

The taxability of maintenance agreements depends upon whether charges for the agreements are included in the selling price of the tangible personal property. See 86 Ill. Adm. Code 140.141 and 140.301. (This is a GIL.)

November 1, 2016

Dear Xxxxx:

This letter is in response to your dated letter July 6, 2016, in which you requested 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:

COMPANY. is a corporation whose primary business is the sales and service of medical imaging equipment and parts. A facet of COMPANY’s business is providing service to CT, MRI, NM and PET Scanners under service agreements. Such service agreements can be either executed at the time of the purchase of the equipment from COMPANY, or simply executed by the customer to cover a scanner that they already have installed. These service agreements can cover both labor and parts, or labor only. All of COMPANY’s service agreements are optional.

Issue 1) Is revenue received from service agreements taxable or non-taxable? COMPANY’s service agreements are not included as part of the sale of equipment, and are always invoiced separately. In the case of a service agreement covering both parts and labor, however, the fee is not separated between the two.

Issue 2) Is shipping taxable on the sale of a part which we are shipping into your state?

Issue 3) If merchandise is returned, but there is a restock fee, is the full amount of tax due back to the customer? Additionally, would the restock charge be taxable?

Issue 4) Is non-contract billable service, (IE: labor and travel time) taxable? The service performed by COMPANY is repairs to medical imaging equipment, such as MRI and CT Scanners. These repairs are not always associated with a machine that we have sold in the past.

Issue 5) Is service taxable if parts are listed separately on the same invoice?

Issue 6) What resale certificate is COMPANY required to receive from the customer? Do you accept a customer's home state resale certificate or is the customer required to be registered in your state? If customer's home state certificate is acceptable are there any stipulations?

## **DEPARTMENT'S RESPONSE:**

### Sales Tax

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 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.

### Maintenance Agreements

The taxability of a maintenance or service agreement depends upon whether the charge for the agreement is included in the selling price of tangible personal property. If the charge for the agreement is included in the selling price of tangible personal property, the charge is part of the gross receipts of the retail transaction and is subject to tax. No tax is incurred on the maintenance services or parts when the repair or servicing is performed.

If a maintenance agreement is sold separately from tangible personal property, the sale of the agreement is not a taxable transaction. However, when maintenance services or parts are provided under the terms of the maintenance agreement, the seller of the maintenance agreement will be acting as a service provider under provisions of the Service Occupation Tax Act. The Service Occupation Tax provides that when a service provider enters into an agreement to provide maintenance services for particular pieces of equipment for a stated period of time at predetermined fees, the service provider incurs Use Tax based on its cost

price of tangible personal property transferred to the customer incident to the completion of the maintenance service. See 86 Ill. Adm. Code 140.301(b)(3). Further, the purchaser of the separate agreement is not charged tax on the labor or tangible personal property that is transferred incident to the completion of the maintenance agreement. If a deductible is charged to the purchaser under the terms of the separate agreement, the deductible is also not subject to tax.

### Service Occupation Tax

Illinois Retailers' 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 businesses providing services (e.g., servicemen) depending upon their activities. For your general information, see of 86 Ill. Adm. Code 140.101 through 140.109 regarding sales of service and Service Occupation Tax.

The servicemen's liability may be calculated in one of four ways: (1) separately stated selling price of tangible personal property transferred incident to service; (2) 50% of the servicemen's entire bill; (3) Service Occupation Tax on the servicemen's cost price if the servicemen are registered de minimis servicemen; or (4) Use Tax on the servicemen's cost price if the servicemen are de minimis and are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of the sale of service. The tax is then calculated on the separately-stated selling price of the tangible personal property transferred. If the servicemen do not separately state the selling price of the tangible personal property transferred, they must use 50% of the entire bill to the service customer as the tax base. Both of the above methods provide that in no event may the tax base be less than the servicemen's cost price of the tangible personal property transferred. See 86 Ill. Adm. Code 140.106.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. See 86 Ill. Adm. Code 140.109. Servicemen may qualify as de minimis if they determine that the annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of the total annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphics arts production). Servicemen do not have the option of determining whether they are de minimis using a transaction-by-transaction basis. Registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon their cost price of tangible personal property transferred incident to the sale of service. Such servicemen should give suppliers resale certificates and remit Service Occupation Tax using the Service Occupation Tax rates for their locations. Such servicemen also collect a corresponding amount of Service Use Tax from their customers, absent an exemption.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Such de minimis servicemen handle their tax liability by paying Use Tax to their suppliers.

If their suppliers are not registered to collect and remit tax, the servicemen must register, self-assess and remit Use Tax to the Department. The servicemen are considered to be the end-users of the tangible personal property transferred incident to service. Consequently, they are not authorized to collect a "tax" from the service customers. See 86 Ill. Adm. Code 140.108.

### Restocking Fee

When a retailer makes a charge for restocking or reshelving returned merchandise, the receipts retained by the retailer to cover the restocking or reshelving fee are not considered taxable gross receipts for purposes of his Retailers' Occupation Tax liability. When a customer returns merchandise to the retailer, the retailer should refund all of the sales tax to the customer even though he will not be refunding the entire purchase price because of a restocking or reshelving policy. 86 Ill. Adm. Code 130.401(b). This same concept applies in all cases when merchandise is returned to the retailer and a full or partial refund is provided by that retailer.

If a retailer can document that it returned all of the tax to the customer that was paid on the initial purchase, it may deduct all the gross receipts from the original sale on its return for the period in which the refund was provided. See 86 Ill. Adm. Code 130.401(b). If it fails to return all of the tax to the customer that was paid on the initial purchase, it may only deduct the amount of gross receipts that correspond to the amount of tax that was refunded. The remainder of the tax that was not returned to the customer represents an over collection of tax. Illinois law requires that all over collections of tax must either be turned over to the Department or refunded to the customer. See 35 ILCS 120/2-40.

### Resale Certificate

A retailer, as a seller required to collect Illinois tax, must either charge and collect tax or document appropriate exemptions when making deliveries in Illinois. In order to document the fact that its sale is a sale for resale, a retailer is obligated by Illinois to obtain a valid Certificate of Resale from the purchaser. See 86 Ill. Adm. Code 130.1405. A Certificate of Resale is a statement signed by the purchaser that the property purchased by him or her is purchased for purposes of resale. In addition to the statement that the property is being purchased for resale, a Certificate of Resale must contain:

- 1) The seller's name and address;
- 2) The purchaser's name and address;
- 3) A description of the items being purchased for resale;
- 4) Purchaser's signature, or the signature of an authorized employee or agent of the purchaser, and date of signing; and
- 5) Registration Number, Resale Number, or a statement that the purchaser is an out-of-State purchaser who will sell only to purchasers located outside the State of Illinois.

The Department provides a standard form for documenting sales for resale (Form CRT-61 Certificate of Resale). This form can be obtained from the Department's website.

The obligations of a seller with respect to accepting a Certificate of Resale were addressed in *Rock Island Tobacco and Specialty Company v. Illinois Department of Revenue*, 87 Ill.App.3d 476, 409 N.E.2d 136, 42 Ill. Dec. 641 (3rd Dist. 1980). The *Rock Island* court

held that when a retailer obtains a proper Certificate of Resale that contains a registration or resale number that is valid on the date it is given, the retailer's liability is at an end. If the purchaser uses that item himself or herself (e.g., it was not purchased for resale), the Department will proceed against the purchaser, not the retailer, provided the above stated conditions are met. The purchaser's registration or reseller number can be verified at the Department's website by clicking on the "Tax registration inquiry" box.

Failure to present an active registration number or resale number and a certification to the seller that a sale is for resale creates a presumption that a sale is not for resale. This presumption may be rebutted by other evidence that all of the seller's sales are sales for resale or that a particular sale is a sale for resale. For example, other evidence that might be used to document a sale for resale, when a registration number or resale number and certification to the seller are not provided, could include an invoice from the purchaser to his customer showing that the item was actually resold, along with a statement from the purchaser explaining why it had not obtained a resale number and certifying that the purchase was a purchase for resale in Illinois. The risk run by a retailer in accepting such other documentation and the risk run by purchasers in providing such other documentation is that an Illinois auditor is more likely to require that more information be provided as evidence that the particular sale was, in fact, a sale for resale.

#### Transportation and Delivery Charges

The Department's regulation regarding transportation and delivery charges, 86 Ill. Adm. Code 130.415, was amended to incorporate the provisions of *Kean v. Wal-Mart Stores, Inc.*, 235 Ill. 2d 351, 919 N.E.2d 926 (2009). At issue in *Kean* was whether shipping charges for certain Internet purchases of tangible personal property were subject to Illinois sales tax. The court found that an "inseparable link" existed between the sale and delivery of the merchandise plaintiffs purchased from Wal-Mart's Internet store. Thus, the court in *Kean* concluded that the outgoing transportation and delivery charges were part of the gross receipts subject to the Retailers' Occupation Tax.

As *Kean* notes, outgoing transportation and delivery charges are part of the gross receipts subject to Retailers' Occupation Tax when there is an inseparable link between the sale of tangible personal property and the outgoing transportation and delivery of the property. The regulation clarifies that an inseparable link exists when the transportation and delivery charges are (1) not separately identified to the purchaser on the contract or invoice, or (2) when the transportation and delivery charges are separately identified to the purchaser on the contract or invoice, but the seller does not offer the purchaser the option to receive the tangible personal property in any manner except by the payment of transportation and delivery charges added to the selling price of the item (e.g., the seller does not offer the purchaser the option to pick up the tangible personal property or the seller does not offer, or the purchaser does not qualify for, a free transportation and delivery option). See 86 Ill. Adm. Code 130.415(b)(1)(B)(ii).

Except for cases in which an inseparable link exists, outgoing transportation and delivery is otherwise considered a service separate and distinct from the sale of tangible personal property and is excluded from the gross receipts subject to the Retailers' Occupation Tax.

The amended regulation provides that retailers who have computed their tax liability for transportation and delivery charges according to the provisions of either the old rule or the amended rule for periods between the *Kean* decision (November 19, 2009) and April 1, 2016 (the effective date of the new rules) shall be considered to have properly collected and remitted tax on those charges. See the Department's regulation at 86 Ill. Adm. Code 130.415(b)(1)(A)(i). The regulation further provides that if a seller of tangible personal property offers the purchaser free transportation and delivery of the property or free transportation and delivery of the property for which the purchaser qualifies (e.g., purchases of \$50 or more receive free delivery), or the option to pick up the property, any separately identified transportation and delivery charges chosen by the purchaser (e.g., amounts paid for expedited transportation and delivery) will be nontaxable, as long as the selling price of the tangible personal property neither increases nor decreases depending on the method chosen by the purchaser to obtain the merchandise. When the selling price of the tangible personal property increases or decreases, the transportation and delivery charges will be subject to Retailers' Occupation Tax to the extent those charges exceed the actual cost of the outgoing transportation and delivery.

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,

Debra M. Boggess  
Associate Counsel

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