

ST 97-41  
Tax Type: SALES TAX  
Issue: Sales v. Service Issues  
Timeliness of Protest (60-Day Limitation)

STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
CHICAGO, ILLINOIS

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TAXPAYER,	)	Docket No.
	)	Reg. No.
Taxpayer	)	Assmt. No.
v.	)	
	)	
THE DEPARTMENT OF REVENUE	)	John E. White,
OF THE STATE OF ILLINOIS	)	Administrative Law Judge

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RECOMMENDATION FOR DISPOSITION

Appearances: Aram Hartunian for TAXPAYER; James Dickett for the Illinois Department of Revenue.

Synopsis:

This matter arose after TAXPAYER ("TAXPAYER" or "taxpayer") protested the Notice of Tentative Determination of Claim the Illinois Department of Revenue ("Department") issued to taxpayer. TAXPAYER filed the claim to request that the Department review its determination that Illinois tax was due following an audit of TAXPAYER's business for the period beginning 7/1/85 through and including 6/30/93. Prior to hearing, the Department conducted a re-audit, and reduced the amount of tax previously determined to have been due.

The parties agreed the issues to be resolved included whether TAXPAYER was subject to retailers' occupation tax, and, if it was, whether TAXPAYER's sales were sales for resale. A hearing on

taxpayer's protest was held at the Department's Office of Administrative Hearings on June 11, 1997. Taxpayer presented evidence consisting of some books and records, the testimony of its sole proprietor, as well as the testimony of customers during the audit period. I have considered the evidence adduced at hearing, and I am including in this recommendation specific findings of fact and conclusions of law. I recommend this matter be resolved in favor of the Department.

**Findings of Fact:**

1. Taxpayer was a sole proprietorship engaged in the business of providing interior design merchandising services to home builders. See Department Group Exhibit Number ("Ex. No.") 2, p. 4.
2. TAXPAYER was the proprietor of taxpayer, and she testified at hearing. See Hearing Transcript ("Tr."), pp. 28-29.
3. The Department conducted an audit of TAXPAYER's business for the period beginning 7/1/85 through and including 6/30/93. Department Group Ex. No. 1, pp. 6-8.
4. One of TAXPAYER's contracts executed or executory during the audit period provided as follows:
  - I. EMPLOYMENT OF DESIGN FIRM  
[Client] employs TAXPAYER to provide the following design merchandising services with respect to the following described community: Chesapeake Farms, Grayslake, Illinois and specifically with respect to the following homes, The Chelsea, The Dalton, and The Easton.
  - II. DESIGN MERCHANDISING SCOPE OF SERVICES
    - A. Review client's plans with recommendations

to improve product or merchandising of the model.

- B. Preparation of the design concept for the above including:
  - 1. Presentation Board, indicating color selections, major finishes, fabrics, wallcovering, etc.
  - 2. Detailed furniture layout illustrating furniture size, type and location.
  - 3. Elevation drawings as necessary of key walls depicting design concepts.
- C. TAXPAYER will act as interior design merchandiser on the interior of the models specified above and shall specifically perform the following services:
  - Select, purchase and install furniture and case goods, art and accessories, custom window treatments, [and] wallcovering[s].
  - TAXPAYER will purchase and forward wallcoverings to [client] for timely installation by your installer.
- D. TAXPAYER shall provide interior specifications for flooring, built-ins, cabinet finishes, countertops, light fixtures and such other finishes and/or materials as may be necessary to implement the design concepts.
- E. TAXPAYER shall be responsible for all freight, warehousing, delivery and installation of the above furnishings, including sales tax.
- F. TAXPAYER shall work with [client's] Architect, Advertising Consultants, and other disciplines in overall design marketing and sales strategy.
- G. TAXPAYER will assist [client] in submission of entries for local and national award programs, with client having final approval and being responsible for payment on all submissions.

Department Group Ex. No. 5, p. 2.

- 5. As a regular part of its business, TAXPAYER completely furnished its client's model homes with tangible personal property TAXPAYER purchased for that purpose. See Department Group Ex. No. 5, pp. 2-8. Some of the items of tangible personal property TAXPAYER sold or transferred to builders included wall coverings,

draperies, artwork, furniture, bedclothes, etc. *Id.*, pp. 3-10. TAXPAYER installed some of the property in the model homes being constructed by TAXPAYER's client/builders and it arranged for other property to be made available to its client's installers. *Id.*, p. 2.

6. The merchandising aspect of TAXPAYER's business derived from TAXPAYER's efforts to help its clients sell the homes they were building in a particular development by making the model home more appealing to potential home buyers. Department Group Ex. No. 5, p. 2 (¶ II(C)); see also Tr. pp. 30-32, 39-46 (TAXPAYER), 74-75 (WITNESS) 90-91 (WITNESS B).
7. With regard to the one TAXPAYER contract admitted as evidence, of the total contract price TAXPAYER charged its customer, 95.6% of the charge was for the tangible personal property (including freight, warehousing, delivery and installation) TAXPAYER purchased and transferred to the customer. Department Group Ex. No. 5, p. 10. On that same contract, TAXPAYER waived its design fee. *Id.* A charge for \$5,500.00, for which no description is visible on the copy of the contract offered as Department Group Ex. No. 5, brought the total contract price to \$127,000.00. *Id.*
8. TAXPAYER billed its customers for the services and property TAXPAYER provided. Tr. p. 62 (TAXPAYER).
9. TAXPAYER received a good portion of its contract price in advance from its customers, so it could purchase the tangible personal property to furnish its customers model homes. *Id.*, pp. 62-63.
10. TAXPAYER did not pay tax to the wholesalers<sup>1</sup> or retailers from

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<sup>1</sup>. TAXPAYER testified that she received and maintained

whom it purchased tangible personal property it intended to transfer to its customers. Tr. pp. 63-64 ( TAXPAYER).

11. TAXPAYER did not give resale certificates to the vendors from whom it purchased the tangible personal property it intended to transfer to its customers. Tr. p. 63 ( TAXPAYER).
12. TAXPAYER did not obtain resale certificates from the customers to whom it transferred tangible personal property. Tr. p. 63 ( TAXPAYER).
13. TAXPAYER filed tax returns for five months during the audit period, i.e., 8/92 through 12/92. Department Group Ex. No. 3. TAXPAYER paid the tax shown to be due on those five returns. Department Group Ex. No. 2, pp. 13, 15. During the audit, the Department credited taxpayer for the payments it made regarding the five returns it filed within the audit period. *Id.*
14. TAXPAYER completed and filed ST-1 worksheets with the five returns it filed with the Department during the audit period. Department Group Ex. No. 3, pp. 4 (worksheet for 8/92 return), 8 (worksheet for 9/92 return), 10 (worksheet for 10/92 return), 12 (worksheet for 11/92 return), 14 (worksheet for 12/92 return).
15. On those worksheets, TAXPAYER described the nature of the amounts it claimed were deductible from taxable gross receipts. Specifically, on each worksheet, TAXPAYER described the claimed deductions as the amounts of tax it collected from persons to whom it made sales of general merchandise at retail. Department

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manufacturers' stock and price lists for furniture and other property and she used those lists to prepare purchase orders for property she then used to furnish her customers' model homes. Tr. pp. 44, 50 ( TAXPAYER)

Group Ex. No. 3, pp. 4, 8, 10, 12 & 14 (line 1A of each worksheet).

16. The worksheets completed and filed with the returns TAXPAYER filed regarding the audit period contained entries on which TAXPAYER could have indicated that it collected tax from persons to whom it transferred general merchandise incident to its sales of service. Department Group Ex. No. 3, pp. 4, 8, 10, 12 & 14 (line 1B of each worksheet).
17. Additionally, the worksheets TAXPAYER completed and filed with each return contained entries on which TAXPAYER could have identified as deductions the amount of receipts it realized from non-taxable sales of service. TAXPAYER, however, did not identify any receipts as being from its sales of service. Department Group Ex. No. 3, pp. 4, 8, 10, 12 & 14 (lines 9A-9C of each worksheet).
18. TAXPAYER signed the five returns TAXPAYER filed regarding the audit period. Department Group Ex. No. 3.
19. Following audit, the Department's auditor presented taxpayer's accountant, ACCOUNTANT ("ACCOUNTANT"), with a return the auditor prepared based on the audit. Department Group Ex. No. 2, p. 2.
20. ACCOUNTANT signed the return prepared and filed by the auditor following the audit. Department Group Ex. No. 2, p. 2. At hearing, TAXPAYER never contended ACCOUNTANT lacked power to sign on TAXPAYER's behalf. The Department issued a Notice of Assessment to taxpayer, instead of a Notice of Tax Liability, because the tax assessed was based on a filed return. See 35 **ILCS** 120/4.

21. Although TAXPAYER argues that it never made any sales at retail during the audit period, the only TAXPAYER contract admitted as evidence provided that TAXPAYER would be responsible for sales tax regarding its purchase of property to furnish its customer's model homes, and TAXPAYER filed state tax returns as a retailer. Department Group Ex. No. 5, p. 2 (¶ II(E)); Department Group Ex. No. 3.
22. TAXPAYER testified at hearing that she never added any markup to her cost price of the tangible personal property she purchased and transferred, installed, etc. to her customers, and that her only profit came from her charges for service. Tr. p. 48.
23. On the only TAXPAYER contract admitted at hearing, TAXPAYER waived its design fee. Department Group Ex. No. 5, p. 10.
24. Prior to hearing, and pursuant to a review of additional books and records not reviewed during the original audit, the Department revised the amount of tax it previously determined was due. See Order dated 9/4/96; Department Group Ex. No. 4.
25. Pursuant to the Department's review of its original audit determination, the total amount of tax it contends is due is \$27,894.00, not including penalties and interest. Department Group Ex. No. 4, p. 2.
26. During the Department's original and re-audits of TAXPAYER, the Department's auditor used TAXPAYER's cost price of the tangible personal property it transferred as the tax base for determining retailers' occupation tax liability. Department Group Ex. No. 2, p. 5 (auditor's comments); Department Group Ex. No. 4 (reaudit calculations), pp. 9, 11-16.

**Conclusions of Law:**

The first issue is whether TAXPAYER is a person who is subject to the Retailers' Occupation Tax Act ("ROTA"). TAXPAYER argues that it is a serviceman and that it has never held itself as being engaged in the business of selling tangible personal property at retail for use in Illinois. Tr. pp. 7-8, 118-19. TAXPAYER argues that it does not sell tangible personal property to its customers, but rather, it purchases tangible personal property on its customers behalf, and arranges to have that property installed or incorporated into its customers' model homes, or installs and incorporates the property itself. Tr. pp. 8-9, 118-20. Additionally, and if TAXPAYER's transfers are deemed to be sales, TAXPAYER argues that such sales are not sales at retail because all of its customers are builders who purchase the property from TAXPAYER for resale to others. Tr. pp. 9, 120-22.

The Department argues that TAXPAYER purchased and paid for tangible personal property in its own name without paying tax, and that it then sold such property to its customers, without paying tax and without obtaining a resale certificate from them. Tr. p. 123. The Department argues that under the ROTA, all transfers of tangible personal property are presumed to be sales at retail, and contends that TAXPAYER introduced no documentary evidence to rebut that presumption. Tr. pp. 123-24. Alternatively, the Department argued that if it were determined that TAXPAYER was a serviceman, it would be subject to SOT. Tr. p. 124.

The relationship between Illinois' Retailers' Occupation and Use

taxes and the Service Occupation and Service Occupation Use taxes was succinctly described by the Illinois supreme court in Hagarty v. General Motors Corp., 59 Ill. 2d 52 (1974):

The Retailers' Occupation Tax Act imposes a tax upon persons engaged in selling tangible personal property at retail. The amount of the tax is computed as a specified percentage of the gross receipts of such sales at retail. [citations omitted] A "sale at retail" is any transfer for a valuable consideration of the ownership of or title to tangible personal property to a purchaser for use or consumption and not for resale. The retailer is required to remit the tax to the Illinois Department of Revenue.

The Use Tax Act complements the Retailers' Occupation Tax Act. It imposes a tax, at the same rate as the retailers' occupation tax, upon the privilege of using in this State tangible personal property purchased at retail. In the usual situation the tax is collected from the purchaser by the retailer, but to the extent that the retailer remits to the Department of Revenue the tax imposed by the Retailers' Occupation Tax Act with respect to the sale of the same property, he is not required to remit the tax imposed by the Use Tax Act.

The Service Occupation Tax Act is intended to place servicemen, as nearly as possible, on a tax parity with retailers to the extent they transfer tangible personal property to the ultimate consumer. It does so by imposing a tax upon all persons engaged in the business of making sales of service. The amount of the tax is computed as a specified percentage of the cost price to the serviceman of all tangible personal property transferred by such serviceman as an incident to a sale of service. Depending on the circumstances, the tax is either collected from the serviceman by his supplier, who then remits it to the Department of Revenue, or is remitted directly to the Department by the serviceman after the transfer of the property to a purchaser.

The Service Use Tax Act complements the

Service Occupation Tax Act. It imposes a tax, at the same rate as the service occupation tax, upon the privilege of using in this State real or tangible personal property acquired as an incident to the purchase of a service from a serviceman. In the usual situation the tax is collected from the purchaser by the serviceman, but to the extent that he pays the tax imposed by the Service Occupation Tax Act with respect to the sale of service involving the incidental transfer by him of the same property, he is not required to remit the tax imposed by the Service Use Tax Act.

Hagarty v. General Motors Corp., 59 Ill. 2d at 54-56.

Other Illinois courts have described the structure of the occupational tax scheme as one in which retailers were taxed based on the goods they sell, and service businesses were taxed based on their cost price of the goods they transfer to customers incident to their sales of service. Mel-Par Drugs, Inc. v. Department of Revenue, 218 Ill. App. 3d 203, 214 (1st Dist. 1991); Dinner Theater Assoc. v. Department of Revenue, 139 Ill. App. 3d 911, 912 (3d Dist. 1985). Even though a transaction may involve both a sale of tangible personal property and the provision of a service, the legislature intended that only one tax be applied on a given item of commerce. Dinner Theater Assoc., 139 Ill. App. 3d at 912.

The test for determining whether a transaction which involves both a sale of tangible goods and a sale of services is one of proportion. *Id.* If a taxpayer's business involves the sale of tangible personal property for which a service is provided only as an incident or as an inducement to customers to make purchases, a retailers' tax should be assessed. If, however, the taxpayer provides a service which includes only a relatively insignificant or incidental transfer of tangible personal property, a service occupation tax is

applicable. *Id.* (citing American Airlines, Inc. v. Department of Revenue, 58 Ill. 2d 251 (1974); Miller v. Department of Revenue 15 Ill. 2d 323 (1958)).

In Elkay Manufacturing Co. v. Sweet, the first district court of appeals held that the Department's correction of a taxpayer's returns includes an implicit determination that the taxpayer is engaged in the business on which tax is assessed. Elkay Manufacturing Co., 202 Ill. App. 3d 466, 474 (1st District 1990). Once the Department's correction of returns or determination of tax due is introduced as evidence at hearing, the burden then falls on the taxpayer to show that it was not engaged in the business upon which tax was based. *Id.* at 474-75. That specific holding was recently reaffirmed in Soho Club, Inc. v. Department of Revenue, 269 Ill. App. 3d 220 (1st Dist. 1995). There, the court again held that the Department's correction of retailers' occupation tax returns filed during an audit period was, ". . . without more, . . . sufficient to establish a *prima facie* case that [the taxpayer] was engaged in a retail occupation during the period of the audit and thus subject to the ROT Act for that period . . ." *Id.* at 229-30.

Here, TAXPAYER filed returns with the Department for five months during the audit period. Department Group Ex. No. 3. Those returns were signed by TAXPAYER. *Id.*, pp. 2, 6, 9, 11, 13. On the worksheets, TAXPAYER identified as deductions from its taxable receipts the amounts of tax it collected from customers on "[g]eneral merchandise retail sales". *Id.*, pp. 3, 7, 10, 12, 14 (line 1A of each page). Had TAXPAYER believed it was a serviceman, it could have identified such deductions as the amounts of tax it collected from

"[g]eneral merchandise service sales". *Id.* (line 1B of each worksheet). Additionally, had any of TAXPAYER's total receipts during the periods covered by the returns been attributable to TAXPAYER's charges for sales of service, it could have identified such receipts as further deductions from taxable receipts. *Id.*, pp. 2, 6, 9, 11, 13 (line 2 of each page), pp. 3, 7, 10, 12, 14 (lines 9A-9C of each worksheet); Soho Club, Inc. v. Department of Revenue, 269 Ill. App. 3d at 229-30 ("If the thing being sold is a personal, professional or other service, and not tangible personal property, receipts therefrom cannot be included in measuring the tax."). In short, TAXPAYER filed tax returns during the audit period to report that it was making sales at retail.

After TAXPAYER filed returns as a retailer during the audit period, the Department reviewed those returns and determined that TAXPAYER had additional ROT liabilities from periods for which it had not filed returns. The Department's original and re-audit determinations of additional tax due were introduced as evidence at hearing. Department Group Ex. Nos. 2, 4. Without more, the Department's determination is sufficient to establish that TAXPAYER was engaged in the business of making sales of tangible personal property at retail. Soho Club, Inc. v. Department of Revenue, 269 Ill. App. 3d at 230. Thereafter, TAXPAYER bore the burden to show that it was not engaged in the retail business, or that its sales were not sales at retail. *Id.* at 230, 232; 35 **ILCS** 120/1. TAXPAYER was required to satisfy that burden by introducing documentary evidence, or evidence that was consistent, probable and identified with TAXPAYER's books and records. A.R. Barnes & Co. v. Department of

Revenue, 173 Ill. App. 3d 826, 833-34 (1st Dist. 1988).

Pursuant to section 1 of the ROTA, 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 subjected to a use for which it was purchased, for a valuable consideration. . . .

"Sale at retail" shall be construed to include any transfer of the ownership of or title to tangible personal property to a purchaser, for use or consumption by any other person to whom such purchaser may transfer the tangible personal property without a valuable consideration, and to include any transfer, whether made for or without a valuable consideration, for resale in any form as tangible personal property unless made in compliance with Section 2c of this Act.

35 **ILCS** 120/1. The Department does not deny that TAXPAYER's business involved both providing services and transferring tangible personal property to others for use in Illinois. Tr. p. 34 (statement of counsel for the Department); see also Department Group Ex. No. 5, p. 2. TAXPAYER offered credible testimony showing the nature of the design services it provided to customers. *E.g.*, Tr. pp. 28-44 (TAXPAYER), 77-81 (TAXPAYER selected the exterior brick, roofing and siding combinations used by one of TAXPAYER's customer/builders). That testimony was closely identified with TAXPAYER's books and records introduced at hearing. Department Group Ex. No. 5, p. 2 (contract outlines services TAXPAYER agreed to provide to customer).

While the evidence clearly established that TAXPAYER's business included providing services to customers, TAXPAYER introduced no credible evidence closely identified with its books and records to corroborate the argument that its transfers of tangible personal

property were "an infinitesimal part of what the company does for the builders." See Tr. pp. 34-35 (argument of taxpayer's counsel). For example, TAXPAYER offered the testimony of one former customer who estimated that 10 to 20% of TAXPAYER's services involved TAXPAYER's purchases of furniture and fixtures. Tr. p. 83 (testimony of WITNESS). TAXPAYER, however, introduced no books and records to corroborate WITNESS's guess.

In contrast to the conclusory testimony TAXPAYER offered to show that it did not sell any property, or that any such sales were merely incidental to TAXPAYER's sales of service, the books and records that were introduced at hearing show that the value of the tangible personal property TAXPAYER transferred was the most significant portion of its total charges to customers. The Department introduced a contract between TAXPAYER and one customer which was executory during the audit period. Department Group Ex. No. 5, p. 2. That contract was the only TAXPAYER contract introduced at hearing. The contract included an itemized list of the tangible personal property TAXPAYER transferred to the customer for that job. *Id.*, pp. 3-10. Over 95% of the approximate \$127,000.00 contract price consisted of TAXPAYER's charges for the tangible personal property it transferred to the customer when furnishing the customer's model homes. Department Group Ex. No. 5, pp. 3-10. Those charges included -- but did not separately state -- TAXPAYER's charges for freight, warehousing, delivery and installation associated with the tangible personal property TAXPAYER transferred. *Id.*

The proportional value of the tangible personal property TAXPAYER transferred in the course of its business is made even more

significant because TAXPAYER waived its design fee in that contract. Department Group Ex. No. 5, p. 10. TAXPAYER's waiver makes me question the veracity of TAXPAYER's testimony regarding how B. TAXPAYER made profits. See Tr. p. 48. Ms. TAXPAYER testified that her company made profit only from providing services, and that it made no profit when it transferred furniture, wallcoverings, etc. to its customers. *Id.* Assuming TAXPAYER never made any direct profit by marking up its cost price for the property it transferred, then when TAXPAYER waived its design fee in the contract introduced as evidence, Ms. TAXPAYER must have either intended to make whatever profits were to be made indirectly, for example, through service charges for freight, warehousing, delivery and installation associated with the property, or she must have intended to lose money on the job.

But even if TAXPAYER never made any profit from transferring tangible personal property to customers, either directly or indirectly, profit is not the linchpin for determining whether ROT is due. See Sprague v. Johnson, 195 Ill. App. 3d 798, 803 (4th Dist. 1990) (*citing Valier Coal Co. v. Department of Revenue*, 11 Ill. 2d 402, 409-10 (1957)). In cases where a business involves both sales of services and transfers of property, one linchpin is the proportionality of the value of the services provided versus the value of the tangible personal property transferred. See Dinner Theater Assoc. v. Department of Revenue, 139 Ill. App. 3d at 912.

After reviewing the evidence, I cannot conclude that TAXPAYER was engaged in a service occupation which included only insignificant or incidental transfers of tangible personal property. Nor can I conclude that TAXPAYER's customers would have paid the same contract

prices for TAXPAYER's services if not for the property TAXPAYER "[s]elect[ed], purchase[d] and install[ed] . . . [or] forward[ed] . . . for timely installation by [the client's] installer." Department Group Ex. No. 5, p. 2 (¶ II(C) of contract). TAXPAYER's transfers of property were a significant part of its business. While these conclusions are premised primarily on my review of a single TAXPAYER contract for one job completed during the audit period, TAXPAYER was in the best position to keep and maintain its business records. Regardless what occupational tax applied to its business, TAXPAYER was required to keep and present such books and records to the Department for audit or inspection. 35 **ILCS** 120/7; 35 **ILCS** 115/11, 12; 86 Ill. Admin. Code §§ 130.801 - 130.815 (ROT regulations regarding books and records required to be kept), § 140.701 (SOT regulations regarding books and records required to be kept). If TAXPAYER had contracts showing that it was primarily engaged in the business of making sales of service, TAXPAYER could have offered such records as evidence at hearing to rebut the Department's *prima facie* case. Here, however, TAXPAYER sought to introduce only one other contract into evidence, and that contract was denied admission because TAXPAYER had not tendered it in response to the Department's statutory demand for production of books and records. See Tr. pp. 43-44 (Taxpayer Ex. No. 3 identified), 55-57 (Taxpayer Ex. No. 3 denied admission).

The testimony TAXPAYER offered to show that its transfers of property to customers were an insignificant part of its total business was not corroborated by any documentary evidence closely identified with TAXPAYER's books and records. Standing alone, such evidence is insufficient to rebut the Department's *prima facie* case. See, e.g.,

A.R. Barnes & Co. v. Department of Revenue, 173 Ill. App. 3d 826, 833-35 (1st Dist. 1988). I conclude that TAXPAYER's business was subject to retailers' occupation tax.

The second issue is whether TAXPAYER's sales were sales for resale. Section 2c of the ROTA provides, in part:

Except as provided hereinabove in this Section, a sale shall be made tax free on the ground of being a sale for resale if the purchaser has an active registration or resale number from the Department and furnishes that number to the seller in connection with certifying to the seller that any sale to such purchaser is nontaxable because of being a sale for resale.

Failure to present an active registration number or resale number and a certification to the seller that a sale is a sale for resale creates a presumption that a sale is not for resale. This presumption may be rebutted by other evidence that all of the seller's sales are for resale, or that a particular sale is for resale.

35 **ILCS** 120/2c. In section 1 of the ROTA, the Illinois General Assembly construed the term "sale at retail" to include any transfer of the ownership of or title to tangible personal property to a purchaser . . . for resale in any form as tangible personal property *unless made in compliance with Section 2c of this Act.*" 35 **ILCS** 120/1 (emphasis added).

Since TAXPAYER did not obtain resale certificates from its customers, the transfers of tangible personal property are presumed to be sales at retail. 35 **ILCS** 120/1, 2c. TAXPAYER argues that the ROTA's presumptions apply only when there's been a sale of tangible personal property. Tr. p. 119. That is not the case. See Soho Club, Inc. v. Department of Revenue, 269 Ill. App. 3d at 232 (dismissing the

contention that the ROTA's presumptions do not apply where the Department and a taxpayer dispute whether the taxpayer is engaged in a retailer's occupation). A serviceman must also comply with section 2c of the ROTA in order to document that certain items of tangible personal property transferred incident to its sale of service were sales for resale. 35 **ILCS** 115/12 (incorporating § 2c of the ROTA into the SOTA). TAXPAYER did not offer evidence sufficient to rebut that presumption.

Generally, TAXPAYER transferred two kinds of tangible personal property to its customers: furniture, including art, draperies, etc.; and fixtures, i.e., property which would become incorporated into the real property being constructed by TAXPAYER's customers, such as wallcoverings. One witness, WITNESS, testified that his company (a former TAXPAYER customer) purchased and installed wallcoverings selected by TAXPAYER in its model homes. Tr. pp. 84, 87-88 (WITNESS). He also testified that his company sold the items furnished by TAXPAYER when it eventually sold its model homes. *Id.* TAXPAYER argues that such evidence shows that all of TAXPAYER's sales were sales for resale. Tr. p. 121. Notwithstanding TAXPAYER's argument, the law in Illinois is settled that when a construction contractor purchases tangible personal property which it then incorporates into real estate pursuant to a construction contract, the contractor is *using* the property, and it is not purchasing the property for later resale to the contractor's customer. Craftmasters, Inc. v. Department of Revenue, 269 Ill. App. 3d 934, 940 (4th Dist. 1994) (*citing* Material Service v. Issacs, 25 Ill. 2d 137, 140-41 (1962); G.S. Lyon & Sons Lumber & Mfg. Co. v. Department of Revenue, 23 Ill. 2d 180, 182-83

(1961)). TAXPAYER's transfers of tangible personal property to customers who incorporated such property into real estate, therefore, were sales at retail, and were not sales for resale.

Nor does the evidence support TAXPAYER's argument that its transfers of furniture to customers were sales for resale. Three witnesses testified that builders hired TAXPAYER to provide services designed to help sell the homes the customer/contractors' built and offered for sale. See Tr. pp. 30-32, 39-46 (TAXPAYER), 74-75 (WITNESS) 90-91 (WITNESS B). WITNESS testified generally regarding how his company used the services of design companies such as TAXPAYER. Tr. pp. 74-75. He testified that his company disposed of furniture it purchased for use in its model homes when the model home units were sold. Tr. pp. 84-85. WITNESS testified directly, however, that on the jobs for which his company hired TAXPAYER, it did not purchase furniture from TAXPAYER. Tr. pp. 85-86, 88. WITNESS B, another home builder, also testified that his former company hired TAXPAYER to provide design services and to purchase furniture for use in the builder's model homes. Tr. pp. 90-92. WITNESS B, however, was not asked whether, and did not testify that, his company ever resold any furniture it acquired from TAXPAYER. See Tr. pp. 90-96. So, while the record contains testimony that some of TAXPAYER's customers subsequently transferred to others furniture the builders purchased from other design companies, that evidence is not sufficient to show that any specific sales by TAXPAYER, or all of TAXPAYER's sales, were sales for resale.

Moreover, and even if one assumed that all of TAXPAYER's customers subsequently transferred title to the furniture TAXPAYER

transferred to them, TAXPAYER presented no argument why, by the time any such transfers would have occurred, TAXPAYER's customers would not have already enjoyed the use of the furniture by attempting to make the homes they hoped to sell more attractive to purchasers. When the builders placed and arranged -- or had TAXPAYER place and arrange -- furniture in the builders' model homes, that action was an exercise of rights or powers incident to the builder's ownership of the furniture. See 35 **ILCS** 105/1 (definition of "use"). TAXPAYER has not rebutted the statutory presumption that TAXPAYER's sales were sales at retail by showing that certain, or all, of its sales upon which tax was measured here were sales for resale. 35 **ILCS** 120/2c. I conclude that TAXPAYER's transfers of furniture to builder/customers for use in model homes were sales for use in Illinois.

Finally, the Department argued in the alternative that, if its auditor erred in determining that TAXPAYER was subject to the provisions of, and the tax imposed by, the ROTA, the tax determined to be due would still be proper pursuant to the Service Occupation Tax Act ("SOTA"). See Tr. p. 124. TAXPAYER argued that the Department had the opportunity to determine what tax applied to its business, and that its auditor made the determination that ROT applied. Tr. pp. 116-19, 127-28. TAXPAYER contends that the Department auditor's mistake regarding which tax applied to TAXPAYER's business bound the Department, and TAXPAYER must be declared to owe no tax whatever regarding its transfers of tangible personal property during the audit period. Tr. pp. 127-28.

Here, TAXPAYER filed five monthly tax returns on which it stated that it made sales at retail. After the Department audited TAXPAYER,

it determined that TAXPAYER had additional liabilities for which TAXPAYER had not filed returns. The Department determined that the liabilities arising from the periods for which no returns were filed were ROT liabilities. TAXPAYER's response is that it cannot be subject to ROT because it is a serviceman and not a retailer. In sum, TAXPAYER wants the fact finder to find that it is a serviceman, and simultaneously ignore that the Illinois General Assembly has imposed a tax on servicemen which is measured by the serviceman's cost price of the tangible personal property transferred incident to his sales of service.

Ordinarily, "[t]he State is not estopped by the mistakes made or misinformation given by the Department's employees with respect to tax liabilities." Brown's Furniture, Inc. v. Wagner, 171 Ill. 2d 410, 432 (1996) (citing Austin Liquor Mart v. Department of Revenue, 51 Ill. 2d 1, 5 (1972)); see also Rentra v. Department of Revenue, 9 Ill. App. 3d 1063, 1071 (1st Dist. 1973). While the errors of the Department's employees may be corrected at hearing, the actions -- or inaction -- of its counsel at hearing can bind the Department. See Department of Revenue v. Vallee Foods, 129 Ill. App. 3d 876, 878 (3d Dist. 1985). In this case, if the evidence TAXPAYER introduced had been found to have rebutted the Department's *prima facie* case, and counsel for the Department had not made the alternative argument, he ran the risk of waiving the opportunity to correct a specific error alleged during TAXPAYER's rebuttal case.

The record contains facts from which the amount of service occupation tax due could be ascertained, as measured by TAXPAYER's cost price of the tangible personal property it transferred to its

customers. In fact, TAXPAYER's retailers' occupation tax base was measured in just that manner. Department Group Ex. No. 2, pp. 4-5, 29-39 (auditor's comments and original audit calculations); Department Group Ex. No. 4, pp. 9, 11-16 (reaudit calculations). TAXPAYER would not have enjoyed any lesser burden to show that its cost price of the tangible personal property transferred was not subject to SOT, had the Department determined that TAXPAYER was a serviceman. The same relevant presumptions, recordkeeping requirements, and duties to file returns and pay tax when due exist under the provisions of each occupation tax act. Compare, e.g., 35 **ILCS** 120/1, 2c, 4, 7-8 with 35 **ILCS** 115/2, 3, 3-5, 6, 9, 11, 12. I conclude that if TAXPAYER were a serviceman, its SOT liability would have been the same as the ROT liability the Department determined was due. See Department Group Ex. No. 4.

Nor can TAXPAYER claim that it lacked notice that SOT might apply to its business. The Department's decision to use TAXPAYER's cost-price for the tangible personal property transferred as the tax base was discussed with TAXPAYER's accountant during the original audit and during the re-audit. See Department Group Ex. No. 2, pp. 4-6; Department Group Ex. No. 4, p. 11. On the original audit report, the tax liabilities determined to be due were set forth under the headings, "A. TAXES DUE PER AUDIT[,] 1. ROT/SOT TAXES". Department Group Ex. No. 1, p. 7. On the Department's re-audit report, the tax liabilities were set forth under the headings, "A. Taxes due per audit[,] 1. Retailers' / service occupation tax". Department Group Ex. No. 4, p. 2. Considering that a large part of TAXPAYER's argument at hearing focused on its contention that it was a serviceman and not a

retailer, it should not have come as a surprise to TAXPAYER when counsel for the Department argued that if TAXPAYER was found to be a serviceman, then SOT should apply to its business.

**Conclusion:**

I recommend the Director finalize the Department's assessment of retailers' occupation tax and penalties as revised by reaudit, with interest to accrue pursuant to statute. I also recommend he finalize the Department's denial of B. TAXPAYER and Company's Claim and Request for Review of Audit for Retailers' Occupation and Related Taxes.

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Date

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John E. White