Issue Paper on
Simplified Exemption Administration Process
(Revised January 12, 2004)

One of the key uniformity and simplification features of the Streamlined Sales Tax System is a simplified exemption administration process. A number of provisions relating to a simplified exemption administration process are included in the Streamlined Sales and Use Tax Agreement approved by the Implementing States on November 12, 2002. The following sections of the Agreement pertain to a simplified exemption administration process:

- 204 Entity-Based Exemption
- 209 Product-Based Exemption
- 214 Use-Based Exemption
- 301 State Level Administration
- 304 Notice of State Tax Changes
- 312 Multiple Points of Use
- 313 Direct Mail Sourcing
- 316 Enactment of Exemptions
- 317 Administration of Exemptions
- 321 Confidentiality and Privacy Protections under Model 1
- 326 Direct Pay Permits
- 327 Library of Definitions
- 328 Taxability Matrix
- 501 Certification of Service Providers and Automated Systems

There are four categories of issues that must be decided to implement and operationalize the provisions relating to a simplified exemption administration process included in the Agreement. They are:

1. Administrative issues
2. Policy and operational issues
3. Systems related issues
4. Audit issues

Following are the recommendations for addressing these issues.
Administrative Issues:

The administrative issues relate to the exemption certificate form – what information is required from the purchaser, what is acceptable as an identification number, what will the uniform exemption certificate form look like and how many exemption forms are needed.

Recommendations for addressing the administrative issues:

• Purchasers who claim exemption from tax will be required to provide their name, address, type of business (see Appendix A), reason for exemption (see Appendix B), ID number, state and country issuing ID number and signature (only required for paper form).

• A uniform paper exemption certificate form will be developed and adopted by all member states. (see Appendix C)

• States will not be allowed to customize the uniform form.

• States will be required to accept the uniform form for all exemptions.

• Purchasers and sellers will be allowed to use substitute forms if they contain the same information as the uniform exemption certificate form.

• Each state will be able to choose whether or not to require an ID number.

• Acceptable ID numbers will be a state issued business or exemption number, federal ID number or driver’s license. Social security numbers will not be requested.

• States will be encouraged to provide a state issued business or exemption number to any person eligible to claim an exemption.

• Sellers often have multiple ways of capturing transactions for their company such as web order entry, order management system and point of sale register. For this reason a standard electronic form will not be developed. Instead, the standard form for claiming an exemption electronically will be a standard set of data elements that the seller needs to obtain from the purchaser at the time of purchase.

• Only one exemption form is needed. Direct, MPU and direct mail are reasons for claiming exemption. Reason codes will be established for these purposes.
Policy and Operational issues:

The policy and operational issues relate to management of the simplified exemption administration process as well as expectations of member states, sellers and purchasers.

- Classification of exemptions
- Do we need uniform exemptions for all exemptions
- What type of reason coding system will be adopted
- Will blanket exemptions be acceptable
- Will member states be allowed to require renewal of exemptions
- How should “at time of sale” be defined
- When will a state be required to honor an exemption certificate
- When will a seller be held harmless for accepting an exemption certificate
- When will an exemption certificate be required
- Does the restriction on member states in section 316B: Enactment of Exemptions relating to the entity based exemptions apply only to pertain to purchases made by an entity

Recommendations for addressing the policy and operational issues:

- States will be required to classify their exemptions as product or other (use or entity) based exemptions in the Taxability Matrix because each type of exemption will be handled differently in the Streamlined Sales Tax System.

- The Project does not need to develop uniform definitions for all exemptions allowed by the states. We should strive to reduce the number of exemptions that must be defined by the Project.

- A high level (rather than a detailed) exemption reason coding system will be developed since sellers will be relieved of the good faith requirement. (see Appendix B)

- All sellers will be required to adopt the exemption reason coding system developed by the Project to assist states in verifying purchasers’ eligibility for claiming exemptions.

- States will be required to accept blanket certificates.

- Blanket certificates will be allowed for all purposes.
• States will not be required to request renewal of blanket certificates, but may do so if they want to.

• For purposes of the agreement provision that requires an exemption certificate be taken “at the time of sale”, sellers have six months from the date of the sale to get an exemption certificate or information from the purchaser. If the exemption certificate or information is not obtained within six months, the seller is not relieved of its burden of proving that the sale was exempt.

• States will be required to honor an exemption certificate filed by any purchaser even if the purchaser is not a resident, resident organization or registered business in a state, except for an over the counter sale when the exemption reason provided by the purchaser does not apply in a state.

• For an over the counter sale, a seller may not accept an exemption certificate if the exemption reason claimed does not apply in that state. However, if the exemption applies in the state, the seller is not expected to police all of the specific requirements of the exemption.

• Sellers will be held harmless for tax on a sale if they obtain the required completed exemption certificate from the purchaser at the time of sale with three exceptions. The first exception is for an over the counter sale when the exemption reason claimed does not apply in a state. The second exception is when the purchaser claims the MPU reason code if the item being purchased is tangible personal property other than direct mail. The third is when a seller fraudulently fails to collects the tax or solicits purchasers in the unlawful claiming of an exemption.

• Sellers must obtain an exemption certificate from the purchaser on all sales of taxable products and services unless a state waives the requirement for the exemption certificate on a sale. For example, some states may choose to waive the requirement for an exemption certificate on prescribed medical equipment.

• The restriction in Section 316B relative to enacting of exemptions only applies to states exacting exemptions on purchases. States are free to enact entity-based exemptions for persons making sales without restriction.
Systems-related issues:

The systems-related issues deal with the effective dates for new product based exemptions, the need for a universal product coding system, and requirements for a valid exemption number database.

Recommendations made to address the systems-related issues:

- States will be required to follow the provisions of section 304 when enacting new product based exemptions since the product taxability matrix will need to be updated.

- A universal product coding system is not required for simplifying exemption administration since it would be too costly and time consuming to develop and keep current and would require all sellers to convert to such a system.

- Sellers or certified service providers will not be required to verify exemption numbers at the time of sale.

- States may require sellers or certified service providers to verify exemption numbers after the time of sale.

- Each state requiring sellers or certified service providers to verify exemption numbers against a state’s exemption database will establish its own procedures for doing so.
Audit issues:

The audit issues relate to expectations of sellers to be relieved of the good faith requirement, the requirements for maintaining proper records of exempt transactions, and the information, format and time frames for providing records of exempt transactions to member states.

Recommendations made to address these audit issues:

- Sellers will be expected to collect the required information on an exempt sale at the time of purchase.

- Sellers will be relieved of the good faith requirement if the required information on the uniform exemption certificate is obtained after the time of purchase if the exemption claimed is valid.

- Sellers will not be relieved of the good faith requirement if they allow exemption on a multiple-item invoice when only some of the items purchased qualify for exemption.

- Sellers will be expected to retain records of exemption certificate for the same number of years that other sales and use tax business records must be retained.

- Certified service providers will be required to collect and provide to member states on a periodic basis information on purchasers claiming exemption from tax. The information on purchasers claiming exemption from tax will be provided to states in a standardized format to facilitate data-extraction and mining by member states to identify the purchasers a member state may want to audit to verify their eligibility to claim exemption from tax. The requirements for the standardized format for reporting information on purchasers claiming exemption from tax are still being developed.

- The governing board will continue working with other sellers to determine the requirements for collecting and providing information on purchasers claiming exemption from tax to the member states as required by Section 317A(6) of the SSUTA Agreement.

- Rules and administrative practices will be established for joint state auditing of exempt transactions.
Appendix A

Business Types
For
Simplified Exemption Administration and Processing

It has been decided that purchasers claiming exemption from tax on their purchases will need to provide certain identifying information, including “type of business.”

Ideally, we would want purchasers to provide their NAICS code to identify their type of business, but many purchasers will not know their NAICS code at the time of purchase. Requiring a purchaser to review a long list of NAICS codes to find the appropriate code for their business will slow down the order-taking process, prompt questions about the codes and could negatively impact on seller/purchaser relationships.

In lieu of providing a NAICS code to identify the type of business, it is recommended that purchasers select one of the following business types:

1. Accommodation and food services
2. Agricultural, forestry, fishing and hunting
3. Construction
4. Finance and insurance
5. Information, publishing and communications
6. Manufacturing
7. Mining
8. Real estate
9. Rental and leasing
10. Retail trade
11. Transportation and warehousing
12. Utilities
13. Wholesale trade
14. Business services
15. Professional services
16. Education and health-care services
17. Nonprofit organization
18. Government
19. Not a business
20. Other _______________
Appendix B

Recommendation
For
The Streamlined Sales Tax Project’s
Exemption Reason Coding System

Decisions made:

- A high-level exemption reason coding system will be used
- All sellers and governing states will be required to adopt the exemption reason coding system
- The exemption reason coding system will facilitate multi-state joint auditing of exempt sales

Recommended Reason Coding System:

A. Federal government
B. State or local government
C. Tribal government
D. Foreign diplomat
E. Charitable organization
F. Religious or educational organization
G. Resale
H. Agricultural production
I. Industrial production/manufacturing
J. Direct pay permit
K. Multiple points of use
L. Direct mail
M. Other ____________________
DRAFT

Appendix C

Draft Streamlined Sales Tax Agreement
Certificate of Exemption

See attached .pdf file
Streamlined Sales Tax Agreement
Certificate of Exemption

Warning to purchaser:
This is a multi-state form. Not all states allow all exemptions listed on this form. Purchasers are responsible for knowing if they qualify to claim exemption from tax in the state that is due tax on this sale. The state that is due tax on this sale will be notified that you claimed exemption from sales tax. You will be held liable for any tax and interest, as well as civil and criminal penalties imposed by the member state, if you are not eligible to claim this exemption. Sellers may not accept a certificate of exemption for sales sourced within the state if an exemption does not apply in the seller’s state.

Enter the two-letter postal abbreviation for the state under whose laws you are claiming exemption.

Check one:
☐ Single purchase certificate. Relates to invoice/purchase order # ____________________.
☐ Blanket certificate. If checked, this certificate continues in force until canceled by the purchaser.

<table>
<thead>
<tr>
<th>Name of purchaser</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business address</td>
</tr>
<tr>
<td>Purchaser’s tax ID number</td>
</tr>
<tr>
<td>If no tax ID number, enter one of the following:</td>
</tr>
<tr>
<td>state of issue number</td>
</tr>
</tbody>
</table>

Name of seller from whom you are purchasing, leasing or renting

<table>
<thead>
<tr>
<th>Seller’s address</th>
</tr>
</thead>
<tbody>
<tr>
<td>City</td>
</tr>
</tbody>
</table>

Type of business. Circle the number that describes your business.

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

Reason for exemption. Circle the letter that identifies the reason for the exemption.

- A Federal government (department)______________________
- B State or local government (name)______________________
- C Tribal government (name)______________________
- D Foreign diplomat #______________________
- E Charitable organization #______________________
- F Religious or educational organization #______________________
- G Resale #______________________
- H Agricultural production #______________________
- I Industrial production/manufacturing #______________________
- J Direct pay permit #______________________
- K Multiple points of use (services, digital goods, or computer software delivered electronically)______________________
- L Direct mail #______________________
- M Other (explain)______________________

I declare that the information on this certificate is correct and complete to the best of my knowledge and belief.

Signature of authorized purchaser | Print name here | Title | Date
Appendix D

Action Steps to Comply with the Requirements
For the Simplified Exemption Administration Process

Governing States:

1. Classify exemptions and exclusions as product-based, use-based and entity-based using the definitions in the Uniform Sales and Use Tax Agreement

2. Complete the Taxability Matrix (four parts)

3. Decide if an ID number will be required for purchasers to claim exemption from tax on purchases sourced to the state

4. Decide if sellers will be required to verify the validity of ID numbers

5. If a state decides sellers will be required to verify ID numbers, the state will establish procedures for doing so after the time of sale

6. Adopt the uniform exemption certificate form for all exemptions. Governing States can not modify or customize the uniform Exemption Certificate form

7. Eliminate the use of other exemption forms

8. Allow sellers sufficient time to update their exemption certificate files and to begin accepting the new uniform exemption certificate form

Sellers:

1. Code taxability of products/services offered for sale using the Taxability Matrix (The default rule used to code the taxability of tangible personal property, digital property and services differs when the taxability of the item being sold is not clear. See Appendix E)

2. Update exemption certificate files to obtain new exemption certificates from purchasers.

3. Review and revise seller’s customized exemption certificate to ensure all required fields of information are requested

4. Ensure seller’s internal procedures are effective so mandatory fields of information are collected at the time of sale when a purchaser claims exemption on a sale
Default Rules
For
Coding the Taxability of Products

Tangible Personal Property:
• Taxable unless specifically exempted or excluded

Digital Property:
• Exempt unless specifically taxed

Services:
• Exempt unless specifically taxed for states that enumerate taxable services, or
• Taxable unless specifically exempted for states that tax all services except those specifically exempted