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Session: #38095

Hidden Compliance Risks: Sales Tax, Exemption Certificates & Unclaimed Property— What Credit Professionals Need to Know

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AGENDA



- 1. Understanding Nexus & Sales Tax Obligations**
- 2. Exemption Certificate Management Best Practices**
- 3. Unclaimed Property: What You Might Be Overlooking**
- 4. Compliance Automation: Saving Time & Reducing Risk**

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Understanding Nexus & Sales Tax Obligations

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SALES TAX OVERVIEW



- There are 45 states plus the District of Columbia that impose a state sales and use tax. In addition, some local jurisdictions either separately administer their sales tax or maintain a different tax base than the state (i.e., locals in Alabama, Arizona, Colorado and Louisiana).
- The states of New Hampshire, Oregon, Montana, Alaska, and Delaware do not impose a state level sales and use tax. Puerto Rico also imposes a sales and use tax.
- Most states sales tax rates ranges from 2.9% to 7.25%. Local taxes, which are often imposed in addition to the state sales tax range from .07% to 5.22%.

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SALES TAX NEXUS



PHYSICAL PRESENCE (OLD RULES)


- Employees in a state – register for payroll taxes
- Locations in a state – paying property taxes
- Sending employees into a state – deliveries, repairs, conferences
- Picking up merchandise with your own trucks
- And more...

ECONOMIC NEXUS (NEW RULES)

- Click-through
- Affiliate
- Sales volumes exceed thresholds
- Marketplace / eCommerce

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ECONOMIC NEXUS - WHAT IS IT?



- Economic nexus is a tax collection obligation imposed on sellers based on their level of economic activity within a state.
- Unlike physical presence, it is based entirely on sales revenue, transaction volume, or both.
- Sales tax compliance is now like income tax; all businesses must address where and when they have an obligation


EVALUATING ECONOMIC NEXUS

VOLUME OF SALES BY STATE

-  • Most states use **total sales**, not just taxable
-  • Most states use **\$100,000 in sales**

And/Or

NUMBER OF TRANSACTIONS BY STATE

-  • Most states use **200 transactions**

Note: Every state is different and each needs to be evaluated independently

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CREDIT REBILLS - SHORT PAYMENTS

Communication/Technology and Documentation Are the Key


- Education and communication with customers at the beginning of the onboarding process can reduce credit rebills and short payments
- Technology available for customers to self-serve themselves prior to invoicing - provide exemption certificates
- Rebilling prolongs order-to-cash in many cases and could extend the net payment terms
- Short payments create balancing amounts that can be hard to reconcile on an on-going basis
- Educate teams in understanding the documentation necessary from customers

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Exemption Certificate Management Best Practices

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EXEMPTION CERTIFICATES



KEY ISSUES FOR SALES TAX EXEMPTION CERTIFICATES

Is the form on file?	Is it the correct form?	Is the information accurate and complete?
<ul style="list-style-type: none"> Is it just a number on file? Can I find the physical papers? Did you assume exemptions for government or exempt organizations? Has it expired? 	<ul style="list-style-type: none"> Is it for the correct state? Does it cover the correct reasons? Is it a homemade form that just lists resale numbers? Is it a current version of the form? 	<ul style="list-style-type: none"> Buyer AND seller name Tax ID number Signature/date Reason for exemption Description of purchase

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EXEMPTION CERTIFICATES



TYPES OF EXEMPTION CERTIFICATES

- Purchase for resale
- Manufacturing exemption
- Purchase by charitable organization
- Purchase by government/non-profit
- Purchases by contractors - pass-through
- Other special exemptions
 - Motor Fuel
 - Telecommunications

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EXEMPTION CERTIFICATES



EXEMPTION CERTIFICATE RULES ARE STATE SPECIFIC

STATE-BY-STATE RULES

- Each state can determine how to tax products
- Exempt organizations are designated by local government
- Forms are normally state-specific

EXPIRATIONS NEED TO BE TRACKED

- Most state forms never expire, and some forms expire based on the form or type of exemption claimed
- Some forms expire based on calendar year; others expire based on the signed date
- **Contractor forms could have a project or pass-through expiration to consider**

Some expiration examples:

State	Resale	Manufacturing
AZ	1 YEAR	1 YEAR
CT	2 YEARS	2 YEARS
CO	2 YEARS	Never Expires
FL	1 YEAR 12/31	5 YEARS 12/31
IL	3 YEARS	5 YEARS
ID	3 YEARS	3 YEARS
LA	3 YEARS	3 YEARS
MD	Never Expires	5 YEARS
PA	4 YEARS	4 YEARS

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EXEMPTION CERTIFICATES



Exemption certificates are acceptable if properly completed with:

- Name of both buyer and seller
- Reason for exemption (resale for drop shipments)
- Correct state form (SST, MTC, state issued) - depends on your preference
- Signature/date (at time of sale for best good faith standards)
- Blanket (for recurring sales) or Single
- Other - depends on form

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EXEMPTION CERTIFICATES



TYPES OF FORMS

- Most States have specific certificates
 - Exemption form
 - Resale
 - Special use
- Multistate Tax Commission (MTC)
- Streamlined Sales Tax (SST)
- Pre-Printed or State Issued forms
 - Direct Pay Permits
 - Florida / Alabama Resale forms (every year)
 - State issued letters of exemption

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EXEMPTION CERTIFICATES



SOME STATES REQUIRE DIFFERENT FORMS FOR EXEMPT REASONS

Texas - Currently about 20 certificates

Resale

Agricultural

Exempt Reason (Exempt Org, Government, Education, Contractor Exemption, Etc.)

Direct Pay

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EXEMPTION CERTIFICATES



MTC FORM – MULTISTATE TAX COMMISSION

- Very simple form to complete
- Valid for most states
- Requires buyer and seller information
- For **resale** use only
- Requires description of what was purchased
- Five pages of supplemental rules. Each state maintains its own rules on how this form may be applied, which may differ from an auditor's position.
- Florida requires for tax id verification/confirmation with the state

UNIFORM SALES & USE TAX RESALE CERTIFICATE—MULTIJURISDICTION

The following states have indicated that this certificate is acceptable as a resale exemption certificate for sales tax use, subject to the instructions and notes on pages 2-4. The issuing State will be responsible for the requirements to determine the proper use of this certificate under applicable law in each state, as those may change from time to time. This form was revised as of October 14, 2022.

Issued to Seller: _____

Address: _____

I am/We are: Individual Sole Proprietor Partnership Limited Liability Company Corporation Trust Other (specify) _____

and is registered for sales tax use with the relevant state and cities within which Seller would deliver purchases to Buyer and that any such purchases are for immediate resale, or shipment or transport to a new product or service to be sold, leased, or rented in the normal course of business. Buyer is in the business of wholesaling, retailing, manufacturing, leasing, renting, or selling the following:

Description of Business: _____

General description of tangible property or realty to be purchased from the Seller:

State	State Registration, Seller's Permit, or ID Number of Purchaser	State	State Registration, Seller's Permit, or ID Number of Purchaser
AL		MO	
AK		NE	
AR		NH	
CA		NC	
CO		ND	
CT		OH	
DC		OK	
FL		OR	
GA		PA	
IA		RI	
IL		SC	
IN		TN	
KS		TX	
KY		VA	
LA		VT	
MA		WA	
MD		WI	
ME		WV	
MI		WY	
MN			
MO			
MS			
MT			
NC			
ND			
NE			
NH			
NJ			
NM			
NV			
NY			
OH			
OK			
OR			
PA			
RI			
SC			
SD			
TN			
TX			
UT			
VA			
VT			
WA			
WI			
WV			
WY			

I further certify that if any property or service is purchased from me that is used or consumed by Buyer so as to make it subject to sales tax use, Buyer will pay the tax due directly to the proper taxing authority when such use is permitted or allowed by the Seller for sales tax use. This certificate shall be kept on file and made available for inspection by the State, county, or other authority having jurisdiction over the tax use of the property or service.

Authorizing Signature: _____
Title: _____
Date: _____

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EXEMPTION CERTIFICATES



MTC Form – Multistate Tax Commission

MTC Most Common Errors

- Not completing the seller’s name, description of business or items purchased sections.
- Use of an older form that includes states that are no longer members (DC removed as of 3/13/19)
- Use of a company created form that duplicates this, but adds additional states

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EXEMPTION CERTIFICATES



SST – STREAMLINE SALES TAX

- In use by many states and very simple to complete
- Requires buyer and seller information
- Requires type of business buyer is in
- Requires reason for exemption
- Does not require description of goods purchased
- Considered a blanket exemption for all purchases
- Never expires, if business relationship continues
- Removes review of tax ID numbers from seller

Streamlined Sales Tax Certificate of Exemption
 Do not send this form to the Streamlined Sales Tax Governing Board. Send the completed form to the seller and keep a copy for your records.

This is a multi-use form for use in the states listed. For all states other than those listed on this form, the purchaser is responsible for ensuring it is eligible for the exemption in the state it is claiming the tax exemption from. Check with the state for exemption information and requirements. The purchaser is liable for any tax and interest, and possible civil and criminal penalties imposed by the state, if the purchaser is not eligible to claim this exemption.

1. Check if this certificate is for a single purchase. Enter the related invoice/purchase order # _____

2. **PURCHASER INFO**

A. BUSINESS ADDRESS (City, State, County, Zip Code)

B. Name of seller from which you are purchasing. (Business name)

C. PURCHASER ADDRESS (City, State, County, Zip Code)

3. **Purchaser's type of business.** Check the number that best describes your business.

01 Accommodation and food services	08 Real estate	15 Professional services
02 Agriculture, forestry, fishing, hunting	09 Rental and leasing	16 Education and health-care services
03 Construction	10 Retail trade	17 Nonprofit organization
04 Finance and insurance	11 Transportation and warehousing	18 Government
05 Information, publishing and communications	12 Utilities	19 Not a business
06 Manufacturing	13 Wholesale trade	20 Other (specify)
07 Mining	14 Business services	

4. **Reason for exemption.** Check the letter that identifies the reason for the exemption.

A Federal government (department) *	H Agricultural Production *
B State or local government (agency) *	I Industrial production/manufacturing *
C Total government (agency) *	J Direct sale *
D Foreign diplomat #	K Direct Mail *
E Charitable organization *	L Other (specify) *
F Religious organization *	M Educational Organization *
G Resale *	

5. **Identification (ID) number.** Enter the ID number as required in the instructions for each state in which you are claiming an exemption. If claiming multiple exemption reasons, enter the letters identifying each reason as listed in Section 4 for each state.

ID number	State/Country	Reason	ID number	State/Country	Reason
AR			IN		
GA			OH		
IA			OK		
IL			RI		
KS			SD		
KY			TN		
MI			UT		
MN			VT		
NC			WA		
ND			WI		
NE			WV		
NJ			WY		

6. **Indicate that the information on this certificate is correct and complete to the best of my knowledge and belief.**
 Signature of purchaser: _____ Date: _____
 Title: _____

SST08 Form F0003 Exemption Certificate (Revised 12/01/2021)

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EXEMPTION CERTIFICATES



SST – Streamline sales tax

SST Most Common Errors

- Not completing all the required sections
- Not signing paper copy
- Use of the generic SST form instead of the SST state specific form
- Using an older form or for a state that does not accept the form

Kansas example:

Arkansas example:

Georgia example:

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Drop Shipments Explained

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DROP SHIPMENT CERTIFICATES




TYPES OF EXEMPTION CERTIFICATES

- **Purchase for resale** ← **Only Type Used for Drop Shipping**
- Manufacturing exemption
- Purchase by charitable organization
- Purchase by government/non-profit
- Purchases by contractors - pass-through
- Other special exemptions
 - Motor Fuel
 - Telecommunications


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DROP SHIPMENT DEFINED




Definition

When a manufacturer accepts an order from a retailer, and the manufacturer delivers the goods to the customer on behalf of the retailer in a state where the manufacturer and customer have nexus.




Manufacturer (Third Party)

Manufacturer/originator/supplier of goods, the "Drop Shipper"



Retailer (Vendor)

Wholesaler/distributor (middleman) between manufacturer and customer




Customer

End user, the final purchaser

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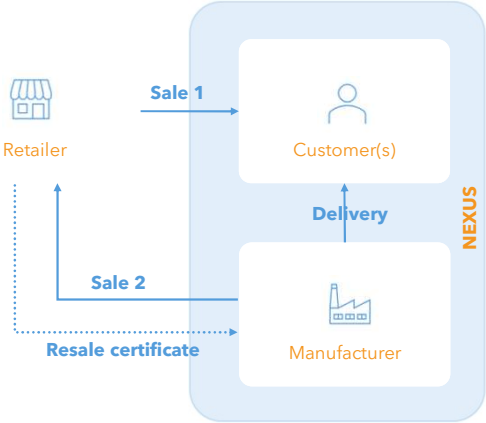
DROP SHIPMENT



Manufacturer (Third Party)
Manufacturer/originator of goods, the "Drop Shipper"


Retailer (Vendor)
Wholesaler/distributor (middleman) between the manufacturer and customer

Customer
End user, the final purchaser



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DROP SHIPMENT - ACCEPTANCE



State Home Rule (Most Common) Acceptance of Drop Shipment Certificate

State	MTC	SST
Alabama	MTC	
Arizona	MTC	
Arkansas	MTC	SST
Colorado	MTC	
Georgia	MTC	SST
Idaho	MTC	
Illinois	MTC	
Indiana		SST
Iowa	MTC	SST
Kansas	MTC	SST
Kentucky	MTC	SST
Maine	MTC	
Michigan	MTC	SST
Minnesota	MTC	SST
Missouri	MTC	
Nebraska	MTC	SST
Nevada	MTC	SST
New Jersey	MTC	SST
New Mexico	MTC	
New York		
North Carolina	MTC	SST
North Dakota	MTC	SST
Ohio	MTC	SST
Oklahoma	MTC	SST
Pennsylvania	MTC	
Rhode Island	MTC	SST
South Carolina	MTC	
South Dakota	MTC	SST
Tennessee	MTC	SST
Texas	MTC	
Utah	MTC	SST
Vermont	MTC	SST
Virginia		
Washington	MTC	SST
West Virginia		SST
Wisconsin	MTC	SST
Wyoming		SST

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UP in Accounts Receivable

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UP 101

Unclaimed Property Overview

- Property not claimed by an “owner” for a specified period of time is considered “abandoned” or “unclaimed”
- The underlying obligation must be fixed and certain
- After statutorily defined holding periods, the “holder” of the property has an obligation to perform due diligence and if no response is received, remit the property to the appropriate state
- Unclaimed property is NOT a tax, so nexus does not apply
- There is an annual filing requirement, and some jurisdictions require negative reporting (i.e., no property to report that year)
- 100+ property types are considered sources of unclaimed property

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UP IN ACCOUNTS RECEIVABLE

UP in Accounts Receivable

- A customer's account is a moving target with fluid balances, making unclaimed property tracking a challenge and open to interpretation
- Credits often appear as an obligation to the customer, but there may be more to a customer's account balance than meets the eye
- Potential AR exposure may be sitting in various general ledger accounts:
 - Trade AR
 - Cash Application/Tolerance Write-Offs
 - Bad Debt Offsets
 - Unapplied Cash/Suspense Accounts

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UP IN ACCOUNTS RECEIVABLE

Open AR

- Current Customers with credit balances
 - Much like a bank account, Holder's can use the **most recent customer generated activity date** to determine the dormancy date for that customer.
 - For example, if the customer has an open credit dated from 2020 but they are an active customer and has made a purchase and payment in 2025, you can use 2025 as the last activity date to determine dormancy.
 - However, a Holder can use the original date of the credit and track it as unclaimed property if they want, but in most cases, we do not see Holder's submitting UP from their current customers
- Holders should also review their customers for related accounts, such as parent/child relationships.

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UP IN ACCOUNTS RECEIVABLE

Open AR

- Inactive Customers with credit balances
 - This is the most typical type of credit that Holders should be tracking as there will be no more customer activity to offset the credits
 - Similar to active customers, if the credits are older, Holders may use the most recent customer generated activity date to determine dormancy, or can use the date of the credit; which ever provides the credit to be least past due
 - Credits can be offset with any open debits or already cleared bad debt for the same customer, leaving the remaining balance as the potential unclaimed property

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UP IN ACCOUNTS RECEIVABLE

Open AR

- Make sure to review credits for these possible scenarios that DO NOT represent UP:
 - Accounting errors – credit should never have been issued, payment applied to wrong or related account, etc.
 - Prompt pay discounts automatically applied but not taken by the customer
 - Customer pays by purchase order vs. invoice amount
 - What agreements are in place with customer?
 - Pre-payments for extended contracts, meaning credits to be use over a longer period of time
 - Did the customer fulfill all of their obligations to earn credit?

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UP IN ACCOUNTS RECEIVABLE

Write Offs

- Generally, no de minimus exemptions; even \$0.01 can be unclaimed property and reportable
- Automatic process at cash application to remove small balances doesn't allow for credits to be tracked and resolved
- Thresholds can be established for internal administration and review
- Amounts cannot be used to offset bad debt from other customers

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UP IN ACCOUNTS RECEIVABLE

Write Offs – Past Transactions

- To properly quantify the potential amount of unclaimed property already written off, we recommend the following:
 - Identify any tolerance threshold already in place
 - Identify the general ledger account that both debit and credit balances are being written off too
 - Pull general ledger transaction reports for the years you have records (up to 15 years) for those accounts and make sure to include the customer number for each transaction, if applicable
 - Net the debit and credit write offs by customer and identify those customers that had a NET CREDIT write off. This is your potential starting unclaimed property population.

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UP IN ACCOUNTS RECEIVABLE

Write Offs – Go Forward Strategy

- As these balances cannot all be worked, Holders can still have an automatic write-off policy, but would suggest updating the policy to include:
 - Rather than writing off the transactions to a misc. expense account, create a suspense account that all tolerance transactions are move to
 - On a semi-annual basis, net the transactions by customer and move any NET CREDIT balances to your unclaimed property liability account for future reporting. Any net debit transactions can be held in the account and used to offset future credits that are written off.

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UP IN ACCOUNTS RECEIVABLE

Unapplied Cash

- Payment is received without reference to account number, customer number, purchase order, invoice number, etc.
- We have seen these posted to:
 - Unknown Customer account in Trade AR
 - Though showing as one balance on Trade AR, these balances should be tracked individually and use the receipt date as the dormancy date
 - Separate general ledger account for unapplied cash
 - Similar to above, each line item should be tracked individually and use the receipt date as the dormancy date
 - As a credit on customer's account if customer is known, but not where to apply
 - These credits can be tracked within the Trade AR and refer to earlier slides for tracking of credits on customer accounts

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Compliance Automation: Saving Time & Reducing Risk

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UP IN ACCOUNTS RECEIVABLE

UP Compliance Automation

- Every jurisdiction requires electronic reporting in NAUPA formatted files
- Multiple software available, as well as outsourcing compliance
- Establishing workflows within ERP to identify and transfer potential unclaimed property to liability account/software
 - Alteryx workflows
 - AI for data cleanup
 - OCR for due diligence responses

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CERTIFICATES RISK OVERVIEW



- Are all documents in an accessible area?
- Are all the documents completed properly?
- Has the correct form been collected?
- Has the document expired? Has it been replaced?
- Can you find the correct document quickly when audited?
- Are your tax documents stored in a secure location?

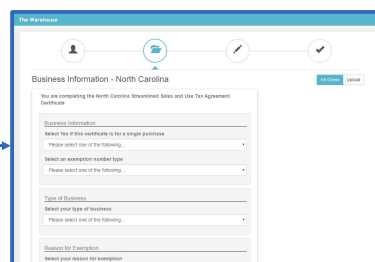
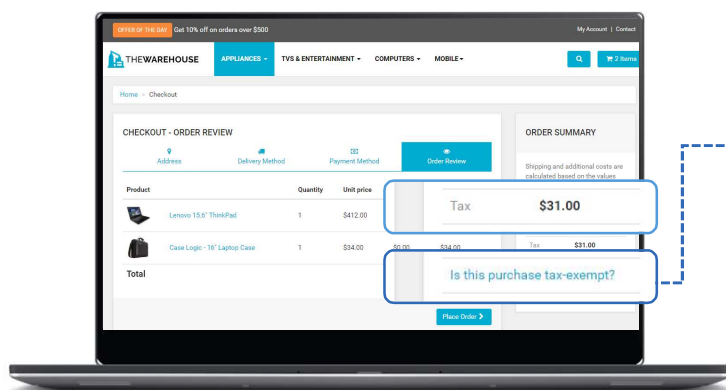


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ExemptionIQ® Connect for Ecommerce



Collect exemption certificates within your existing on-line buy workflows



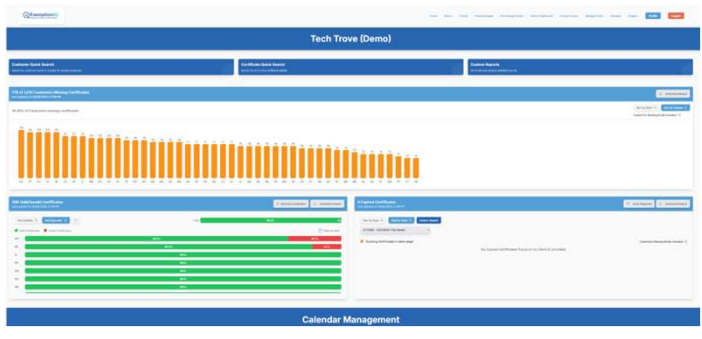
- Collect tax
- Collect and store certificates
- Apply the exemption to customer's transaction in real-time

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ExemptionIQ® Analytics Software



- Real-Time Dashboard
- Exposure Calculator
- Activity Calendar
- Certificate Health Monitoring
- Automated Request Engine



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