

When a construction contractor permanently affixes tangible personal property to real property, the contractor is deemed the end user of that tangible personal property. As the end user, the contractor incurs Use Tax on the cost price of that tangible personal property. See 86 Ill. Adm. Code 130.1940 and 86 Ill. Adm. Code 130.2075. (This is a GIL.)

December 3, 2015

Dear Xxxxx:

This letter is in response to your letter dated August 27, 2015 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:

ABC ("the "Company") respectfully requests a ruling concerning the applicability of sales tax to: a) labor costs in commercial equipment installation; and b) interest and fees paid on a capital lease used to finance the equipment and its installation. The Company requests and [sic] exemption from paying both labor costs associated with the installation of commercial equipment and interest and fees associated with the capital lease of commercial equipment.

#### A. STATEMENT OF FACTS

1) Taxpayer Information:

a) COMPANY

b) Formation

COMPANY is a Limited Partnership formed under the laws of the state of State 1 on DATE.

2) Facts relating to the request:

ABC ("the "Company") uses debt capital from accredited investors to finance energy efficiency upgrades to commercial buildings (the "Business" of the Company). The Company pays a contractor (the "Contractor") to obtain and install the energy efficiency equipment (the "Equipment") such as LED lights, or HVAC equipment. The Company pays the Contractor directly on behalf of the recipient of the Equipment (the "Customer") for the Equipment and labor, just as the Customer would pay the

Contractor for those services. The Company enters into a capital lease (the "Capital Lease") with the Customer who makes lease payments to the Company in monthly installments. The Company itemizes that the cost of labor (the "Labor Cost"), the cost of the Equipment (The "Equipment Cost") and fees and interest on the Equipment Cost and the Labor Cost (the "Interest/Fees") in the Customer's lease. The Customer may purchase the Equipment for a nominal cost of one dollar (\$1.00) at the conclusion of the Capital Lease.

3) Payment of sales tax:

The Company pays the Contractor for the equipment, it provides the Contractor with a resale certificate and obtains title to the Equipment. The Company is then responsible for collecting and remitting sales tax. Sales taxes due on the equipment are collected on monthly lease payments in the form of the Illinois stream tax.

## B. RULING REQUESTED

The following rulings are respectfully requested:

- 1) That the Company be exempt from paying sales tax on the Labor Cost in accordance with Illinois State Statute §14-113.06.
- 2) That the Company be exempt from paying sales tax on the Interest/Fees in accordance with Illinois State Statute §14-113.05.
- 3) That the way in which the Company has itemized the Equipment Cost, Labor Cost, and Interest/Fees within its Capital lease -as shown in Exhibit B, Table 2 and 3- is sufficient for the purpose of exempting Labor Cost and Interest/Fees from sales tax. The method by which The Company plans to pay sales tax is acceptable.

## C. STATEMENT OF LAW

Illinois State Statute § 14-113.06 states the following:

Installation Charges. If a charge for alteration, installation, or other special service in connection with the transfer of tangible personal property is included in the selling price, then it must be included in gross receipts. As with freight, however, if such a charge is separately contracted for, such charge need not be included in gross receipts.

Illinois State Statute § 14-113.05 states the following:

Finance Charges. Interest and finance charges (if clearly identified in a retailer's books and records) on installment sales contracts are not considered to be part of the "selling price" and therefore need not be included in "gross receipts" for ROT calculation.

**In light of the above language, the Company requests exemptions from paying state sales tax on both Labor Costs and Interest/Fees. Further, the Company requests a ruling on whether the Capital Lease is sufficiently itemized to achieve these exemptions (see below).**

## **DEPARTMENT'S RESPONSE:**

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 the 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 their Retailers' Occupation Tax liability incurred on those sales.

A contract that provides for both the sale and installation of tangible personal property that is permanently affixed or incorporated into a structure is considered a construction contract. See 86 Ill. Adm. Code 130.1940 and 130.2075. The term construction contractor includes general contractors, subcontractors, and specialized contractors such as landscape contractors.

In Illinois, construction contractors are deemed end users of tangible personal property purchased for incorporation into real property. As end users of such tangible personal property, these contractors incur Use Tax liability for such purchases based upon their cost price of the tangible personal property. See 86 Ill. Adm. Code 130.1940 and 86 Ill. Adm. Code 130.2075. Therefore, any tangible personal property that a construction contractor purchases that will be permanently affixed to or incorporated into real property in this State will be subject to Use Tax. If such contractors did not pay the Use Tax liability to their suppliers, those contractors must self assess their Use Tax liability and pay it directly to the Department. If the contractors have already paid a tax in another state regarding the purchase or use of such property, they will be entitled to a credit against their Illinois Use Tax liability to the extent that they have paid tax that was properly due to another state. See 86 Ill. Adm. Code 150.310. The Illinois Use Tax rate incurred by an out-of-State construction contractor on purchases of materials from an unregistered supplier located outside of this State is generally 6.25% as described in subsection (c) of Section 130.2075.

It is important to note that since construction contractors are the end users of the materials that they permanently affix to real estate, their customers incur no Use Tax liability and the construction contractors have no legal authority to collect the Use Tax from their customers. However, many construction contractors pass on the amount of their Use Tax liabilities to customers in the form of higher prices or by including provisions in their contracts that require customers to "reimburse" the construction contractor for his or her tax liability. Please note that this reimbursement cannot be billed to a customer as "sales tax," but can be listed on a bill as a reimbursement of tax. The choice of whether a construction contractor requires a tax reimbursement from the customer or merely raises his or her price is a business decision on the construction contractor's part.

It appears that your company contracts for the improvement of real estate. Because this is a construction contract between your company and the contractor who installs the equipment, the construction contractor owes Use Tax on the cost price of the tangible personal property that is installed. Though the contractor may choose to pass on the cost of the tax to your company in the form of a reimbursement, your company is not technically responsible for the tax. If the construction contractor requires you to reimburse him for the amount of his tax liability, your company can similarly recoup its costs through contractual agreements with your customer. Please also note that your company cannot utilize a resale certificate when entering a construction contract for the improvement of real estate. Instead, the construction contractor pays tax on the cost of the tangible personal property when he purchases it to permanently affix the items into real estate.

Although your letter mentions a lease, the transaction you describe in your letter does not appear to involve a purchase of tangible personal property for leasing purposes. Instead, the transaction appears to be a construction contract. If these facts change in any way, the tax liabilities involved could also change. However, please be advised that Illinois does not have a tax on leases of tangible personal property. For State-administered tax purposes, sales and use taxes do not apply to lease receipts. See 86 Ill. Adm. Code 130.220.

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,

Cara Bishop  
Associate Counsel

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