ST 10-0006-PLR 09/30/2010 SALE FOR RESALE

This letter addresses a sale for resale situation. See 86 Ill. Adm. Code 130.1405. (This is a PLR.)

September 30, 2010

Dear Xxxxx:

This letter is in response to your letter dated December 2, 2009 in which you requested a Private Letter Ruling on behalf of COMPANY. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

Review of your request disclosed that all the information described in paragraphs 1 through 8 of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to COMPANY for the issue or issues presented in this ruling, and is subject to the provisions of subsection (e) of Section 1200.110 governing expiration of Private Letter Rulings. Issuance of this ruling is conditioned upon the understanding that neither COMPANY nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request. In your letter you have stated and made inquiry as follows:

> Pursuant to Illinois Regulation 2 Ill. Admin. Code 1200.110, we are seeking a private letter ruling as to your state's sales and use tax treatment of installation services for direct to home satellite equipment performed by third party installers on behalf of our Client, COMPANY.
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> The relevant facts with respect to the COMPANY's operations are discussed below.
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> During the inquiry period, COMPANY was in the business of providing satellite television services to customers located in Illinois. In conjunction with the provision of satellite television services, COMPANY leased hardware, in the form of a satellite dish, a remote control and a receiver box, to each customer for the duration of the customer's subscription.
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> Throughout the inquiry period, physical installation of the hardware was outsourced to independent third parties who performed the following functions:

1. Installation and activation (including labor, equipment, vehicle and allocated direct and indirect costs)
2. General Service Calls
3. Upgrade Service Calls

Prior to installation COMPANY purchased the hardware for resale from unspecified manufacturer(s), and subsequently resold and delivered it to a third party installer. Upon receipt of the hardware, title passed to the installer who then procured insurance to cover the risk of loss. Upon completion of the installation services and activation of the hardware, COMPANY re-purchased the hardware from the third party installer on a resale certificate for the hardware only at a zero mark-up. As such, the installer earned no profits on the purchase and sale of hardware. All charges to COMPANY were related to installation fees. The purpose of the sale and re-purchase was incidental to the installation service and was done so to facilitate the installation and transfer the risk of loss from COMPANY to the installer. As stated above, the equipment was ultimately leased to the end-user/subscriber of COMPANY satellite television services.

Installation Services

The relationship between COMPANY and third party installers described above involved three discrete transactions:

1. The installation of the hardware
2. The sale of the equipment back to our Client
3. The sale of extra installation services on the installer's own account, which was separately stated

The transactions for equipment and installation services were separately billed and distinctive in nature, and therefore not considered a bundled transaction according to the terms of the contract between the two parties. The third party did not send a traditional paper invoice to COMPANY. Rather, the third party installer's commission was based on activation of the customer under his/her dealer account for each job via an integrated work tracking system, which COMPANY maintained, i.e, the invoice/billing from the installer to COMPANY was tracked electronically for each unique job.

In essence, there are two distinct transactions which occurred in every instance that satellite services were sold to a customer:

1) The provision of television services, including installation and activation, by COMPANY to customers in exchange for a subscription fee
2) The provision of installation services by third-party installers to COMPANY in exchange for a service charge

Issues:

1) Are the installation services provided by third-party installers subject to sales tax in Illinois?

2) In the event the installation services are deemed to be taxable, is the incidence of tax on the in-state registered installer, COMPANY or subscriber (COMPANY's customer)?

3) In the event the installation services were deemed to be taxable, may the service provider seek reimbursement from the customer?

4) Are the service provider and the installer jointly and severally liable for the payment of sales and use tax?

Analysis

The analysis that follows outlines the various Illinois Sales and Use Tax statutes, administrative regulations, and administrative decisions which have bearing on the facts above and our interpretation of the proper application of the cited authority to said facts.

We seek a letter ruling response that either confirms the merits of our interpretation or alternatively provides a proper tax treatment.

1) Are the installation services provided by third-party installers subject to sales tax in Illinois?

Illinois imposes both a Retailer's [sic] Occupation Tax ('ROT') and Service Occupation Tax ('SOT'). It is the position of our Client that the installation services and charges related thereto are exempt from both the ROT and SOT.

The ROT is imposed upon persons engaged in the business of selling tangible personal property to purchasers for use or consumption[i]. As explained above, the installation services provided by third-party installers on behalf of COMPANY did not involve the sale of tangible property for consumption. The user, or consumer, of the satellite equipment in all cases was the cable service subscriber. Additionally, according to Section 130.450 of the Illinois Administrative Code the measure of the ROT does not include installation charges when such charges are separately agreed upon between the parties involved. As noted above, the charge from the third-party installers to COMPANY is an installation fee which is electronically billed to COMPANY.

Finally, Section 130.2015(c) unambiguously exempts from the ROT any person engaged in the business of servicing tangible personal property, as the person is not engaged in the selling of tangible personal property.

Based on the foregoing, the installation services are not subject to the ROT.

The SOT is imposed on 'servicemen' engaged in the business of making sales of service and is based on the tangible personal property transferred incident to the sale[ii]. A serviceman is defined by Section 140.120 of the Illinois Administrative Code as a person who sells tangible personal property as an incident to a sale of service. The transfer of the satellite equipment from the third-party installers back to COMPANY do not constitute a sale of tangible personal property as they are sales for resale. As noted above, COMPANY is not the consumer of the tangible personal property and subsequently leases the equipment to the consumer.

Based on the foregoing, the installation services are not subject to the SOT as there is no sale of tangible personal property involved.

2) In the event the installation services were deemed to be taxable, is the incidence of tax on the in-state registered installer, COMPANY or subscriber?

The incident of tax would be on the third-party installer pursuant to Illinois Administrative Code Section 130.1405(a), which states that a seller must obtain a resale certificate to alleviate the incident of tax. As COMPANY does not resell the installation service, the final sale of the installation is from the installer to COMPANY. If the installation charge were deemed to be taxable, the incident of tax would rests [sic] with the installer.

3) In the event the installation services were deemed to be taxable, may the service provider seek reimbursement from the customer?

No, COMPANY may not collect tax from its customers. Since COMPANY has presented installation services as free of charge, any effort to collect tax would essentially violate a separate and distinct transaction for installation between itself and the customer. Absent a transaction, tax cannot be assessed against the customer. The tax must have a basis pursuant to pursuant to [sic] Sec. 3-45. [35 ILCS 105/3-45], which states in relevant part:

> The tax imposed by this Act shall be collected from the purchaser by a retailer maintaining a place of business in this State or a retailer authorized by the Department under Section 6 of this Act, and shall be remitted to the Department as provided in Section 9 of this Act, except as provided in Section 3-10.5 of this Act.
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> The tax imposed by this Act that is not paid to a retailer under this Section shall be paid to the Department directly by any person using the property within this State as provided in Section 10 of this Act.
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> Retailers shall collect the tax from users by adding the tax to the selling price of tangible personal property, when sold for use, in the manner prescribed by the Department. The Department may adopt and promulgate reasonable rules and regulations for the adding of the tax by retailers to selling prices by prescribing bracket systems for the purpose of enabling the retailers to add and collect, as far as practicable, the amount of the tax.

4) Are the service provider and the installer jointly and severally liable for the payment of sales and use tax?

Yes, COMPANY and the installer are jointly and severally liable for the payment of sales and use tax pursuant to Section 3-45 of the Retail [sic] Occupation Tax Act. As stated above, the Section states that 'retailers shall collect the tax from users by adding the tax to the selling price of tangible personal property, when sold for use, in the manner prescribed by the Department.'

<u>Conclusion</u>

- The charges for installation are not subject to the ROT since the installation services provided by third-party installers do not constitute a sale of tangible personal property and in any event are separately determined and charged. Additionally, the ROT regulations exempt from tax persons who repair or provide other services to property which they do not sell.

- The charges for installation are not subject to the SOT since there is no sale of tangible personal property upon which to base a tax. Stated differently, the third-party installers do not fall within the meaning of servicemen for purposes of the SOT.

- COMPANY may not collect tax on the installation absent a transaction between itself and the customer that serves as basis for the tax.

- Our Client and the installer are jointly and severally liable for the payment of sales and use tax.

Should you have any questions or desire further clarification as to the above fact pattern, please contact me.

DEPARTMENT'S RESPONSE:

The Illinois Retailers' Occupation Tax Act imposes a tax upon persons engaged in this State in the business of selling tangible personal property to purchasers for use or consumption. See 86 Ill. Adm. Code 130.101. In Illinois, Use Tax is imposed on the privilege of using, in this State, any kind of tangible personal property that is purchased anywhere at retail from a retailer. See 86 Ill. Adm. Code 150.101. These taxes comprise what is commonly known as "sales" tax in Illinois. If the purchases occur in Illinois, the purchasers must pay Use Tax to the retailer at the time of purchase. The retailers are then allowed to retain the amount of Use Tax paid to reimburse themselves for the Retailers' Occupation Tax liability incurred on those sales.

When a seller engages in the business of selling tangible personal property at retail, and such tangible personal property is installed by the retailer, the receipts from such installation charges must be included in the gross receipts upon which the Retailers' Occupation Tax liability is measured if such installation charges are included in the selling price of the property being sold. If, however, the seller and buyer agree upon the installation charges separately from the selling price of the tangible personal property which is sold, then the receipts from the installation charges are not a part of the "selling price" of the tangible personal property which is sold. Instead such charges constitute a service charge, separately contracted for, which need not be included in the figure upon which the seller computes his Retailers' Occupation Tax liability. See Section 130.450.

When a person purchases an item of tangible personal property with the intention of reselling it to a purchaser for use or consumption, that person engages in conduct equivalent to holding himself out as a retailer. This makes the initial purchase a purchase for resale, and the subsequent sale is a taxable sale at retail subject to Illinois Retailers' Occupation and Use Tax liabilities. See 86 Ill. Adm. Code 130.201 and 130.210.

For general information regarding resale certificates, the Department's regulation for resale certificates, "Seller's Responsibility to Obtain Certificates of Resale and Requirements for Certificates of Resale," is found at 86 Ill. Adm. Code 130.1405. If an electronic resale certificate is kept, it should contain all of the information required under 86 Ill. Adm. Code 130.1405.

The State of Illinois taxes leases differently for Retailers' Occupation Tax and Use Tax purposes than the majority of other states. For Illinois sales tax purposes, there are two types of leasing situations: conditional sales and true leases.

A conditional sale is usually characterized by a nominal or one dollar purchase option at the close of the lease term. Stated otherwise, if a lessor is guaranteed at the time of the lease that the leased property will be sold, this transaction is considered to be a conditional sale at the outset of the transaction. Persons who purchase items for resale under conditional sales contracts can avoid paying tax to suppliers by providing certificates of resale that contain all the information set forth in 86 Ill. Adm. Code 130.1405. All receipts received by a retailer under a conditional sales contract are subject to Retailers' Occupation Tax. See 86 Ill. Adm. Code 130.2010.

A true lease generally has no buy-out provision at the close of the lease. If a buy-out provision does exist, it must be a fair market value buy-out option in order to maintain the character of the true lease. Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See 86 Ill. Adm. Code 130.220. As end users of tangible personal property located in Illinois, lessors owe Use Tax on their cost price of such property.

The State of Illinois imposes no tax on rental receipts. Consequently, lessees incur no tax liability. As stated above, in the case of a true lease, the lessors of the property being used in Illinois would be the parties with Use Tax obligations. The lessors would either pay their suppliers, if their suppliers were registered to collect Use Tax, or would self-assess and remit the tax to the Department. If the lessors already paid taxes in another state with respect to the acquisition of the tangible personal property, they would be exempt from Use Tax to the extent of the amount of such tax properly due and paid in such other state. See subsection (a)(3) of 86 Ill. Adm. Code 150.310.

Under Illinois law, lessors may not "pass through" their tax obligation to the lessees as taxes. However, lessors and lessees may make private contractual arrangements for a reimbursement of the tax to be paid by the lessees. If lessors and lessees have made private agreements where the lessees agree to reimburse the lessors for the amount of the tax paid, then the lessees are obligated to fulfill the terms of the private contractual agreements.

It is the Department's understanding that COMPANY purchases the COMPANY hardware (satellite dish, remote control and receiver box) for resale directly from the manufacturer. It is the Department's understanding, under the terms of the agreement provided with the request, that COMPANY sells the COMPANY hardware to the third-party installer prior to installation. COMPANY then purchases the COMPANY hardware from the installer after installation of the hardware and provides the installer with a resale certificate. It also is the Department's understanding, under the terms of the agreement, that charges for the installation of the COMPANY hardware are agreed upon separately from the selling price of the COMPANY hardware. COMPANY leases the COMPANY hardware to COMPANY's subscribers.

COMPANY may provide its suppliers with resale certificates when purchasing COMPANY hardware from its suppliers. When an installer purchases COMPANY hardware from COMPANY, the installer may provide COMPANY with resale certificates since the COMPANY hardware will be resold to COMPANY When the installer sells the COMPANY hardware to COMPANY, the installer is liable for Retailers' Occupation Tax liability on the gross receipts received for the COMPANY hardware and must collect Use Tax from COMPANY. COMPANY may not give the installer resale certificates for COMPANY hardware that COMPANY purchases and subsequently leases to its subscribers unless the leases qualify as conditional sales. There is no Retailers' Occupation Tax or Use Tax liability on the separately agreed upon installation charges billed by the installer to COMPANY

It is the Department's understanding, under the terms of the agreement between COMPANY and the third-party installer, that the installer is required to provide the necessary materials (*e.g.*, coaxial cable, cable fittings, cable clips or ties) for completion of the installation service. The third-party installer is considered to be making sales of service and is subject to tax on the tangible

personal property transferred incident to those sales of service. Tangible personal property that is transferred to a service customer may result in either Service Occupation Tax liability or Use Tax liability for the servicemen depending upon his activities. See 86 Ill Adm. Code 140.101 et seq.

The factual representations upon which this ruling is based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the factual representations recited in this ruling are correct and complete. This Private Letter Ruling is revoked and will cease to bind the Department 10 years after the date of this letter under the provisions of 2 Ill. Adm. Code 1200.110(e) or earlier if there is a pertinent change in statutory law, case law, rules or in the factual representations recited in this ruling.

I hope this information is helpful. If you have questions concerning this Private Letter Ruling, you may contact me at (217) 782-2844. If you have further questions related to the Illinois sales tax laws, please visit our website at www.tax.illinois.gov or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Terry D. Charlton
Chairman, Private Letter Ruling Committee

TDC:RSW:msk

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[i] 86 Illinois Administrative Code 130.101.
[ii] 86 Illinois Administrative Code 140.101.