

ST 17-0002-PLR 02/09/2017 MANUFACTURING MACHINERY & EQUIPMENT

A de minimis serviceman incurring a Use Tax liability may claim exemptions predicated upon either the exempt status of his customer or upon exemptions claimed by his customer based on nontaxable uses of the tangible personal property transferred by the serviceman. These exemptions include sales to customers who are able to properly document the manufacturing machinery and equipment exemption. 86 Ill. Adm. Code 140.108(a)(2).

February 9, 2017

Re: Request for Private Letter Ruling-Application of Illinois Retailer Occupation Tax to Purchases of Pan Glazing/Coating Materials.

Dear Xxxxx:

This letter is in response to your letter dated October 17, 2016 in which you requested 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.

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 COMPANY 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 COMPANY 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:

COMPANY, a division of CORPORATION (“COMPANY”) writes to respectfully request a private letter ruling from the Illinois Department of Revenue (“Department”) on application of the Illinois Retailer Occupation Tax to purchases of pan glaze chemicals (“Glaze”) used in its Illinois facility. COMPANY believes purchases of Glaze are exempt and asks the Department to concur with its conclusion for the reasons stated herein.

**I.) Facts**

COMPANY is a division of CORPORATION, a S Corporation organized in STATE with its headquarters in STATE. COMPANY operates various plants nationwide including its COMPANY CITY facility located at ADDRESS. COMPANY is in the business of refurbishing pans that are used in the commercial baking industry. Most pans and bakeware used in the industry are designed to be used in automated conveyor ovens. To operate properly, the pans must be straight to align with the conveyor mechanism. The pans must also be coated with special chemicals that enable baked products to release properly from the pan. Over time, the pans get disfigured from repeated use and ovens heat; the chemical non-stick coating also wears away. At this point, the pans no longer work properly. COMPANY refurbishes the pans by first cleaning the pan using a proprietary process that completely strips the pan of all carbon, residue, and old coating. The pans are next straightened to their original shape. Finally, the pans are coated with Glaze which is cured in an oven and becomes a component part of the pan. The pans are finally packaged and shipped to the customer. COMPANY does not take title to the pans at any time; the pans remain property of the customer.

The Glaze COMPANY uses is a proprietary product; COMPANY purchases Glaze from several vendors nationwide that produce the Glaze for COMPANY's use. Vendors have historically charged Illinois Retailer Occupation tax on purchases of Glaze used in its CITY facility. COMPANY has historically accrued use tax in instances where ROT was not charged.

## **II.) Conclusion/Ruling Requested**

COMPANY believes the application of Glaze is performed on items that qualify as manufacturing machinery and equipment as its customers are industrial bakers that manufacture baked goods. COMPANY understands such commercial/industrial bakers are exempt from ROT on certain purchases of certain equipment including pans that are refurbished by COMPANY. COMPANY believes the exemption afforded its industrial baking customers "flows through" to COMPANY and allows COMPANY to purchase Glaze exempt from Retailers Occupation Tax or Retailer's Use Tax since COMPANY is performing a service on exempt equipment.

COMPANY thus respectfully requests the Department to rule as follows:

- i.) COMPANY is properly considered to be a Deminimis Serviceman
- ii.) COMPANY is entitled to exemptions available to its customers for exempt use of Glaze transferred to its customers.
- iii.) COMPANY can purchase Glaze exempt from Retailers Occupation Tax and need not accrue use tax on purchases where ROT was not charged.

## **III.) Analysis**

### **A.) COMPANY is Properly Characterized as a Deminimis Service Provider**

The pans that COMPANY refurbishes remain the property of its customers; COMPANY does not take title to pans at any time. Thus, COMPANY is not a manufacturer of

tangible personal property and is properly characterized as a service provider. The Glaze that COMPANY purchases, however, is impregnated onto the pan and thus becomes an item of tangible personal property that is sold and “transferred” to the customer as part of the refurbishment process.

Section 140.108 (a) of the Illinois Service Occupation Tax provides that if the service provider’s cost ratio of tangible personal property transferred to its customer is less than 35% of revenue received from the service, the service provider is considered a “deminimis serviceman”.

The cost of the Glaze per pan transferred to the customer is less than 35% of the revenue per pan received for the refurbishment service. Therefore, COMPANY is properly characterized as a “Deminimis serviceman” as it provides a service and the cost of Glaze transferred is less than 35% of per unit revenue.

B.) As a Deminimis Serviceman, COMPANY is entitled to its customers’ exemptions for nontaxable use of the Glaze transferred to its customers

Section 140.108 (a)(2) provides that the deminimis serviceman is the end user of tangible personal property transferred to its service customers. However, this same section provides:

“The Department has determined that a deminimis serviceman incurring a use tax liability [on cost of tangible personal property transferred] may claim exemptions predicated upon either the exempt status of the customer or upon exemptions claimed by his customer based on nontaxable uses of the tangible personal property transferred by the serviceman.”

As previously noted, the Glaze COMPANY purchases becomes a component part of the customer’s pan and is transferred to the customer. COMPANY’s customers use the pans in commercial baking operations which is an exempt use as described below

Section 130.330 of the Illinois Retailers Occupation Tax exempts sales at retail when the goods sold are machinery and equipment primarily used in manufacturing of tangible personal property for wholesale or retail sale. Equipment is further defined as an independent device or tool that is separate from the machinery but is essential to an integrated manufacturing process.

Section 130.330(d) of the Illinois Retailer’s Occupation Tax provides examples of when machinery and equipment are primarily used in manufacturing such that the use is exempt:

(F) “the production or processing of food, including the use of baking equipment such as ovens to bake bread or other bakery items, whether that baking is performed by a central bakery or a retail grocery store”

COMPANY’s customers use the pans in an exempt manner as equipment used in an industrial bakery. Pans that COMPANY refurbishes are designed for repeated use in

industrial and commercial ovens and are essential to the production of baked goods. Hence, the pans meet the definition of equipment used in an integrated industrial process. Furthermore, COMPANY's customers are engaged in the "production and processing of food" which is an example of an exempt primary use.

Since the Glaze is used in an exempt manner by its customers, COMPANY can reasonably accept an exemption certificate from its customers. Using this exemption, COMPANY can therefore purchase Glaze exempt from tax from its suppliers and does not need to accrue use tax on Glaze purchased from suppliers where tax is not charged.

Thank you in advance for consideration given to this ruling request. If you require any additional information or have any questions, please contact the undersigned at #####.

#### **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.

Under the Service Occupation Tax Act, businesses providing services (*i.e.* servicemen) are taxed on tangible personal property transferred as an incident to sales of service. See 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 his activities. The serviceman's liability may be calculated in one of four ways: (1) Service Occupation Tax on the separately stated selling price of tangible personal property transferred incident to service; (2) Service Occupation Tax on 50% of the serviceman's entire bill; (3) Service Occupation Tax on the serviceman's cost price if the serviceman is a registered *de minimis* serviceman; or (4) Use Tax on the serviceman's cost price if the serviceman is a *de minimis* serviceman and is 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 then calculated on the separately-stated selling price of the tangible personal property transferred. If the servicemen do not separately state the selling price of the tangible personal property transferred, they 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. 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. See 86 Ill. Adm. Code 140.109. Servicemen may qualify as *de minimis* if they determine that the annual aggregate cost price of tangible personal property transferred incident to the sale of service is less than 35% of

the total annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphics arts production). Servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis. Registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon their cost price of tangible personal property transferred incident to the sale of service. Such servicemen should give suppliers resale certificates and remit Service Occupation Tax using the Service Occupation Tax rates for their locations. Such servicemen also collect a corresponding amount of Service Use Tax from their customers, absent an exemption.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. This method applies to COMPANY if it makes no retail sales and is therefore not required to be registered as a retailer under Section 2a of the Retailers' Occupation Tax Act and its aggregate annual cost price of all tangible personal property transferred incident to sales of service is less than 35% of its annual gross receipts from all sales of service. 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. See 86 Ill. Adm. Code 140.108.

The rules governing de minimis servicemen provide that: "[t]he de minimis serviceman incurring Use Tax liability is considered to be the end user of the tangible personal property transferred to service customers. In this situation, the de minimis serviceman's customer incurs no tax liability, since the customer is not the "user" of the tangible personal property transferred to him by the serviceman. Although liability rests with a serviceman, the Department has determined that a de minimis serviceman incurring a Use Tax liability may claim exemptions predicated upon either the exempt status of his customer or upon exemptions claimed by his customer based on nontaxable uses of the tangible personal property transferred by the serviceman." 86 Ill. Adm. Code 140.108(a)(2). The rule goes on to state: "[f]or instance, these exemptions would include, but not be limited to, sales to customers who are able to properly document the . . . manufacturing machinery and equipment . . . exemption[]." 86 Ill. Adm. Code 140.108(a)(2)(B).

As described in this letter, the baking pans glazed by COMPANY are exempt equipment used in a manufacturing process by COMPANY's customers. The glaze that is impregnated onto the baking pans by COMPANY becomes a part of that exempt equipment. Therefore, when COMPANY purchases the glaze from its Illinois suppliers it may do so tax-exempt based on the nontaxable use of the glaze by its service customers. Further, when COMPANY purchases glaze from its out-of-state suppliers who are not registered to collect Illinois Use Tax, COMPANY does not incur and is not required to self-assess Use Tax on these purchases. To document the exemption, COMPANY should follow the procedures set out in 86 Ill. Adm. Code 140.108(a)(2)(A) regarding customers who are "E" number holders. In place of providing suppliers your customer's "E" number, you should provide a copy of your customer's completed ST-587 as described in 86 Ill. Adm. Code 130.330(g), or, in cases where you purchase glaze from out-of-state suppliers who are not registered to collect Illinois Use Tax, in which case you would be required to self-assess Use Tax, you should keep your customer's completed ST-587 in your records.

It is important to note that the manufacturing machinery and equipment exemption extends to baking equipment used in the production or processing of food. 86 Ill. Adm. Code 130.330(c)(3)(F). The exemption does not extend to the preparation of food and beverages by restaurants, food service establishments, and other retailers. 86 Ill. Adm. Code 130.330(b)(7). For any of COMPANY's customers that are restaurants, food service establishments, or other retailers, the exemption does not 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 further 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](http://www.tax.illinois.gov) or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Richard S. Wolters  
Chairman, Private Letter Ruling Committee

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