

AN ALERT FROM THE BDO STATE AND LOCAL TAX PRACTICE

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SUBJECT

CHICAGO RULES PERSONAL PROPERTY LEASE TRANSACTION TAX APPLIES TO CLOUD COMPUTING AND THE AMUSEMENT TAX APPLIES TO ELECTRONICALLY DELIVERED AMUSEMENTS

SUMMARY

The City of Chicago (the “City”), Department of Finance (the “Department”) recently issued two rulings in which it applies the Amusement Tax to electronically delivered amusements (e.g., streamed movies) and the Personal Property Lease Transaction Tax (“Lease Tax”) to cloud computing. See Amusement Tax Ruling #5 (“Ruling #5”) and Lease Tax Ruling #12 (“Ruling #12”), respectively. Each ruling is effective July 1, 2015. However, the Department will limit the application of Ruling #5 to taxable periods beginning on or after September 1, 2015, and Ruling #12 to taxable periods beginning on or after January 1, 2016.¹

DETAILS

Applicability of the Amusement Tax to Electronically Delivered Amusements

The 9% Amusement Tax applies to an admission fee or other charge for the privilege to enter, view, or participate in an amusement.

In Ruling #5, the Department clarifies that the tax applies to a charge for the privilege to enter, view or participate in an amusement that is delivered electronically. Examples of a taxable charge include a charge for the privilege to: (i) watch electronically delivered television shows, movies or videos;

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¹ City of Chicago, Department of Finance, at http://www.cityofchicago.org/city/en/depts/fin/provdrs/tax_division/news/2015/june/PersonalPropertyLeaseTransactionTax12Effective7-1-2015.html (last visited August 14, 2015).

(ii) listen to electronically delivered music; and (iii) participate in online games. The Amusement Tax does not apply to a sale of a show, movie, video, music, or a game (normally accomplished by permanent download), but rather applies to a rental of a show, movie, video, music, or a game (normally accomplished by streaming or temporary download).

Applicability of the Lease Tax to Cloud Computing

Taxability of Cloud Computing

The 9% Lease Transaction Tax applies to a charge for the use of personal property, including a charge paid pursuant to a non-possessory computer lease, unless the charge is exempt under Exemption 11.

In Ruling #12, the Department clarifies that the tax applies to a charge for the following: (i) to perform a function such as cloud computing, cloud service, hosted environment, software as a service (or SaaS), platform as a service (or PaaS), and infrastructure as a service (or IaaS); and (ii) to obtain real estate listings and prices, car prices, stock prices, marketing data, and similar information that has been compiled, entered and stored on a provider's computer. The tax does not apply to a charge for a service where the customer accesses the deliverable electronically (e.g., a charge to write a report, article or similar document that consists primarily of the provider's own observations, opinions, ideas or analysis).

Exemption 11

In Ruling #12, the Department explains that an exempt use under Exemption 11 may be access to information or data which is entirely passive without interactive use, or access to materials that are primarily proprietary. An example of the former is a one-way dissemination of current stock prices where there is no search function and the charge is predominately for information transferred to the customer. An example of the latter is a subscription fee for an application that allows a subscriber to download or access materials such as copyrighted newspapers, newsletters or magazines that the subscriber would otherwise have to purchase at a bricks-and-mortar store.

Nexus, Sourcing and Bundled Charges under Ruling #5 and Ruling #12

Nexus

The Department noted that, while the discussion of nexus is generally outside the scope of a ruling, the Amusement Tax applies only to an amusement that takes place in the City, and the Lease Tax applies only where the customer's use takes place in the City.

Sourcing

The Department also noted that it will utilize the rules in the Mobile Telecommunications Sourcing Conformity Act, 35 ILCS § 638, to determine sourcing for purposes of the Amusement Tax and the Lease Tax. This means that the Amusement Tax and the Lease Tax will generally apply to a customer whose residential address or primary business address is located in the City as reflected by a credit card billing address or other reliable information.

With respect to the Lease Tax, where some employees use a provider's computer from terminals within the City and other employees without the City, and the provider has information regarding the customer's use, Ruling #12 provides rules for apportioning use within the City. However, no Lease Tax is due from a provider where it has no information to indicate that any of its customer's use takes place in the City, or if the customer has 10 or more employees and the customer gives the provider written confirmation from the Department that the customer is registered to pay the Lease Tax. The customer may, however, still be liable for the Lease Tax.

Bundled Charges

The Department reminded taxpayers that if a charge has a taxable and a non-taxable component, the entire charge is subject to the Amusement Tax or the Lease Tax where the charge is primarily for the privilege to enter, view or participate in an amusement, or for the use of a non-possessory computer lease, respectively.

BDO INSIGHTS

- ▶ Taxpayers that have not previously set-up their systems to collect, report, and remit the Lease Tax on charges for cloud computer or the Amusement Tax on charges for electronically delivered amusements will need to update their systems for collecting Amusement Tax on charges for electronically delivered amusements before their first taxable period beginning on or after September 1, 2015 and for Lease Tax on charges for cloud computing before their first taxable period beginning on or after January 1, 2016.
- ▶ The City is presently contemplating relief from the “cloud tax” for small businesses and start-ups that may be placed at a competitive disadvantage as a result of the imposition of Lease Tax on cloud computing. The City has not been clear as to what the relief will look like, but it anticipates issuing guidance in the near term.²

² Adrienne Hurst, *Chicago Will Protect Startups from the New ‘Cloud Tax,’* Chicago Magazine (July 14, 2015), at <http://www.chicagomag.com/city-life/July-2015/Chicago-Will-Protect-Tech-Startups-from-the-New-Cloud-Tax> (last visited August 14, 2015).

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