

Under the Retailers' Occupation Tax Act, the manufacturing machinery and equipment exemption is available for blasting agents, high explosives, detonators, lead-in line and blasting machines used in the extractive process of quarrying if they are used primarily to manufacture or assemble tangible personal property for wholesale or retail sale or lease. See 86 Ill. Adm. Code 130.330. (This is a PLR.)

September 9, 2021

Dear NAME:

This letter is in response to your letter dated August 12, 2021, 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.

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 COMPANY1., 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 COMPANY1., 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:

**Re: COMPANY1.
Revised Private Letter Ruling Request**

Greetings:

As counsel for, and on behalf of COMPANY1, doing business as COMPANY2, ("COMPANY2"), we, pursuant to 2 Ill. Admin. Code §1200. 110, hereby formally request a Private Letter Ruling ("PLR") regarding how COMPANY2 should collect Use Tax ("UT") from its customers and remit Retailer's Occupation Tax," ("ROT") (collectively, "sales taxes"). COMPANY2 is not currently under audit by the Illinois Department of Revenue ("Department") regarding this issue. In

addition, COMPANY2 is not aware of any authority contrary to its views expressed in this request. Furthermore, we ask that our client's name, address, and any contracts or exhibits attached be kept confidential and deleted from the publicly disseminated version of the PLR.

Please note that this request is a revision of a request submitted in December 2020, to which the Department issued GIL ST-21-0020 on May 25, 2021. Following informal discussions, COMPANY1 and the Department held a phone conference in July 2021 during which the Department asked several clarifying questions. COMPANY2 now responds to these questions in the following, narrowed request for a PLR.

FACTS

COMPANY2 sells explosives and provides licensed explosives services to customers that need to break up rock masses for excavation for mining and quarrying purposes. Illinois and other states tightly regulate the use of high explosives, so COMPANY provides various services in addition to the explosive materials that it sells. Each of these are discussed in turn below.

a. COMPANY2'S Services

Safely breaking a large rock mass into smaller pieces requires diligent preparation and expert skill. To this end, COMPANY2'S explosives workers evaluate each rock mass and determine the combination of explosive materials best suited to the task. This combination depends on environment factors such as the type, density, moisture levels, bedding, and size of the rock masses that will be broken up. Explosives workers also consider the area surrounding the detonation site and weather conditions. Once the workers determine the correct combination of materials, they prepare the rock face by drilling "boreholes" into the rock surface at appropriate depths and intervals. The workers then place the explosive materials into the boreholes, set up the blast management system, and safely break up the rock face by detonating the explosives. In some instances, COMPANY2 may pump explosive materials into boreholes, combine these materials with additional chemicals to form an explosive, and then detonate using a blast management system. For purposes of this Request, we refer to these services collectively as the "Services".

b. COMPANY2'S Products

The exact combination of explosive materials used varies from job to job, but always includes some combination of blasting agents, high explosives, boosters and a blast management system to provide the Services (the "Products"). Each of these items plays a complementary role in breaking up rock masses.

Chemical blasting agents are used with explosive compositions to enhance reactivity at detonation. For example, ANFO, a common blasting agent, is produced by mixing ammonium nitrate and fuel oil to create an explosive. The ammonium nitrate "oxidizes" the composition, helping to absorb the fuel oil uniformly and enhance the detonation. Chemical blasting agents detonate and create a blast but are not classified as an "explosive" under Illinois law.

COMPANY2'S explosives are modern, refined versions of the what we commonly think of as "dynamite". These explosives include Titan® and Blastex® products which produce a powerful detonation reaction when triggered by a blast management system. COMPANY2 also uses certain "gassed" emulsions, which are pumped into a borehole and mixed with additional chemicals to form an explosive. The explosive(s) used depends on the conditions at the detonation site. Some explosives, such as Titan are ideal for wet conditions, while others, such as DYNOMIX™, are best suited for dryer conditions and soft to medium rock types. Explosives workers may also use a chemical booster to detonate the explosives.

Importantly, these Products are stable and will not detonate without an external initiation signal from a blast management system. COMPANY'S2 explosives workers set up these systems by connecting the placed explosive materials to a detonator device. This can be done using wires that will conduct an electric signal or a "lead line" that will conduct a nonelectric signal. Once everything is safely in place, the explosives worker triggers the detonator device and initiates the detonation reaction.

COMPANY2'S blasting agents, high explosives, and boosters are all single- use, while some components of the detonator delivery systems can be used repeatedly.

c. Transaction at Issue

COMPANY2'S original request contemplated three different ways in which COMPANY2 invoices its customers for product-plus-service transactions. For purposes of obtaining a private letter ruling, COMPANY2 has narrowed its request to just one transaction

type and requests the Department's guidance on the correct sales tax treatment of Products in instances where COMPANY2 invoices its customers for Services only and does not list the Products as a separate line item. COMPANY2 believes that any Products used in this situation are exempt manufacturing equipment.

ILLINOIS LAW & ANALYSIS

Illinois generally imposes ROT on all retail sales of tangible personal property, but exempts machinery and equipment used primarily to manufacture tangible personal property. 35 ILCS 120/2-5(14) and 86 Ill. Admin Code 130.330. Illinois also provides an identical exemption from UT. 35 ILCS 105/3-5(18).

"Manufacturing", as defined in the regulation, is the production of any article of tangible personal property, whether it be a finished product or an article for use in manufacture of a different article of tangible personal property. 86 Ill. Admin Code 130.330(b)(1). The production process must occur by procedures commonly regarded as manufacturing, processing, fabricating, or refining that changes some existing materials into a material with a different form, use, or name. *Id.* This change must be substantial and significant. *Id.*

"Machinery" is defined as a major mechanical machine or major components of a machine contributing to a manufacturing or assembling process and "equipment" is defined as an independent device or tool separate from machinery, but essential to an integrated manufacturing process. 35 ILCS 120/2-45. Exempt equipment includes chemicals and chemicals acting as catalysts if they effect a direct and immediate change upon a product being manufactured. *Id.* Manufacturing machinery and equipment is exempt "whether the materials used in the process are owned by the manufacturer or some other person". 35 ILCS 120/2-5(14); 35 ILCS 105/3-5(18).

Although extractive industrial activities are not generally considered to be "manufacturing", the regulation specifically states that blasting agents, high explosives, detonators, lead-in line, and blasting machines used the extractive processes of mining or quarrying constitute exempt manufacturing equipment. 86 Ill. Admin. Code 130.330(b)(4).

The Department directly addressed a nearly-identical set of facts in a 2009 GIL, concluding that explosives and blasting equipment used in quarries for the purpose of fragmenting rock

masses into a manageable size qualified as exempt manufacturing machinery and equipment ("MME"). ST 09-0149-GIL (11/09/2009). Although this GIL is obsolete due to age, the Department's conclusion relies on the same sections of the Retailers' Occupation Tax Act and regulation cited above, the relevant language of which has not been amended since the Department issued the GIL.

LEGAL ANALYSIS

During the July 2021 conference, the Department asked two additional questions to confirm whether COMPANY2'S Products are exempt:

1. What percentage of COMPANY2'S sales are product-only and do not include services?

Roughly 20% of COMPANY2'S Illinois gross receipts are Product-only sales in which COMPANY2 delivers Product but does not detonate the explosive materials. COMPANY2 charges Illinois sales taxes for these transactions unless the customer provides a properly executed exemption certificate. For the avoidance of doubt, these transactions are not included in the factual situation for which COMPANY2 seeks a ruling.

2. What percentage of aggregate produced during the blasting process is sold at retail or wholesale to a third party?

Per the general manager of COMPANY2'S Illinois site, the "vast majority" of aggregate produced from COMPANY2'S Services is either (i) sold directly to a third party or (ii) used as an ingredient in an additional manufacturing process. This is true regardless of how the produced aggregate is measured, whether that be by volume, by dollar value, or by the number of jobs/transactions.

Based on these responses, the Department should rule that COMPANY2 is not required to remit ROT or UT on Products used in the transaction described above. COMPANY2 uses Products to convert masses of rock into smaller pieces of rock. The blasting agents, high explosives, and boosters which create the detonation reaction are all chemicals specifically designated by the Department as exempt manufacturing equipment in certain circumstances. 35 ILCS 120/2-5(14) and 120/2-45; 35 ILCS 105/3-5(18); ST 09-0149-GIL (11 /09 / 2009). More specifically, these items qualify as exempt when used as a catalyst to affect a direct and immediate change upon the product being manufactured. 35 ILCS 120/2-45; 86 Ill. Admin. Code 130.330(b)(4).

Illinois defines "manufacturing" broadly to include the production of any article of tangible personal property, whether it be a finished product or an article for use in the manufacture of a different article of tangible personal property, and occurs when existing materials undergo substantial and significant changes which result in a material with a different form, use, or name. 86 Ill. Admin. Code 130.330(b)(l). The manufactured products must be sold at wholesale or retail by either the taxpayer claiming the exemption or the entity which owns the materials used in the manufacturing process in order for the exemption to apply. 35 ILCS 120/2-5(14). Here, the chemicals affect a direct and immediate change on rock masses through the detonation reaction, beginning the process of turning large, unusable rock into manageable aggregate which may be further processed for a variety of other construction and landscaping uses. As stated by the Department, a majority of this aggregate must be sold or used as an ingredient for further manufacturing in order for the exemption to apply. In the transaction contemplated, the vast majority of the aggregate COMPANY2'S Products and Services produce is either (i) sold at retail or wholesale by COMPANY2 or the entity which owns the mine or quarry; or (ii) used as an ingredient for additional manufacturing. Accordingly, COMPANY2 is engaged in manufacturing and these chemicals are exempt from sales and use taxes because they are used solely to affect this process. The detonator delivery systems COMPANY2 uses have also been defined as exempt manufacturing equipment in the regulation. See 86 Ill. Adm in. Code 130.330(b)(4). This equipment is essential to the manufacturing process because it provides the external stimulus necessary to trigger a detonation reaction. Accordingly, COMPANY2 is engaged in a manufacturing process and the Products used are exempt from ROT and UT.

REQUEST FOR RULING

Pursuant to 2 Ill. Admin. Code Section 1200.110, Taxpayer respectfully requests that the Department issue a private letter ruling declaring that:

- (i) In the facts outlined in this Request, COMPANY2'Ss Products are used in a manufacturing process and are exempt from ROT and UT.

If you concur, please issue your favorable ruling to the undersigned. If you do not concur, please advise so that we may discuss your reasoning before an adverse ruling is issued. A Power of Attorney authorizing or- representation of COMPANY2 is enclosed.

DEPARTMENT'S RESPONSE:

The 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. 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.

Retailers' Occupation Tax and Use Tax do not apply to sales of service. Under the Service Occupation Tax Act, businesses providing services (i.e., servicemen) are taxed on tangible personal property transferred as an incident to sales of service. 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. The serviceman'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 serviceman's entire bill;
- 3) Service Occupation Tax on the serviceman's cost price if the serviceman is a registered de minimis serviceman; or
- 4) Use Tax on the serviceman's cost price if the serviceman is de minimis and is not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

The Retailers' Occupation Tax Act does not apply to sales of machinery and equipment used primarily (over 50%) in the manufacturing or assembling of tangible personal property for wholesale or retail sale or lease. See 86 Ill. Adm. Code 130.330. Accordingly, the Service Occupation Tax Act also does not apply to these sales, and the provisions of Section 130.330 are used to determine whether a piece of equipment, transferred incident to a sale of service, qualifies for the manufacturing machinery and equipment exemption. See 86 Ill. Adm. Code 140.125(o).

"Manufacturing", as defined in Section 130.330, is the production of articles of tangible personal property, whether such articles are finished products or articles for use in the process of manufacturing or assembling different articles of tangible personal property, by procedures commonly regarded as manufacturing, processing, fabricating, or refining which changes some existing material or materials into a material with a different form, use or name. These changes must result from the process in question and be substantial and significant. See 86 Ill. Adm. Code 130.330(b)(1).

Manufacturing equipment, as noted in Section 2-45 of the Act and in Section 130.330(c)(2), includes any independent device or tool separate from any machinery but essential to an integrated manufacturing or assembling process, including any subunit or assembly comprising a component of any machinery or auxiliary, adjunct, or attachment parts of machinery, such as tools, dies, jigs, fixtures, patterns, and molds, and any parts that require periodic replacement in the course of normal operation. As Section 2-45 of the Act notes, the exemption also includes chemicals or chemicals acting as catalysts but only if the chemicals or chemicals acting as catalysts effect a direct and immediate change upon a product being manufactured or assembled for sale or lease.

Generally, the types of equipment and material that you describe in your letter may qualify for the manufacturing machinery and equipment exemption. As Section 130.330(b) of the Department's regulations states, a manufacturing process occurs when an existing material is changed into a material with a different form, use or name by a process commonly regarded as manufacturing. The extractive processes of mining or quarrying may constitute manufacturing. See *Nokomis Quarry v. Department of Revenue*, 295 Ill. App. 3d 264 (5th Dist. 1998) (holding that a calculated blasting method that is performed with specific desired results, which changes limestone deposits into materials with a different form, possessing new qualities or combinations, constitutes manufacturing). Blasting agents, high explosives, detonators, lead-in line and blasting machines are all examples of tangible personal property that is often used in the extractive process of quarrying and may qualify for the exemption. See 86 Ill. Adm. Code 130.330(b)(5).

The manufacturing machinery and equipment exemption is a use-based exemption. As a result, items do not qualify in and of themselves, but only if they are used primarily (over 50%) in a qualifying manner. See 86 Ill. Adm. Code 130.330(a)(3). If the blast management systems, detonator delivery systems, and other manufacturing equipment (such as drills to make boreholes) are used primarily in a qualifying manner (used to produce rock offered for wholesale or retail sale or lease or used to produce rock used in another manufacturing process in which the end product is offered for wholesale or retail sale or lease), these items qualify for the manufacturing machinery and equipment exemption. See *Illinois Valley Paving, Inc. v. Department of Revenue*, 294 Ill. App. 3d 1123 (1998). (If a Company's customer subsequently uses the rock to make and lay asphalt pursuant to a construction contract, the items are not being used in a qualifying manner.) The blasting agents, boosters, and high explosives also qualify for the manufacturing machinery and equipment exemption if used in a qualifying manner.

You state in your letter that approximately 20% of the Company's gross receipts are product-only sales in which the Company delivers product but does not detonate the explosive materials. For the single-use items (i.e., blasting agents, boosters, and high explosives) and any other items sold separately, the Company may

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provide its supplier with an exemption certificate stating that 80% of these items will be used in the manufacturing process and qualify for manufacturing machinery and equipment exemption and 20% of the items qualify for the resale exemption. Any tangible personal property that you sell at retail (product-only sale) is subject to Retailers' Occupation Tax, including any applicable local taxes.

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 further 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,

Richard S. Wolters
Chairman, Private Letter Ruling Committee

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COMPANY1/NAME

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