ST 03-0093-GIL 07/10/2003 SALE OF SERVICE

This letter discusses the tax consequences of various sales of service. See 86 Ill. Adm. Code 140.101. (This is a GIL.)

July 10, 2003

Dear Xxxxx:

This letter is in response to your letter dated March 6, 2003. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120 subsections (b) and (c), which can be found at http://www.revenue.state.il.us/legalinformation/regs/part1200.

In your letter, you have stated and made inquiry as follows:

AAA provides various products and services to STATE customers. One of the products AAA offers to its customers is what is referred to as convenience copiers. The documentation used between AAA and their customers vary but the essence of the transaction is the same.

All convenience copiers are placed at various locations at the customer's place of business.

The customers are charged a base amount that allows them to make a certain amount of copies and an additional charge per copy over the allotted amount.

It is not unusual that the customer has the right to terminate the agreement by providing a written notice 60 days prior to the termination and paying, if applicable, an early termination charge. The convenience copiers are usually combined with other unrelated equipment and services under a single agreement but work independently of each other. During the term of the agreement the customer may negotiate for a different copier if they desire i.e. higher volume, color etc..

It is AAA's responsibility to maintain the copiers and provide the toner, developer and fuser. AAA may or may not provide paper depending on the terms of service on a client-by-client basis. The customer has exclusive use of the copiers and has the right to direct the manner of the use i.e. the customer operates the copiers choosing different control functions and have the copiers available for their use anytime of day during the agreed upon period, usually 3 years.

The question I have is whether the agreement between AAA and their customer is a lease/rental or is AAA providing a service? Please provide an official ruling on this

question. The Illinois Dept.of Revenue on this issue is not auditing us. This is the first instance in which are requesting a ruling on this matter from the Dept.

Thank you for your assistance in this matter.

We cannot be certain how the transactions referenced in your letter will be structured. We are, however, providing the following general information and hope that it will be helpful.

Illinois Retailers' Occupation and Use Taxes do not apply to sales of service that do not involve the transfer of tangible personal property to customers. Sales of service that do not involve the transfer of tangible personal property are not subject to sales tax in Illinois. However, sales of service in which tangible personal property is transferred incident to such sales, are subject to tax under the Service Occupation Tax Act.

Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred as an incident to sales of service. See the enclosed copy of 86 Ill. Adm. Code 140.101. The purchase of tangible personal property that is transferred to the service customer may result in either Service Occupation Tax liability or Use Tax liability for the servicemen depending upon which tax base the servicemen choose to calculate their tax liability. The servicemen may calculate their tax base in one of four ways: (1) separately stated selling price of tangible personal property transferred incident to service; (2) 50% of the servicemen's entire bill; (3) Service Occupation Tax on the servicemen's cost price if the servicemen are registered de minimis servicemen; or (4) Use Tax on the servicemen's 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 the sale of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If the servicemen do not wish to separately state the selling price of the tangible personal property transferred, the servicemen must use 50% of the entire bill to the service customer as the tax base. Both of the above methods provide that in no event may the tax base be less than the servicemen's cost price of the tangible personal property transferred.

The third way servicemen may account for 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 the servicemen determine that the annual aggregate cost price of tangible personal property transferred as an incident of the sale of service is less than 35% of the servicemen's annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). This class of registered de minimis servicemen is authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to the sale of service. 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.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under the Retailers' Occupation Tax Act. Such de minimis servicemen handle their tax liability by paying Use Tax to their suppliers. 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 a "tax" from the service customers.

In Illinois, sales of copies have been determined to be sales of service subject to taxation under the principles discussed above. If customers are charged a per copy fee for the use of a photo-copy machine, and the charge for the paper and ink is not separately stated, the tax base must be determined under either the 50% or one of the de minimis methods. The purchase of copy machines for use in these circumstances is subject to Illinois Use Tax.

Situations where businesses collect fees for allowing customers to use equipment, such as computers or printers, whether such equipment is located on or off the premises of the equipment provider, are treated as leases of that equipment. Lessors of tangible personal property in Illinois are deemed end users of property purchased for the purpose of leasing and incur Use Tax liability on their cost price of such property, except automobiles rented for periods of one year or less. Please refer to 86 Ill. Adm. Code 130.2010, enclosed. This Use Tax liability is incurred whether or not other tangible personal property, such as paper, is transferred incident to the lease or rental. Retailers' Occupation Tax is not due upon the fees charged for usage of the equipment.

Materials, such as toner for the machines or the machines themselves, that are used by a business and not transferred to the customer are subject to Use Tax whether the business is a lessor or a service provider. Use Tax must be paid to registered suppliers or self-assessed and paid directly to the Department.

We cannot determine if you are more aptly characterized as a serviceman or a lessor without more information and a review of your contracts. However, I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

Martha P. Mote
Associate Counsel

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Enc.