

Under the Service Occupation Tax, servicemen are taxed on tangible personal property transferred incident to a sale of service. See 86 Ill. Adm. Code Part 140. (This is a GIL.)

February 3, 2017

RE: Tax advice related to Door Hanger Advertising and Door to Door Delivery

Dear Xxxxx:

This letter is in response to your letter dated September 15, 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 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:

On behalf of my client, an unidentified taxpayer, we respectfully request tax advice related to their sales and distribution of door hangers within your state. We are currently working with the client to develop sales and use tax processes to properly administer your states sales and use tax. The taxpayer is not currently operating in your state, as such; they do not currently have any pending administrative matters before your tax agency.

As background, the taxpayer provides turnkey front-door marketing services including developing marketing strategies, creative services, targeting & analytics, print services, distribution and delivery verification. The taxpayer's customers include local and national businesses in a variety of industries. Generally, the customers provide finished artwork digitally and a marketing piece is developed by the taxpayer. The finished artwork is then sent to a third party printer for printing. The printed material (door hangers) are then shipped by the printer directly to an independent distribution center where independent contractors pick up the product and distribute it to the residential addresses within a targeted geographic area.

The residents (third party recipients) receive the door hanger at no cost and they become the owner of the printed material. The taxpayer's customers do not obtain possession of the door hangers during any point of the printing or distribution processes. The taxpayer's employees perform audit verification services during the distribution process to confirm and validate distribution by the independent contractors.

Generally, the taxpayer contracts with customer for a fixed price per thousand of distributed door hangers. The contracted price includes the development of the printed material, the actual printing cost, audit verification services and the distribution cost for the independent carrier to distribute the printed materials to customers. The customer is billed upon final distribution of the product. In addition, the customer is billed for any shipping cost from the printer to the distribution center. We respectfully request tax advice related to the taxability of our products and services in your state. We would also like to confirm if the taxability changes, if we contract or bill our customers differently. Please assume that our client will have nexus in your state when making this determination.

Assuming the taxpayer bills lump-sum amounts for the delivered door hangers:

1. Is the sale of printed materials (door hangers) for a delivered price subject to sales or use tax in your state?
 - a. If yes, are any deductions allowed for the below charges included in the billed amount:
 - i. Creative development
 - ii. Independent contractor - distribution charges
 - iii. Audit services – delivery verification

Assuming the taxpayer bills customers for separately amounts for the above items, does the taxability change?

2. Below is a list of the potential separate charges:
 - a. Printed material (door hangers)
 - b. Creative development
 - c. Independent contractor distribution charges
 - d. Audit Services – delivery verification
 - e. Freight or shipping charges

Depending on the answers to question 1 and 2 above, can the taxpayer's [sic] purchase the following items for resale?

- a. Printed materials (door hangers)
- b. Independent contractor – distribution fees

Thank you in advance for your assistance with properly administering your states sales and use tax. If you have any questions or need any clarification on any of the above facts or questions, please do not hesitate to contact me at ###.

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 at retail to purchasers for use or consumption. See 86 Ill. Adm. Code 130.101. In Illinois, a Use Tax is also 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.

Service Occupation Tax

Custom work performed for customers would be considered a sale of service. As such, under Illinois law, businesses that engage in a service occupation are deemed servicemen. The purchase of tangible personal property that is transferred to service customers may result in either Service Occupation Tax liability or Use Tax liability for servicemen, depending upon which tax base they choose to calculate their liability. Servicemen may calculate their tax base in one of four ways: (1) separately stated selling price; (2) 50% of the entire bill; (3) Service Occupation Tax on cost price if they are registered de minimis servicemen; or (4) Use Tax on 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 sales of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If servicemen do not wish to separately state the selling price of the tangible personal property transferred, those servicemen must use the second method where they will use 50% of the entire bill to their service customers as the tax base. Both of the above methods provide that in no event may the tax base be less than the cost price of the tangible personal property transferred. Under these methods, servicemen may provide their suppliers with Certificates of Resale when purchasing the tangible personal property to be transferred as a part of sales of service. They are required to collect the corresponding Service Use Tax from their customers.

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. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). See 86 Ill. Adm. Code 140.101(f). This class of registered de minimis servicemen is authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to sales of service. Servicemen that incur Service Occupation Tax collect the Service Use Tax from their customers. They remit tax to the Department by filing returns and do not pay tax to their suppliers. They provide suppliers with Certificates of Resale for the tangible personal property transferred to service customers.

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. Servicemen may qualify as de minimis if they determine that the annual aggregate cost price of tangible personal property transferred as an incident of sales of service is less than 35% of the servicemen's annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). 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.

Multi-service situations exist where a primary serviceman subcontracts work to a secondary serviceman. In multi-service situations, a primary serviceman's cost price is determined either by the separately stated selling price of the tangible personal property transferred from a secondary serviceman, or if the secondary serviceman does not separately state the cost of goods, it is presumed that the primary serviceman's cost price is 50% of the secondary serviceman's total charge. See 86 Ill. Adm. Code 140.301(a).

When both primary servicemen and secondary servicemen are registered, primary servicemen provide secondary servicemen with a Certificate of Resale. A primary serviceman would then incur Service Occupation Tax based upon the separately stated selling price of the property, 50% of the bill to the service customers or as outlined in method three described above. Upon selling their product, servicemen are required to collect the corresponding Service Use Tax from their customers. Please note that if an unregistered de minimis serviceman subcontracts service work to another unregistered de minimis secondary serviceman, the primary serviceman does not incur a Use Tax liability if the secondary serviceman (i) has paid or will pay Use Tax on his or her cost price of any tangible personal property transferred to the primary serviceman and (ii) certifies that fact in writing to the primary serviceman. This certification option is only available in multi-service situations when both the primary and secondary servicemen are unregistered and de minimis. If the primary serviceman is registered and the secondary serviceman is unregistered it will not work.

Delivery Charges

Whether amounts charged by a serviceman to his customers in order to secure delivery of the tangible personal property to its customers are taxable depends upon the method used by the serviceman to calculate his tax liability. See 86 Ill. Adm. 140.301(b).

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.

I hope this information is helpful. If you require additional information, please visit our website at 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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