

This letter concerns purchases for resale of natural gas that is converted into Compressed Natural Gas (CNG) for sale as a motor fuel. See 86 Ill. Adm. Code 470.145. (This is a PLR).

January 26, 2012

Dear XXXXX:

This letter is in response to your Private Letter Ruling request dated October 12, 2011. 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.

Review of your request disclosed that all the information described in paragraphs 1 through 8 of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to TAXPAYER for the issue or issues presented in this ruling, and is subject to the provisions of subsection (e) of Section 1200.110 governing expiration of Private Letter Rulings. Issuance of this ruling is conditioned upon the understanding that neither TAXPAYER nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request. In your letter you have stated and made inquiry as follows:

We are writing on behalf of our client ('Taxpayer') to request a private letter ruling pursuant to 86 Ill. Admin. Code 1200.110 on the tax consequences related to the following transactions.

Representations

- The Department has not ruled on the issue outlined below for TAXPAYER, nor has TAXPAYER previously submitted this issue to the Department.
- TAXPAYER does not have an audit or pending litigation with the Department.
- TAXPAYER is not aware of any private letter rulings or general information letters previously issued by the Department that address this question, nor is it aware of any contrary authorities.

- TAXPAYER requests a response for the current tax period and all future tax periods.
- TAXPAYER requests that all names of companies and suppliers be redacted for purposes of the published opinion.

Facts

Taxpayer is an Illinois corporation that has established a Compressed Natural Gas (CNG) fueling station in Illinois. The Taxpayer is registered for Retailers [sic] Occupation Tax and Use Tax.

The Taxpayer purchases metered natural gas from a vendor located inside Illinois and currently pays Gas Revenue Tax on these purchases. The natural gas is delivered to Taxpayer's facility in Illinois where it is converted to CNG. The natural gas to CNG conversion process involves taking natural gas from a pipeline and running the gas through an inlet gas dryer to prepare the natural gas to be compressed. The natural gas is then fed into a compressor or compressors which convert the natural gas into compressed natural gas (CNG), a product that is suitable for use as a motor fuel in vehicles equipped to burn CNG. The CNG (which is pressurized at 2900-3600 psi and occupies a volume of 1% of the equivalent natural gas at standard atmospheric pressures) is stored under pressure in vessels awaiting use. The CNG is then pumped through a dispensing unit into vehicles owned by the taxpayer for on-highway and off-highway use in Illinois. In the near future, the facility will also be used to fuel vehicles owned by third parties through a fuel purchasing card program operated by an unrelated vendor.

We spoke to INDIVIDUAL from your office and he advised that this factual situation has not been addressed in the Department's regulations or prior private letter rulings or general information letters and requested that we submit our request for guidance in writing to the Department.

Guidance Requested

1. Can the Taxpayer purchase the natural gas under the resale exemption for Gas (Revenue/Use) Tax as the natural gas is being used as a raw material incorporated into a product that will be subject to sales/use and motor fuel taxes?
2. When the Taxpayer uses the self-produced CNG in its own vehicles, does Illinois use tax apply? If so, what is the proper tax base for Use Tax purposes?

Discussion

Purchase of Natural Gas to Produce CNG as a Purchase for Resale

In addition to the State of Illinois taxes imposed under the Retailer's [sic] Occupation Tax, the Illinois Use Tax, and the Motor Fuels [sic] Tax, Illinois has a Gas Revenue Tax (35 ILCS 615) and a Gas Use Tax (35 ILCS 173/5). In addition, the VILLAGE imposes

a municipal Gas Use Tax. Discussions related to the exemption for resale should be construed to include a resale exemption for both state and municipal gas taxes.¹

The Gas Revenue Tax is a tax is [sic] imposed upon persons engaged in the business of distributing, supplying, furnishing or selling gas to persons for use or consumption and **not for resale** at the rate of 2.4 cents per therm of all gas which is so distributed, supplied, furnished, sold or transported to or for each customer in the course of such business, or 5% of the gross receipts received from each customer from such business, whichever is the lower rate as applied to each customer for that customer's billing period. 35 ILCS 615/2. Gross receipts means the consideration received for gas distributed, supplied, furnished or sold to persons for use or consumption and **not for resale**. 35 ILCS 615/1.

The Gas Use Tax is a tax imposed upon the privilege of using in Illinois gas obtained in a purchase of out-of-state [sic] gas at the rate of 2.4 cents per therm or 5% of the purchase price for the billing period, whichever is the lower rate. Such tax rate shall be referred to as the self-assessing purchaser tax rate. 35 ILCS 173/5-1. To fall within the meaning of the statute, some key pieces need to be in place. Namely, a delivering supplier, who is any person engaged in the business of delivering gas to persons for use or consumption and **not for resale**, and [sic] who, in any case where more than one person participates in the delivery of gas to a specific purchaser, is the last of the suppliers engaged in delivering the gas prior to its receipt by the purchaser. At the same time, the purchase price means the consideration paid for the distribution, supply, furnishing, sale, transportation, or delivery of gas to a person for use or consumption and not for resale. 35 ILCS 173/5-5.

The sales of gas that are subject to the aforementioned taxes are considered to be retail sales. While the Gas Revenue and Gas Use Taxes do not specifically define 'use or consumption' or 'sale for resale', these concepts are addressed in the Retailers [sic] Occupation Tax and Use Tax Acts. Under these Acts, a sale at retail means any transfer of the ownership of or title to tangible personal property to a purchaser, for the purpose of use or consumption, and **not for the purpose of resale** in any form as tangible personal property to the extent not first subject to a use for which it was purchased, for a valuable consideration, provided that the property purchased is deemed to be purchased for the purpose of resale, despite first being used, to the extent to which it is resold as an ingredient of an intentionally produced product or byproduct of manufacturing. 86 Ill. Adm. Code 130.201(a).

It has been established that the sale of tangible personal property to a purchaser for the **purpose of resale** in any form as tangible personal property, to the extent not first subjected to a use for which it was purchased, is not subject to Retailers' Occupation Tax. 86 Ill. Adm. Code 130.210(a). Moreover, tangible personal property that will become a component part of a product that is subsequently sold generally will qualify for the resale exemption. 86 Ill. Adm. Code 130.210(b), ST 10-0025-GIL.

From the customary applications of the Gas Revenue and Gas Use Tax Acts, it appears that the intention of the General Assembly was to tax natural gas provided in a utility context which is directly consumed in the form delivered to generate heat. This notion is supported by the fact that natural gas is exempted from Retailers [sic] Occupation Tax and Use Tax even though it is clearly tangible personal property. (ST 99-0118-GIL). This is further supported by the types of exemptions that are available for natural gas, such as sales to building operators who resell to their tenants in the Gas Revenue

Tax Act and the exemption for natural gas used in the production of electricity under the Gas Use Tax Act.

Neither Act contemplates the emerging use of natural gas used as a raw material to produce Compressed Natural Gas for use in motor vehicles. As noted in the facts section, substantial processing of natural gas must take place in order to produce CNG, which exists in a different form and requires special storage conditions not needed for regular natural gas. Based on these facts, it would be reasonable to conclude that the natural gas being used as CNG was purchased to be resold and not to be used in its original form.

Further, CNG which is used in motor vehicles will be subject to Motor Fuel Excise Tax as a 'Special Fuel' under the Motor Fuel Excise Tax Act as well as potential Retailers [sic] Occupation Tax or Use Tax. (35 ILCS 505/1.13) The rate of this Motor Fuel Tax will be 19 cents per gallon for the Part A rate and 12.8 cents per gallon for the Part B rate effective January 1, 2011 (Informational Bulletin FY 2011-06). Both sales and use taxes and excise taxes are commonly structured to avoid multiple imposition of the same type of tax. In this case, a determination that the purchase of the natural gas was exempt from Gas Revenue or Gas Use Tax under a resale exemption but taxable under Motor Fuel Excise Tax (both excise taxes) would be consistent with this foundational policy.

Use Tax – CNG Produced for Own Use/Consumption

The Illinois Use Tax is a privilege tax imposed on the privilege of using, within Illinois, any kind of tangible personal property that is purchased anywhere at retail from a retailer. 86 Ill. Adm. Code 150.101. The rate of the use tax is 6.25% of the selling price of the tangible personal property involved, provided that if the property that is purchased at retail from a retailer is acquired outside Illinois and used outside Illinois before being brought to Illinois for use. The sale price is the applicable base on which the use tax is computed and shall be reduced by an amount which represents a reasonable allowance for depreciation for the period of such prior out-of-State use. 86 Ill. Adm. Code 150.105(a).

An exception applies to the general use tax rules when tangible personal property is produced by the user himself. The user is not taxable on the value of the finished product in which he produces himself but the user will be taxable on the purchase price of the tangible personal property that he purchases and incorporates into such finished product that is used within Illinois when such tangible personal property was purchased at retail or purchased for use. 86 Ill. Adm. Code 150.305(a) & (b).

In this instance the taxpayer will be using the self-produced CNG to power a select number of the vehicles in their fleet. As discussed previously, the exclusive type of tangible personal property purchased and incorporated into the self-produced CNG is natural gas. The CNG used by the taxpayer would theoretically be subject to Illinois use tax. However, in calculating the use tax base for the self-produced CNG, the property that is incorporated into the CNG is natural gas, a product that is specifically excluded from the definition of tangible personal property by the ROT and UT statutes. Customarily, when the manufacturer of self-produced goods pays Use Tax on the cost price of the materials used to produce the item, the manufacturer is in effect paying the Use Tax it would have paid absent the resale exemption. We were unable to find any authority addressing the cost price of an item not subject to ROT or UT in the context of

self-produced goods, however, applying the foregoing logic, the Use Tax due on the natural gas would be \$0 because the natural gas is not subject to this tax.

Rulings Requested

We respectfully request that the Department issue a private letter ruling confirming the following conclusions:

1. That the purpose of natural gas for the purpose of producing compressed natural gas (CNG) should be considered a sale for resale for purposes of the Gas Revenue Tax and the Gas Use Tax (and corresponding municipal taxes.)
2. That the Use Tax base on that portion of the CNG which is both produced and used by they [sic] Taxpayer should be \$0 as the calculation is being made on the cost price of an item not subject to ROT or SOT.

If the Department does not reach a favorable conclusion, I would ask that the Department contact me to indicate what further needs to be provided, or to allow the taxpayer to rescind the ruling request.

Please do not hesitate to contact me if you have any questions. We would be pleased to meet with you or representatives of the Department to discuss any aspect of this ruling request.

DEPARTMENT'S RULING:

The Department cannot provide you with a binding ruling in regards to a local tax such as the municipal gas use tax referenced in your letter that is collected and administered by the local government imposing that tax. Any questions regarding that tax should be directed to that local government.

The State of Illinois taxes transactions involving natural gas under two different tax acts.

GAS REVENUE TAX

The Gas Revenue Tax Act imposes a tax upon persons engaged in the business of distributing, supplying, furnishing or selling gas to persons for use or consumption and not for resale at the rate of 2.4 cents per therm of all gas which is so distributed, supplied, furnished, sold or transported to or for each customer in the course of such business, or 5% of the gross receipts received from each customer from such business, whichever is the lower rate as applied to each customer for that customer's billing period. 35 ILCS 615/2; 86 Ill. Adm. Code 470.110(a). The Department's rules provide that "gas furnished to other taxpayers engaged in this business of distributing, supplying, furnishing or selling to their customers the gas so received is for resale and is not within the Act." 86 Ill. Adm. Code 470.145.

The Gas Revenue Tax is not a tax or fee imposed on the consumer of the gas. This tax is an occupation tax. It is imposed upon taxpayers engaged in the business of distributing, supplying, furnishing or selling gas to persons for use or consumption and not for resale. However, distributors/suppliers of gas are authorized under the Public Utilities Act to collect a "reimbursement"

from purchasers of gas. 220 ILCS 5/9-222. Although such a reimbursement is authorized, distributors/suppliers of gas are not required to collect it.

GAS USE TAX

The Gas Use Tax Law imposes a tax on the privilege of using in this State gas obtained in a purchase of out-of-state gas at the rate of 2.4 cents per therm or 5% of the purchase price for the billing period, whichever is the lower rate. See 35 ILCS 173/5-10 and 86 Ill. Adm. Code 471.105. A “purchase of out-of-state gas” is defined as a transaction for the purchase of gas from any supplier in a manner that does not subject the seller of that gas to liability under the Gas Revenue Tax Act. 35 ILCS173/5-5; 86 Ill. Adm. Code 471.101.

Delivering suppliers maintaining a place of business in this State shall collect, from the purchasers of gas who have elected the alternate tax rate, the tax that is imposed at the alternate 2.4 cents per therm rate. 35 ILCS173/5-15; 86 Ill. Adm. Code 471.120.

Any purchaser of gas that does not pay tax to his or her delivering supplier, when that delivering supplier is registered to collect that tax under the provisions of Section 471.120 of the Department’s rules, must register with the Department as a self-assessing purchaser and pay tax directly to the Department at the self-assessing purchaser rate. A purchaser registering as a self-assessing purchaser cannot revoke that registration for at least one year. 86 Ill. Adm. Code 471.115(a).

CNG PRODUCED FOR TAXPAYER’S OWN USE

Your letter states that TAXPAYER intends to use natural gas that is received from a vendor in this State and convert that gas into Compressed Natural Gas (CNG). The CNG that is produced is intended to be used as a motor fuel in the TAXPAYER’s vehicles. Gas Revenue Tax is imposed upon taxpayers engaged in the business of distributing, supplying, furnishing or selling gas to persons for use or consumption. The use of the gas by TAXPAYER to burn as a fuel for its vehicles is considered a use or consumption of that gas and the furnishing of the gas to TAXPAYER is subject to Gas Revenue Tax. The fact that TAXPAYER compresses the gas prior to its use as a motor fuel does not change the taxability of the transaction for the acquisition of the gas. In these situations, the gas is being used or consumed and is not being resold. No resale exemption is applicable in these situations. The purchase of the gas in these situations is not subject to Retailers’ Occupation Tax or Use Tax.

The use of CNG as a motor fuel will subject TAXPAYER to Motor Fuel Tax. See Section 2 of the Motor Fuel Tax Law, 35 ILCS 505/2.

CNG PRODUCED BY TAXPAYER FOR RESALE

Your letter states that TAXPAYER intends in the future to sell some of the CNG that it has produced to third parties for use as a motor fuel. Gas Revenue Tax is imposed upon taxpayers engaged in the business of distributing, supplying, furnishing or selling gas to persons for use or consumption and not for resale. The Department’s rules recognize sales for resale to other taxpayers engaged in this business of distributing, supplying, furnishing or selling to their customers. See 86 Ill. Adm. Code 470.145. Those rules do not contemplate reselling the natural gas provided in a different form such as CNG to be used as a motor fuel. However, we believe that the statutory language, “not

for resale,” would also apply in situations where the natural gas is converted for resale as CNG. TAXPAYER may make purchases of natural gas for resale by providing the utility with a resale certificate for the natural gas that it purchases for compression into CNG for sale to a third party. Please note that the utility providing the natural gas has the discretion whether to accept that resale certificate or not. TAXPAYER may want to make separate purchases of the natural gas that are for resale from its purchases for use or it may provide a percentage exemption certificate for the natural gas to be sold as CNG. If TAXPAYER provides a percentage exemption certificate for natural gas and claims exemption on part of the gas that is used in its vehicles instead of being resold, then it will have to register and remit Gas Use Tax on the purchase of that natural gas.

The CNG sold by TAXPAYER to a third party for use as a motor fuel would be subject to Retailers' Occupation Tax, including any applicable local occupation taxes. In addition, TAXPAYER will need to register as a distributor and remit Motor Fuel Tax on the sale of the CNG along with any local Motor Fuel Taxes that may apply.

The factual representations upon which this ruling is based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the factual representations recited in this ruling are correct and complete. This Private Letter Ruling is revoked and will cease to bind the Department 10 years after the date of this letter under the provisions of 2 Ill. Adm. Code 1200.110(e) or earlier if there is a pertinent change in statutory law, case law, rules or in the factual representations recited in this ruling.

I hope this information is helpful. If you have questions concerning this Private Letter Ruling, you may contact me at (217) 782-2844. If you have further questions related to the Illinois sales tax laws, please visit our website at www.tax.illinois.gov or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Terry D. Charlton
Chairman, Private Letter Ruling Committee

TDC:msk

¹ The VILLAGE imposes municipal gas use tax on the privilege of using or consuming gas in the village that is not purchased for resale. VILLAGE Municipal Code Section 4.11.030. A provision is contained in the municipal code which defers to state tax treatment in the event of a conflict between the State of Illinois law and the municipal code provisions. VILLAGE Municipal Code Section 1.04.180.