

The Service Occupation Tax is a tax imposed upon servicemen engaged in the business of making sales of service in this State, based on the tangible personal property transferred incident to sales of service. See, 35 ILCS 115/3. (This is a PLR.)

May 3, 2006

Dear Xxxxx:

This letter is in response to your letter dated February 14, 2005, 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 1200.1120. 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 ABC 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 ABC 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:

TAXPAYER REPRESENTATIONS

1. This ruling request is submitted in conformance with the requirements established in 86 Ill. Admin. Code 1200.110.
2. The issues addressed in this ruling request are not involved in the taxpayer's returns for any period that is under examination by the Department as part of an audit.
3. The issues addressed in this ruling request are not part of a case pending in litigation involving the taxpayer or a related party.
4. The Department previously issued Private Letter Ruling ST 92-0361 (7/7/1992) to the taxpayer in connection with similar transactions. However, the taxpayer's facts have materially changed since that ruling was issued. Neither the taxpayer

nor the taxpayer's representative has subsequently submitted a ruling request on this same or similar issue.

5. The taxpayer has no knowledge of any authorities that are contrary to the taxpayer's conclusions as provided in the 'Taxpayer Analysis' section below.
6. The taxpayer requests that all confidential information be deleted pursuant to 86 Ill. Admin. Code 1200.110(c) prior to dissemination of the Department's ruling to the public.

STATEMENT OF THE FACTS

The taxpayer is a distributor of direct mail materials both inside and outside Illinois. The majority of the taxpayer's business involves the distribution of direct mail materials that are printed by its customers and delivered to the taxpayer's distribution facilities for processing and mailing. However, the taxpayer also contracts with various third-party printers to print different types of printed advertising materials on behalf of certain customers. The taxpayer assembles these two categories of printed materials into a single cooperative direct mail package¹ for delivery to residential addresses both inside and outside Illinois. These packages are delivered by the US Postal Service to residential recipients at no charge to the recipient.

The taxpayer has no processing, distribution, warehousing, or inventory facilities in Illinois. Instead, all of the print materials mailed by the taxpayer to Illinois residents are processed at the taxpayer's facilities in other states. Once the direct mail packages are assembled for delivery, a representative of the US Postal Service weighs the material and verifies the postage required for mailing. Postal representatives are located on site at each of the taxpayer's processing facilities outside Illinois. The assembled packages are then loaded onto trucks owned and operated by third-party carriers, who transport the materials to postal facilities for delivery by the US Postal Service. Some of the assembled packages are delivered to postal facilities inside Illinois for delivery to Illinois residential addresses.

The taxpayer has two sales offices in Illinois (at CITY1 and CITY2). Illinois sales management is also located in CITY2. However, as outlined hereafter, the taxpayer approves all customer orders in STATE—not at the taxpayer's sales offices inside Illinois.² Customer orders are managed as follows:

1. A salesperson solicits the customer to purchase a particular product at a specified volume for a particular date.
2. Assuming the customer agrees, the salesperson will contact a customer service person with the content of the customer's order. If the salesperson is from an Illinois sales office, initial order entry will occur in either CITY1, CITY2, or the taxpayer's Customer Service Center in STATE—depending on the specific customer. All customer orders are entered into the taxpayer's order management system, which is maintained in STATE.
3. Approximately two weeks before the tentative order enters the fulfillment process, the taxpayer's Collections personnel begin a series of financial checks—referred to as the 'Payment Release' process. These Collections

personnel are all located in STATE. All customer orders are subject to the Payment Release process before an order can enter the fulfillment process.

4. The orders for customers who do not pass the criteria for the Payment Release process are placed on hold, pending resolution of the outstanding payment issue. The taxpayer's Collections personnel in STATE provide two notices of the hold status to the customer's sales representative and/or customer service representative. Those representatives attempt to resolve the payment issue with the customer prior to a pre-determined Payment Release deadline.
5. If the Payment Release deadline arrives and the payment issue is not resolved, the taxpayer's STATE Collections personnel reject the customer order, and the order never enters the fulfillment process. The Collections personnel will continue to reject any future orders until the customer resolves its outstanding payment issues.

ISSUES FOR RULING

1. Are any of the taxpayer's sales of print subject to an SOT or SUT tax collection obligation?
2. If the taxpayer's sales of print are not subject to SOT or SUT tax collection, is the taxpayer obligated to self-assess Use Tax on its print sales?

TAXPAYER ANALYSIS

Issue 1: Are any of the taxpayer's sales of print subject to an SOT or SUT tax collection obligation?

The taxpayer is engaged in the business of making sales of services in Illinois and, as such, is required to evaluate the rules of the Service Occupation Tax ('SOT') instead of the Retail Occupation Tax. 86 Ill. Admin. Code 140.01(a).

The taxpayer believes the Service Use Tax ('SUT') rules—as the complementary tax to the SOT—apply to all of its print material distributed inside Illinois. If the taxpayer distributed its print materials from inside Illinois, the SOT rules would apply. However, the taxpayer has no processing, distribution, warehousing, or inventory facilities in Illinois. Instead, all of the print materials distributed by the taxpayer in Illinois are processed at the taxpayer's facilities in other states. Nevertheless, the Department has concluded that maintaining a sales office inside Illinois is still sufficient to impose a tax collection obligation on a company that has no fulfillment operations or inventory inside Illinois. IL Gen. Info. Ltr. ST 95-0321; see also 86 Ill. Admin. Code 160.130(c). Because of the taxpayer's two Illinois sales offices, the taxpayer may be required to collect either SOT or SUT from its customers who distribute print materials inside Illinois.

Because of the recent changes in the taxpayer's order acceptance policies, the taxpayer believes the SOT rules do not apply to the taxpayer—in contrast to the Department's conclusion in the taxpayer's prior ruling. In that earlier ruling, the Department concluded that the taxpayer approved orders in Illinois, thereby causing the taxpayer's print sales to be subject to SOT. However, the taxpayer has now modified and centralized its order approval process in STATE³ as described above. The Department has concluded that a direct mail firm exercises no power or control over custom printed materials in Illinois

when the direct mailer accepts orders outside Illinois and conducts all of its printing and mailing operations outside Illinois. Ill. Gen. Info. Ltr ST 02-0174. Even when a tentative order originates in Illinois, the Department has concluded that the final step in the order approval process determines where a sale is sourced. Ill. Priv. Ltr Ruling ST 01-0020 (citing the credit approval process as the determinative step). As described above, the taxpayer's final step in the order process is the approval or termination of the order by its Collections personnel located in STATE. Consequently, the taxpayer's sales should be sourced to STATE. Notwithstanding these sourcing rules, the Department has concluded that if a serviceman performs no fulfillment or selling activities in Illinois (but still has a physical presence in the state), the SUT rules will apply. As such, the taxpayer believes the SUT rules apply to its sales in Illinois.⁴

Based on the SUT rules, the taxpayer believes its customer's purchases of printed materials for distribution inside Illinois are not subject to tax. The Department has concluded that a serviceman's customer must make 'use' of the tangible personal property in Illinois before the vendor is required to collect SUT on the transaction. Ill. Gen. Info. Ltr ST 02-0174. Furthermore, the Department has concluded that no Illinois use occurs when custom printed materials are placed into a US Postal Service mail unit at a direct mailer's distribution facility outside Illinois. Ill. Priv. Ltr Ruling ST 01-0026. Consequently, the taxpayer believes its customers make no taxable use of the printed materials in Illinois and that the taxpayer is not required to collect SUT as a result.

Issue 2: If the taxpayer's sales of print are not subject to SOT or SUT tax collection, is the taxpayer obligated to self-assess Use Tax on its print sales?

As stated previously, the taxpayer makes sales of services in connection with each type of printed product that the taxpayer has printed for distribution in Illinois. Said in another way, customer advertising appears on every article of tangible personal property that the taxpayer has printed for distribution, and the taxpayer bills a customer for services and incidental costs of tangible personal property in connection with every article of material the taxpayer has printed for distribution. As such, the SOT and SUT rules apply to each of the taxpayer's printed products. More specifically, because the taxpayer does not approve orders in Illinois, the SUT rules apply to each of the taxpayer's printed products (strictly because of the taxpayer's sales offices in Illinois). In order for the Use Tax ('UT') to apply to the taxpayer's printed products, the taxpayer would have to be classified as a de minimis serviceman under the SOT rules. However, the de minimis serviceman classification does not apply to the SUT. 86 Ill. Admin. Code 160.110(h). Because the de minimis rules do not apply to servicemen subject to SUT collection obligations, the taxpayer believes the UT self-assessment rules do not apply to its print products distributed in Illinois.

TAXPAYER CONTACTS

NAME/ADDRESS

SIGNATURES

This ruling request is submitted on behalf of ABC and in conformance with the requirements established in 86 Ill. Admin. Code 1200.110. Furthermore, ABC has granted a Power of Attorney (original attached) to INDIVIDUALS to act on our behalf in

connection with this ruling request. INDIVIDUAL will serve as the Department's primary point of contact.

If you have questions or require further clarification, please contact us at your earliest convenience. If you believe the Department may issue a ruling contrary to our conclusions above, we ask that you contact us in advance of issuing the ruling.

DEPARTMENT'S RESPONSE

Application of Service Occupation Tax and Service Use Tax

Based upon the facts presented in your letter and your follow up of February 9, 2006, we do not believe that ABC will incur any Service Occupation Tax liability on these transactions. We reach this conclusion based upon the fact that no sales of service have occurred in the State of Illinois. The facts presented indicate that the customer's purchase order is accepted by ABC's facility in STATE. The customer's order is also printed at an out-of-State printing facility.

Similarly, we do not believe that ABC will incur a Service Use Tax collection obligation on these sales. When a serviceman incurs a Service Occupation Tax liability, he is generally required to collect a corresponding amount of Service Use Tax from his Illinois customer. There are also instances in which a serviceman located outside of Illinois is required to collect the Service Use Tax from its Illinois customers. However, Service Use Tax liability is predicated upon a customer's use, in Illinois, of tangible personal property that is the subject of a sale of service. Section 2 of the Service Use Tax Act states that "'use' means the exercise by any person of any right or power over tangible personal property incident to the ownership of that property...." 35 ILCS 110/2. Consequently, a person makes a "use" of tangible personal property when he makes a gift of it in Illinois to another person. In the situation you have described, there is no "use" by the service customer in Illinois. The materials are "used" outside Illinois when they are turned over to a third party carrier for delivery into the Postal Service mail unit. At that point, it is our understanding that the service customer loses any ability to exercise control over (e.g. recall) the materials.

Application of Use Tax

Your second issue involves application of the Illinois Use Tax to these transactions. You request a ruling that ABC is not under an obligation to collect or to pay Illinois Use Tax on the cost of tangible personal property printed at out-of-State facilities and distributed by the Postal Service into Illinois as described.

A "de minimis" serviceman may incur a Use Tax liability with respect to his sales of service. If the serviceman qualifies as de minimis, he may remit either Service Occupation Tax. or Use Tax on his cost price of the tangible personal property transferred to service customers. See, Section 140.105. The type of tax remitted depends upon the activities of the serviceman. Section 2 of the Service Occupation Tax Act provides that a sale of service made by a de minimis serviceman not otherwise required to be registered as a retailer under Section 2a of the Retailers' Occupation Tax Act is not subject to tax under the Service Occupation Tax Act. Rather, it provides that the purchase of tangible personal property by the serviceman is subject to tax under the Retailers' Occupation Tax Act and the Use Tax Act. See 35 ILCS 115/2. When a serviceman elects to remit Use Tax, he is considered the end user of the tangible personal property transferred to his service customers. The serviceman, and not his customers, incurs a Use Tax liability.

You have indicated that ABC is a de minimis serviceman and could elect to pay Use Tax on the cost price of the tangible personal property it transfers incident to sales of service. However, we do not believe that this liability applies. Section 3 of the Use Tax Act imposes tax upon the privilege of using tangible personal property in Illinois. See 35 ILCS 105/3. Section 2 of the Use Tax Act defines "use" as "the exercise by any person of any right or power over tangible personal property incident to ownership of that property...." See 35 ILCS 105/2. The materials that ABC transfers are printed solely outside of Illinois and are deposited with a third party carrier outside Illinois for delivery to a Postal Service mail unit. ABC exercises no control over these materials inside the State of Illinois. As a result, ABC does not "use" any of the tangible personal property in Illinois. Consequently, Use Tax does not apply to these transactions.

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.

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,

Martha P. Mote
Associate Counsel

MPM:msk

¹ Cooperative direct mail is a form of direct mail advertising whereby the advertisements of several unrelated advertisers are assembled into a single package for delivery at no cost to prospective consumers. By combining their advertisements in a single package, advertisers can take advantage of lower postage costs and targeted distribution services.

² At the time the Department issued the prior ruling to the taxpayer, customer orders were approved by field personnel.

³ In its prior ruling to the taxpayer, the Department indicated that the SUT would apply to the taxpayer's sales if it no longer approved orders in Illinois.

⁴ If the Department were to conclude that the SOT de minimis serviceman rules did apply to the taxpayer, the taxpayer still believes its print products would not be subject to UT because the taxpayer does not make a taxable 'use' of the print products in Illinois. See Ill. Priv. Ltr. Ruling ST 01-0026 (custom printed direct mail materials not subject to UT when deposited in a US postal unit at the direct mailer's distribution facility outside Illinois).