

This letter concerns tax imposed on tangible personal property transferred incident to sales of service. See 86 Ill. Adm. Code Part 140. (This is a GIL.)

March 5, 2012

Dear Xxxxx:

This letter is in response to your letter dated February 6, 2012, in which you request information. 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](http://www.tax.illinois.gov) to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

This is a request for an advisory opinion on the application of Sales and Use Tax for services provided by ABC in the State of Illinois. The details are as follows:

**Facts**

ABC is in the business of providing document management, mailroom and other ancillary facility services. ABC operates facility centers on the customers' premises in Illinois. ABC operations are similar, as the company your Department referred to in Illinois Dept. of Rev. General Information Letter No. ST 03-0153-GIL, 10/07/2003, copy attached.

**De Minimis Serviceman**

Our understanding is that ABC is classified as a 'De Minimis Serviceman.' Based on 86 Ill. Adm. Code 140-105(a), we calculate cost ratio by dividing the annual total cost of equipment, maintenance, repairs, and supplies (representing the tangible portion of the service), generated in the State of Illinois; by the Annual gross receipts for the entire business in the state. As an illustration, if a company's annual aggregate costs are \$25,000 and Annual gross receipts are \$100,000, then the cost ratio will be  $25,000/100,000 = 25\%$ . As the cost ratio calculated is lower than 35%, the company will qualify as a De Minimis Serviceman.

In General Information Letter No. ST 03-0153-GiL [sic], 10/07/2003, your department was asked the following three questions listed below 'these are extracts from the letter ruling':

1. Would machinery or equipment purchased, rented or leased by the Company in connection with providing the services qualify for a sales and use tax exemption?
2. Would supplies and materials purchased by the Company and used in the various operations be exempt from sales tax?
3. Would all amounts paid under contract be considered as taxable gross receipts? If yes, can we take deduction (sic) from gross receipt [sic] for the cost of equipment, labor or service cost and other related materials used in performing services under the contract? Should the client be billed taxes on the entire gross receipts as per the contract?

We agree with the answers provided for the questions listed above from the letter ruling.

We seek further clarification as follows:

**501(c)(3) Tax Exempt Entity**

1. What if the customer is a 501(c)(3) tax exempt organization, would your answer to question [sic] 1 to 3 above be different?
2. What are ABC [sic] tax obligations for sales of service to a tax exempt entity?

**De Minimis Serviceman**

1. Is the methodology of the De Minimis Serviceman cost ratio calculation correct as described earlier?
2. If a company is classified as a 'De Minimis Serviceman' what are the tax obligations in providing services to a 501(c)(3) tax exempt customer?
3. If a company is not qualified as a de minimis serviceman, what would its tax obligations be when doing business with a 501(c)(3) tax exempt entities? [sic]

We appreciate your assistance and respectfully await your response.

**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. The tax is measured by the seller's gross receipts from retail sales made in the course of such business. "Gross receipts" means the total selling price or the amount of such sales. The retailer must pay Retailers' Occupation Tax to the Department based upon its gross receipts, or actual amount received, from the sale of the tangible personal property. 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 35 ILCS 105/3; 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 the 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 their Retailers' Occupation Tax liability incurred on those sales. If the retailer does not collect the Use Tax

from the purchaser for remittance to the Department, the purchaser is responsible for remitting the Use Tax directly to the Department. See 86 Ill. Adm. Code 150.130.

Illinois Service Occupation and Use Taxes do not apply to sales of service that do not involve the transfer of tangible personal property to customers. However, if tangible personal property is transferred incident to sales of service, this will 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. The purchase of tangible personal property that is transferred to the service customer may result in either Service Occupation Tax liability or Use Tax liability for the servicemen depending upon his activities.

A serviceman may incur either Service Occupation Tax or Use Tax liability when transferring tangible personal property incident to retail sale of service. The type of tax liability incurred depends upon several factors. The single most important factor is determining the cost ratio between the annual aggregate cost of tangible personal property transferred incident to sales of service and the annual gross receipts from all sales of service. If this cost ratio is 35% or greater (75% or greater in the case of servicemen transferring prescription drugs or engaged in graphic arts production), the serviceman is required to register and remit Service Occupation Tax on his selling price, as explained in Section 140.106. See 85 Ill. Adm. Code 140.105. It should be noted that the rule refers to "the annual aggregate cost of tangible personal property transferred incident to sales of service", not the serviceman's cost of doing business. Therefore, the cost of equipment, maintenance, repairs and supplies are generally not included when computing the ratio. Only the cost of tangible personal property that is actually transferred to the service customer is used in the calculation.

Organizations that are recognized as non-profit under Internal Revenue Code Section 501(c)(3), are not necessarily exempt organizations pursuant to Illinois tax law. Such organizations must obtain an exemption identification number (an "E number") to qualify. See 86 Ill. Adm. Code 130.2007.

Organizations that make application to the Department of Revenue and are determined to be exclusively religious, educational, or charitable, receive an E number. The E number evidences that the Department recognizes the organizations as exempt from incurring Use Tax when purchasing tangible personal property in furtherance of their organizational purposes. If an organization does not have an E number, then its purchases are subject to tax. Please be aware that currently only sales to organizations holding the E number are exempt, not sales to individual members of the organization.

Companies selling tangible personal property or transferring tangible personal property incident to sales of service to these organizations must be provided with an E number for the sales to be tax exempt, unless another exemption can be documented.

A serviceman who incurs SOT on his or her selling price is authorized to claim any exemption provided for in the Service Occupation Tax Act. For example, he or she may claim the interstate commerce exemption or accept various exemption certificates from his or her customers (e.g., Certificates of Resale, exemption identification numbers). 86 Ill. Adm. Code 140.106(d). A de minimis serviceman incurring Service Occupation Tax liability on his or her cost price also is authorized to claim any of the various exemptions provided for in the Service Occupation Tax Act. For example, he may claim the interstate commerce exemption or accept various exemption certificates from his customers (e.g., he can accept Certificates of Resale). 86 Ill. Adm. Code 140.109 (a)(3). The Department has also determined that a de minimis serviceman incurring a Use Tax liability may claim any of the exemptions, except as provided in subsection (a)(2)(C), authorized under the Service Occupation Tax Act. De minimis servicemen incurring Use Tax liability may likewise claim the interstate commerce exemption, which is more fully explained at 86 Ill. Adm. Code 130.605. 86 Ill. Adm. Code 140.108(a)(2)(B).

Generally, the tax exempt status of lessees does not affect the tax liability of lessors. However, please note that Illinois does have two exemptions for leases to entities that have active E numbers. The first exemption is for certain purchases of tangible personal property by persons who are leasing that property to exempt hospitals that have an active E number issued by the Department. See 86 Ill. Adm. Code 130.2011. The second exemption is for purchases of tangible personal property by persons who are leasing that property to a governmental body that has an active E number issued by the Department. See 86 Ill. Adm. Code 130.2012.

I hope this information is helpful. If you require additional information, please visit our website at [www.tax.illinois.gov](http://www.tax.illinois.gov) or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Richard S. Wolters  
Associate Counsel

RSW:mzk