing franchise tax or any other tax. There may be a reason why your company is not. But this is a good time to make sure.

"It forces people to ask the question again," Lenhart says. "Circumstances may change. It's a good time to take a big picture look and make sure you're not missing returns that need to be filed."

Payroll tax filings can tell you where your company has employees. Do you have a new customer in a certain jurisdiction? Yetter asks. Are you filing there or do you need to consider it?

4. Check resale certificates

Review the resale exemption certificate file; obtain new ones for those that have expired.

Some state resale exemption certificates expire each year. Others expire every five years. Lenhart suggests focusing on your largest customers—that is, your largest exposures to collection liability—first.

"Some companies get a resale certificate and never look at it again," he says.

Be sure to retain expired certificates. Lenhart recalls a client who got the new certificates and immediately disposed of the old certificates. Wrong! Keep the old certificates until corresponding audit periods have closed. Getting copies could be tough if a customer has gone out of business or the business relationship has soured.

"Even if a state doesn't have a hard expiration date, it's a good idea to update periodically," Yetter says. "I recommend every three to five years."

She suggests dividing your list of customers into thirds or fifths and doing that much each year.

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5. Follow legislation

Devise a system to track legislative developments affecting sales and use tax in your state.

Appoint a sales tax staff member to follow developments in the legislative session that begins this year, suggests **B.J. Pritchett**, president of **Pritchett Sales & Use Tax Consulting** in Hot Springs National Park, Arkansas. Track bills that will affect sales and use tax rates and exemptions.

But don't just stand on the sidelines. Fight legislation that will hurt your bottom line. Get to know your local legislator, she says.

But can a medium-sized business make a difference? You don't have to do it all yourself, notes **Yetter**. Join industry associations, professional societies for CPAs, the chamber of commerce. For instance, in Illinois, numerous small software companies defeated a 2003 proposed tax on computer services.

Contrarily, Pritchett notes that Arkansas veterinarians failed to mobilize and now find their services taxable.

6. Educate employees

Create a plan to educate employees about what triggers sales tax liabilities.

Companies should make sales tax education a thorough, ongoing affair, Pritchett says. Don't just send the comptroller or managers to sales tax seminars; send the people who will be handling sales taxes daily, those in accounts receivable and accounts payable, perhaps.

"You need to send the right people to the seminars to get the end result of saving your company money," Pritchett says. "The supervisor may have all the knowledge but doesn't necessarily disseminate it."

Analyze the results of last year's and ongoing state audits of your company. Decide what changes you should make to improve compliance and avoid previous mistakes. Pass that information onto your staff. Be ready by the end of the first quarter to spread that knowledge through the other departments of the company.

Educate yourself. Study the law and the regulations for certain sales tax exemptions. The law is binding, but the regulations are only guiding. You may discover an assessment that should be opposed.

Be sure after your research to create cheat sheets, notes to keep at your desk or stuck on your computer, to cover differences among jurisdictions.

Editor's note: *Lenhart can be reached at (770) 985-9573; Yetter at (312) 701-1800; Pritchett at (501) 922-4327.* ♦

■ CHEMICAL CATALYSTS QUALIFY

'Apparatus' expands industrial machinery exemption in Tennessee Supreme Court

A recent taxpayer victory at the Tennessee Supreme Court further expanded the sales and use tax exemption for industrial machinery while checking the Dept. of Revenue's resistance to an earlier decision by the court.

In *Eastman Chemical Co. v. Johnson*, Dkt. No. M2002-02114-SC-R11-CV, the state Supreme Court ruled that catalysts are exempt as industrial machinery.

Function over appearance

"They (the justices) looked to the function of the item rather than its appearance or traditional conceptions of equipment," says **Michael G. Stewart** of **Waller Lansden Dortch & Davis**. "Any manufacturer with operations in Tennessee will benefit because they can rely on an expansive reading."

New industries take note

Stewart points to the chemical and biotech industries as beneficiaries of the decision.

"The case provides a lot of support for taxpayers who are fighting attempts by authorities to limit exemptions to traditional, old economy manufacturing operations that have already qualified," he adds. "Obviously, in this day and age, we are moving from a hard manufacturing economy to an economy that includes biotechnology, high-tech manufacturing, types of manufacturing that have components that don't look like traditional machines that have gears and spindles."

Manufacturers that have been paying tax on catalysts or other items that may qualify under the newly expanded definition of industrial equipment should apply for refunds, Stewart advises.

DOR pushes back

Don't look for the state to quit trying to read the statute narrowly, though.

Deputy Attorney General Larry Lewis represented the state. "This decision obviously decided chemical catalysts," Lewis allows.

"It was our position that a chemical catalyst is not a piece of industrial equipment," says **Christine Lapps**, senior tax counsel for the DOR. "These chemical catalysts are like an ingredient you add in a recipe to get a desired result. It's an ingredient that doesn't become part of the finished product."

Lapps doesn't see a broad victory for taxpayers. "I can't think of any other industries," she says.

At issue was whether the catalysts constitute "machinery, apparatus and equipment with all associated parts, appurtenances and accessories" as defined in Tenn. Code Ann. §67-6-102(13)(A) (1998). In denying Eastman its refund, the Dept. of Revenue was pushing back against an earlier decision by the Tennessee Supreme Court, the seminal *AFG Indus. Inc. v. Cardwell* (1992), Stewart notes.

In that case, the court held that tin ingots were exempt when melted to form a bath on which molten glass was conveyed and shaped.

The court ruled that the dictionary definition of "apparatus" includes "the totality of means by which a designated function is performed or a specific task executed."

The *AFG* decision expanded the definition of industrial machinery and equipment after legislators changed the wording in 1984:

Machinery, apparatus and equipment with all associated parts, appurtenances and accessories, including hydraulic fluids, lubricating oils, and greases necessary for operation and maintenance, repair parts and any necessary repair or taxable installation labor therefor, which is necessary to, and primarily for, the fabrication or processing of tangible personal property for resale and consumption off the premises...where the use of such machinery, equipment or facilities is by one who engages in such fabrication or processing as one's principal business...

The court consequently reversed an earlier decision, so that in *Tibbals Flooring Co. v. Huddleston* (1994) a system of fans and vacuums which removed sawdust and wood shavings from a wood cutting and sanding operation and delivered the shavings to boilers for creating steam and electricity was exempt.

'Totality of means'

In *Eastman Chemical*, the Supreme Court ruled that the catalysts are not raw materials or ingredients used in the production of the goods. "Like the tin ingots in *AFG Indus.*, the catalysts used by Eastman are components of the equipment and apparatus used in the manufacturing process, and do not become part of the final product," the justices ruled. "The catalysts are an integral part

of the totality of means whereby the manufacturing process is accomplished."

Editor's note: *Stewart can be reached at (615) 850-8856; Lewis at (615) 741-2968; Lapps at (615) 253-0600.* ♦

■ DESPITE DOMICILED ELSEWHERE

Alabama trucking firms 'up in arms' over long-haul use tax assessments

A series of Administrative Law Div. decisions have upheld use tax assessments on long-haul tractors and trailers, causing concern among Alabama trucking companies.

"This is a relatively new issue, but a lot of trucking companies are up in arms," observes **Bruce P. Ely** of **Bradley Arant Rose & White LLP** in Birmingham. "And the dollars can be quite substantial."

The latest, *Boyd Brothers Transportation Inc. v. Alabama Dept. of Revenue*, Dkt. No. S. 04-203, likewise held that Alabama use tax is due on truck tractors and trailers purchased outside Alabama and used in interstate commerce.

In *Boyd Brothers*, Judge Bill Thompson cited his own decision in another Administrative Law Div. case, *Glenn McClendon Trucking Co. Inc. v. State*, Dkt. No. S01-206, as well as a pending federal bankruptcy case, notes **James M. Sizemore Jr.**, an attorney in Montgomery, who represented Boyd Brothers.

Sizemore adds that the truck tractors in *Boyd* were domiciled outside Alabama. Boyd Brothers, headquartered in Clayton, Alabama, bought 740 truck tractors and 500 trailers tax-free outside Alabama. The trucks and trailers were first used outside Alabama. Boyd brothers were assessed over \$900,000.

The issue in the case is whether the tractors and trailers were subject to the use tax levied on motor vehicles under Code of Ala. 1975, §40-23-61(c) or the "alternative" use tax levied at Code of Ala. 1975, §40-23-619(e).

"The tax applies if property is bought or used in Alabama," Sizemore says. "There must be evidence of intent (to use in Alabama)."

But Boyd Brothers trucks plied Alabama highways over a year after purchase, he adds.

Fleming Foods cited

Judge Thompson cited the Alabama Supreme Court decision in *Ex parte Fleming Foods Inc.* (1994), which found use tax under §40-23-61(c) due on trucks purchased outside of Alabama, then used in Alabama and other states. In that decision, the justices ruled that the Alabama use tax is a nonrecurring transac-

tional tax on a discrete intrastate event, i.e. the use of tangible personal property in the state. The use tax "is not imposed upon revenues derived from carrying on interstate business or interstate commerce...This is not taxation of interstate commerce," according to the justices. That decision also found a substantial nexus created by Fleming Foods' trucks operating in Alabama. Likewise, the Alabama use tax satisfied the four-pronged Commerce Clause test of the U.S. Supreme Court decision in *Complete Auto Transit Inc. v. Brady* (1977).

In *McLendon*, the tractors were purchased tax-free outside of Alabama, and also registered and placed into service outside Alabama. The taxpayer maintained the trucks are not subject to use tax because they were first used outside the state, citing Dept. Reg. 810-6-5-.25(1): "Where the owner of tangible personal property has purchased such property for use outside of Alabama and has, in fact, used it outside of Alabama, no use tax will be due by the owner because of the later storage, use or consumption of it in Alabama."

McLendon is currently on appeal to the Randolph County Circuit Court. *Whatley Contract Carriers LLC v. State*, Dkt. No. U. 03-372, is on appeal to the Henry County Circuit Court. In *Whatley Contract Carriers*, the taxpayer purchased trucks in Alabama tax-free using the sales tax drive-out exemption, then used them in multiple states including Alabama.

Attacking 'domicile'

Boyd Brothers Transportation asserts that its case is different than the other two cases because tractors and trailers were domiciled in other states. Yet Judge Thompson cited the U.S. Bankruptcy Court for the Middle District of Alabama *In re Culverhouse Inc.*, Dkt. No. 03-12288-WRS, to attack the concept of domiciling trucks in other states. That decision states that "the reference to domicile was descriptive rather than limiting."

Sizemore states that if Alabama attempts to tax tractors domiciled in other states, it would have to tax those vehicles as interstate commerce and apportion the tax among other states, as well.

"I don't think it (Alabama) can," he says.

Controlling decision far off

Ely notes that several years could pass before an appeal results in a precedent-setting decision made by a higher court.

"I feel an appellate court will resolve this case in favor of the taxpayer, though it may take a while to get there," says Sizemore.

Editor's note: *Ely* can be reached at (205) 521-8681; *Sizemore* at (334) 265-1121. ♦

Retail giants settle Illinois whistleblower suits

Three large retailers have agreed to pay Illinois more than \$2.4 million to settle lawsuits alleging that they improperly failed to collect Illinois use tax on Internet sales in the past. Illinois Attorney General Lisa Madigan announced the settlements with Wal-Mart Stores, Inc., and its affiliate, Wal-Mart.com, Inc.; Target Corp. and its affiliate, Target.Direct, LLC; and Office Depot, Inc., and its affiliate, Viking Office Products, Inc.

According to a Dec. 10, 2004 press release from the attorney general, actions against the retailers, and numerous others, were originally filed by the Chicago law firm of Beeler, Schad, and Diamond, P.C. under the Illinois Whistleblower Reward and Protection Act. Attorney General Madigan subsequently joined those actions. The complaints alleged that, despite the dot.com subsidiaries' assertion that they lacked nexus with Illinois, the subsidiaries had established a presence in the state when their brick-and-mortar affiliates in Illinois accepted returns of merchandise bought online.

There are reported to be approximately 60 similar lawsuits still pending in the circuit court against other retailers. The same law firm that initiated the Illinois lawsuits brought similar *qui tam* actions against online retailers in Tennessee. However, all of the Tennessee actions were dismissed, and the Tennessee Legislature amended state law to prohibit future suits. ♦

SALES TAX SEMINARS

The Sales Tax Institute has slated two seminars in Dallas, Texas in February. Register early to save.

A morning seminar on Feb. 1, 2005, at The Adolphus, 1321 Commerce Street, "Sales Tax Concepts," covers definitions, major exemptions, inter-company transactions and administrative issues regarding tax collection, remittance and reporting. Price: \$135 if received by Jan. 11, 2005; \$160 thereafter.

"Basics of Sales and Use Tax" is a three-day seminar for individuals with less than four years sales tax experience. Topics will include constitutional basis for the tax, leading cases, tax basis and administration of the tax including collection and remittance procedures and audit defense. The course also includes industry-specific sections. The format is lecture, case study and group discussion. Price: \$625 if received by Jan. 5, 2005; \$650 thereafter.

Visit www.salestaxinstitute.com or call (312) 701-1800.

STATE UPDATES

ALABAMA

An out-of-state taxpayer who provided health and medical record processing services by using employees in Alabama to either scan and save records to the taxpayer's facility outside Alabama or to mail photocopies of records to customers was not subject to Alabama sales and use tax on the certain fees. Exempt fees included those for electronically accessing the records via the Internet, scanning, postage, tracking and confirming the status of information being delivered, certifying and notarizing the information, affirming that the information was suitable to be used in a legal deposition, or electronically storing the information. (*Revenue Ruling No. 04-003, Dept. of Revenue*)

ARIZONA

A transaction privilege and use tax rule regarding contractor reporting requirements is repealed because it contains redundant, erroneous, and misleading information. The requirement to report on a progressive billing or cash receipts basis is redundant and also confusing because "progressive billing" and "cash receipts" are not defined in the rule. The rule provision allowing unused portions of allowable deductions to be carried forward is incorrect because a deduction arises from and operates on the gross proceeds or gross income of an individual transaction. The requirement that homebuilders must report the total selling price as income at the time of closing escrow or transferring title is misleading because it assumes that the taxpayer is a party to the close of escrow or transfer of title. The requirement incorrectly allows taxpayers to delay reporting until their project is complete. (*R15-5-617, DOR, repealed effective Feb. 5, 2005*)

CALIFORNIA

John Chiang was unanimously elected to serve as the new chair of the State Board of Equalization, replacing Carol Migden who stepped down to assume her seat in the State Senate. Member Claude Parrish was re-elected to service as Vice-Chair of the SBE. Chiang identified several key issues for the SBE for the next year, including implementation of the sales and use tax amnesty, cracking down on the sale of counterfeit cigarettes in the underground economy, and the e-waste recycling fees imposed on sales of televisions and computer monitors. (*News Release 62-G, SBE, Dec. 14, 2004*)

A taxpayer's motion for class certification in his challenge of a city's decision to refund only a portion of the revenue from a local utility users' tax that had been declared invalid failed because the taxpayer was unable to provide signed verifications by individual

members of the purported class. Subsequent to the 2000 general election, the city began collecting a utility users' tax even though the measure had not passed by the required two-thirds supermajority. Following a court decision declaring the tax invalid, the city repealed the ordinance. However, the city had adopted a claims ordinance in August 2001 prohibiting class claims on tax refunds unless each member of the class files an individual claim and establishing a one-year statute of limitations on tax claims. (*Ozenick v. City of Roseville, Court of Appeal, Third Appellate District, Docket No. C046459*)

COLORADO

The following taxes now are reported on Form DR 7050, Colorado Monthly Fuel Tax Return: (1) aviation gasoline and/or jet fuel (previously, Form DR 0120); (2) environmental response surcharge (previously, Form DR 0129); and (3) gasoline and/or special fuel distributor taxes (previously, Form DR 7057). (*FYI General 15, Dept. of Revenue, December 2004*)

CONNECTICUT

The Dept. of Revenue Services has notified several thousand businesses by mail that they will be required to pay sales and use taxes and file sales and use tax returns electronically beginning with payments and returns due on or after March 31, 2005. The department estimates that for most affected businesses, this requirement will apply beginning with their February 2005 monthly sales and use tax return and payment due on or before March 31, 2005. Taxpayers will be able to make an electronic payment via Fast-File or Electronic Funds Transfer (EFT), but Fast-File is the only option for filing a return. (*Press Release, DRS, Dec. 17, 2004*)

FLORIDA

Sales and use taxpayers that collected in excess of \$1,000 during the period of July 1, 2003, through June 30, 2004, will be required to remit payment and file a return on a monthly basis beginning with the initial collection period of Jan. 1-31, 2005. Although technically due on the first of the following month, returns will not be deemed late provided the filings are postmarked on or before the 20th day of the following month. Moreover, in the event the 20th day of the following month falls on a Saturday, Sunday, or federal or state holiday, the deadline will be extended until the next business day. Taxpayers may request permission to file using their previous filing frequency if the \$1,000 collected during July 1, 2003, through June 30, 2004, was not a result of recurring business activity. (*Tax Information Publication, No. 0401A-12, Dept. of Revenue*)

Beginning Jan. 1, 2005, taxpayers who paid more than \$1,000 in communications services tax during the period from July 1, 2003, through June 30, 2004, are required to file monthly. Taxpayers who are not required to file electronically will receive a personalized return, Form DR-700016, monthly. Monthly returns are due on the first day of the month and are late after the 20th day of the month following the reporting period. Returns for the quarterly, semiannual, or annual reporting period ending Dec. 31, 2004, are still due no later than Jan. 20, 2005. (*Tax Information Publication, No. 04A19-07, Dept. of Revenue*)

A Dept. of Revenue publication explains the sales tax credit for motor vehicles brought into the state from another state in which a like tax was lawfully imposed and paid. The publication provides a state-by-state breakdown of (1) the rate of sales tax charged in other states; (2) whether Florida grants a credit for the other state's tax, and vice versa; and (3) the application of other states' taxes on sales of motor vehicles. The publication also contains information concerning the imposition of Florida use tax on motor vehicles exported to territories or foreign countries. (*Tax Information Publication, No. 04A01-14, DOR*)

Sales and use tax taxpayers that file electronically will not be automatically receiving a coupon book or instructions for the forthcoming tax year. However, sales tax electronic filers will continue to receive an annual resale certificate, and use tax electronic filers will continue to receive a 2005 Discretionary Sales Surtax Rate Sheet (Form DR-15DSS). (*Tax Information Publication, No. 04A1-11, Dept. of Revenue*)

ILLINOIS

The Dept. of Revenue adopted regulations to implement P.A. 93-31 (SB1733) of 2003, which repealed the gas revenue tax exemption for charges for gas or gas services to customers that purchased gas from out-of-state suppliers on or before March 1, 1995. Additionally, the law enacted the Illinois gas use tax. P.A. 93-31 is effective for tax years beginning on or after Oct. 1, 2003. The regulations provide that the Illinois gas use tax is imposed on the purchase of natural gas from outside Illinois for use or consumption in the state. The gas use tax for self-assessing purchasers is imposed at a rate of 2.4 cents per therm or 5% of the purchase price for the billing period, whichever is lower. Purchasers may elect to pay the "alternate tax rate" of 2.4 cents per therm. The regulations further provide that a delivering supplier is responsible for collecting, reporting, and paying the gas use tax to the DOR unless a customer elects to become a self-assessing purchaser, in which case, the customer must report and pay the tax directly to the DOR.

STATE UPDATES

Finally, the regulations provide that purchasers who are subject to the gas use tax are exempt from the gas revenue tax. (86 Ill. Adm. Code §§470.171, 470.172, 471.101, 471.105, 471.110, 471.115, 471.120, 471.125, DOR, effective Nov. 30, 2004)

INDIANA

The information bulletin describing sales and use tax requirements on the sale or lease of motor vehicles has been updated to include information on trailers and watercraft. The bulletin states that the sale or lease of any motor vehicle, trailer or watercraft is subject to sales and use tax unless the transaction is entitled to a statutory exemption as shown on Indiana Form ST-108E. (Information Bulletin No. 28, Dept. of Revenue)

KANSAS

When a single shipment to a customer contains taxable and nontaxable goods, the seller must collect retailers' sales tax on the basis of the percentage of the shipping charge allocated to taxable goods in the shipment. The seller may allocate the shipping charge between taxable and nontaxable goods by (1) dividing the amount charged for the taxable goods by the total amount charged for all of the goods being shipped, or (2) dividing the weight of the taxable goods by the total weight of the shipment. The percentage resulting from either computation is multiplied by the total shipping charge to determine the taxable amount of the shipping charge. A seller's invoice must contain all information needed to calculate the seller's allocation of the shipping charges. (Questions and Answers, Dept. of Revenue, Dec. 10, 2004)

The resale of a service of installing portable office equipment is exempt from retailers' sales tax if the equipment will not be affixed to real property and the purchaser of the service gives the seller/service provider a properly completed resale exemption certificate. The purchaser of the service should collect the tax on the installation service from the consumer who purchased the office equipment. (Private Letter Ruling No. P-2004-058, Dept. of Revenue)

LOUISIANA

Pursuant to the recently enacted Uniform Local Sales Tax Administrative Procedure Act, Act 469 (SB825) of 2004, the Dept. of Revenue has expanded the existing state sales and use tax rules to include provisions for local sales and use taxes. In addition to the expanded rules governing collecting, reporting, and remitting sales tax, the department has adopted additional provisions outlining the imposition of sales tax on lease and rental transactions. The lease or rental transaction

rule requires initial local taxes incurred at the transfer of possession of the underlying property to be paid to the local taxing jurisdiction where the transfer occurred. In subsequent rental or lease periods, the tax will be paid to the local jurisdiction where the property is located. If the property is used outside of its primary local taxing jurisdiction, then the tax will be paid to the nonprimary local taxing jurisdiction; however, a credit for the taxes paid may be applied to the tax owed to the primary local taxing jurisdiction. (LAC 61:1.4301, 4303, 4307, 4311, 4401, DOR, effective Dec. 20, 2004)

MINNESOTA

The Dept. of Revenue has modified Revenue Notice No. 1991-06 regarding isolated or occasional sales. The modified notice states that generally, sales of tangible personal property primarily used in a trade or business do not qualify for the isolated or occasional sales tax exemption. However, the modified notice expands the types of sales of assets used in a trade or business that qualify for the isolated or occasional sales exemption to include instances where a sale occurs in a transaction subject to or described in specified IRC sections and where a sale is between members of a controlled group as defined in IRC Sec. 1563(a). (Revenue Notice No. 91-06, Sales/Use Tax —Isolated or Occasional Sales, DOR)

NEVADA

The period during which relief is available from penalties and interest for failure to make timely filing of sales and use tax has been extended to June 30, 2005 (formerly, it was set to expire on Dec. 31, 2004). This relief applies only to taxes and fees that are due and payable before July 1, 2005 (formerly, Jan. 1, 2005). (NAC §360.407, Dept. of Taxation, effective Dec. 13, 2004)

NEW YORK

Internet access charges imposed by an Internet cafe are exempt from sales and use tax. Although the charges include the use of a computer workstation, the use of the workstation is incidental to the provision of Internet access, and the charges are not subject to sales tax. (TSB-A-04(27)S, Commissioner of Taxation and Finance)

The Dept. of Taxation and Finance has issued a memorandum summarizing the sales and use tax legislative changes enacted in 2004. (TSB-M-04(8)S, DTF)

The Dept. of Taxation and Finance has issued a memorandum listing the local sales and use tax rates in counties and cities where clothing and footwear costing less

than \$110 per item or pair remain subject to local tax during the one-week exemption period beginning Jan. 31, 2005, through Feb. 6, 2005, and the counties and cities where no tax applies during the exemption period. (TSB-M-04(9.1)S, DTF)

NORTH DAKOTA

The date by which state law would be conformed to the requirements of the Streamlined Sales and Use Tax Agreement would be moved up by three months, under legislation recently prefiled. North Dakota was one of the first states to pass conformity legislation, in April 2003, but it only takes effect for taxable events occurring after Dec. 31, 2005. The pending legislation would change that date to Sept. 30, 2005. (SB2050, prefiled Dec. 3, 2004)

OHIO

The Dept. of Taxation has adopted rules implementing the state's conformity to the Streamlined Sales and Use Tax Agreement. An adopted rule contains provisions allowing vendors and sellers to register with a multistate central registration system for the collection of Ohio sales and use tax. Also, an adopted rule discusses the effective dates of changes in county and transit authority sales and use tax rates and the electronic databases that will be provided by the state. Finally, adopted rules address the treatment of delivery charges and discuss the application of rate change effective dates to services. (Rules 5703-9-50, 5703-9-51, 5703-9-52, and 5703-9-53, DT, effective Dec. 9, 2004)

The Dept. of Taxation has revised an Information Release on collection and remittance of sales and use tax under the Direct Payment Authority Program. During an audit, permit holders will be required to provide requested information electronically and use statistical sampling for expenses. The DT will impose a minimum penalty of 7.5% for permit holders within the compliance range of 80-90%. Permit holders failing to meet 80% compliance will be subjected to a minimum penalty of 15%. (Sales and Use Tax Information Release ST 2003-01, DT)

VIRGINIA

Announcing his proposed budget amendments to the House Appropriation, House Finance, and Senate Finance Committees, Gov. Mark R. Warner proposed reducing sales tax imposed on food by 1.5% in July of 2005, rather than phasing in the reduction as scheduled over the next three years. (Governor's Statement Before the House Appropriations, House Finance, and Senate Finance Committees, Dec. 17, 2004)

Sales and use tax incentives—Illinois

The following is excerpted from the Business Incentives Guide, a CCH book and online service detailing state-by-state business exemptions, incentives and credits. Unless otherwise indicated, all statutory references are to Chapter 35 of the Illinois Compiled Statutes (ILCS).

The sales and use taxes are combined in four separate acts. The retailer's occupation tax (ROT) is imposed on persons engaged in the business of selling tangible personal property at retail. The use tax (UT) is imposed on the privilege of using tangible personal property in Illinois that is purchased anywhere at retail from a retailer. The service occupation tax (SOT) is imposed on persons engaged in the business of making sales of services. The service use tax (SUT) is imposed on the privilege of using real or tangible personal property in Illinois that is received as an incident to a purchase of service from a serviceman or service provider.

Generally, the basic statewide rate is 6.25%. There are higher rates where there are home rule, county water commission, regional transportation authority and/or transit district taxes. The ROT is sales tax. Retailers are charged this tax for the privilege of carrying on their profession in Illinois. The retailer is responsible for the amount due, based on gross receipts. The UT is imposed on the purchaser for the privilege of using property in the state that was purchased at retail. The SOT is imposed on servicemen. It is measured by the selling price of the tangible personal property transferred by a service person as an incident to a sale of service. The SUT is imposed upon the purchaser for the privilege of using property that was acquired incident to the purchase of a service from a serviceman (§§120/14 et seq., 105/1 et seq., §115/1 et seq. and §110/1 et seq.).

MANUFACTURING (§§105/3-50, 120/2-45, 110/2, 115/2, 105/3-85, AND 100/3-70)

This exemption applies to the ROT, the UT, the SOT, and the SUT. Machinery, equipment and material that are used primarily in a manufacturing process or an assembling process are exempt. The manufacturing or assembling process must result in the production of tangible personal property for sale or lease. Machinery and equipment used to repair or maintain other exempt machinery or equipment, or to manufacture exempt machinery and equipment for in-house use are also exempt. Lessors of qualified machinery and equipment also qualify for the exemption.

A manufacturing machinery and equipment purchase credit (MPC) is available to a purchaser who qualifies for the manufacturing machinery and equipment exemption from the ROT, SOT, UT, or SUT. The credit is based on a statutory percentage of state use tax or service occupation tax that the manufacturer would have paid if the transaction had not been exempt. The credit percentage for purchases made after July 1, 1997, is 50%.

The MPC was reinstated as of Sept. 1, 2004. Previously, the MPC was repealed on July 1, 2003. However, MPC amounts earned prior to Sept. 1, 2004, cannot be used on qualifying purchases made prior to Sept. 1, 2004. Purchases made on or after Sept. 1, 2004, earn the purchaser a manufacturer's purchase credit that can be used against Illinois use tax or service use tax on: (1) manufacturing machinery and equipment, and (2) graphic arts machinery and equipment.

The credit may be used to satisfy the ROT, SOT, UT, or SUT due on subsequent purchases of production-related tangible personal property that does not otherwise qualify for the manu-

facturing machinery and equipment exemption. The credit must be used within two years after the date it is issued. Moreover, it is not transferable.

The manufacturer should report the credit on Form ST-17 prior to June 30 of the year following the calendar year in which the credit was earned. The credit must be used before Dec. 31 of the calendar year that is two years from the year in which the credit arose. The manufacturer must maintain records that identify as to each purchase, the vendor (including the vendor's registration number, if applicable, or the vendor's federal employers identification number), the purchase price and the amount of the MPC used on each purchase.

COMPUTER SOFTWARE (§§105/3, 105/3-25, 110/3-25, 115/3-25, AND 120/2-25)

Each of the following are exempt from sales and use tax:

- Software that is adapted to specific individualized requirements of a purchaser;
- Custom-made and modified software designed for a particular or limited use by a purchaser; and
- Software used to operate exempt machinery and equipment used in the process of manufacturing or assembling tangible personal property for wholesale or retail sale or lease.

POLLUTION CONTROL EQUIPMENT (§§105/2A, 110/2A, 115/2A, AND 120/1A)

This exemption applies to a system, method, construction, device or appliance appurtenant thereto, sold or used or intended for the primary purpose of eliminating, preventing or reducing air and water pollution. The exemption also includes systems and devices that have the primary purpose of treating, modifying or disposing of a potentially dangerous solid, liquid or gaseous pollutant. The exemption includes the pollution control equipment along with necessary replacement parts. A regulation provides that the exemption does not extend to chemicals used in such equipment or to fuel used in operating such equipment. Despite the limitation contained in the regulation, however, an Illinois appellate court has held that chemicals used in a pollution control facility were exempt from the UT.

AGRICULTURE (§§105/3-5, 110/3-5, 115/3-5, AND 120/2-5; 86 ILL. ADMIN. CODE §§130.305, 130.1201, 130.1995, 130.2100, AND 130.2110)

Sales of new or used farm machinery and equipment certified by the purchaser to be used primarily for production agriculture or state or federal agricultural programs, and replacement parts for such machinery and equipment, are exempt from the ROT, SOT, UT, and SUT. Included are computers, sensors, software, and related equipment used primarily in the computer-assisted operation of production agriculture facilities, equipment, and activities such as the collection, monitoring, and correlation of animal crop data for purposes of formulating animal diets and agricultural chemicals. Also included is precision farming equipment that is installed or purchased for installation on farm machinery and equipment including tractors, harvesters, sprayers, planters, seeders, or spreaders. Precision farming equipment includes soil testing sensors, computers, monitors, software, global positioning and mapping systems, and other such equipment.