

A medical appliance is defined as an item which is intended by its manufacturer for use in directly substituting for a malfunctioning part of the body. See 86 Ill. Adm. Code 130.311. (This is a GIL.)

August 16, 2011

Dear Xxxxx:

This letter is in response to your letter dated April 13, 2011, in which you request a Private Letter Ruling. 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 our client, TAXPAYER, we are requesting a Private Letter Ruling ('PLR') regarding the sale of certain medical devices and related services. An executed Power of Attorney form authorizing FIRM to represent the Taxpayer in this matter is enclosed. To the best of the knowledge of Taxpayer and FIRM: (1) the Illinois Department of Revenue ('Department') has not previously ruled on the same or similar issue for the Taxpayer or a predecessor; (2) the same or similar issue was not previously submitted and withdrawn by Taxpayer or FIRM prior to the Department's issuance of a PLR; and (3) Taxpayer is not under audit by or involved in litigation with the Department.

#### **DESCRIPTION OF SERVICES**

The Taxpayer is a provider of device-based therapies for patients with advanced heart failure. The Taxpayer develops, manufactures and markets these medical devices to customers in Illinois.

The Taxpayer's product and service offerings can be segregated into nine distinct categories, as follows:

#### **(1) Prosthetic Devices**

This category includes devices that are worn on or in a patient to replace or assist in the functioning of the human heart. The devices are generally used in patients whose hearts have been diagnosed with the inability to supply sufficient blood flow to meet the body's needs. They provide left, right or bi-ventricular support for advanced heart failure support.

These devices are intended for long-term use, and the devices may be implantable or paracorporeal. The paracorporeal devices are attached to the patient at all times. These devices are sold or provided by the Taxpayer either directly to hospitals, or prescribed by licensed physicians for the treatment of patients and dispensed accordingly.

## **(2) External Component of Prosthetic Devices**

This category includes the external components of the prosthetic devices that, together with the internal device, work interdependently as one device to assist in the functioning of the heart as described in (1).

These components include power sources, cables, monitors, controller units, etc. which are attached to the device and necessary to its function.

## **(3) Circulatory Support Pump and Related Parts**

One device provided by the Taxpayer is a pump that provides short-term circulatory support. This pump provides circulatory support while a patient is hospitalized. The pump is connected to the patient using standard surgical techniques in which certain tubing (cannulae) is implanted in the patient. The pump has not been qualified for long-term use (that is, use longer than ten days). The 'related parts' sold with the circulatory support pump are a motor and console which are necessary for it to function.

## **(4) Medical Instruments Used During Implantation**

Certain instruments are used during the implantation of the prosthetic devices. These instruments are for single-use and are consumed during the surgical process.

## **(5) Supplies of Prosthetic Devices**

The Taxpayer provides certain supplies of prosthetic devices to its patients. Some of these items assist with the functionality of the prosthetic devices described in (1), and others are more key to the functionality of the devices. They include, but are not limited to:

- (a) Vests/holsters that allow the external components of the device to be carried more freely
- (b) Shower kits to protect the external components of the device from getting wet while the patient is bathing
- (c) Rapid charger stations that allow the power sources (i.e., the batteries) described in (2) to be charged more quickly.

## **(6) Full-Service Maintenance Agreement**

The Taxpayer provides maintenance agreements for a flat fee that include service for any necessary labor and parts as the need arises. This service agreement is optional, and there is no deductible associated with this agreement. The billing is a lump sum, and does not specify values for services versus parts.

### **(7) Service Labor**

When requested, the Taxpayer will provide labor on its devices for an hourly rate. This service is optional.

### **(8) Service Parts**

When requested, the Taxpayer will provide replacement parts on its devices for the cost of the part. This service is optional.

### **(9) Training**

The Taxpayer provides certain training on the implantation of its devices. This training is mandatory for providers that are implanting the device for the first time, and optional otherwise. While certain materials (manuals) may be provided as part of the training, the charge is billed as a lump sum and no charge is made for the materials/manuals.

## **RULINGS REQUESTED**

**(1)** Taxpayer's sales of prosthetic devices (Category 1) are subject to Illinois sales and use taxes (ROT, SOT, SUT and UT) at a reduced rate when sold in Illinois, because the devices are qualifying medical appliances.

**(2)** Taxpayer's sales of external components of prosthetic devices (Category 2) are subject to Illinois sales and use taxes (ROT, SOT, SUT and UT) at a reduced rate when sold in Illinois, because the components are qualifying medical appliances.

**(3)** Taxpayer's sales of circulatory support pumps and related parts (Category 3) are subject to Illinois sales and use taxes (ROT, SOT, SUT and UT) at a reduced rate when sold in Illinois, because the items are qualifying medical appliances.

**(4)** Taxpayer's sales of medical instruments (Category 4) are subject to Illinois sales and use taxes (ROT, SOT, SUT and UT) at the full rate when sold in Illinois.

**(5)** We request clarification on the application of Illinois sales and use taxes (ROT, SOT, SUT and UT) for sales of the following supplies of prosthetic devices (Category 5) when sold in Illinois:

- (a) Supplies that Enhance Use of Device
- (b) Supplies that Protect Device from Damage
- (c) Supplies that Provide Emergency Support for Device

**(6)** Taxpayer's sales of full service maintenance agreements (Category 6) are subject to Illinois sales and use taxes (ROT, SOT, SUT and UT) and not subject to tax when sold in Illinois.

**(7)** Taxpayer's sales of service labor (Category 7) are subject to Illinois sales and use taxes (ROT, SOT, SUT and UT) at a reduced rate when sold in Illinois, because the labor relates to the repair of qualifying medical appliances.

**(8)** Taxpayer's sales of service parts (Category 8) are subject to Illinois sales and use taxes (ROT, SOT, SUT and UT) at a reduced rate when sold in Illinois, because the parts relate to the repair of qualifying medical appliances.

**(9)** Taxpayer's sales of training services (Category 9) are not subject to Illinois sales and use taxes (ROT, SOT, SUT and UT) when sold in Illinois, because the services are not enumerated as taxable services.

## **BASIS FOR OUR RULINGS REQUESTED**

### **(1) Prosthetic Devices**

In Illinois, medical appliances are subject to tax at a reduced rate of 1%.<sup>1</sup> A medical appliance is defined as an item that is used to directly substitute for a malfunctioning part of the human body<sup>2</sup> and includes an item that becomes part of the human body by substituting for any part of the body that is lost or diminished because of congenital defects or disease such as a heart pacemaker.<sup>3</sup> However, medical devices that are used for diagnostic or treatment purposes do not qualify for the lower tax rate.<sup>4</sup> Accordingly, since the prosthetic devices replace the function of the human heart by providing blood flow to the body, they would be considered medical appliances subject to tax at the reduced rate.

### **(2) External Components of Prosthetic Devices**

The Department has held that batteries for hearing aids qualify for the reduced rate as a qualifying medical appliance.<sup>5</sup> Generally, accessories which are necessary for the operation of a qualifying medical appliance qualify for the lower rate of tax.<sup>6</sup> Since the components are necessary to the function of the prosthetic device and assist in providing blood flow to the body, they would be considered qualifying medical appliances and subject to tax at the reduced rate.

### **(3) Circulatory Support Pump and Related Parts**

In Illinois, there is no requirement that a device be worn in or on a person to qualify as a medical appliance. Generally, an item that is used directly to substitute for a malfunctioning part of a human body would qualify for the reduced rate.<sup>7</sup> The Department does distinguish that items for diagnostics and treatment purposes do not qualify for the lower tax rate.<sup>8</sup> However, the circulatory pump and its related parts are act [sic] as a pump to provide circulatory support while a patient is hospitalized for inadequate blood circulation, so its sale would be subject to tax at the reduced rate.

### **(4) Medical Instruments Used During Implantation**

In general, surgical instruments used in the treatment of patients do not qualify for the reduced rate as they are not used to directly substitute for a malfunctioning part of the human body.<sup>9</sup> In addition, supplies do not qualify for the reduced rate;<sup>10</sup> however, the Department has noted that syringes and needles used in treating diabetes in human beings,<sup>11</sup> sterile dressings, bandages and gauze<sup>12</sup> do qualify for the reduced rate of tax.

The medical instruments provided by the Taxpayer are designed for single use and are consumed during the surgical process. As there does not appear to be a specific exemption for medical instruments consumed during the surgical process, sales of such instruments are subject to tax at the full rate.

## **(5) Supplies of Prosthetic Devices**

Although generally medical supplies do not qualify for the reduced rate,<sup>13</sup> based on our reading of the Illinois guidance, the supplies sold by the Taxpayer appear to be akin to accessories used with the devices. The Department notes that accessories which are necessary for the operation of a qualifying medical appliance qualify for the lower rate of tax. However, these parts and accessories must be integral to the operation of the medical appliance.<sup>14</sup>

The items sold by the Taxpayer which are supplies include vests, shower kits and rapid charger stations. The treatment of these items under Illinois law appears quite fact-specific, and thus subjective. As such, we request your clarification on how tax applies to these categories:

(a) *Supplies that Enhance Use of Device*

We believe that certain of these supplies, such as the vests which allow the external components of the device to be carried more freely, serve to enhance the ease with which the equipment is used.

(b) *Supplies that Protect Device from Damage*

Shower kits, which are also a supply provided by the Taxpayer, are slightly different than a vest or a charger in that they prevent the prosthetic from being damaged.

(c) *Supplies that Provide Emergency Support for Device*

Rapid charger stations allow the power sources (i.e., the batteries) described in Category (2) to be charged more quickly. There are circumstances in which use of these charger stations may be crucial to the functionality of the device, and thus, a patient's survival.

We request a clarification of the application of sales and use tax to sales of these types of supplies of prosthetic devices in Illinois.

## **(6) Full-Service Maintenance Agreement**

In Illinois, special service charges sold separately from the tangible personal property are not considered part of the selling price of the tangible personal property which is sold.<sup>15</sup> The Department has noted that this applies to maintenance agreements which are sold separately from tangible personal property and sales of such agreements are not taxable transactions.<sup>16</sup> Therefore, the maintenance agreements sold by the Taxpayer would not be subject to sales or tax [sic].

## **(7) Service Labor**

The service labor provided by the Taxpayer is for the repair of its devices. The Department has noted that repairs and replacement parts which are necessary for the

operation of a qualifying medical appliance would qualify for the lower rate of tax.<sup>17</sup> The service labor provided by the Taxpayer is separately stated and not bundled with the service parts described in (8). As such, the service labor provided by the Taxpayer would not be subject to tax.

### **(8) Service Parts**

The Department has noted that replacement parts and accessories which are necessary for the operation of a qualifying medical application would generally qualify for the lower rate of tax.<sup>18</sup> The service parts provided by the Taxpayer are separately stated and not bundled with the service labor described in (7). As such, the service parts provided by the Taxpayer would be subject to tax at the reduced rate.

### **(9) Training**

Generally, sales of personal services are not subject to tax in Illinois.<sup>19</sup> Although general training charges are not specifically exempted from tax, the statute notes that charges for training in relation to computer software are not subject to tax.<sup>20</sup> Accordingly, the charges for training services would not be subject to tax.

### **REQUESTED ACTION**

We request that the Illinois Department of Revenue review the stated facts and issue a ruling confirming the Taxpayer's conclusions regarding the taxability of the aforementioned items.

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A copy of our executed Power of Attorney, Form IL-2848, is enclosed. If you have any questions, please contact me.

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

The Department's regulation "Public Information, Rulemaking and Organization" provides that "[w]hether to issue a private letter ruling in response to a letter ruling request is within the discretion of the Department. The Department will respond to all requests for private letter rulings either by issuance of a ruling or by a letter explaining that the request for ruling will not be honored." 2 Ill. Adm. Code 1200.110(a)(4). Due to the lack of pertinent information about each of the specific items subject to this request which is necessary for the Department to issue a Private Letter Ruling, the Department has declined to issue a Private Letter Ruling and has decided to respond with a General Information Letter.

Please see the Department's regulation at 86 Ill. Adm. Code Section 130.311, which is its regulations governing Drugs, Medicines, Medical Appliances, and Grooming and Hygiene Products. Those products that qualify as drugs, medicines and medical appliances are taxed at a lower State rate of 1% plus any applicable local taxes. Those items that do not qualify for the low rate of tax are taxed at the general merchandise rate of 6.25% plus applicable local taxes.

As you have noted, a medical appliance is an item that is intended by its manufacturer for use in directly substituting for a malfunctioning part of the human body. Items that would be considered medical appliances, and qualify for the low rate, are such items as artificial limbs, dental prostheses

and orthodontic braces, crutches and orthopedic braces, wheelchairs, heart pacemakers, and dialysis machines (including the dialyzer). Corrective medical appliances such as hearing aids, eyeglasses and contact lenses also qualify for the low rate.

As you can see, in order for a medical appliance to qualify for the reduced rate, the medical appliance itself must be used in a manner that directly substitutes for a malfunctioning part of the body, not items that simply enhance the use of a device that may be intended by its manufacturer for use in directly substituting for a malfunctioning part of the body.

Generally, a maintenance agreement or extended warranty that is not included as part of the selling price of tangible personal property, but is sold as a separate agreement for a predetermined fee, is not subject to tax. The serviceman that provides service under the separate maintenance agreement or extended warranty is required to pay tax to his supplier on the cost price of the tangible personal property that is transferred incident to the completion of the maintenance agreement. See 86 Ill. Adm. Code 140.301(b)(3). The purchaser of the separate agreement or warranty is not charged tax on the labor or tangible personal property that is transferred incident to the completion of the maintenance agreement. The tax consequences do not change whether the separate agreement is sold at the time of the sale of the equipment or at a later date.

Regarding accessories or parts, please be advised that repairs, replacement parts, and accessories which are necessary for the operation of a qualifying medical appliance, generally qualify for the low rate of tax. Please note, though, that these parts and accessories must be integral to the operation of the medical appliance and they must be a part of the equipment which qualifies as a medical appliance. For example, items such as wheelchair cushions or pack bags sold separately from wheelchairs would be high rate as they do not directly substitute for a malfunctioning part of the body, nor are they necessary for the operation of the wheelchair.

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.

Very truly yours,

Debra M. Boggess  
Associate Counsel

DMB:msk

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<sup>1</sup> Ill. Admin. Code tit. 86, § 130.311(a).

<sup>2</sup> Ill. Admin. Code tit. 86, § 130.311(d).

<sup>3</sup> Ill. Admin. Code tit. 86, § 130.311(d)(1).

<sup>4</sup> Ill. Dept. of Rev. General Information Letter ST 00-0099-GIL (01/25/2000).

<sup>5</sup> Ill. Dept. of Rev. General Information Letter ST 06-0170-GIL (08/11/2006).

<sup>6</sup> Ill. Dept. of Rev. General Information Letter ST 97-0369-GIL (07/07/1997).

<sup>7</sup> Ill. Admin. Code tit. 86, § 130.311(d).

<sup>8</sup> Ill. Dept. of Rev. General Information Letter ST 00-0009-GIL (01/25/2000).

<sup>9</sup> Ill. Admin. Code tit. 86, § 130.311(d)(5).

<sup>10</sup> Ill. Admin. Code tit. 86, § 130.311(d)(6).

<sup>11</sup> Ill. Dept. of Rev. General Information Letter ST 97-0131-GIL (03/05/1997).

<sup>12</sup> Illinois Dept. of Rev. General Information Letter ST 99-0178-GIL (05/19/1999); Illinois Dept. of Rev. General Information Letter ST 99-0397-GIL (12/23/1999).

<sup>13</sup> Ill. Admin. Code tit. 86, § 130.311(d)(6); Ill. Admin. Code tit. 86, § 140.141.

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<sup>14</sup> Illinois Dept. of Rev. General Information Letter ST 97-0131-GIL (03/05/1997).

<sup>15</sup> Ill. Admin. Code tit. 86, § 130.450(b).

<sup>16</sup> Illinois Private Letter Ruling No. ST 99-0007-PLR (02/24/1999).

<sup>17</sup> Illinois Dept. of Rev. General Information Letter ST 95-0063-GIL (02/06/1995); Illinois Dept. of Rev. General Information Letter ST 97-0369-GIL (07/07/1997).

<sup>18</sup> Illinois Dept. of Rev. General Information Letter ST 97-0369-GIL (07/07/1997).

<sup>19</sup> Ill. Admin. Code. Tit. 86, § 140.125(c).

<sup>20</sup> Ill. Admin. Code. Tit. 86, § 140.125 (x).