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July 24, 2007

Dear Xxxxx:

This letter is in response to your letter dated January 29, 2007, 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](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:

This is a request for a general information letter on the taxability under the Illinois Retailers' Occupation Tax ('ROT'), Service Occupation Tax ('SOT'), Service Use Tax ('SUT') and Use Tax ('UT') of the sale of a steam conversion service.

The facts are as follows. A manufacturing corporation that used steam in its manufacturing process split into two separate entities. Both resulting corporations continued to be located next to each other on the same industrial site. Both corporations (hereinafter 'Company A' and 'Company B') continued to need steam for manufacturing production purposes. Both companies purchase their water from the same municipal water company. However, each company has its own separate metered line.

In order to continue to use steam in its production process, Company A has to rely upon steam made by Company B's boilers. As a result, the Companies have entered into a service agreement in which Company A pipes water it obtains from the municipal water company through a metered line to a holding tank for Company B's boilers. The amount of water piped to Company B is metered to insure it equals the amount of steam needed to be produced from such water. The holding tank also includes water piped there by Company A that Company A also purchases from the same municipal water company for its own use in making steam for its own production process.

Steam is generated by Company B's boilers using the water from the holding tank and then piped to Company A based on the amount of steam needed that corresponds to the water supplied by Company A. Company B does not provide steam to any other

company. At the end of each month, a true-up is undertaken to insure that the amount of water being supplied equals the amount of steam received. At all times, Company A retains ownership over the water (both in steam and liquid form) it supplies and then receives back in steam form from Company B. Company B charges Company A a service fee for converting Company A's water into steam and piping it back to Company A.

## **Analysis**

The Illinois ROT and UT are imposed on the sale of or privilege of using tangible personal property purchased at retail from a retailer. 35 ILCS 105/3; 35 ILCS 120/2. When no title or ownership of property is being transferred in the sale of a service, no ROT, SOT, SUT or UT is due. 86 Ill. Admin. Code Sec. 130.120(d); Sec. 140.101; Sec. 130.201(a)(1); See also Sec. 130.2156(b) (Vendors of steam incur no ROT liability 'so long as no tangible personal property is transferred to the purchaser.')

In Private Letter Ruling ST 94-0399 (9/26/94) PLR, the Department acknowledged that the sale of steam generated from water supplied from the steam buyer is not a sale subject to Illinois ROT, SOT, SUT or UT. The seller/service provider in that case was a combined electric and natural gas public utility that sold steam heat. The steam was also used to make electricity. One of its steam heat customers was a manufacturer of alcohol products. The manufacturing customer provided the utility with water from its wells that it piped to the utility. The utility used the water to make steam and used that steam to make electricity that it sold to other customers. The steam was then piped to the manufacturing customer who used it in its manufacturing operation. The manufacturing customer retained the condensate, but could return it with additional water to the utility to continue the same process. The manufacturing company at all times retains ownership over the water (in both steam and liquid form). The utility charged the manufacturing customer a service charge for converting the water into steam and piping it to the manufacturing customer.

The Department of Revenue held that such an arrangement was not subject to the ROT, SOT, SUT or UT.

The situation addressed in this letter is virtually identical to the one in ST 94-0399. Here, Company A supplies water to Company B to make steam for Company A. The water is piped to Company B's holding tank where it retains water for its boilers. Company B has no other steam customers. Therefore, the only water in the holding tank is Company A's and Company B's water. Since the water is purchased from the identical supplier, it is completely fungible and identical in all respects. Company B only uses its boilers to make steam for itself and steam for Company A. Company B makes sufficient steam for Company A based on the amount of water supplied by Company A. To insure sufficient water to make steam is supplied by Company A to Company B, the water and steam are metered or otherwise calculated by the Companies. At the end of the process the water (now contaminated condensate) is retained and cleaned by Company A for disposal or further use.

Throughout the entire process, Company A retains ownership of the water (both in liquid and steam form) and supplies sufficient water for the steam conversion service provided by Company B. To make certain that only the service of steam conversion is being purchased from Company B and not any tangible personal property, a true-up is performed each month to make sure any minor discrepancies are immediately resolved.

Based on the above, we request a general information letter confirming that the purchase of steam conversion services by Company A from Company B is not subject to ROT, SOT, SUT or UT. If you have any questions, please call.

#### **DEPARTMENT'S RESPONSE:**

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. 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 86 Ill. Adm. Code 150.101. Similarly, Service Occupation Tax and Service Use Tax are imposed on tangible personal property transferred incident to a sale of service. See 86 Ill. Adm. Code 140.101 and 160.101.

In general, if one business provides tangible personal property to another business and the second business returns the same tangible personal property back to the first business in a different form, then no Retailers' Occupation Tax, Use Tax, Service Occupation Tax, or Service Use Tax is owed for this transaction by either business. This same rule applies if the tangible personal property provided by the first business is fungible tangible personal property and that fungible tangible personal property is commingled with other identical fungible tangible personal property by the second business before being returned to the first in a different form. An example of this is when water is provided by one business to another and the second business commingles this water with its own water from an identical source and generates steam from the water and returns steam to the first business in an amount equal to the amount of water provided by the first business.

However, if any additional tangible personal property is transferred to the first business in connection with the property being returned to the first business, that tangible personal property is subject to Service Occupation Tax or Use Tax, depending upon which tax base the serviceman chooses to calculate his or her liability. In the example above, if the steam returned to the first business contains chemicals or other tangible personal property that was not in the water provided by the first business, Service Occupation Tax or Use Tax would be owed on the chemicals or other tangible personal property. This response assumes that the second business can ensure that the amount of property returned in another form (such as steam) to the first business corresponds correctly with the amount of property (such as water) supplied by the first business.

It should also be noted that while tangible personal property such as water from the same source is truly fungible, there may be instances where items that might be considered fungible in general practice may not be considered fungible for these purposes because they are not truly identical. The Department's position in this letter is limited to commingling water that comes from an identical source.

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. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Sincerely,

Samuel J. Moore  
Associate Counsel

SJM:msk