

When Tax-Exempt Does Not Exactly Mean Tax Exempt

How the *post-Wayfair* World Applies to Non-Profit Organizations

A Town Hall Presentation for The Nonprofit Alliance
with Martin Eisenstein and Jamie Szal
February 8, 2024

The Issues Covered In This Webinar

- ▶ Duty to Pay Sales Taxes
- ▶ Who is required to comply
- ▶ What is Taxable?
- ▶ Exemptions

Key Concepts

- ▶ Every state with a sales tax has a use tax.
- ▶ A retailer has the duty to collect/remit the sales and use tax in a state where it has nexus, unless the transaction is exempt.
- ▶ A purchaser is liable for the use tax of the state where the direct mail materials and services are mailed/used and the purchaser has nexus
- ▶ Every state taxes the retail sale of tangible personal property, unless the item is exempt or another exemption applies.



The Interface of Sales Tax and Direct Mail

- ▶ IMPORTANT CONCEPT: EVERY STATE TREATS THE PROVISION OF DIRECT MAIL MATERIALS AS THE SALE OF TANGIBLE PERSONAL PROPERTY
- ▶ A printer is treated as a seller of tangible personal property and possibly ancillary services.
- ▶ A producer may be a printer of mailing materials, a reseller of tangible personal property (printed materials) to the customer or an agent for the customer
- ▶ The taxability of direct mail materials is determined based on the state where the materials are distributed, and not where the printer/mail house seller or the mail house/postal user is located.



Key Concepts Regarding Services

- ▶ Only a handful of states tax services in general but several states tax selected services such as shipping/handling
 - ▶ Purchases directly from the U.S. Post Office are not taxable to the purchaser, but may be taxable if the commercial mail producer is not acting as its customer's agent.
- ▶ Sourcing of services is not as straightforward as sourcing of the sale of tangible personal property.
- ▶ A bundle of taxable and nontaxable products/services may cause the price for the entire bundle to be taxable.

Taxability Of Various Services

- ▶ Preliminary Materials: Photographs, Design, Pre-press and Copy.
 - ▶ Is it Tangible Personal Property?
 - ▶ Does statute exempt preliminary materials?
 - ▶ How are materials transmitted to the Printer? To the mailer?
 - ▶ Who prepares the materials?
- ▶ Manufacturing Charges: Printing, Binding, Collating.
 - ▶ Generally taxable.
 - ▶ Need to determine the purchaser.

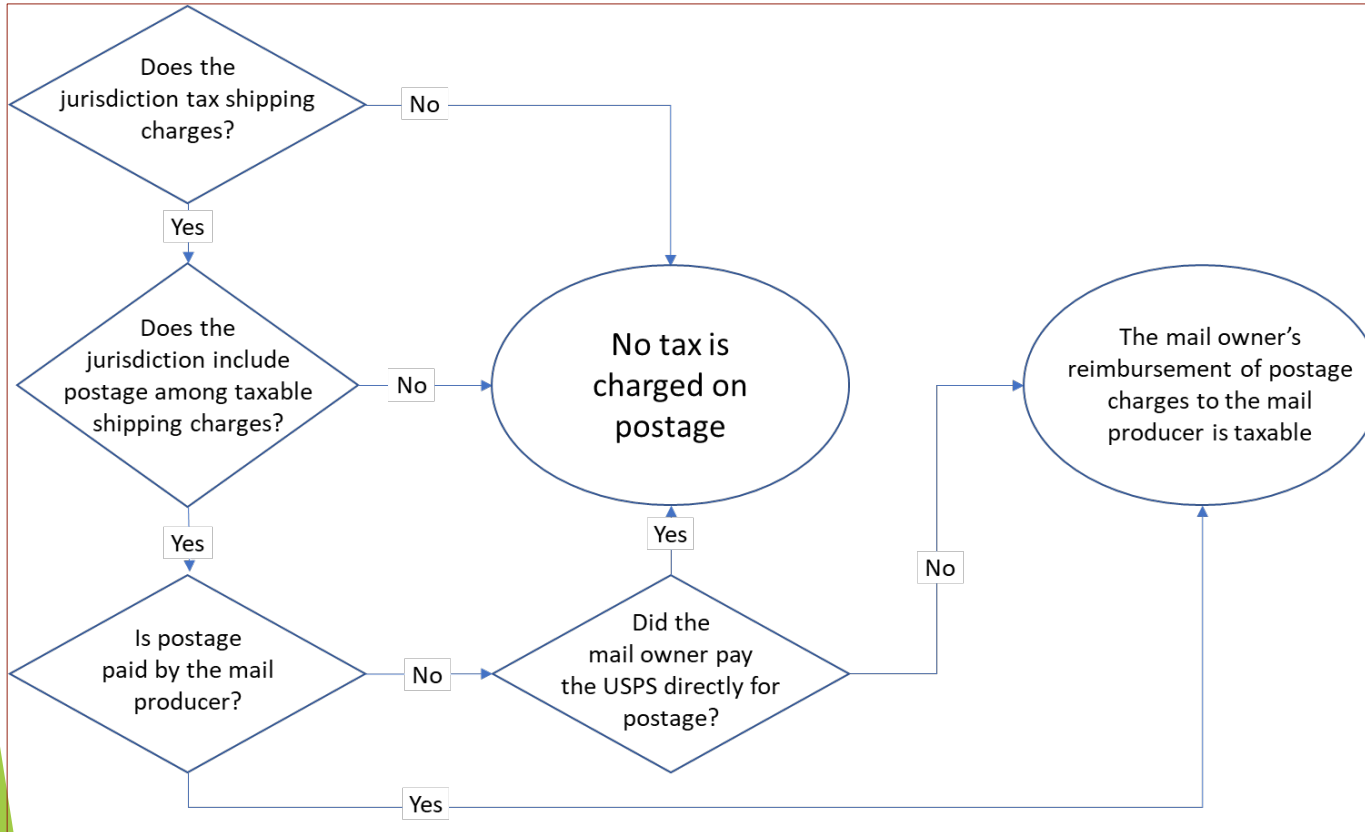
Taxability Of Other Cost Components

- ▶ Mailing Services:
 - ▶ Collating; sorting; metering; addressing.
 - ▶ Not taxable in several states if separately charged.
- ▶ Sale of Names from Mailing List.
 - ▶ Not taxable in most states because treated as a service and not the sale of tangible personal property. See, e.g. *Grolier Enterprises, Inc. v. Gruppo*, (Ct. Sup. Ct. 2/28/92).
 - ▶ DC: Taxable as sale of an information service. See <https://otr.cfo.dc.gov/page/taxable-and-non-taxable-services>.

Taxability Of Other Cost Components

- ▶ Shipping charges for bulk shipment:
 - ▶ Example: Loading one PO truck with materials from several customers going to the same geographic area/post office Distribution Center.
 - ▶ Should not be taxable because it is a service.
 - ▶ Taxability may vary if the product is promotional direct mail vs “other” direct mail
- ▶ Data Processing charges:
 - ▶ E.g. manipulating and managing data to optimize mailings.
 - ▶ Taxable in only a handful of states.

Taxability Of Postage



- ▶ Payments to the Post Office are not taxable
 - ▶ Payments to producer as agent for the customer should not be taxable
 - ▶ Customer deposits to producer's Computerized Meter Resetting System
- ▶ Resale of postage (i.e. Producer invoices for postage) are taxable, unless state exempts shipping and handling

Itemizing Charges On The Invoice

- ▶ Cardinal Principle: Separately price and invoice separate charges for different services/products.
- ▶ Separate pricing of products/services has limits:
 - ▶ If service is auxiliary or related to main product that is taxable then the auxiliary service may be deemed taxable.
 1. E.g. shipping and handling combined into a single charge.
 2. TX rule regarding related services (information services):
 - a. 34TAC3.330(e)(3) (Charges for services/expenses related to and incurred while providing the taxable service are taxable and may not be separated from taxable charges. Examples would be charges for meals, telephone calls.)
 - b. 34TAC3.330(e)(1) provides that a service is unrelated if it is commonly sold on a stand alone basis and is a distinct service from the information service.

So What Exemptions Are Out There?

▶ Three considerations for exemptions:

1. Is what you produce exempt in its own right?
2. Is your customer purchasing items with the intent to resell to its own clients?
3. Does your customer prefer to be responsible, on its own, for any sales or use tax that may be due on its purchase from you?

So What Exemptions Are Out There?

▶ Organization Based Exemptions

- ▶ 26 states provide broad based exemptions for all entities that qualify as non-profit organizations
- ▶ 14 states provide more limited exemptions for certain types of identified non-profit organizations
 - ▶ Religious organizations are often among those limited exemptions

▶ Product Based Exemptions

- ▶ Promotional direct mail is exempt in 12 states
 - ▶ CA, FL, IL, MI, MA*, MO, NY, OH, PA, WI, WY, VA
- ▶ In 11 of these 12 states, fundraising solicitations qualify as promotional direct mail and are eligible for the exemption
 - ▶ CA explicitly excludes fundraising and campaign materials from its printed sales messages exemption
- ▶ MA exemption is limited by page count (max 6 pages)

Product Based Exemptions

▶ Statutory exemptions:

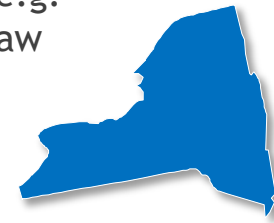
- ▶ California “printed sales messages” exemption (Cal. Rev. & Tax. Code § 6379.5; Cal. Code Regs. § 1541.5).
- ▶ Florida exemption for free advertising publications published regularly. (Fla. Stat. § 212.08(7)(ccc))
- ▶ Massachusetts “direct and cooperative direct mail promotional advertising materials” exemption for materials of 6pgs or less (Mass. Gen. L. ch. 64H, § 6(ff)).
- ▶ New York “promotional materials” exemption (NY Tax Law § 1115(n)(4)).
- ▶ Ohio exemption for direct marketing materials (Ohio Rev. Code Ann. § 5739.02(B)(35)(a)-(b))
- ▶ Pennsylvania exemption for direct mail advertising literature or materials distributed by USPS; producer must provide all services and materials on which printing provided. (72 Pa. Stat. Ann. § 7204(35), (50); 61 Pa. Code §32.36(b))
- ▶ Wisconsin exemption for advertising and promotional direct mail (Wis. Stat. Ann. §77.54(25), (25m), (59))

Product Based Exemptions

- ▶ Exemptions by court decision or administrative ruling for materials delivered from outside the state by U.S. Mail:
 - ▶ Illinois (see Ill. DOR Gen. Info. Letter ST 01-0003-GIL (Jan. 5, 2000)).
 - ▶ Missouri (see Office Depot, Inc. v. Dir. Of Revenue, Mo. Admin. 12-2190 (Apr. 30, 2015) (citing May Dep't Stores Co. v. Dir. Of Revenue (Mo. 1988)(en banc)).
 - ▶ Michigan (Sharper Image Corp. v. Dep't of Treasury, 550 N.W.2d 596 (Mich. App. 1996)).
 - ▶ Virginia (see Ruling of Virginia Tax Comm'r, P.D. 97-61 (Feb. 10. 1997)).

Example Of Specific State Law: New York Promotional Materials Exemption

- ▶ Three elements of exemption under NY Tax Law § 1115(n)(4).
 - ▶ Element 1: Printed promotional materials and promotional materials upon which services are performed.
 - ▶ Broad definition includes advertising material, related tangible personal property (e.g. free gifts, complimentary maps, applications, order forms and return envelopes), raw materials and envelopes used exclusively for delivering materials.
 - ▶ Exempt are all ancillary services, shipping, postage
 - ▶ Element 2: Shipment via mail/common carrier.
 - ▶ Does not include shipment by printer's trucks or by contract carrier. TSB-A-13(16)S; TB-ST-692 (2014)
 - ▶ Element 3: Without charge to the purchaser's customers.



Example Of Specific State Law: California Printed Sales Messages Exemption



- ▶ Three elements of exemption under California Tax Regulation 1541.5
 - ▶ Element 1: Printed to the special order of the purchaser
 - ▶ E.g., by special request, and includes additional or supplemental orders if the original print job was a special order
 - ▶ Element 2: Shipment via USPS or common carrier, or delivery by the seller.
 - ▶ Element 3: Without charge to the ultimate recipient
- ▶ “Printed sales message” means catalogs, letters, circulars, brochures, and pamphlets printed for the principal purpose of advertising or promoting goods or services
 - ▶ Explicitly excludes campaign literature, fund-raising materials, newspapers, or periodicals

Examples Of Specific State Laws: Florida

- ▶ Statute (Fla. Stat. §212.08(7)(w)) exempts:
 - ▶ Free;
 - ▶ Circulated publications;
 - ▶ Published on a regular basis;
 - ▶ Composed of primarily advertising; that are
 - ▶ Distributed through the mail, home delivery or newsstand.
- ▶ Department strictly construes the exemption, but honors it when all conditions are met. See FL DOR Tech. Assist. Adv. 18A-015 (Aug. 31, 2018).



How do you secure the exemptions: Action Plan

- ▶ Rules vary state by state
 - ▶ Identify the exemption certificates that are accepted in the states in which the printer/producer and the non-profit have nexus
- ▶ Institute an annual certificate renewal practice
 - ▶ Several states (notably FL and MI) limit the time period during which the certificate is valid

How do you secure the exemptions: Organization-Based Exemptions

- ▶ Rules vary state by state
 - ▶ State-issued exempt organization certificate
 - ▶ This may require the non-profit to register with state departments of revenue to be recognized as an exempt organization for state sales/use tax purposes
 - ▶ SSUTA multistate exemption certificate
 - ▶ IRS 501(c)(3) approval letter

How do you secure the exemptions: Product-Based Exemptions

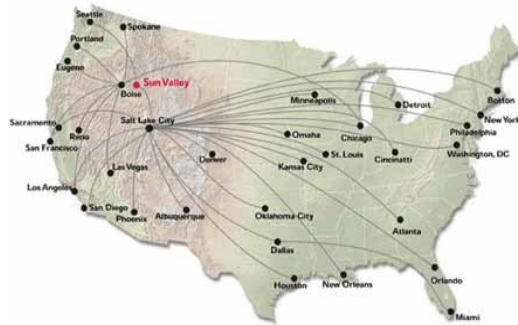
- ▶ Ensure you meet the criteria in each state
- ▶ Exemption Certificates are necessary in the following states that offer exemptions for promotional direct mail:
 - ▶ CA, FL, MI, MA, MO, NY, OH, PA, WI, WY, VA
 - ▶ IL does not require an exemption certificate, but we recommend a letter documenting
- ▶ Printers/Producers: Pre-populate the key areas of the exemption certificate:
 - ▶ Vendor name and address
 - ▶ Blanket v. Single Use Certificate
 - ▶ Select the Exemption for Direct Mail

Direct Pay Permits

- ▶ Under the SSUTA and the laws of some other states (e.g., TX), a seller is relieved of the obligation to collect tax where the purchaser provides a direct pay permit or a “direct mail certificate” indicating that the purchaser will report tax. See SSUTA, Section 313.A.2, B.2.
- ▶ Some states provide express exemptions from tax for direct mail materials delivered to locations outside the state. (Such exemptions do not mean that the destination state’s tax is inapplicable, however.).

Sourcing Sales

- ▶ The majority rule is “destination” sourcing, i.e., the sales/use tax is determined under the law of the jurisdiction where the tangible materials are ultimately delivered.
 - ▶ Ex - The SSUTA generally provides for “destination” sourcing (Sections 310, 313)



- ▶ To complicate matters, a “use” might occur in a state even when the sales transaction does not.
 - ▶ Ex - A non-profit engages a printer in Wisconsin to produce and send a campaign catalogue to a prospective donor in Massachusetts. The non-profit “uses” the catalogue in Massachusetts and, if nexus exists, may be subject to tax on the purchase price of that catalog
- ▶ Is this an opportunity to capitalize on exemptions such as the interstate exemption or the lack of nexus with the transaction.

Sourcing Issues

- ▶ The SSUTA permits “origin” sourcing, under which the sales/use tax is determined based on the point of sale, for intrastate sales (see SSUTA, Section 313.1), although this has been adopted so far by only two member states (UT, WA).
- ▶ In addition, several non-SSUTA states (e.g., AZ, CA, PA) have a general rule that calls for “origin” sourcing, however:
 - ▶ “Origin” sourcing rules may apply only to intrastate transactions/deliveries; and
 - ▶ In the case of interstate sales, including the delivery of direct mail to other states, general rules are typically superseded by express exemptions, rules, or enforcement practices that acknowledge underlying constitutional principles applicable to interstate commerce (and thus result in destination sourcing based on the “use” of direct mail in the state(s) where it is delivered).

Sourcing Issues: Taxability

- ▶ The structure of a direct mail transaction may create challenges in determining what state's law applies.
 - ▶ If a printer does not also arrange for mailing to end user recipients, but instead delivers in bulk to a purchaser or letter shop to complete the mailing, aspects of the tax treatment may change, such as exemptions, sourcing, and even tax on postage.
 - ▶ Privacy issues: Even if printer is responsible for mailing, how long does the printer maintain the files?
 - ▶ How does a printer measure its exposure to sales taxes?
 - ▶ How does a non-profit evaluate its exposure in states where it does not have nexus?
 - ▶ Will the states use a proxy for states of distribution?

Sourcing Issues: Taxability

- ▶ If a printer lacks sufficient information to allocate and source a sale of direct mail based on the delivery location(s), the printer may be required to collect sales tax under a default assumption, which in turn depends on the type of printed material at issue
 - ▶ Promotional/Advertising Direct Mail : The SSUTA requires the printer to source to the shipping location (where the materials are printed) (SSUTA, Section 310.A.5)
 - ▶ Transactional/Other Direct Mail: The SSUTA requires the printer to source to the address of the purchaser for “other” direct mail. (SSUTA, Section 313.A.4, B.1.)
 - ▶ SSUTA/SD/MN - Merely having access to a mailing list does not constitute having sufficient information to know the delivery destination
- ▶ Non-SSUTA states may vary, creating challenges for the printer.

Sourcing Issues: Double Taxation?

- ▶ SSUTA default rules create a risk of double taxation.
 - ▶ For promotional direct mail, where the printer lacks detailed destination information at the time of sale, the default rule is the location from which the materials were sent (SSUTA Section 313.A.4).
 - ▶ Non-SSUTA, destination sourcing states may seek tax on some portion.
 - ▶ SSUTA provides that member states may disallow credits if default applies.
 - ▶ Collection and remittance obligations in two or more jurisdictions.
 - ▶ For “other direct mail,” default rule is the purchaser’s business address (SSUTA Section 313.B.1).
 - ▶ Applies whenever purchaser fails to give a direct pay permit or direct mail certificate, even when purchaser provides shipping information.
 - ▶ If the printer has nexus in both the purchaser’s home state and one or more destination states to which mail is delivered, the printer could be subject to tax collection and remittance obligations in two or more jurisdictions.

Any questions?

Martin Eisenstein

meisenstein@brannlaw.com



Jamie Szal

jszal@brannlaw.com

