

Construction contracts for the improvement of real estate consisting of engineering, installation, and maintenance of voice, data, video, security, and all telecommunication systems incur Use Tax, rather than Retailers' Occupation Tax, on these items if they are sold at one specified contract price. See 35 ILCS 120/1 and 86 Ill. Adm. Code 130.1940(c)(3). (This is a GIL.)

November 18, 2008

Dear Xxxxx:

This letter is in response to your letter dated February 19, 2008, 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.

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:

We are in the process of updating our taxability guidelines as they relate to specialty contractors (i.e. security systems, fire alarm systems and HVAC system), and exempt entity exemptions. Attached are two matrices we would like for you to complete. Fact patterns are as follow [sic]:

Matrix 1 – Exemption Applicability & Contractor Flow-through Provisions

Contractor A installs security, fire alarm, and HVAC systems for various businesses and exempt entities. The exempt entities often claim they are exempt from sales tax, however, the contractor needs to confirm if the exemption is a flow-through exemption (i.e. the contractor can purchase the items tax exempt on behalf of the exempt entity), or if the exemption requires the exempt entity purchase all exempt items direct from the supplier. Contractor A also would like to confirm they [sic] type of exemption documentation he must obtain and maintain if there is a flow-through exemption.

Matrix 2 – Contractor Taxability Guidelines

Contractor A installs security, fire alarm, and HVAC systems. Contractor A also provides remodeling, repair and service/maintenance assistance on the systems. The bids are structured as both lump sum or time & material contracts based on the customer's request. Contractor A would like to confirm the taxability of his products and services per the attached matrix. All systems are installed (hard-wired) into the customer's reality. Contractor A does not sell any mobile equipment.

We appreciate your assistance with this inquiry. Please contact me with any additional questions or if you would like an electronic copy of the matrices. Please forward your response to my attention at your earliest convenience.

DEPARTMENT'S RESPONSE:

The Department generally does not approve the accuracy of private legal publications or complete surveys or matrices. We advise you to consult Illinois statutes and administrative rules as well as Department publications on these matters.

A contract to incorporate tangible personal property into real property is considered a construction contract. The term "construction contractor" includes general contractors, subcontractors, and specialized contractors such as landscape contractors. The tax liabilities regarding construction contractors in Illinois may be found at 86 Ill. Adm. Code 130.1940 and 130.2075 on the Department's Internet website.

In Illinois, construction contractors are deemed end users of tangible personal property purchased for incorporation into real property. As end users of such tangible personal property, contractors incur Use Tax liability for such purchases based upon their cost price of the tangible personal property. See 86 Ill. Adm. Code 130.1940 and 86 Ill. Adm. Code 130.2075. Therefore, any tangible personal property that a construction contractor purchases that will be permanently affixed to or incorporated into real property in this State will be subject to Use Tax.

If a contractor does not pay the Use Tax liability to its suppliers, the contractors must self assess Use Tax liability and pay it directly to the Department. If the contractor has already paid a tax in another state regarding the purchase or use of such property, it will be entitled to a credit against its Illinois Use Tax liability to the extent that it has paid tax that was properly due to another state. See 86 Ill. Adm. Code 150.310. The Illinois Use Tax rate incurred by an out-of-State construction contractor on purchases of materials from an unregistered supplier located outside of this State is generally 6.25% as described in subsection (c) of Section 130.2075.

It is important to note that since construction contractors are the end users of the materials that they permanently affix to real estate, their customers incur no Use Tax liability, and the construction contractors have no legal authority to collect the Use Tax from their customers. However, many construction contractors pass on the amount of their Use Tax liabilities to customers in the form of higher prices or by including provisions in their contracts that require customers to "reimburse" the construction contractor for his or her tax liability. Please note that this reimbursement cannot be billed to a customer as "sales tax," but can be listed on a bill as a reimbursement of tax. The choice of whether a construction contractor requires a tax reimbursement from the customer or merely raises his or her price is a business decision on the construction contractor's part.

In the specific case of installers of security systems, Section 1 of the Retailers' Occupation Tax, in an attempt to ease the burden of administration, provides specifically that "[c]onstruction contracts for the improvement of real estate consisting of engineering, installation, and maintenance

of voice, data, video, security, and all telecommunication systems do not constitute engaging in a business of selling tangible personal property at retail within the meaning of this Act if they are sold at one specified contract price.” The Department’s administrative rules elaborate on this further by stating “[t]his provision applies to all of the items . . . even if they are not incorporated into real estate.” See 86 Ill. Adm. Code 130.1940(c)(3).

As a result of the statutory and regulatory language, installers of security systems described in subsection (c)(3) of Section 130.1940 are authorized to pay Use Tax to their providers on all equipment and supplies they purchase related to the security systems they sell and install, even if some of those supplies are not technically incorporated into real estate, such as the cameras, computers and monitors. This provision applies only if the sale and installation of the security systems are packaged for one specified contract price.

Sales to exempt organizations (organizations that qualify as exclusively religious, charitable, or educational) and governmental entities are subject to tax unless the exempt organization or governmental entity has obtained an active exemption identification number (“E” number) from the Department. See 86 Ill. Adm. Code 130.2007 and 130.2080. Persons or businesses selling tangible personal property to these organizations or governmental entities must be provided with an “E” number for the sales to be tax exempt, unless another exemption can be documented. It is important to note that only sales of tangible personal property invoiced to the organization or governmental entity itself are exempt. Sales made to an individual member or client of an exempt organization or entity are generally subject to tax. Purchases of tangible personal property by a construction contractor for incorporation into the real estate owned by an exempt organization or governmental entity that possesses a valid “E” number at the time of sale may be made free of Illinois Retailers’ Occupation Tax and Use Tax under the provisions of 86 Ill. Adm. Code 130.2075(d).

In claiming the exemption from tax, the construction contractor must provide its supplier with a certification stating that its purchases are for conversion into real estate under a contract with an exempt organization or governmental entity, identifying the organization or entity by name and address and stating on what date the contract was entered into. The construction contractor must also provide the “E” number issued by the Department to the organization or entity for which the purchasing contractor is acting. See 86 Ill. Adm. Code 130.2075(d)(4).

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,

Richard S. Wolters
Associate Counsel

RSW:mzk