

Sellers of special order machines are considered to be engaged primarily in a service occupation, rather than being engaged in the business of selling tangible personal property, if the test set out in 86 Ill. Adm. Code 130.2115(b) is met. See 86 Ill. Adm. Code 130.2115. (This is a GIL.)

September 19, 2011

Dear Xxxxx:

This letter is in response to your letter dated February 14, 2011, 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:

On behalf of XYZ Company, we are respectfully requesting a General Information Letter ('GIL') pursuant to 2 Ill. Adm. Code 1200.120. The purpose of this request is to obtain clarity regarding the application of sales and use tax or service occupation tax pursuant to 35 ILCS 115/1, 35 ILCS 120/2 and 86 Ill. Adm. Code 140.101 and 140.109 respectively on the provision of engineering design services in conjunction with the sale of tangible personal property pursuant to the facts described below.

XYZ Company is not involved in a dispute regarding the same or substantially similar issue with the Internal Revenue Service or Illinois Department of Revenue in connection with an active examination, audit of the company or related party.

#### **STATEMENT OF FACTS**

XYZ Company ('Company') is a manufacturer of custom-designed prefabricated bridges. The Company designs, fabricates and delivers the bridge to the job site. Based on the size of the bridge, it may be necessary to deliver the bridge in component pieces and assemble at the job site. The Company does not provide onsite labor to assemble or install the bridge.

If needed, the Company provides drawings and/or instructions for the assembly and installation of the bridge components. In some cases, the Company may also provide additional engineering services related to the bridge such as abutment design. When separate engineering and design services are requested they are normally included as part of the same purchase order and contract with the bridge.

The abutment is what the bridge sits on to transfer the loads from the bridge to the soil. Every structure requires an abutment/foundation. Generally, the Company sells a bridge without providing abutment design services. In these cases, the customer's engineer takes the loads that we provide and designs the appropriate abutment to fit the bridge that the Company sold.

The Company's customers are under no obligation to use the Company's engineering services but because of their extensive engineering expertise and/or cost advantage, a customer may request the Company to provide engineering services such as abutment design. In this case, an additional amount is charged to the customer for this engineering work. This additional amount is separately stated on the invoice and clearly identified as engineering services.

Additionally, the Company has a staff of highly qualified, certified engineers and, on occasion, a customer may ask them to provide engineering and design services unrelated to the sale of any tangible personal property.

The Company produces two types of bridges, truss bridges and precast bridges, each of which is described below.

### *Truss Bridges*

The truss bridge is a custom-made bridge made of steel or aluminum and designed to meet the specific needs of the customer. After consulting with the customer, the engineer produces drawings used to custom-fabricate the steel or aluminum bridge. The raw materials are then cut to specification, welded and painted. Depending on the bridge span, the bridge may be (1) fully assembled at the Company's fabrication shop and delivered in one piece; or (2) the bridge may be partially assembled and delivered to the customer in pieces. To the extent assembly is required; the customer will complete the assembly process using instructions provided by the Company. In the cases where the bridge is fully assembled, it is then lifted into place by crane or hoist and then attached to the real property. In other cases, one end component of the bridge will be put in place and attached to the real property abutments; then subsequent components will be attached until the full bridge span is completed.

### *Precast Bridges*

The precast bridges are also custom-designed by Company engineers to meet the customer's specific application. The precast bridges are made of concrete and are fabricated by pouring concrete into Company-owned forms for individual component parts of the bridge. Due to the expense of transporting the concrete components, the Company may subcontract part of the manufacturing process to third-party precasters that are located near the job site. The Company will provide the precaster with the forms for pouring the bridge component and the precaster pours the concrete for the component parts. The component parts may be delivered to the job site by the precaster or the Company may arrange for the delivery to the job site by a third-party

transporter. The Company provides the customer with drawings and an onsite consultant to provide technical support during the installation process. The Company does not provide any onsite assembly or installation labor. The customer is fully responsible for the installation. Precast bridges are assembled simultaneously with the attachment to the realty. The precast bridges are specifically designed to the customer's application to meet the width, span, load requirements, etc. needed by the customer. Therefore, the individual components are not interchangeable, useable or saleable in other applications. If the individual components were not used in the complete bridge assembly, they would only have a scrap value.

Both the truss bridges and the precast bridges are billed to the customer for one lump sum price. Any additional services (such as engineering services) are priced separately either on a separate invoice or as [sic] separately stated line item on the invoice that includes the bridge.

## **ISSUES**

1. Are the separately stated engineering and design services exempt from sales tax when they are provided in conjunction with the sale of tangible personal property?
2. Are engineering and design services provided to a customer apart from the sale of tangible personal property exempt from the sales tax?

We appreciate your consideration of this request for a General Information Letter. If you should have any questions or need additional information, please call or email.

## **DEPARTMENT'S RESPONSE:**

In general, the sale of an item that one designs, engineers and manufactures for a customer consists of either a sale at retail subject the Retailers' Occupation Tax or the provision of a service subject to the Service Occupation Tax.

### **Sale at retail:**

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. These taxes comprise what is commonly known as "sales" tax in Illinois. If the purchases occur in Illinois, the purchasers must pay Use Tax to the retailer at the time of purchase. The retailers are then allowed to retain the amount of Use Tax paid to reimburse themselves for the Retailers' Occupation Tax liability incurred on those sales.

In computing Retailers' Occupation Tax liability, no deductions shall be made by a taxpayer from gross receipts or selling prices on account of the cost of property sold, the cost of materials used, labor or service costs, idle time charges, incoming freight or transportation costs, overhead costs, processing charges, clerk hire or salesmen's commissions, interest paid by the seller, or any other expenses whatsoever. Costs of doing business are an element of the retailer's gross receipts subject to tax even if separately stated on the bill to the customer. See 86 Ill. Adm. Code 130.410.

## Sale of service

The issue of whether a person incurs Retailers' Occupation Tax or Service Occupation Tax liability depends upon the nature of the items being produced and the nature of the design work involved. If the item being produced is substantially similar to stock or standard items, even though custom-made, the sale of that item would result in Retailers' Occupation Tax liability. The test for special order items that result in Service Occupation Tax liability is set forth in subsection (b) of the Department's rule "Sellers of Machinery, Tools and Special Order Items" at 86 Ill. Adm. Code 130.2115. The seller of a special machine, tool, die, jig, pattern, gauge or other special order item is engaged primarily in a service occupation, rather than in the business of selling tangible personal property, and so does not incur Retailers' Occupation Tax liability with respect to the sale, if the following tests for exemption are all met in the transaction:

- A) The purchaser employs the seller primarily for his engineering or other scientific skill to design and produce the property on special order for the purchaser and to meet the particular needs of the purchaser;
- B) the property has use or value only for the specific purpose for which it is produced; and
- C) the property has use or value only to the purchaser. 86 Ill. Adm. Code 130.2115(b).

These inquiries are very fact-specific. The seller must determine in each situation whether the sale qualifies for exemption under the provisions of 130.2115(b).

As to the requirement that the seller be employed primarily for his engineering or other scientific skill to design and produce the property, it is sufficient if the seller is responsible for making a substantial contribution to the designing of the property that is to be produced on special order. See subsection (b)(2) of Section 130.2115.

In the case where sellers of special order property are not subject to Retailers' Occupation Tax in accordance with Section 130.2115, the purchase of tangible personal property that is transferred to service customers may result in either Service Occupation Tax liability or Use Tax liability for the servicemen, depending upon which tax base the servicemen use to calculate their liability. Servicemen may calculate their tax base in one of four ways: (1) Service Occupation Tax on the separately stated selling price; (2) Service Occupation Tax on 50% of the entire bill; (3) Service Occupation Tax on cost price if they are registered de minimis servicemen; or, (4) Use Tax on cost price if the servicemen are de minimis and are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of sales of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If servicemen do not wish to separately state the selling price of the tangible personal property transferred, those servicemen must use the second method where they will use 50% of the entire bill to their service customers as the tax base. Both of the above methods provide that in no event may the tax base be less than the cost price of the tangible personal property transferred. Under these methods, servicemen may provide their suppliers with Certificates of Resale when purchasing the tangible personal property to be transferred as a part of the sales of service. Upon selling their product, they are required to collect the corresponding Service Use Tax from their customers. See 86 Ill. Adm. Code 140.106.

The third way servicemen may account for their tax liability only applies to de minimis servicemen 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. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal

property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). See 86 Ill. Adm. Code 140.101(f). This class of registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to sales of service. Servicemen that incur Service Occupation Tax collect the Service Use Tax from their customers. They remit the tax to the Department by filing returns and do not pay tax to suppliers. They provide suppliers with Certificates of Resale for the property transferred to service customers. See 86 Ill. Adm. Code 140.108.

The final method of determining tax liability may be used by de minimis servicemen not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). Such de minimis servicemen may pay Use Tax to their suppliers or may self assess and remit Use Tax to the Department when making purchases from unregistered out-of-State suppliers. Those servicemen are not authorized to collect "tax" from their service customers because they, not their customers, incur the tax liability. Those servicemen are also not liable for Service Occupation Tax. It should be noted that servicemen no longer have the option of determining whether they are de minimis using a transaction-by-transaction basis. See 86 Ill. Adm. Code 140.109.

### **No Tangible Personal Property Transferred**

Retailers' Occupation and Use Taxes do not apply to sales of service. The Service Occupation Tax Act and Service Use Tax are imposed on the transfer of tangible personal property incident to sales of service. 86 Ill. Adm. Code 140.101 and 160.101. However, if no tangible personal property is transferred incident to a sale of service, the Service Occupation Tax and Service Use Tax do not apply. If a transaction does not involve the transfer of any tangible personal property to the customer, then it generally would not be subject to Retailers' Occupation Tax, Use Tax, Service Occupation Tax, or Service Use Tax.

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.

Sincerely,

Samuel J. Moore  
Associate Counsel

SJM:mzk