

ILLINOIS REGISTER

DEPARTMENT OF REVENUE

NOTICE OF PROPOSED AMENDMENT

- 1) Heading of the Part: Use Tax
- 2) Code Citation: 86 Ill. Adm. Code 150
- 3)

<u>Section Numbers:</u>	<u>Proposed Action:</u>
150.306	Amendment
150.310	Amendment
- 4) Statutory Authority: 20 ILCS 2505/2505-90
- 5) A Complete Description of the Subjects and Issues Involved:

Section 150.306 is being amended to replace the current rulemaking for that Section that expired on May 27th, 2008. The Illinois Automobile Dealers Association (IADA) filed an objection to that rulemaking. Discussions with the IADA and the Chicago Automobile Trade Association have resulted in the changes incorporated into this rulemaking. Beginning July 1, 2008, this proposed rulemaking sets out 3 criteria that, if they occur, would prohibit the availability of the exemption for those items in those specific situations. It also provides a safe harbor for the use of items for which the interim use exemption is claimed as long as the retailers meet 6 criteria in regards to those items. If the use of the item does not fall either under the specific prohibitions or under the safe harbor provisions, another set of criteria is provided to determine if the exemption applies. The rules also make clear that manufacturers who are registered as retailers and claim the interim use exemption are subject to the same requirements as other retailers beginning on July 1, 2008.

Section 150.310 is being amended to reference the exemption from Use Tax for nonresidents who claim the drive-away decal exemption described in 130.605(b)(1). The rulemaking also provides notice that, beginning July 1, 2008, if the motor vehicle is then used in this State for 30 or more days in a calendar year, the purchaser is liable for Use Tax on the purchase price of that motor vehicle. The rules reference that, if the purchaser incurs tax under this provision, a credit will be given for any tax that was properly due and paid in another state; and any assessment of tax under that provision is limited to the period for which the Department may issue a notice of tax liability under the Use Tax Act.

Section 150.310 is being further amended to describe the fly-away aircraft exemption for aircraft that is purchased in this State, temporarily located in this State for the purpose of a prepurchase evaluation, and temporarily located in this State for the purpose of a post-sale customization, which was created by Public Act 95-305, effective August 20, 2007. That Section is also amended to reference the ending date for the exemption for the temporary storage of property purchased from an Illinois retailer by a taxpayer engaged in centralized purchasing activities in Illinois.

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- 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>
150.340	New Section	

- 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:

Terry D. Charlton
Senior Counsel, Sales & Excise Taxes
Illinois Department of Revenue
Legal Services Office
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: Automobile dealers and other retailers who claim the interim use exemption and nonresident purchasers of automobiles and other vehicles for which the drive-away permit exemption may be claimed.
- B) Reporting, bookkeeping or other procedures required for compliance: None
- C) Types of professional skills necessary for compliance: None
- 14) Regulatory Agenda on which this rulemaking was summarized: The rulemaking for 150.306 was not included on the January 2008 Regulatory Agenda because the previous rulemaking

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on this issue had already been filed. The rulemaking for 150.310 regarding the Use Tax liability of purchasers who claimed the drive-away permit exemption was not included on the January 2008 Regulatory Agenda because it arose out of discussions with the Illinois Automobile Dealers Association and the Chicago Automobile Trade Association after that Regulatory Agenda had been prepared. The rulemaking for the changes to 510.310 regarding the fly-away aircraft exemption was listed on the January 2008 Regulatory Agenda.

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

Section 150.306 Interim Use and Demonstration Exemptions

a) Interim Use Exemption

1) Except as otherwise provided in this subsection (a) and in subsection (c) of this Section, tangible personal property purchased by a retailer for resale, and used by the retailer or his agents prior to its ultimate sale at retail, is exempt from Use Tax, provided that the tangible personal property is of the same general type of property sold by that retailer and is carried as inventory on the books of the retailer or is otherwise available for sale during the interim use period. Beginning July 1, 2008, the following provisions apply to persons claiming the interim use exemption:

A) The interim use exemption may not be claimed for any item if any of the following circumstances exist:

i) title to the item is held by any party other than the retailer, except that such title may be held by the retailer, the manufacturer of that item, or a captive finance company;

ii) the retailer elects to claim an Internal Revenue Code Section 179 deduction on the item as a depreciable business asset; or

iii) if the item is leased or rented by the retailer, the aggregate gross receipts received from all leasing or renting of the item by the retailer exceeds the retailer's selling price of the item.

B) Safe Harbor Rule. For items that are not excluded from the exemption under subsection (a)(1)(A), interim use will be deemed to occur if the retailer satisfies all of requirements (i) through (vi) below:

i) The item is one of the following:

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- listed in the retailers records as part of inventory;
 - not depreciated by the retailer under Internal Revenue Code Section 167; or
 - otherwise shown by the retailer's records, documents, or through its operations as available for sale during the interim use period.
- ii) The period of use or lease of the item by the retailer is less than 24 months.
- iii) The item is of the same general type of property sold by the retailer.
- iv) The item is ultimately sold by the retailer.
- v) If the retailer receives revenues from the lease of the same general type of property as the item for which interim use is claimed, then the annual total of such lease revenues must be less than the annual total of the sales revenues received from such property.
- vi) If the item is leased under a lease agreement for more than 30 days, the lease agreement must contain a provision that if the retailer locates a buyer for the item (i) the lease may be terminated within 7 days or (ii) the lessee receive comparable property substituted by the retailer for the item within 7 days.
- C) If the item is not excluded from the exemption under subsection (a)(1)(A) and (1) does not fall under the safe harbor provisions of subsection (a)(1)(B) and (2) if the item is leased, the retailer is primarily a retailer as provided by subsection (a)(3), then the Department shall review all applicable and available facts to determine if the interim use exemption applies, including, but not limited to:
- i) The retail sales history or records of the type of items in question.
 - ii) Inventory records.
 - iii) Advertising of the item and, if the item is a vehicle, any advertisements on the vehicle and at the location of the vehicle.

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- iv) Manufacturer's contract terms, conditions, discounts and rebates.
 - v) Length and location of use or lease prior to sale.
 - vi) Whether depreciation under Internal Revenue Code Section 167 was taken by the retailer.
 - vii) Ownership and control documents, including but not limited to books, records, titles and insurance documents.
 - viii) In addition, if the item is leased, whether the contracts signed by lessee indicates the vehicle is available for recall, substitution allowance, and sale, during lease period;
- D) For purposes of this subsection (a)(1), the term "captive finance company" means a wholly owned subsidiary of a manufacturing company that finances wholesale or retail purchases from that manufacturing company.
- 2) To the extent provided by and limited under subsections (a) and ~~Except as limited in subsection~~ (c), the leasing of tangible personal property by persons who are primarily engaged in the business of selling such property at retail is within the interim use exemption. Except as to motor vehicles described in subsection (a)(4), the interim use exemption is not available to persons who purchase tangible personal property with the intent to engage in the business of leasing such property and who sell such property only as an incident to their leasing activity. Persons who are primarily engaged in the business of leasing motor vehicles may not claim an interim use exemption when purchasing motor vehicles for use in their business even though such lessors are subject to Retailers' Occupation Tax on the sale of used motor vehicles pursuant to 35 ILCS 120/1c. Motor vehicles of the first division as defined in Section 1-146 of the Illinois Vehicle Code [625 ILCS 5/1-146] are exempt from Use Tax if the vehicles purchased are to be rented under lease terms of one year or less. (See 35 ILCS 105/3-5(10))
- 3) In determining whether a taxpayer is "primarily" a retailer, the Department will examine only the activities of his Illinois operations. In addition, the Department will examine the activities of divisions of a corporate entity that are not separately registered with the Department. If divisions of a corporate entity are separately registered, however, their activities will not be examined in making this determination.

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- 4) To the extent provided by and limited under subsection (a), the ~~The~~ leasing of motor vehicles by motor vehicle dealers is within the interim use exemption. For example, many times motor vehicle dealers enter into leases of motor vehicles with lessees and simultaneously sell both those motor vehicles and leases to third parties. If a motor vehicle dealer enters into a lease of a motor vehicle with a lessee and simultaneously sells that motor vehicle to a third party, the interim use exemption is available to the dealer in regard to the purchase of the motor vehicle when it was purchased by the dealer for lease provided that the motor vehicle otherwise qualifies for the exemption under subsection (a). However, the dealer's sale of the motor vehicle, with or without the lease, to the third party is taxable and the third party incurs a Use Tax liability.

 - 5) Until June 30, 2008, the ~~The~~ leasing of motor vehicles by motor vehicle manufacturers to their employees is within the interim use exemption if the leased motor vehicles are carried as inventory on the books of the manufacturers or are otherwise available for sale during the lease period. Beginning on July 1, 2008 and thereafter, a manufacturer may claim the interim use exemption for tangible personal property leased to its employees, or is otherwise used by its employees, only when the manufacturer is registered as a retailer and the use of that property would qualify under all of the requirements of this subsection (a) and subsection (c).
- b) Demonstration Use Exemption
- 1) Except as provided in subsection (c), tangible personal property purchased for resale and used by its owner for demonstration purposes is not subject to Use Tax.
 - 2) The leasing of tangible personal property by a retailer to prospective buyers for the purpose of allowing them to ascertain whether or not the property suits their particular needs and for the purpose of trying to induce them to buy such property is a use for demonstration purposes, except as provided in subsection (c).
 - 3) The demonstration use exemption may not be claimed for tangible personal property purchased for resale which is consumed or destroyed in order to promote or demonstrate the product available for sale or is given away to a prospective customer as an inducement to make future purchases. For example, a retail grocer offering free samples of pizza to customers in his store in order to promote the sale of a new frozen pizza would not be able to claim a demonstration use exemption on his purchase price of the pizza consumed in the promotion.

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- 4) A vendor may not claim a demonstration use exemption on the use of a competing product, not available for sale by that vendor, even though the vendor uses the competing product to assist in the demonstration of the product which he sells. Nor may a vendor claim a demonstration use exemption on ancillary items used in the demonstration of a product (i.e., a microwave used to heat the pizza samples in the above example). The demonstration use exemption is available only to a vendor of the product being demonstrated.
- c) [Aircraft and Watercraft](#)
- For watercraft or aircraft, if the period of demonstration use or interim use by the retailer exceeds 18 months, the retailer shall pay Use Tax on the original cost price of the aircraft or watercraft, and no credit for that tax is permitted if the aircraft or watercraft is subsequently sold by the retailer. For purposes of this Section, the term "watercraft" means a Class 2, Class 3 or Class 4 watercraft as defined in Section 3-2 of the Boat Registration and Safety Act [625 ILCS 45/3-2], a personal watercraft, or any boat equipped with an inboard motor.

(Source: Amended at 32 Ill. Reg. _____, effective _____)

Section 150.310 Exemptions to Avoid Multi-State Taxation

- a) To prevent actual or likely multi-state taxation, the tax shall not apply to the use of tangible personal property in this State under the following circumstances:
- 1) The use, in this State, of tangible personal property acquired outside this State by a nonresident individual and brought into this State by such individual for his or her own use while temporarily within this State or while passing through this State:
 - 2) the use, in this State, of tangible personal property by an interstate carrier for hire as rolling stock moving in interstate commerce; or by lessors under a lease of one year or longer executed or in effect at the time of purchase of tangible personal property to interstate carriers for hire for use as rolling stock moving in interstate commerce as long as so used by such interstate carriers for hire. When tangible personal property is purchased by a lessor, under a lease for one year or longer, executed or in effect at the time of purchase to an interstate carrier for hire, who did not pay Use Tax to the retailer, such lessor (by the last day of the month following the calendar month in which such property reverts to

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the use of such lessor) shall file a return with the Department and pay the tax upon the fair market value of such property on the date of such reversion. For more details concerning this exemption, see 86 Ill. Adm. Code 130.340 of the Retailers' Occupation Tax Regulations; the same principles apply for Use Tax purposes;

- 3) *the use, in this State, of tangible personal property that is acquired outside this State and caused to be brought into this State by a person who has already paid a tax in another state in respect to this sale, purchase or use of that property, to the extent of the amount of the tax properly due and paid in the other state; for this purpose, "state" includes the District of Columbia [35 ILCS 105/3-55(d)];*
- 4) the temporary storage, in this State, of tangible personal property which is acquired outside this State and which, subsequent to being brought into this State and stored here temporarily, is used solely outside this State or is physically attached to or incorporated into other tangible personal property that is used solely outside this State, or is altered by converting, fabricating, manufacturing, printing, processing or shaping, and, as altered, is used solely outside this State;
- 5) the temporary storage in this State of building materials and fixtures which are acquired either in this State or outside this State by an Illinois registered combination retailer and construction contractor, and which such purchaser thereafter uses outside this State by incorporating such property into real estate located outside this State;
- 6) *beginning on January 1, 2002 [and through June 30, 2011](#), the use of tangible personal property purchased from an Illinois retailer by a taxpayer engaged in centralized purchasing activities in Illinois who will, upon receipt of the property in Illinois, temporarily store the property in Illinois for the purpose of subsequently transporting it outside this State for use or consumption thereafter solely outside this State or for the purpose of being processed, fabricated, or manufactured into, attached to, or incorporated into other tangible personal property to be transported outside this State and thereafter used or consumed solely outside this State. [35 ILCS 105/3-55(j)]*
 - A) "Centralized purchasing" means the procurement of tangible personal property by persons who purchase tangible personal property solely for use or consumption outside Illinois, who take delivery of that tangible personal property in Illinois and who temporarily store that tangible personal property in Illinois prior to transporting it outside the State for use or consumption solely outside Illinois.

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- i) For example, a business that maintains offices in several states and maintains storage facilities in Illinois purchases office equipment from an Illinois retailer, takes delivery of those items in Illinois and then stores them at its Illinois warehouse until they are shipped to its offices outside Illinois for use there can qualify for the exemption.
 - ii) For example, a lessor that purchases an item from an Illinois retailer specifically to fulfill its obligations under an existing lease with a lessee located outside Illinois, takes delivery of that item in Illinois and then stores that item at an Illinois warehouse until it is shipped to its lessee's out-of-State location can qualify for the exemption so long as the item is used solely outside Illinois.
 - iii) However, a lessor who purchases an item that is not dedicated to an existing lease with an out-of-State lessee, takes delivery of that item in Illinois and then places it in an Illinois rental inventory cannot qualify for the exemption even if the item is subsequently leased to an out-of-State lessee. This is true because, in Illinois, lessors are deemed to be the users of items purchased for rental inventories and placing an item in a rental inventory does not constitute storage.
- B) "Good standing" means the taxpayer has no final liability that the taxpayer is failing to pay. For purposes of this Section, final liability includes a notice of tax liability that has become final, an admitted liability, or a math error.
- C) Persons who wish to take advantage of this expanded temporary storage exemption must apply in writing to the Department to obtain an Expanded Temporary Storage Permit. Expanded Temporary Storage Permits cannot be assigned or transferred except when the holder of the permit is purchasing from an unregistered de minimis serviceman providing services as described in 86 Ill. Adm. Code 140.108. Other than this, only the person to whom the Expanded Temporary Storage Permit was issued by the Department may use that permit as described in this Section.
- D) Persons holding a valid Expanded Temporary Storage Permit may claim the expanded temporary storage exemption by providing their Illinois suppliers with a certification that the tangible personal property received in Illinois will be temporarily stored in Illinois for the purpose of being

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subsequently transported outside this State for use or consumption thereafter solely outside this State or for the purpose of being processed, fabricated, or manufactured into, attached to, or incorporated into other tangible personal property to be transported outside this State and thereafter used or consumed solely outside this State. Such certification must identify the seller, the purchaser, and the property, and include the purchaser's Expanded Temporary Storage Permit number and signature.

- i) If all of an Expanded Temporary Storage Permit holder's purchases qualify for the expanded temporary storage exemption, the Expanded Temporary Storage Permit holder may provide his supplier a blanket certificate of expanded temporary storage.
 - ii) If an Expanded Temporary Storage Permit holder knows that a certain percentage of all his purchases from a given seller will qualify for the expanded temporary storage exemption, he may provide a blanket certificate of expanded temporary storage stating that a designated percentage of purchases qualify for the expanded temporary storage exemption.
- E) In the event that tangible personal property for which the expanded temporary storage exemption has been claimed is taken out of storage and not transported outside this State for use or consumption, but is instead used or consumed in Illinois, the purchaser shall pay the tax that would have been due, in the same form that the retailer would have paid the tax (i.e., Retailers' Occupation Tax and local Retailers' Occupation Tax, if applicable), at the rate applicable at the location of the retailer from which the tangible personal property was purchased. For example, if tangible personal property purchased from a retailer in Naperville is temporarily stored in Illinois, then, instead of being transported outside the State for use or consumption, is removed from inventory and used in Illinois, tax will be due at the retailer's rate applicable in Naperville. The permit holder must pay the tax directly to the Department on forms prescribed by the Department, not later than the twentieth day of the month following the month in which the property was removed from inventory.
- F) In the event that tangible personal property for which the expanded temporary storage exemption has been claimed is temporarily stored in Illinois and transported outside this State for use or consumption, but subsequently returned to Illinois and used here, the purchaser shall pay the tax that would have been due, in the same form that the retailer would

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have paid the tax (i.e., Retailers' Occupation Tax and local Retailers' Occupation Tax, if applicable), at the rate applicable at the location of the retailer from which the tangible personal property was purchased. For example, if tangible personal property purchased from a retailer in Naperville is temporarily stored in Illinois and transported outside this State for use or consumption, but subsequently returned to Illinois and used here, tax will be due at the retailer's rate applicable in Naperville. Depreciation will be allowed as provided in Section 150.105(a). Also, credit shall be given for tax paid in another state in respect to the sale, purchase or use of such property, to the extent of the amount of the tax properly due and paid in the other state, as provided in subsection (a)(3) of this Section.

- G) Permit holders who assume the liability for the Retailers' Occupation Tax and any applicable local Retailers' Occupation Tax are subject to the same rights, remedies, privileges, immunities, powers and duties, and are subject to the same conditions, restrictions, limitations, penalties, and definitions of terms and employ the same modes of procedures as are prescribed for retailers under the Retailers' Occupation Tax Act. For example, if a permit holder fails to timely file the proper return or make the proper payment of tax, that permit holder is not entitled to the 1.75% vendor discount applicable to the sales reported on that return and is subject to penalties and interest under the Uniform Penalty and Interest Act [35 ILCS 735].

7) the use, in this State, of a vehicle for which a drive-away decal has been issued under the provisions of 86 Ill. Adm. Code 130.605(b)(1). However, beginning July 1, 2008, if the purchaser of a motor vehicle claims the exemption provided in Section 130.605(b)(1) and the motor vehicle is then used in this State for 30 or more days in a calendar year, the purchaser is liable for Use Tax on the purchase price of that motor vehicle, subject to credit for tax properly due and paid to any other state as provided in subsection (a)(3) of this Section. The assessment of tax under this subsection by the Department is limited to the period for which it may issue a notice of tax liability under the Use Tax Act.

8) beginning July 1, 2007, the use, in this State, of an aircraft, as defined in Section 3 of the Illinois Aeronautics Act, that is:

A) purchased in this State, if all of the following three conditions are met:

- i) the aircraft leaves this State within 15 days after the later of either the issuance of the final billing for the purchase of the aircraft or the

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- authorized approval for return to service, completion of the maintenance record entry, and completion of the test flight and ground test for inspection as required by 14 C.F.R. 91.407;
- ii) the aircraft is not based or registered in this State after the purchase of the aircraft; and
 - iii) the purchaser provides the Department with a signed and dated certification, on a form prescribed by the Department, certifying that the requirements of this subsection (8)(A) are met. The certificate must also include the name and address of the purchaser, the address of the location where the aircraft is to be titled or registered, the address of the primary physical location of the aircraft, and other information that the Department may reasonably require.
- B) temporarily located in this State for the purpose of a prepurchase evaluation if all of the following conditions are met:
- i) the aircraft is not based or registered in this State after the prepurchase evaluation;
 - ii) the purchaser provides the Department with a signed and dated certification, on a form prescribed by the Department, certifying that the requirements of this subsection (8)(B) are met. The certificate must also include the name and address of the purchaser, the address of the location where the aircraft is to be titled or registered, the address of the primary physical location of the aircraft, and other information that the Department may reasonably require; and
- C) temporarily located in this State for the purpose of a post-sale customization if all of the following conditions are met:
- i) the aircraft leaves this State within 15 days after the authorized approval for return to service, completion of the maintenance record entry, and completion of the test flight and ground test for inspection, as required by 14 C.F.R. 91.407;
 - ii) the aircraft is not based or registered in this State either before or after the post-sale customization;

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iii) the purchaser provides the Department with a signed and dated certification, on a form prescribed by the Department, certifying that the requirements of this subsection (8)(C) are met. The certificate must also include the name and address of the purchaser, the address of the location where the aircraft is to be titled or registered, the address of the primary physical location of the aircraft, and other information that the Department may reasonably require; and

D) The exemption provided under subsections (a)(8)(B) and (C) does not apply to tax incurred on any service transactions performed on the aircraft.

E) For purposes of subsection (a)(8):

“Based in this State” means hangared, stored, or otherwise used, excluding post-sale customizations as defined in this subsection (a)(8)(E), for 10 or more days in each 12-month period immediately following the date of the sale of the aircraft.

“Post-sale customization” means any improvement, maintenance, or repair that is performed on an aircraft following a transfer of ownership of the aircraft.

“Prepurchase evaluation” means an examination of an aircraft to provide a potential purchaser with information relevant to the potential purchase.

“Registered in this State” means an aircraft registered with the Department of Transportation, Aeronautics Division, or titled or registered with the Federal Aviation Administration to an address located in this State.

F) If tax becomes due under this subsection (a)(8) because of the purchaser's use of the aircraft in this State, the purchaser shall file a return with the Department and pay the tax on the fair market value of the aircraft. This return and payment of the tax must be made no later than 30 days after the aircraft is used in a taxable manner in this State. The tax is based on the fair market value of the aircraft on the date that it is first used in a taxable manner in this State. [35 ILCS 105/3-55(h-2)]

b) Since exemptions described in subsections (a)(1), (3) and (4) do not exist as far as the Retailers' Occupation Tax is concerned, and since it would therefore serve no purpose to say that the exemptions exist for Use Tax purposes insofar as the seller is merely

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collecting Use Tax to reimburse himself for Retailers' Occupation Tax on the same transaction, the Department believes that the legislative intention in these references to the acquisition of tangible personal property outside this State was to make the references apply to cases in which the only tax liability that could be involved is Use Tax liability.

- c) Therefore, exemptions described in subsections (a)(1), (3) and (4) would not apply except when the tangible personal property is acquired outside Illinois by the purchaser in such a way that there is no Retailers' Occupation Tax liability on the part of the seller in the same transaction.
- d) For information as to when sellers do or do not incur Retailers' Occupation Tax liability when shipping the tangible personal property from outside Illinois, see Section 130.610 of the Retailers' Occupation Tax Regulations.

(Source: Amended at 32 Ill. Reg. _____, effective _____)