

Avalara



# Exemption Certificate Validation – Getting the *Right* Certificate

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# Today's Discussion – Validation Best Practices

- What are certificates... and what is so tricky about them
- Validation Basics
- Exemption and Certificate Types
- The Really Tricky ones
  - Miscellaneous Details
  - Drop Shipments
- How to Improve your Process
- Q&A





# What are exemption certificates...

...and what is so tricky about them?

# Why Are There Exemption Certificates?

- State legislatures decide what comprises the tax base – what is taxable and what is not
  - Product based – food (but not candy), Rx & services
- Legislature also allows for exceptions to otherwise taxable items
  - Use based – the exemption is based on how the item/service is used
  - Entity based – the exemption is based on who is purchasing the the item/service
- 5 states do not charge sales tax at a state level
  - NOMAD (NH, OR, MT, AK, DE)



# DOTS – Depends On The State

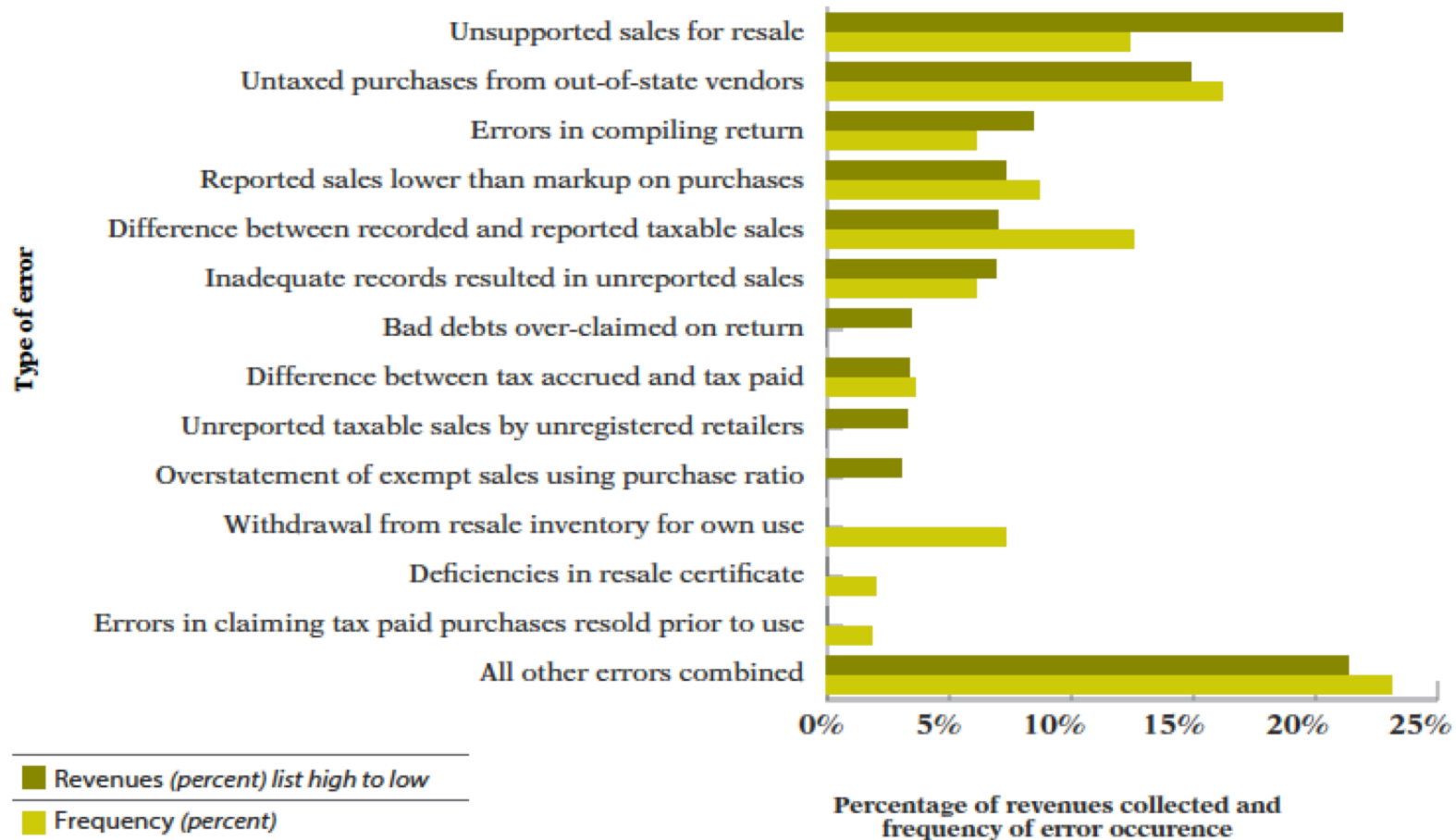
- NO universal rules on taxability or exemptions
- Each state decides
  - What is taxable
  - What exemptions to allow
  - How they define those exemptions
  - How to document the exemptions
- For instance:
  - About half the states require non-profits to pay sales tax
  - Several states require state/local gov entities to pay sales tax (CA, WA, AZ, etc.)



# CA BOE Annual Report FY 2012-13

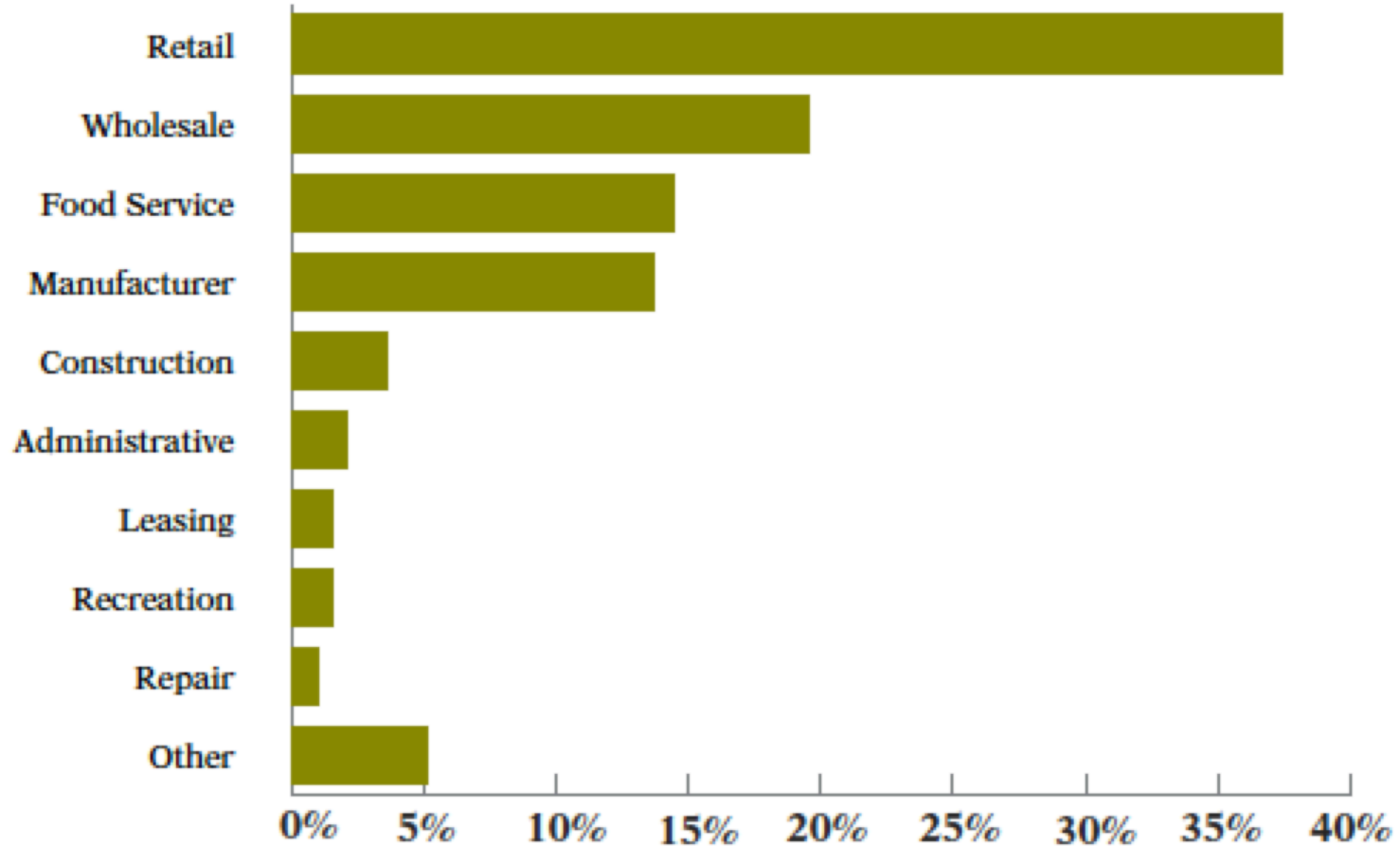
## Top Ten Areas of Noncompliance by Revenues Collected and Frequency

Publication 306, December 2013



"The program audits one percent of active accounts each year, concentrating on those considered most likely to be inaccurate in their tax reporting. In FY 2012-13, the sales and use tax audit program disclosed net deficiencies of more than \$528 million."

### Noncompliance by NAICS\* Industry Class Percentage of Revenues Collected



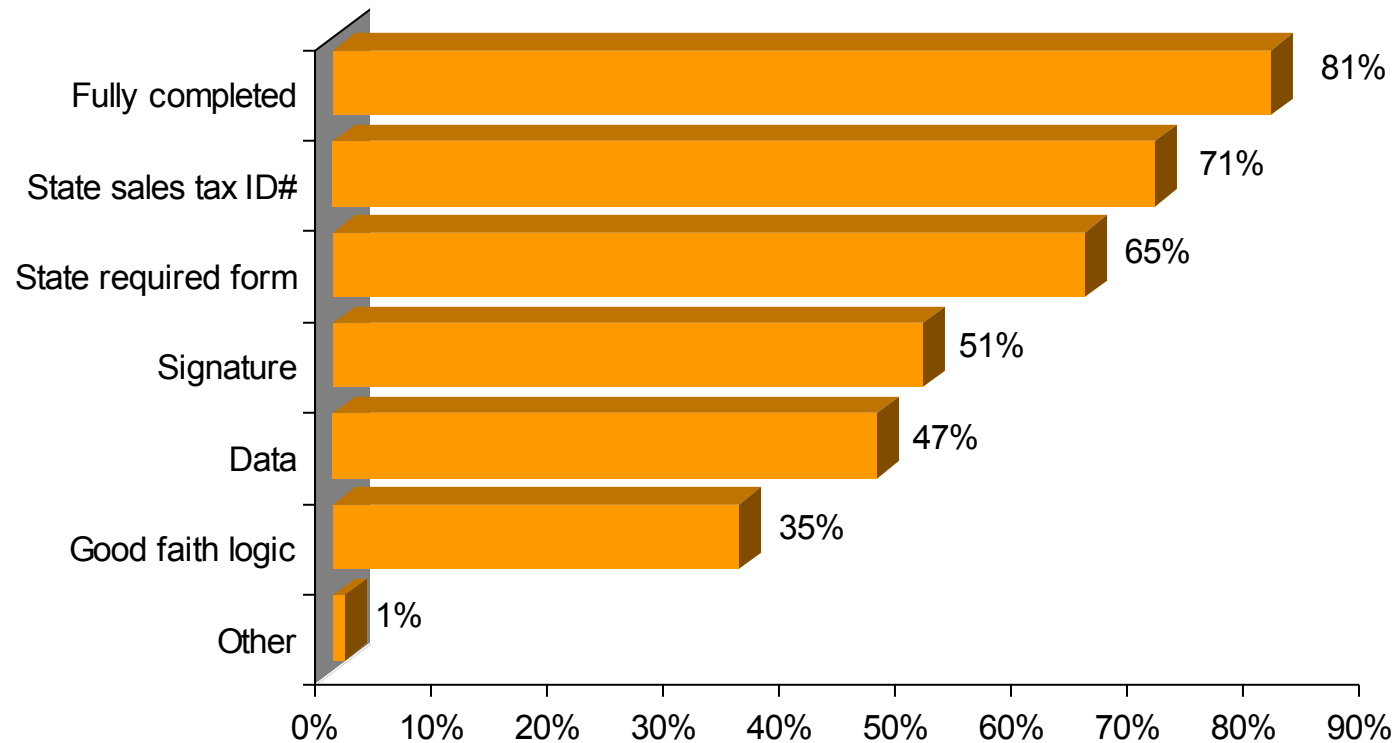




# Validation Basics

# Validation Criteria

What areas are critical to evaluate when accepting a certificate:



Based on 72 responses

Source: CRF "Sales Tax Exemption Certificate Follow-Up" 2006



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# What constitutes a valid certificate?

- Minimum Legal Components

- 1) Name of the buyer AND seller
- 2) Buyer's permit number (or explanation why number not needed)
- 3) Description of the property being purchased
- 4) Nature of the business
- 5) Signature
- 6) Date
- 7) Any other criteria identified on specific documentation

**Note:** It is tempting, but strongly advised against, to create "one size fits all" certificates as a short cut. You don't want to go through the work of collecting certificates only to have an auditor throw out homemade versions due to the wrong questions/data points.



# For Example...



STATE OF GEORGIA  
DEPARTMENT OF REVENUE  
SALES TAX CERTIFICATE OF EXEMPTION  
GEORGIA PURCHASER OR DEALER

To: \_\_\_\_\_  
(SUPPLIER) (DATE)

\_\_\_\_\_  
(SUPPLIER'S ADDRESS) (CITY) (STATE) (ZIP CODE)

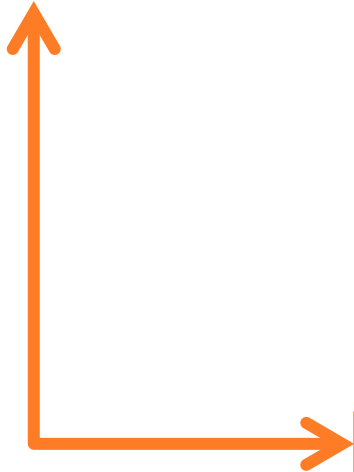
THE UNDERSIGNED DOES HEREBY CERTIFY that all tangible personal property purchased or leased after this date will be for the purpose indicated below and that this certificate shall remain in effect until revoked in writing. Any tangible personal property obtained under this certificate of exemption is subject to the sales and use tax if it is used or consumed by the purchaser in any manner other than that indicated on this certificate. (Check appropriate box.)

1. Purchases or leases of tangible personal property or services for resale. O.C.G.A. § 48-8-30.

Under penalties of perjury I declare that this certificate has been examined by me and to the best of my knowledge and belief is true and correct, made in good faith, pursuant to the sales and use tax laws of the State of Georgia.

O.C.G.A. § 48-8-3(15),(39),(41),(56),(59),and(71).

4. Materials used for packaging tangible personal property for shipment or sale. Such materials must be used solely for packaging and must not be purchased for reuse by the shipper or seller. O.C.G.A. § 48-8-3(94). A Georgia sales and use tax number is not required for this exemption.
5. Aircraft, watercraft, motor vehicles, and other transportation equipment manufactured or assembled in this state sold by the manufacturer or assembler for use exclusively outside of this state when possession is taken by the purchaser within this state for the sole purpose of removing the property from this state under its own power due to the fact that the equipment does not lend itself more reasonably to removal by other means. A Georgia sales and use tax number is not required for this exemption. O.C.G.A. § 48-8-3(32).
6. The sale of aircraft, watercraft, railroad locomotives and rolling stock, motor vehicles, and major components and replacement/repair parts of each, which will be used principally to cross the borders of this state in the service of transporting passengers or cargo by common carriers in interstate or foreign commerce under authority granted by the United States government. Private and contract carriers are not exempt. O.C.G.A. § 48-8-3(33)(A).
7. For use by a federally chartered credit union, credit unions organized under the laws of this state, and credit unions organized under the laws of the United States and domiciled within this state. A Georgia sales and use tax number is not required for this exemption. 12 U.S.C.S. 1768; O.C.G.A. § 48-6-97.



PURCHASER'S BUSINESS ACTIVITY

Under penalties of perjury I declare that this certificate has been examined by me and to the best of my knowledge and belief is true and correct, made in good faith, pursuant to the sales and use tax laws of the State of Georgia.

Business Name: \_\_\_\_\_ Sales Tax Number: \_\_\_\_\_

Business Address: \_\_\_\_\_ City: \_\_\_\_\_ State: \_\_\_\_\_ ZIP Code: \_\_\_\_\_

Purchaser's Name: \_\_\_\_\_ Signature: \_\_\_\_\_ Title: \_\_\_\_\_

A dealer must secure one properly completed certificate of exemption from each buyer making tax exempt purchases. Certificates of exemption must be obtained by the dealer within 90 days of the exempt sale being completed. The dealer must maintain a copy of the certificate of exemption presented for audit purposes.



# Good Faith

- In order to satisfy Good Faith, sellers must perform sufficient due diligence that it pass the “smell test” or reasonable “gut check”.
- In order to do this, sellers are required to have a familiarity with:
  - Exemptions available in nexus states
  - Exemptions available that can be reasonably performed with type of property sold
  - Customer business types
- In addition to basic items in last slide, includes:
  - Type of exemption claimed
  - Correct form
  - Completely filled out
- *Note: Validity Checklist available on request*





# Exemption Types and Certificates

# Use Based

- **RESALE** – most common exemption
- Manufacturing/production –
  - Material handling/inventory control?
  - Repair and replacement parts?
- Agriculture –
  - Works directly on product (animal/crop)
  - Manages processes like irrigation
  - Storage/transportation of product
- R&D, teleproduction, interstate commerce, pollution control, packing materials...



# Entity Based

- Government
  - Federal
  - State/Local – public education
  - Tribal
- Non-profit
- Religious
- Hospital – profit vs non profit vs gov run





# Both/Neither

- Direct Pay
- Documentation of sale details - Bill of Lading, Purchase Order, etc.
- Enterprise Zone (for community redevelopment efforts)
- Products made with lumber that was cut down due to Boll Weevil infestations



# Types of Certificates

- MultiState Tax Commission MultiJurisdictional (MTC MJ)
  - Resale ONLY
  - Only for states that approve it
  - Caveat on several states listed that it can only be used if NOT registered in the state (basically a “gotcha”)
- Streamlined Sales Tax
  - Provides limitation of seller liability if complete and timely
  - All exemption types should be approved (but some states are unclear and seem to dispute this)
  - Limited states but can have multiple on the form
- State Specific Forms
  - Fill In forms
  - State Issued forms – NM NTTTC, WA Resale Permit, etc
  - Combo - FL Annual Resale Certificate DR 13



# How do I know which to accept?

- There may be many valid certificates, as long as it is one of them, you are okay
- In order to have reasonable familiarity for due diligence, be sure you understand:
  - Exemptions in your nexus states
  - what you sell
  - how your customers are using it
- For example: Definition of manufacturing varies widely from state to state
  - Some include inventory control such as forklifts or conveyor systems, some do not
  - Some include repair parts to manufacturing equipment, other only include the initial purchase of equipment (in GA, ST-5 is for manufacturing purchases, ST-5M for repair and replacement parts – and the SST for either)





# Tricky Ones

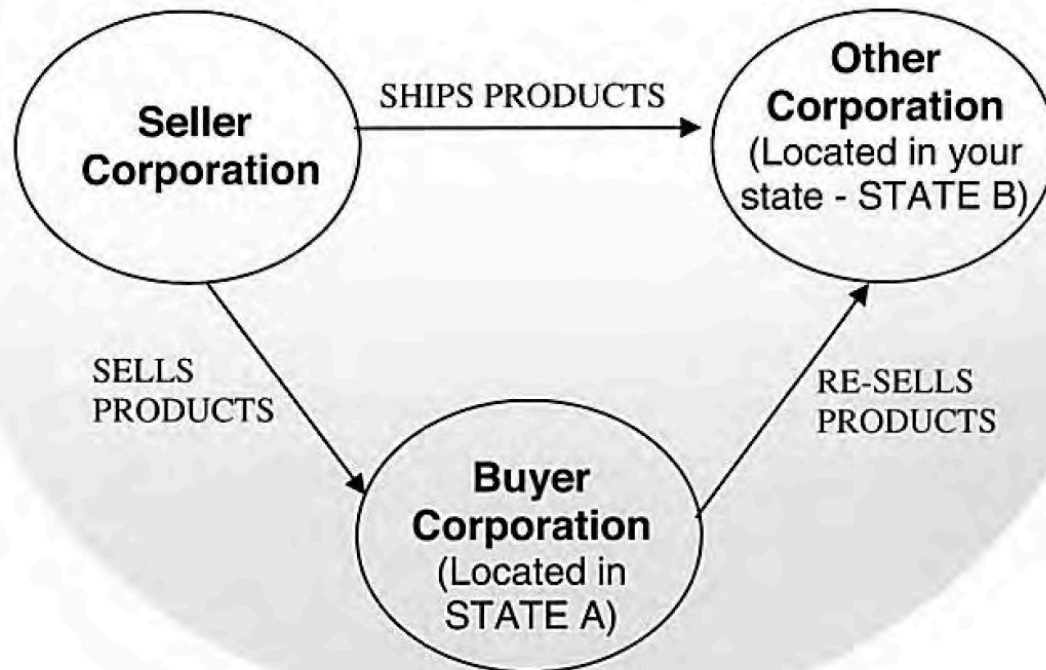
# Miscellaneous details

- Name on certificate must match name on customer account
- Method of payment for Gov or Exempt Orgs should be monitored
- State regulations change
  - WA & LA in 2009 for resale
  - TX in 2012 & GA in 2013 for agricultural
  - CA Manufacturing this year
- Blanket vs Single sale certificates
- Timely received- DOTS but the sooner the better in all cases
- Invalid Certificates
  - Keep even obviously flawed certificates, something is better than nothing
  - When you receive updated certificates, keep the older ones for historical data needed to back up previous transactions in audits



# 3<sup>rd</sup> Party Drop Shipments

When your customer is not directly receiving the goods, but having them sent to their own customer. This third party customer is not invoiced, but may be in a different state than you and your customer.



# 3<sup>rd</sup> Party Drop Shipments - details

- If you do not have nexus in shipping state you are fine
- If you do have nexus in shipping state you must collect a certificate or collect the tax
  - If your customer is registered in the shipping state, it is regular resale transaction regardless of how many different end customers you ship to
  - If your customer is not registered in the shipping state
    - MOST states will allow the resale transaction to hold
      - Customer should still issue you a resale certificate for the shipping state
      - Include their home state permit/registration number and include statement of No Nexus
    - Some states will not allow the resale transaction and you are forced to charge tax (FL)
    - Some states have additional caveats depending on where the product is shipped from (CA)

## 2014 Third-Party Drop Shipment Survey from IPT, 12th Edition June 2014

This monographic survey of forty-five states and the District of Columbia presents a third-party drop shipment fact pattern with 10 questions asked relating to each state's treatment of the transaction. The cost of the survey is \$175.00 for IPT members, \$200 for staff of IPT member companies and \$250 for non members, inclusive of shipping. U.S. Funds only, and Georgia residents should include applicable sales tax. [IPT Publications Order Form](#)

[https://www.ipt.org/IPT/Publications/Books\\_and\\_Surveys/IPT/Publications/Books%20and%20Surveys.aspx?hkey=fe47761f-df23-4fba-b974-a29d911c7088](https://www.ipt.org/IPT/Publications/Books_and_Surveys/IPT/Publications/Books%20and%20Surveys.aspx?hkey=fe47761f-df23-4fba-b974-a29d911c7088)





# How to improve your process?



# Make it a priority

- Be sure you know which states you have nexus in and standard Good Faith due diligence items
- Learn basic rules
- Work with your audit management team to identify your weaknesses
- Be pro-active
- Find others who view this as important and work together to get others on board



# Tools Available - Purchased

- Tax Research databases online – RIA Checkpoint or CCH
- Exemption Certificate Management Software
  - Specialized software (Saas) to manage:
    - Customer communication with form attached
    - Missing, incomplete, expired documents
    - Tax changes and documentation requirements
    - Visibility into compliance and potential liability
    - [www.CertCapture.com](http://www.CertCapture.com) for example
- Certificate Management Software AND Outsourcing
  - Outsourcer can do heavy lifting of clean up and software to keep ongoing compliance
  - Do not recommend having outsourcer or consultant alone – one time clean ups rarely work as a solution is not put in place for ongoing compliance



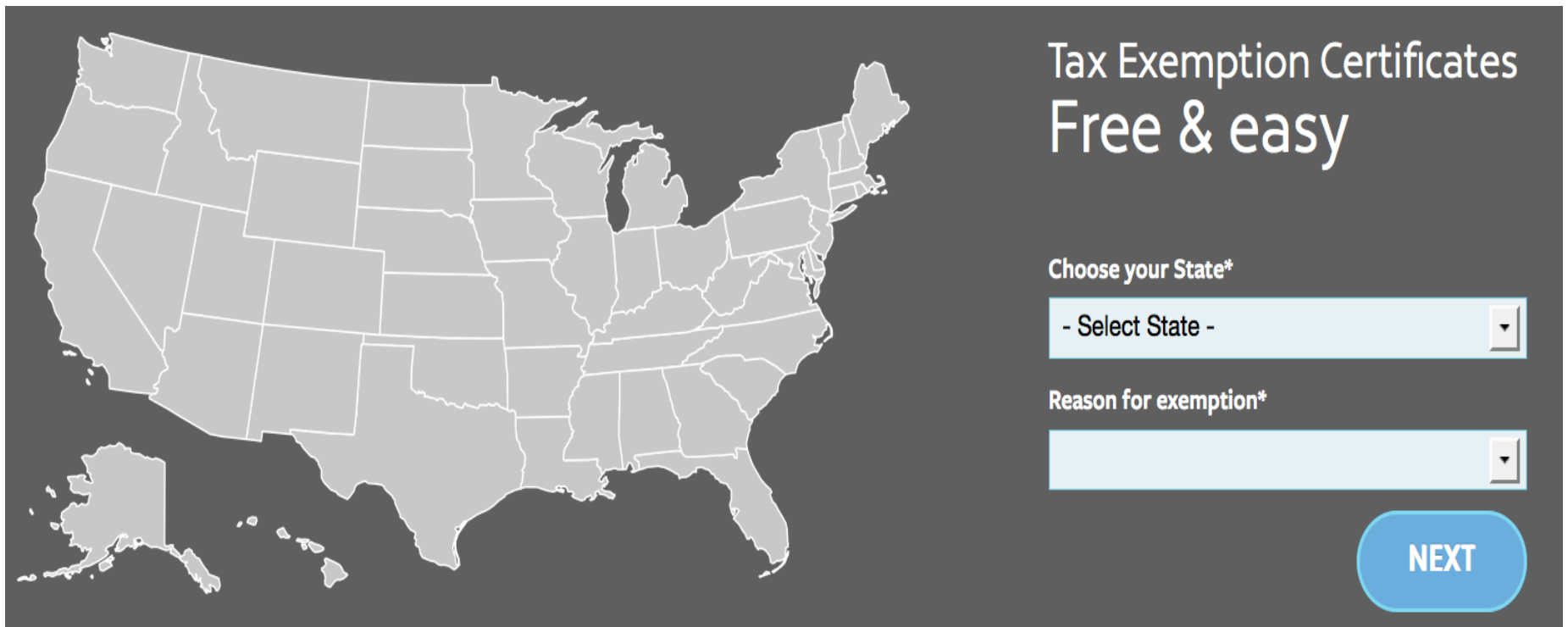
# Free Tools Available

- CertExpress – free online certificate creation wizard
  - [www.certexpress.com](http://www.certexpress.com)
- Validity checklist, white papers from Avalara
  - <http://www.avalara.com/resources/whitepapers>
- Sales Tax Blog and message boards including certificate topics
  - <http://www.taxrates.com/blog/>
  - <http://www.salestaxsupport.com/blogs/sales-use-tax/category/sales-tax-exemption-certificate/>
  - [community.avalara.com](http://community.avalara.com) and [https://community.avalara.com/avalara/categories/avalara\\_exemption\\_certificates](https://community.avalara.com/avalara/categories/avalara_exemption_certificates)
- Sales Tax Webinars – nexus, certificates, audits, etc.
  - <http://www.avalara.com/resources/webinars>
  - <http://www.avalara.com/resources/thought-leaders>
- State Department of Revenue Websites



# www.CertExpress.com

- CertExpress – free online certificate creation/submission wizard
- Buyers – easily issue and track certificates for all your vendors
- Sellers – provide to customers to ensure accurate tax exempt documentation without burdening your customers



Tax Exemption Certificates  
Free & easy

Choose your State\*

- Select State -

Reason for exemption\*

NEXT



# Removes burden of extensive tax knowledge

## Choose your State\*

New York

New Mexico

New York

North Carolina

North Dakota

Ohio

Oklahoma

## Reason for exemption\*

Purchase will be resold

Purchase will be resold

Purchase will be used in manufacturing activities

Purchase will be used in R&D activities

Purchase will be used by a non-profit organization

Purchase will be used by a government agency

Purchase will be used in agriculture activities

Purchases are taxable

Single Purchase Certificate\*

Principally Sell\* computer equipment

Select Business Description\* Retail trade


Select Registration Status\* New York State Vendor

Authority Number\* 223345678

Select Items Purchased\* Tangible Personal Property

Signature\*

[Clear signature](#)



Signer Name\* Barbara Smith

Signer Title\* Bookkeeper

Date\* 02/18/2014



# Include Certificate Collection in Customer processes

The screenshot displays the UniPunch website interface. At the top left, the UniPunch logo is accompanied by the tagline "SPEED WITHIN REACH". To the right, there are navigation links for "Español", "About UniPunch", "Photo Gallery", "News / Events", and "Contact Us", along with the phone number "1-800-828-7061". A search bar and two call-to-action buttons, "REQUEST A QUOTE" and "JOIN OUR MAILING LIST", are also visible. A horizontal menu below the header lists various services: "SYSTEM CAPABILITIES", "WHY USE UNIPUNCH", "HOW THE TOOLING WORKS", "TAILORED SYSTEMS", "PARTS BOOK", and "GET FAST TECH SUPPORT". The main content area features a breadcrumb trail "HOME » CONTACT US » CUSTOMER FORMS" and a sidebar with links to "Dealer Locator", "Request Quote", "Request Literature", and "Customer Forms". The central focus is the "CUSTOMER FORMS" section, which includes a text prompt: "Click the image below to create and submit your Sales Tax Exemption Certificate to UniPunch." Below this prompt is a promotional banner for "Tax exempt? Free certificates available" powered by "Avalara CertExpress".

Sign up for a free seller account to automate certificate submission at [https://certexpress.avalara.com/ace/seller\\_signup](https://certexpress.avalara.com/ace/seller_signup)



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# Questions?

[community.avalara.com](https://community.avalara.com)

[https://community.avalara.com/avalara/categories/avalara\\_exemption\\_certificates](https://community.avalara.com/avalara/categories/avalara_exemption_certificates)

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Find or start a tax topic, or offer suggestions/praise...



## Conversations

ALL

QUESTIONS

IDEAS

PRaise

PROBLEMS

ANNOUNCEMENTS

### Recent Conversations



Some states have a couple of forms for the same thing. How do I know which is the right form, or does it matter?

Michaela Dearborn, 2 weeks ago · Last reply: Wendy Leonard, 2 weeks ago

? Question · Answered

+ 1 · 1



Our customers get so fussy... Do I really need to get their title or printed name or whatever odd stuff on the form they forgot?

Sophia Hamilton, 2 weeks ago · Last reply: Wendy Leonard, 2 weeks ago

? Question · Answered

+ 1 · 1

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