

This letter discusses Service Occupation Tax liability involving multi-service situations. See 86 Ill. Adm. Code 140.106, 140.109, and 140.145. (This is a GIL.)

April 1, 2009

Dear Xxxxx:

This letter is in response to your letter dated August 28, 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 requesting a ruling on the following facts and circumstances.

Facts:

CORPORATION is engaged in the manufacture of custom-made corrective eyeglasses for optometrists, opticians, and medical doctors. CORPORATION is located in Illinois. These doctors resell these corrective eyeglasses to their patients at retail prices. All of CORPORATION's sales are for resale to optometrists, opticians, and medical doctors. We have no retail sales. CORPORATION collects resale exemption certificates from some customers when they are registered with Illinois. If a customer is not registered, CORPORATION collects tax from the customer. CORPORATION's invoices do not separately state labor, services, or materials.

Issue:

Is tax due from the taxable customers on 50% of the total invoice including labor, service and material charges?

Ruling Requested:

Tax is due from the taxable customers on 50% of the total invoice including labor, service and material charges.

Reasoning and Authority:

When an optometrist or oculist buys eyeglasses or frames in finished form from an optician, subcontracting part of the work creates a multi-service situation. The primary serviceman must determine the cost price either by using the selling price of the tangible personal property listed on the invoice from the secondary serviceman or, if no selling price is separately stated, 50% of the total invoice including labor and service charges. ILCS Chapter 35 §115/3-10; Ill. Admin. Code 86 §140.126(c)(3); Ill. Admin. Code 86 140.140(h); Ill. Admin. Code 86 §140.145(f).

The selling price of each item of tangible personal property transferred as an incident of a sale of service may be shown as a distinct and separate item on the serviceman's billing to the service customer. If the selling price is not so shown, the selling price of the tangible personal property is deemed to be 50% of the serviceman's entire billing to the service customer.

Ill. Admin. Code 140.126 provides that 'If the optometrist purchased the lenses from an optical lab which ground the lenses to his special order prescription, a multi-service situation would exist. See Section 140.145 for further information.'

Ill. Admin. Code 140.145(f) states that 'Except as provided in subsection (a) of this Section, when a primary serviceman purchases tangible personal property from a secondary serviceman, the primary serviceman shall determine his cost price either by using the separately stated selling price of tangible personal property set forth on the invoice from the secondary serviceman or, if no selling price is separately stated, 50% of the total invoice including labor and service charges, in the absence of proof (e.g., the secondary serviceman's purchase invoices showing his cost price) of the consideration paid by the secondary serviceman for the purchase of such property.'

Illinois Private Letter Ruling No. ST 90-0166-PLR, 04/24/1990 contains a similar situation to our own set of facts. The ruling given allowed a 50% taxable price to the customer.

Any assistance you can provide is greatly appreciated. Please do not hesitate to contact me if you need any further information.

DEPARTMENT'S RESPONSE:

The Department's regulation 86 Ill. Adm. Code 130.310, "Food, Drugs, Medicines and Medical Appliances." describes how sales of products that qualify as drugs, medicines and medical appliances can be subject to the low 1% rate under the Retailers' Occupation Tax Act. Local sales taxes may also apply, depending upon where sales are made. Those items that do not qualify for the low rate are taxed at the State rate of 6.25%, plus applicable local taxes. The same rate distinctions apply under the Service Occupation Tax Act. See 86 Ill. Adm. Code 140.126.

The definition of a medical appliance is "an item which is intended by its manufacturer for use in directly substituting for a malfunctioning part of the body." Examples of qualifying items include prescription eyeglasses or prescription contact lenses.

When health care professionals such as optometrists render service, they are not subject to Retailers' Occupation Tax liability. See 86 Ill. Adm. Code 130.1980. They are, however, subject to liability under the Service Occupation Tax Act to the extent they transfer tangible personal property incident to their rendering of service. Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred as an incident of their sales of service. Servicemen incur either Service Occupation Tax liability or Use Tax liability in these transactions. The tax consequences depend upon the method used to calculate the liability. Servicemen may calculate their tax base in one of four ways: 1) Separately-stated selling price; 2) 50% of serviceman's entire bill; 3) Service Occupation Tax on his or her cost price if he or she is a registered de minimis serviceman; or, 4) Use Tax on his cost price if he or she is an unregistered de minimis serviceman that is not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. See 86 Ill. Adm. Code 140.101.

Optical labs, opticians, and others who grind lenses to order for licensed optometrists are secondary servicemen in multi-service situations. Multi-service situations exist where a primary serviceman subcontracts work to a secondary serviceman. See 86 Ill. Adm. Code 140.145.

The method used by a secondary serviceman to calculate tax is determined by the status of the serviceman (*i.e.*, whether or not the serviceman is registered with the Department) and whether the servicemen qualifies as a de minimis serviceman (*i.e.*, the annual aggregate cost price of tangible personal property transferred incident to the sale of service is less than 35% of the total annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphics arts production)).

Secondary servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act and that qualify as de minimis may use the fourth method of determining tax liability. Such de minimis servicemen satisfy their tax liability by paying Use Tax to their suppliers on the cost price of the tangible personal property. See 86 Ill. Adm. Code 140.126(c)(3). If their suppliers are not registered to collect and remit tax, the servicemen must register, self-assess and remit Use Tax to the Department. The servicemen are considered to be the end-users of the tangible personal property transferred incident to service. Consequently, they are not authorized to collect "tax" from primary servicemen. See 86 Ill. Adm. Code 140.108. Furthermore, secondary servicemen cannot accept certificates of resale from primary servicemen, regardless of the primary servicemen's status. A primary serviceman may request from a secondary serviceman a certification that states that the secondary serviceman has paid, or will remit to the Department, Illinois Use Tax on his or her cost price of the tangible personal property transferred to the primary serviceman. See 86 Ill. Adm. Code 140.145(a).

Secondary servicemen that are registered and that do not qualify as de minimis may use the first or second method for determining their tax liability. Using the first method, secondary servicemen may separately state the selling price of each item transferred as a result of the sale of service. The tax is then calculated on the separately-stated selling price of the tangible personal property transferred. If secondary servicemen do not separately state the selling price of the tangible personal property transferred, they must use 50% of the entire bill to the primary servicemen as the tax base. Both of the these methods provide that in no event may the tax base be less than the servicemen's cost price of the tangible personal property transferred. Secondary serviceman that incur Service Occupation Tax on their selling price should collect Service Use Tax from their primary servicemen and provide Certificates of Resale to their suppliers when purchasing tangible personal property that will be transferred to primary servicemen. See 86 Ill. Adm. Code 140.106. Registered primary servicemen may give Certificates of Resale to registered secondary servicemen for any tangible personal property purchased from secondary servicemen. See Section 140.145(c). Primary

servicemen would be liable for Service Occupation Tax and for collecting Service Use Tax from their customers.

Secondary servicemen that are registered and that qualify as de minimis may also elect to use the first or second method for determining their tax liability. In addition, secondary serviceman 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 and qualify as de minimis may use the third method for determining their tax liability. See 86 Ill. Adm. Code 140.109. Under the third method, registered de minimis secondary servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon their cost price of tangible personal property transferred to primary servicemen incident sales of service. Secondary servicemen should give their suppliers resale certificates and remit Service Occupation Tax using the Service Occupation Tax rates for their locations. Secondary servicemen collect a corresponding amount of Service Use Tax from their customers, absent an exemption. See 86 Ill. Adm. Code 140.109. Secondary servicemen may accept resale certificates from registered primary servicemen under the third method, as well

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,

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