



December 15, 2017

Jim Kelleher  
Senior Manager  
State and Local Tax  
Ernst & Young US LLP  
560 Mission Street, Suite 1600  
San Francisco, CA 94105

City of Chicago  
Rahm Emanuel, Mayor

Re: [REDACTED] - Private Letter Ruling

Department of Law

Dear Mr. Kelleher:

Edward N. Siskel  
Corporation Counsel

I am writing in response to your letter dated June 28, 2017 ("Request") (copy attached), requesting a private letter ruling ("PLR") concerning the application of the Chicago Personal Property Lease Transaction Tax ("Lease Tax"), Chapter 3-32 of the Municipal Code of Chicago ("Code"), to the fees charged by [REDACTED].

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Based on the facts set forth in your Request, along with our subsequent communications, including our conference call on September 8, 2017, we agree that the Transaction Fees (as defined in your Request) are not subject to the Lease Tax. We also agree that the Subscription Fees (as defined in your Request) are subject to the Lease Tax, at the lower rate provided by Code Section 3-32-030(B.1).

This PLR is based on the text of the Lease Tax Ordinance as of the date of this letter and the facts as represented in the Request being true. The opinions contained herein are expressly intended to constitute written advice that may be relied upon pursuant to Code Section 3-4-325.

Very truly yours,

Weston W. Hanscom  
Deputy Corporation Counsel  
City of Chicago, Law Department  
Revenue Litigation Division  
30 N. LaSalle, Suite 1020  
Chicago, IL 60602  
312-744-9077

Cc: Joel Flores, Department of Finance



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**Tax Advisor/Client Communication  
Privileged and Confidential**

June 28, 2017

Mr. Weston Hanscom  
Deputy Corporation Counsel  
Revenue Litigation Division  
City of Chicago Department of Law  
30 N LaSalle St, Ste 1020  
Chicago, IL 60602-4054

Dear Mr. Hanscom:

On behalf of [REDACTED] or the "Company", Ernst & Young LLP ("EY") respectfully requests a private letter ruling ("PLR") regarding the applicability of the Chicago Personal Property Lease Transaction ("PPLT") Tax to the fees described in this letter. Attached is a properly executed power of attorney. To the best of Company's knowledge and belief, [REDACTED] is neither under audit nor other investigation by the Department of Revenue (the "Department"). [REDACTED] believes that the fees are not subject to the PPLT Tax for the reasons stated below, and seeks certainty by filing this PLR request. Nevertheless, if you determine that [REDACTED] fees are subject to the PPLT Tax, we respectfully request that the Company's fees not be considered taxable until the month following issuance of this PLR as the Company reasonably believed that these fees were non-taxable.

**Facts**

[REDACTED] or the "Company" provides cloud-based eCommerce payment processing services, fraud management services, customer support services, and order management solutions for the back-office operations of manufacturers' and retailers' internet websites. Through the [REDACTED], a Software as a Service ("SaaS") based platform, manufacturers and multi-channel retailers can leverage the available inventory of local retailers as well as various retail storefronts and distribution centers when fulfilling customer's online orders. The order management software also allows clients to utilize advanced capabilities, such as in-store pickup, ship-from-store, inventory lookup, and vendor drop-ship.

The Company enters into contracts with clients to provide the above-mentioned services. The contracts typically include a fixed, one-time implementation fee to create an online store for the client and a monthly subscription fee ("Subscription Fee") to access the SaaS platform. Clients may purchase access to [REDACTED] SaaS platform independent of [REDACTED] payment processing and fraud management services discussed below. Such clients generally already have their own payment processing and customer service operations in place or expect to have all of their orders fulfilled by third-party fulfillment partners. Currently, around 500 clients use [REDACTED] SaaS platform to power eCommerce or order management on their websites.

[REDACTED] also charges a "per shipment" fee ("Per Shipment Fee"), a payment processing fee ("Payment Processing Fee"), and a transaction processing fee ("Transaction Processing Fee")



(collectively, the "Transactional Fees") separate from the Subscription Fee for clients that act as the order fulfiller. The Transactional Fees cover payment processing and fraud management services through the Company's credit card processing arrangements, customer phone support, and email support teams. Approximately 25 out of the 500 clients that pay the Subscription Fee fulfill their own orders and therefore pay Transactional Fees. [REDACTED] also has 4,500 clients who act exclusively as third-party fulfillment partners for orders placed on the websites of 450 out of the 500 clients that use the SaaS platform. The 4,500 third-party fulfillment partners do not use the SaaS platform whatsoever and accordingly, do not pay any Subscription Fees. However, the 4,500 third-party fulfillment partners must pay Transactional Fees on each order they fulfill for the 450 clients that do not fulfill their own orders. It is therefore possible for different parties to pay the Subscription Fee and the Transactional Fees with regard to a single order.

The Per Shipment Fee is a separate, fixed dollar amount charged for each individual order. The Per Shipment Fee defers the cost of customer support and per transaction credit card processing costs for low-dollar value or zero-dollar value orders such as product giveaways and promotions. [REDACTED] clients expect [REDACTED] to provide customer support for all orders including product giveaways and promotions. The Per Shipment Fee therefore helps manage customer support costs and credit card processing costs for low-dollar value and zero-dollar value orders.

For example, a [REDACTED] client gives away free coupons at a trade show to promote a new product. A customer will go home and place the zero-dollar order. If the customer has trouble during checkout (e.g. unable to complete the checkout process), the customer can call a toll-free number staffed by [REDACTED] customer service agents to help the customer complete checkout. In the event of a large promotion involving thousands of coupons, the customer support burden could be substantial because customer support volumes tend to correspond with the number of shipments made.

The Company charges a Payment Processing Fee (i.e., merchant processing fee) to process the credit card transactions and a Transaction Processing Fee (also referred to as a customer service fee) per transaction for the management and processing of the orders. Both of these charges are based on a percentage of the total order charge. For some contracts, these two fees are separately stated in the contract; other contracts provide a combined single charge that covers both elements. The combined charge is called an "order management fee".

[REDACTED] charges the Payment Processing Fee for merchant processing. [REDACTED] uses its own merchant processing accounts to process all credit card transactions for its clients in a single, combined account. [REDACTED] processes credit card payments for a fee of 2.5 percent to 4.0 percent per transaction.

[REDACTED] charges the Transaction Processing Fee for the following services: the evaluation of fraud risk at point-of-sale (e.g., evaluation of the location of IP addresses to identify fraud), chargeback protection to make clients whole if they suffer losses due to fraud, and customer support services (e.g., addressing card charge issues, handling customer satisfaction issues, dealing with returns requests, and helping customers with other order issues). Fraud prevention services are provided via a team of fraud analysts and managers. Depending on the season and order volumes, there could be six to twelve people (or more) engaged in fraud analysis and customer interactions related to fraud prevention. When transactional fraud is

identified, additional analysis is required to determine the extent of fraud, determine if a claim can be made against a fulfillment partner or customer, to make claims for re-payment of transactions to various card processors and providers, and to calculate losses to report back to clients and [REDACTED] finance. In addition to fraud costs, the company also bears the cost of bad debts associated with uncollected accounts. The Transaction Processing Fee is approximately 3.75 percent.

Customer support services are provided by a team of customer support representatives and managers based in various locations. Depending on the season and order volumes, there could be twenty-five to fifty (or more) customer support representatives providing customer support services. Customer support services include 24/7/365 phone-based order support for customers who have purchased products from [REDACTED] manufacturer and retailer client websites. Customer support services also include email and text-based order support for customers. Types of scenarios handled by [REDACTED] customer support representatives include: providing estimated shipping and delivery times for customers, fielding product questions and directing customers to the best resource online or phone-based for help, and authorizing returns or exchanges of products. Customer support services are provided in multiple languages including English, French, Italian, and German.

The Transaction Processing Fee and Payment Processing Fee are deducted from the total amounts received through the merchant interchange on goods sold via credit card. Thus, the Company remits to its clients the total charge (order value plus all taxes and shipping/handling costs) less the Transaction Processing Fee and Payment Processing Fee. All other fees, such as implementation and subscriptions, are billed separately. When an order is returned, the Company refunds the Transaction Processing Fee and Payment Processing Fee but retains the Per Shipment Fee.

In [REDACTED] acquired [REDACTED]. In [REDACTED] [REDACTED] formed [REDACTED] a unified omnichannel commerce company, which is now the parent company of [REDACTED]

#### Requested Ruling

[REDACTED] respectfully requests that the Department confirm the following:

1. Transactional Fees charged by [REDACTED] encompass transactional services including merchant processing, fraud prevention, and customer support services. [REDACTED] performance of such services does not require the lease or rental of personal property. Rather, the transactional services are pure services. As such, the Transactional Fees do not represent fees collected in connection with a taxable nonpossessory computer lease and are therefore not subject to the Chicago PPLT Tax.
2. [REDACTED] collects Transactional Fees only for the provision of transactional services (merchant processing, fraud prevention, and customer support). This means payment of the Transactional Fees does not give clients a license to access [REDACTED] SaaS platform. In other words, clients receive nothing more than the transactional services when paying the Transactional Fees. The primary (and only) purpose or true object of [REDACTED] Transactional Fees is therefore the transactional services. Because the dominant purpose of the Transactional Fees does not entail a taxable nonpossessory computer lease, the Transactional Fees are not subject to the Chicago PPLT Tax.

3. Even where the Subscription Fees are considered taxable under the Chicago PPLT Tax, the Transactional Fees are not bundled together with Subscription Fees (i.e., fees related to a taxable nonpossessory computer lease) such that the Transactional Fees are not subject to the Chicago PPLT Tax.
4. Even if the Transactional Fees are considered bundled together with Subscription Fees, it is clear that the Transactional Fees are consideration paid for a benefit separate and distinct from the lease of rental of personal property. As such, the Transactional Fees are not subject to the Chicago PPLT Tax.

#### **Authority**

Chicago imposes the PPLT Tax on “(1) the lease or rental in the city of personal property, or (2) the privilege of using in the city personal property that is leased or rented outside the city.”<sup>1</sup> The PPLT Tax applies to payments for the lease or rental of personal property, including charges incurred pursuant to a nonpossessory lease.<sup>2</sup>

The term “nonpossessory lease” means a lease or rental wherein use but not possession of the personal property is transferred and includes . . . leased time on or use of any and all personal property not otherwise itself rented . . . and specifically includes a “nonpossessory computer lease.”<sup>3</sup>

The term “nonpossessory computer lease” means a “nonpossessory lease” in which the customer obtains access to the provider’s computer and uses the computer and its software to input, modify or retrieve data or information, in each case without the intervention (other than de minimis intervention) of personnel acting on behalf of the provider.<sup>4</sup>

Examples of charges incurred pursuant to a taxable nonpossessory computer lease include: access to applications available through a lessor’s<sup>5</sup> computer and its software (i.e. SaaS), performance of online database searches, and attainment of data or information compiled and stored on the lessor’s computer.<sup>6</sup>

Examples of services not subject to the PPLT Tax include retaining a provider to write a report or create a database that the customer later accesses electronically.<sup>7</sup> While the provider may have delivered the report electronically, the charge pertains to the service of writing or creating a database. The primary purpose of the charge does not relate to the customer’s use or control of the provider’s computer. The customer is therefore not subject to PPLT Tax, despite having to retrieve the completed report or database by accessing the provider’s computer.

<sup>1</sup> Chicago Muni. Code Sec. 3-32-030(A).

<sup>2</sup> Chicago Muni. Code Sec. 3-32-020(I).

<sup>3</sup> Chicago Muni. Code Sec. 3-32-020(I).

<sup>4</sup> Chicago Muni. Code Sec. 3-32-020(I).

<sup>5</sup> The “lessor” refers to any person who leases or rents personal property to users and receives consideration for that lease or rental. Chicago Muni. Code Sec. 3-32-020(M).

<sup>6</sup> Chicago Dept. of Rev. Personal Property Lease Transaction Tax Ruling, No. 12, June 9, 2015 at para. 6.

<sup>7</sup> Chicago Dept. of Rev. Personal Property Lease Transaction Tax Ruling, No. 12, June 9, 2015 at para. 7.

The Illinois Supreme Court has articulated the following standard for what constitutes a sale of service:

If the article sold has no value to the purchaser except as a result of services rendered by the vendor and the transfer of the article to the purchaser is an actual and necessary part of the service rendered, then the vendor is engaged in the business of rendering service and not in the business of selling at retail.<sup>8</sup>

In other words, the services remain the “true object” or dominant purpose of the transaction even where the seller incidentally provides an article as part of the services rendered.

Where a contract involves both a sale of a service and the lease or rental of personal property, the lease price or rental price should separately state the taxable and non-taxable elements.<sup>9</sup> For example, optional maintenance charges separately stated from lease or rental charges associated with use of the lessor’s computer and computer software.<sup>10</sup> If the charge is “bundled” or fails to distinguish the non-lease or non-rental portion from the rental portion for purposes of the PPLT Tax, the entire charge will be deemed taxable unless “it is clearly proven that at least 50% of the price is not for the use of any personal property.”<sup>11</sup> Thus, a bundled charge is fully taxable if it relates primarily to the customer’s use or control of the provider’s computer.<sup>12</sup>

If a contract for the lease or rental of personal property include fees such as late, membership, or club fees, such fees are also taxable unless it is demonstrated that they are not part of the consideration for the lease or rental of personal property.<sup>13</sup> For example, a membership fee that allows members to lease or rent video tapes for free, at a discount, or in advance of others is a taxable fee. The membership fees here represent consideration paid for the ability to lease or rent personal property. Unless it is shown that the membership fee also includes benefits apart from the lease or rental of video tapes, the membership fee is fully taxable.

### Discussion

██████████ believes that the Transactional Fees are not consideration for the use of SaaS solutions, such that the Transactional Fees are not fees related to a taxable nonpossessory computer lease. The Transactional Fees are, therefore, not subject to the Chicago PPLT Tax.

██████████ provides merchant card processing and fraud management for transactions along with customer phone and e-mail support. For these services, ██████████ charges the Transactional Fees, which include a Per Shipment Fee, a Payment Processing Fee, and a Transaction Processing Fee. ██████████ charges a Per Shipment Fee on all orders including zero dollar orders. This flat fee arises out of the additional customer support service burden each new order creates. It does not relate to the use of ██████████ SaaS platform. The Company charges a separate Payment Processing Fee to process credit card transactions for

<sup>8</sup> *Spagat v. Mahin*, N.E.2d 834, 837-38 (1971).

<sup>9</sup> Chicago Dept. of Rev. Personal Property Lease Transaction Tax Ruling, No. 3, June 1, 2004 at para. 5. See also Chicago Muni. Code Sec. 3-32-020(K).

<sup>10</sup> Chicago Dept. of Rev. Personal Property Lease Transaction Tax Ruling, No. 5, Aug. 6, 2013 at para. 4.

<sup>11</sup> Chicago Dept. of Rev. Personal Property Lease Transaction Tax Ruling, No. 3, June 1, 2004 at para. 5.

<sup>12</sup> Chicago Dept. of Rev. Personal Property Lease Transaction Tax Ruling, No. 12, June 9, 2015 at para. 14.

<sup>13</sup> Chicago Dept. of Rev. Personal Property Lease Transaction Tax Ruling, No. 6, June 1, 2004 at para. 2.

merchants. [REDACTED] also charges a Transaction Processing Fee to cover fraud and chargeback protection services and customer support services. Fraud prevention services are provided via a team of fraud analysts and managers who identify and address fraud in transactions that occur on manufacturer and retailer client websites. Customer support services are provided by a team of customer support representatives and managers who interact directly with customers to resolve questions or issues. This support relates to end consumers who use the Company's manufacturer and retailer websites; the customer support does not relate to the SaaS product licensed by the Company to the manufacturer or retailer.

None of the services covered by the Transactional Fees require manufacturers or retailers to access applications or software available on [REDACTED] servers or retrieve data or information from [REDACTED] servers. The Transactional Fees are not charges incurred pursuant to a nonpossessory computer lease because they do not involve accessing software or retrieving information on [REDACTED] servers. As such, the Transactional Fees should not be subject to the PPLT Tax.

**[REDACTED] believes that the dominant purpose of the Transactional Fees is the provision of transactional services rather than a nonpossessory computer lease. The Transactional Fees are therefore not subject to Chicago PPLT Tax.**

As established above, [REDACTED] provides merchant card processing, fraud management, and customer support services to clients who choose to purchase these transactional services. [REDACTED] charges such clients - generally third-party fulfillment partners or clients who wish to fulfill their own orders - the Transactional Fees for the transactional services. The primary purpose of the Transactional Fees is not access to [REDACTED] SaaS platform, the use of which likely constitutes a nonpossessory computer lease. Rather, the true object of the Transactional Fees is the provision of transactional services to clients who do not have their own credit card processing arrangements or customer support teams. Consequently, the Transactional Fees should not be subject to the PPLT Tax.

**[REDACTED] believes that the Transactional Fees are not bundled together with Subscription Fees (i.e., fees related to a taxable nonpossessory computer lease). It is clear that the Transactional Fees provide a benefit separate and distinct from the use of any personal property such that the Transactional Fees are not subject to Chicago PPLT Tax.**

[REDACTED] services involve both a sale of services and a lease or rental of personal property. The Transactional Fees represent fees charged for the sale of services, while the Subscription Fees represent fees charged pursuant to a taxable nonpossessory computer lease. [REDACTED] separately states the Subscription Fees (lease portion) from the Transactional Fees (non-lease portion) in both its Statement of Work and Master Services Agreement documents. Subscription Fees are found under charges for "eCommerce and Order Management Hosted Application" or "eCommerce and Website Hosted Application," whereas Transactional Fees are found under "Transaction and Payment Processing." The two types of fees are also broken out under different headings. Further, the two types of fees are not billed together. Subscription Fees are a monthly fee while the Transactional Fee are netted from amounts received through merchant interchange. Further, the transaction and payment processing services are provided separately and often at different times from the manufacturers' or retailers' use of SaaS.

No part of the services provided pursuant to the Transactional Fees grants the benefit of accessing applications or software hosted on [REDACTED] servers. Likewise, no part of the services provided pursuant to the Subscription Fee gives the benefit of payment processing services, fraud and chargeback protection services, or customer support. Thus, it is clear that Transactional Fees cover [REDACTED] services that are separate and distinct from the rental or lease of personal property.

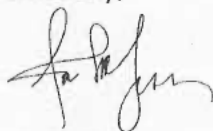
Because [REDACTED] contracts and invoices distinguish between non-lease charges and lease charges, only the lease charges are taxable under the PPLT Tax. The Transactional Fees are unrelated to the use of any personal property. Thus, the PPLT Tax should not apply to the Transactional Fees.

**Conference Requested**

Should you have any questions or reservations about issuing the requested rulings, we would respectfully request an in-person conference with you before any ruling is issued.

If you have any questions or need additional information, please contact me at (213) 977-1551.

Sincerely,



Jim Kelleher  
Senior Manager  
State and Local Tax