

Sellers of special order machines are considered to be engaged primarily in a service occupation, rather than being engaged in the business of selling tangible personal property, if the test set out in 86 Ill. Adm. Code 130.2115(b) is met. See 86 Ill. Adm. Code 130.2115. (This is a GIL.)

March 10, 2014

Dear Xxxxx:

This letter is in response to your letter dated August 7, 2013, 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 to review regulations, letter rulings and other types of information relevant to your inquiry.

In your letter you have stated and made inquiry as follows:

On behalf of our client, ABC, we are requesting a Private Letter Ruling related to the applicability of Illinois Retailers' Occupation Tax, Service Occupation Tax or Use Tax to the production and sale of custom-designed precast concrete building components manufactured in Illinois and sold in Illinois and surrounding states. For your convenience, I have enclosed a copy of form IL-2848 "Power of Attorney" authorizing me to make this inquiry.

ABC (Company) is not involved in any dispute regarding this or similar issues, nor is it under audit by the Department of Revenue (Department). To the best of our knowledge, neither this matter nor any similar issue has been ruled on by the Department for the Company, and the Company has not submitted any previous request for a ruling on this or any similar issue.

Statement of Facts

The Company is a manufacturer of precast concrete building components for commercial buildings and bridge construction. Its manufacturing facility is located in Marseilles, Illinois and its business offices are located in Westchester, Illinois. Substantially all of its customers are governments, property owners and general contractors. Work is obtained via competitive bidding and negotiated contracts with customers. The components produced may be engineered and/or designed by the Company or these functions may be performed by the customer. However, this inquiry relates only to those components where the Company retains contractual responsibility

for the engineering and/or design functions, as its expertise in these areas is essential to produce the building components and meet its customers' particular needs.

The precast concrete building components include bridge beams, wall panels, support pillars and beams, decking, stairs, etc. In those cases where the Company retains engineering and/or design responsibility, the components are designed to meet customer specifications by engineers employed directly by the Company or by engineering firms subcontracted by the Company. The components are produced by pouring concrete into forms, which have been modified to meet the individual specifications for each component. Production may be performed entirely by the Company, or may be subcontracted in whole or in part to other precast concrete companies. Depending on customer requirements, the Company's contracts may include delivering and/or installing these components at construction sites in Illinois and surrounding states.

Each building component is specifically designed to meet customer requirements for dimensions, load capacity, reinforcement, fire rating, insulation value, connections, openings and esthetics, and is specifically identified by a unique piece mark. Generally, a component must be positioned at an exact location in the building and is not interchangeable with any other component. If for any reason a component is not used for its designed purpose, it generally cannot be sold to any other buyer and would be scrapped.

Completed components may be picked up by customers or delivered to construction sites, generally by common carrier.

If the Company's contract includes installation of components, a sub-contractor is engaged to perform the installation.

The Company typically invoices customers as work progresses. These invoices may or may not specifically identify engineering and/or design as a separate charge.

Issues

Based on the description above, please address the following in the Private Letter Ruling:

1. Would building components sold by the Company, where it retains responsibility for the engineering and/or design functions, be exempt from Retailers' Occupation Tax under Title 86 Part 130 Section 130.2115(b) of the Illinois Department of Revenue Regulations?
2. Would Illinois Service Occupation Tax, Use Tax or related sales type tax apply to the sale of building components where the Company retains contractual responsibility for the engineering and/or design functions?

Thank you for your consideration of this matter. Should you require additional information or if I can be of other assistance, please contact me directly at (xxx) xxx-xxxx, or at the address above.

DEPARTMENT'S RESPONSE:

The Department's regulation "Public Information, Rulemaking and Organization" provides that "[w]hether to issue a private letter ruling in response to a letter ruling request is within the discretion of the Department. The Department will respond to all requests for private letter rulings either by issuance of a ruling or by a letter explaining that the request for ruling will not be honored." 2 Ill. Adm. Code 1200.110(a)(4). The Department recently met and determined that it would decline to issue a Private Letter Ruling in response to your request. We hope however, the following General Information Letter will be helpful in addressing your questions.

The issue of whether a person incurs a Retailers' Occupation Tax or Service Occupation Tax liability depends upon the nature of the items being produced and the nature of the design work involved. If the item being produced is substantially similar to stock or standard items, even though custom-made, the sale of that item would result in Retailers' Occupation Tax liability. The test for special order items that result in Service Occupation Tax liability is set forth in subsection (b) of the Department's rule "Sellers of Machinery, Tools and Special Order Items" at 86 Ill. Adm. Code 130.2115. The seller of a special machine, tool, die, jig, pattern, gauge or other similar item is engaged primarily in a service occupation, rather than in the business of selling tangible personal property, and so does not incur Retailers' Occupation Tax liability with respect to the sale, if the following tests for exemption are all met in the transaction:

- A) the purchaser employs the seller primarily for his engineering or other scientific skill to design and produce the property on special order for the purchaser and to meet the particular needs of the purchaser;
- B) the property has use or value only for the specific purpose for which it is produced; and
- C) the property has use or value only to the purchaser. 86 Ill. Adm. Code 130.2115(b).

Please note that if a manufacturer constructs and sells 50 or more identical sets of a particular product in a single repeat order or simultaneous orders from a user (so-called multiple orders), those sales will be deemed to be volume production and will be subject to Retailers' Occupation Tax (rather than Service Occupation Tax) liability based on the total amount received by the manufacturer from such volume production orders. Also, even items that qualify for exemption from the Retailers' Occupation Tax, if sold subsequently without material change to the purchaser for use (so-called repeat orders), will become subject to the Retailers' Occupation Tax because the skill that is involved after the first item is made is production skill and not specialized engineering and design skill. See 86 Ill. Adm. Code 130.2115(a)(4). If a manufacturer also makes retail sales of tangible personal property, such as other non-manufactured products, that manufacturer will incur Retailers' Occupation Tax liability on those sales.

Please note, further, contractors having contracts with customers to sell and permanently affix tangible personal property to realty incur a Use Tax liability on their cost price of such materials permanently affixed. If the contractors do not remit this tax to Illinois registered suppliers, the contractors must register and self-assess and remit the Use Tax to the Department. See 86 Ill. Adm. Code 130.2075.

These inquiries are very fact-specific. The seller must determine in each situation whether the sale qualifies for the exemption under the provisions of 130.2115(b).

As to the requirement that the seller be employed primarily for his engineering or other scientific skill to design and produce the property, it is sufficient if the seller is responsible for making a substantial contribution to the designing of the property that is to be produced on special order. See subsection (b)(2) of Section 130.2115. A manufacturer who takes a customer's blueprints and prepares its own drawings that set out the materials, dimensions, and the method of manufacture necessary to create a customized product and then uses those drawings to manufacture that product, will generally be considered to be responsible for making a substantial contribution to the designing of the property as long as the manufacturer is contractually responsible for the engineering and/or design. This is not affected by the fact that the manufacturer may subcontract out the engineering work to another as long as the manufacturer is contractually responsible for the engineering work. It is important to note that this requirement of the test is not met if the product is manufactured simply from the blueprints or drawings provided by the customer. One indication that the seller made a substantial contribution to the designing of the product is if the seller signs the designs or drawings after making that substantial contribution.

In the case where sellers of special order property are not subject to Retailers' Occupation Tax in accordance with Section 130.2115, 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 the servicemen, depending upon which tax base the servicemen use 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 the sales of service. Upon selling their product, they are required to collect the corresponding Service Use Tax from their customers. 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. 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 are 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 the tax to the

Department by filing returns and do not pay tax to suppliers. They provide suppliers with Certificates of Resale for the property transferred to service customers. See 86 Ill. Adm. Code 140.108.

The final method of determining tax liability may be used by de minimis servicemen 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 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). Such de minimis servicemen may pay Use Tax to their suppliers or may self assess and remit Use Tax to the Department when making purchases from unregistered out-of-State suppliers. Those servicemen are not authorized to collect "tax" from their service customers because they, not their customers, incur the tax liability. Those servicemen are also not liable for Service Occupation Tax. It should be noted that servicemen do not have the option of determining whether they are de minimis using a transaction-by-transaction basis. See 86 Ill. Adm. Code 140.109.

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

DMB:lkM