

OKLAHOMA TAX COMMISSION

TAX POLICY AND RESEARCH DIVISION
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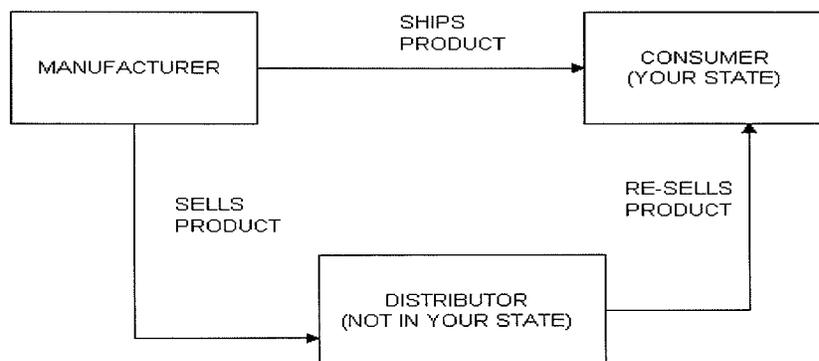
November 20, 2003

Re: Our file Number LR-03-158; Sales tax on drop-shipments

Dear

This is in response to your inquiry concerning sales tax on drop-shipment situations. Your diagram, fact situations, and questions are set out below. Each question is followed by our response.

Your Diagram



Your Facts:

A Manufacturer sells a product to a Distributor in a vendor relationship. The Distributor re-sells the same product to a Consumer in a vendor relationship. However, the product is shipped directly from the Manufacturer to the Consumer. The Consumer is located in your state. The Manufacturer is registered to collect sales tax in your state. But the Distributor is not registered because it does not have nexus with your state.

Your Questions:

- 1) If the Manufacturer is registered in the Consumer's state (Your State) but the Distributor is not, is the Manufacturer required to collect sales tax on its sale to the Distributor? Are there any factors regarding location of inventory or delivery method that can change the answer?

Our Response: Oklahoma will recognize that the sale from Manufacturer to Distributor is an **exempt** sale for resale so long as the physical delivery of the products is not transferred by Manufacturer to either Distributor or Consumer in this state. The applicable rule specifies that possession is taken inside Oklahoma if:

- physical delivery is made by the seller to the buyer in this state, or
- delivery is made in this state by delivery in the seller's own vehicles, or
- the tangible personal property is installed in this state by the seller or the seller's agent.

If delivery is made in this state, while the sale to Distributor Corporation would still be a sale for resale, it would not qualify as being exempt unless Distributor Corporation held an Oklahoma Sales Tax Permit.

This response is based on Oklahoma Tax Commission Rules 710:65-13-200 and 710:65-15-1

- 2) If the Manufacturer is required to collect the tax on the sale to the Distributor, what is the tax basis — the selling price to the Distributor, the Distributor's price to Consumer, or some other value? Are there any factors regarding location of inventory or delivery method that can change the answer?

Our Response: If the Manufacturer is required to collect the tax on the sale to the Distributor, the tax should be computed on the total gross receipts of the sale to the distributor. Gross Receipts is defined in Oklahoma Tax Commission Rule 710:65-1-9.

- 3) If the Manufacturer is required to collect tax from the Distributor, can the Distributor reimburse itself for the tax amount paid to the Manufacturer by passing through the tax paid on its invoice to the Consumer? If so, how should this tax reimbursement be displayed on the Distributor's invoice? Does this tax reimbursement amount reduce the Consumer's use tax base?

Our Response: If the tax is due on the sale between the Manufacturer and the Distributor because physical delivery of the goods sold was made in Oklahoma and the Distributor's purchase does not qualify as an exempt purchase for resale, there is no statute or rule that allows the tax to be reimbursed to the Distributor.

- 4) If the Manufacturer is not required to collect tax on its sales to the Distributor, what documentation can the Manufacturer accept from the Distributor?
- a) Home state resale certificate of the Distributor?
 - b) Consumer state (Your State) resale certificate with a no-nexus statement of Distributor?
 - c) Affidavit/statement of no nexus in Consumer state by the Distributor?

Our Response: If the Manufacturer is not required to collect sales tax on its sales to the Distributor, a home state resale certificate should be obtained to show that the Distributor is recognized in its home state as being engaged in the business of reselling the articles purchased and that the articles were, in fact, purchased for resale.

- 5) If the Distributor's home state certificate is acceptable documentation, but the Distributor's only presence is in a state without sales tax, what alternate documentation will be accepted since the Distributor will not have a home state sales tax registration number or certificate?

Our Response: A statement that their only presence is in a state without a sales tax and that therefore they cannot provide a copy of their permit to show that they are engaged in the business of reselling the articles being purchased and a statement that they are so engaged.

- 6) If the Consumer qualifies for an exemption (resale, direct pay, exempt organization or exempt use) can the Distributor provide the Consumer's exemption certificate to the Manufacturer to exempt the transaction between the Manufacturer and the Distributor?

Our Response: No.

- 7) If the Manufacturer acts as a fulfillment agent in the Consumer's state for the out-of-state Distributor, does this activity create nexus for the Distributor in the Consumer's state? Which of the following activities creates this nexus when performed by the Manufacturer?
- a) Packing and shipping orders when inventory is owned by the Manufacturer until the Manufacturer is directed by the Distributor to ship to the Consumer?
 - b) Packing and shipping orders of inventory owned by the Distributor before the Manufacturer receives any shipping instructions from the Distributor?

- c) Operating an order fulfillment service on the Distributor's behalf, including: Accepting phone and mail orders addressed to Distributor, processing payments made payable to Distributor, and packing and shipping inventory that is owned by the Manufacturer prior to shipment to the Consumer?
- d) Operating an order fulfillment service on the Distributor's behalf, including accepting phone and mail orders addressed to the Distributor, processing payments made payable to the Distributor, and packing and shipping inventory owned by the Distributor before shipment to the Consumer?
- e) Accepting and processing product returns on the Distributor's behalf, including evaluation of product defect, crediting the Consumer and maintaining product return inventory which is charged back to the Manufacturer by the Distributor such that the Manufacturer owns the returned inventory?
- f) Accepting and processing product returns on the Distributor's behalf, including evaluation of product defect, crediting the Consumer and maintaining product return inventory owned by the Distributor?

Our Response: Since the operations are located in Oklahoma, all of the operations set out in this question would result in the creation of nexus for the Distributor with Oklahoma.

Please refer to the rule Oklahoma Tax Commission Rule 710:65-1-8.

- 8) What authority (statutes, regulations, administrative rules or court cases) supports your conclusions?

Our Response: Please refer to the rules set out with each response.

- 9) We anticipate publishing these responses, either in full or summary format. We request permission to publish the information provided.

Our Response: You may publish the responses.

- 10) Would you provide contact information in case we have follow-up questions?

Our Response: Questions concerning these responses should be addressed to:

Tax Policy Division
Oklahoma Tax Commission
2501 North Lincoln Blvd.
Oklahoma City OK 73194

(405) 521-3133

This response applies only to the circumstances set out in your request of August 11, 2003. Pursuant to Commission Rule 710:1-3-73(e), this Letter Ruling may be generally relied upon **only** by the entity to whom it is issued, assuming that all pertinent facts have been accurately and completely stated, and that there has been no change in applicable law.

If I can be of further assistance, please feel free to contact me.

Sincerely,
OKLAHOMA TAX COMMISSION

A handwritten signature in cursive script, appearing to read "Michael G. Pillow".

Michael G. Pillow
Tax Policy Analyst