

ST 25-0034-GIL 05/21/2025 SERVICE USE TAX

Every out-of-State serviceman maintaining a place of business in this State must register and collect Service Use Tax from service customers, unless such serviceman is authorized to pay Use Tax as provided in 86 Ill. Adm. Code 140.108. 86 Ill. Adm. Code 160.130(c). (This is a GIL).

May 21, 2025

NAME  
COMPANY  
EMAIL

Dear NAME:

This letter is in response to your email dated January 3, 2025, 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 <https://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 email you have stated and made inquiry as follows:

We were recently notified by one of our accounting vendors that we have passed a threshold of gross sales of \$XX for a client who uses our cloud based software in CITY, IL. We provide the client “COMPANY1” with an application and software that they use. We have no physical presence in the state of Illinois nor any employees in Illinois. Our desktop software is internet based and has no physical download. The mobile application they use is a free download provided on the Apple and Google Play store where they gain access to use by purchasing licensing from us.

To ensure compliance with the state of Illinois, we have applied for a sales license and the information is below:

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Account Type	Account ID/License no.
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IL Business Income Tax	XX-XX
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Sales/Use Tax & E911 Surcharge	XX-XX
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We are asking you to review our current client contract and advise whether we should be taxing this client and paying the state taxes.

Note\* I have attached a copy of their purchase order agreement as well as a link to our [Master Services Agreement \(MSA\)](#) for your review which they are bound to.

Please advise if you need any further information or have any additional questions. We appreciate your attention to this inquiry.

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

##### Retailers' Occupation Tax and Use Tax

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. 86 Ill. Adm. Code 130.101. The Use Tax Act imposes a tax upon the privilege of using in this State tangible personal property purchased at retail from a retailer. 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. If the purchases occur outside Illinois, purchasers must self-assess their Use Tax liability and remit it directly to the Department.

##### Service Occupation Tax

Retailers' Occupation Tax and Use Tax do not apply to sales of service. 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 transfer of tangible personal property to service customers may result in either Service Occupation Tax liability or Use Tax liability for servicemen, depending upon which tax base they choose to calculate their liability.

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 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 de minimis 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 sales of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If servicemen do not wish to separately state the selling price of the tangible personal property transferred, those servicemen must use the second method where they will use 50% of the entire bill to their service customers as the tax base. Both of the above methods provide that in no event may the tax base be less than the cost price of the tangible personal property transferred. Under these methods, servicemen may provide their suppliers with Certificates of Resale when purchasing the tangible personal property to be transferred as a part of sales of service. They are required to collect the corresponding Service Use Tax from their customers.

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. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). See 86 Ill. Adm. Code 140.101(f). 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 sales of service. Servicemen that incur Service Occupation Tax collect the Service Use Tax from their customers. They remit tax to the Department by filing returns and do not pay tax to their suppliers. They provide suppliers with Certificates of Resale for the tangible personal 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 Section 2a of the Retailers' Occupation Tax Act. Servicemen may qualify as de minimis if they determine that the annual aggregate cost price of tangible personal property transferred as an incident of sales 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). 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.

If a transaction does not involve the transfer of any tangible personal property to the customer, then it generally would not be subject to Retailers’ Occupation Tax, Use Tax, Service Occupation Tax, or Service Use Tax.

#### Service Use Tax

The Service Use Tax is a privilege tax imposed on the privilege of using, in this State, tangible personal property that is received anywhere as an incident to a purchase of service from a serviceman. However, if the serviceman would not be taxable under the Service Occupation Tax despite all elements of the sale of service occurring in Illinois, then the tax imposed by the Service Use Tax Act does not apply to the use of such property in this State. Any evidence that property was sold by any person for delivery to a person residing in or engaged in business in this State shall be prima facie evidence that such property was sold for use in this State.

Effective October 1, 2018, an out-of-State serviceman making sales of service to Illinois purchasers with gross receipts totaling \$100,000 or more or making 200 or more separate sales of service transactions meets the definition of “serviceman maintaining a place of business in this State”. Out-of-State servicemen must determine on a quarterly basis whether they meet either of the tax remittance thresholds for the preceding 12-month period. If a threshold is met, the serviceman will be required to register and collect and remit Service Use Tax from their Illinois customers for one year. At the end of that one-year period, the serviceman may reassess on a yearly basis looking at the last four quarters. See 35 ILCS 110/2.

Every out-of-State serviceman maintaining a place of business in this State must register and collect Service Use Tax from service customers, unless such serviceman is authorized to pay Use Tax as provided in 86 Ill. Adm. Code 140.108. 86 Ill. Adm. Code 160.130(c). If the serviceman meets the definition of a “serviceman maintaining a place of business in this State” in Section 2 of the Service Use Tax Act, 35 ILCS 110/2, and either (1) his or her cost ratio is equal to or greater than 35% (75% in the case of servicemen transferring prescription drugs or engaged in graphic arts production), or (2) he or she is required or elects to register under Section 2a of the Retailers’ Occupation Tax Act, the serviceman must register with the Department to collect and remit Service Use Tax on sales of service to Illinois purchasers from locations outside of Illinois. The Department is authorized to require these servicemen to act as tax collectors because they have established sufficient contacts, or nexus, with Illinois. For servicemen with a cost ratio greater than 35%, this Service Use Tax would be based on the selling price of the tangible personal property transferred incident to the sale of service if stated separately on the

invoice from the serviceman. If not stated separately, then the tax will be imposed on 50% of the entire billing from the serviceman. For registered de minimis servicemen, the Service Use Tax will be imposed on the serviceman's cost price of the tangible personal property transferred.

Out-of-State servicemen who also make retail sales to Illinois customers that are sourced outside of Illinois, even if those sales are a small part of their business, are required to register with the Department and remit, with respect to those transactions, Retailers' Occupation Tax, if they meet the definition of "retailer maintaining a place of business in this State". Any out-of-State serviceman maintaining a place of business in this State who is required or has elected to register under Section 2a of the Retailers' Occupation Tax Act must register with the Department to collect and remit Service Use Tax on all of their sales of service to Illinois customers. If such serviceman is a de minimis serviceman, the Service Use Tax for such serviceman is based upon the serviceman's cost price of tangible personal property transferred incident to the serviceman's sales of service. 86 Ill. Adm. Code 160.115.

Finally, out-of-State servicemen who are not required to register under the Retailers' Occupation Tax Act and whose cost ratio is less than 35% (less than 75% in the case of servicemen transferring prescription drugs or engaged in graphic arts production) are not required to register with the Department to collect and remit Service Use Tax on their sales of service to Illinois consumers. This is true even if a serviceman meets the definition of "serviceman maintaining a place of business in this State" (e.g. has met a tax remittance threshold of \$100,000 or more in gross receipts from sales of service to purchasers in Illinois). Such servicemen would owe use tax on their cost price of the tangible personal property that they transfer in Illinois incident to sales of service and pay that use tax to their supplier. If that supplier is located outside of Illinois, no Illinois tax is imposed.

#### Computer Software

"Computer software" means a set of statements, data, or instructions to be used directly or indirectly in a computer in order to bring about a certain result in any form in which those statements, data, or instructions may be embodied, transmitted, or fixed, by any method now known or hereafter developed, regardless of whether the statements, data, or instructions are capable of being perceived by or communicated to humans, and includes prewritten or canned software." 35 ILCS 120/2-25. Computer software includes all types of software including operational, applicational, utilities, compilers, templates, shells, and all other forms. 86 Ill. Adm. Code 130.1935(a). Generally, sales of "canned" computer software are taxable retail sales in Illinois. Canned computer software is considered to be tangible personal property regardless of the form in which it is transferred or transmitted, including tape, disc, card, electronic means, or other media. 86 Ill. Adm. Code 130.1935. The sale or transfer by a retailer of computer software which is subject to manufacturer licenses

restricting the use or reproduction of the software is also taxable. 86 Ill. Adm. Code 130.1935(a). However, if all of the criteria provided in subsection (a)(1) of Section 130.1935 are met, then neither the sale or transfer of the software nor the subsequent software updates are subject to Retailers' Occupation Tax. Specifically, a license of software is not a taxable retail sale if:

- A) It is evidenced by a written agreement signed by the licensor and the customer;
- B) It restricts the customer's duplication and use of the software;
- C) It prohibits the customer from licensing, sublicensing or transferring the software to a third party (except to a related party) without the permission and continued control of the licensor;
- D) The licensor has a policy of providing another copy at minimal or no charge if the customer loses or damages the software, or permitting the licensee to make and keep an archival copy, and such policy is either stated in the license agreement, supported by the licensor's books and records, or supported by a notarized statement made under penalties of perjury by the licensor; and
- E) The customer must destroy or return all copies of the software to the licensor at the end of the license period. This provision is deemed to be met, in the case of a perpetual license, without being set forth in the license agreement.

86 Ill. Adm. Code 130.1935(a)(1).

Please note that it is very common for software to be licensed over the internet and the customer to check a box that states that he or she accepts the license terms. Acceptance in this manner does not constitute a written agreement signed by the licensor and the customer for purposes of subsection (a)(1)(A) of Section 130.1935. To meet the signature requirement for an exempt software license, the agreement must contain the written signature of the licensor and customer.

Software as a service is generally defined as a cloud computing service model where the provider licenses the use of computer software to a client and manages all needed physical and software resources. The possession and ownership of software remains with the provider, and the client accesses the software on web-enabled devices over the internet. The software is often provided on a subscription basis. A provider of software as a service is acting as a serviceman. As a serviceman, the seller does not incur Retailers' Occupation Tax.

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Computer software is defined broadly in the Retailers' Occupation Tax Act. However, computer software accessed through a cloud-based delivery system – a system in which computer software is never downloaded onto a client's computer and is only accessed remotely – is not subject to tax. If a provider of such a service provides to the subscriber an API, applet, desktop agent, or a remote access agent to enable the subscriber to access the provider's network and services, the subscriber is receiving computer software. A serviceman may provide such software along with a subscription for software as a service in a single transaction. Although there may not be a separate charge to the subscriber for the computer software, it is nonetheless subject to tax, unless the transfer qualifies as a non-taxable license of computer software.

If an Illinois customer downloads computer software (such as an App, API, applet, desktop agent, or remote access agent) for free from an out-of-State retailer's or serviceman's web site or server that is also located out of State, the retailer or serviceman, even though it is donating tangible personal property to the customer, has exercised no power or control over the property in Illinois. In this instance, the donor would not have made any taxable use of the property in Illinois. The customer, the donee, would incur no Use Tax liability for the retailer or Service Use Tax liability for the serviceman to collect and remit to Illinois.

The Department does not consider the viewing, downloading or electronically transmitting of video, text, and other data over the internet to be the transfer of tangible personal property. See 86 Ill. Adm. Code 130.2105(a)(3). However, if a company provides services that are accompanied with the transfer of tangible personal property, including computer software, such service transactions are generally subject to tax liability under the Service Occupation Tax Act and corresponding Service Use Tax Act. If a transaction does not involve the transfer of any tangible personal property to the customer, then it generally would not be subject to Retailers' Occupation Tax, Use Tax, Service Occupation Tax, or Service Use Tax. Illinois does not tax subscriptions of software as a service.

I hope this information is helpful. If you require additional information, please visit our website at <https://tax.illinois.gov/> or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

*Thomas Grudichak*

Thomas Grudichak  
Associate Counsel

TG:slc