



We'll get you there.

Sales Tax Issues for the Manufacturing & Distribution Industries

June 2022

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Presenters

- Muthu Periakaruppan – Indirect Tax Leader
- Joe Solana – Principal, Telecom Industry
- Nick Sowden – State and Local Tax Consulting
- Matt Corley – State and Local Tax Consulting



At the end of this session, you will be able to:

- Recognize sales tax exemption opportunities within the M&D industry
- Identify the process to file sales tax refund claims and recovery
- Identify exemption certificate management requirements and opportunities to streamline
- Recognize utilities used in manufacturing exemption and how the exemption can be claimed





Sales Tax Exemptions

Muthu Periakaruppan and Nick Sowden

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Manufacturing Exemptions

- Generally: Manufacturers' Sales and Use Tax Exemption (M&E) provides a retail sales and use tax exemption for machinery and equipment used directly in a manufacturing operation or research and development operation.
- Most states have robust exemptions for Manufacturing Equipment, repair parts, consumables, and other supply items
- Most common exemptions available to M&D Industry
- Application of the exemption varies widely by State

Who Are Manufacturers?

- Most commonly a manufacturing process transforms TPP to create a new product
- Can also apply to other industries not commonly thought of as manufacturing, i.e. Technology and Construction & Restaurants
- Manufacturing (M&D) is an umbrella term:
 - Manufacturing Equipment
 - Replacement Parts
 - Consumables
 - **R&D**, Testing, Quality Control
 - Software
 - Utilities



Intricacies of the Manufacturing Exemption

- Each state provides its own definition
- Questions states ask:
 - What qualifies as Manufacturing?
 - Where does the manufacturing process begin and end?
 - Do repair parts qualify? How long do they have to last?
 - Do charges for repair labor qualify
- Taking advantage of every exemption becomes difficult
- Manufacturers most often overpay
- Exposure to underpayment may still exist in certain circumstances

Maryland Manufacturing Exemptions – Case Study

- No sales tax on purchase of tangible personal property used directly in the production process
 - Machinery and equipment
 - Repair parts
 - Items consumed in production activity, within one year of use
- Manufacturing includes
 - Quality Control
 - Employee safety
 - Repair of production equipment



California Manufacturing Exemption – Case Study

- Sales tax applies to purchases of tangible personal property used directly in the production process lasting longer than one year
 - Sales Tax charged at a reduced rate (full state and local tax rate less statutory amount – 3.975%)
 - Be primarily engaged in certain types of business, also known as being a "qualified person."
 - Purchase "qualified tangible personal property."
 - Use that qualified tangible personal property in a qualified manner.
- Repair parts qualify only if capitalized



How do we claim the exemption?

- Understand:
 - Your state and local laws – what is exempt and taxable
 - Where your manufacturing process begins and ends
- Provide:
 - Exemption Certificates
 - More out of state vendors will be charging tax due to *Wayfair*
- Review:
 - Invoices for Manufacturing Equipment – Fixed Assets
 - Invoices for Repair and Maintenance Vendors
 - Create a Vendor onboarding process



What can we do if we think we overpaid Sales Tax?

- Sales and Use Tax Reverse Audits
- **“It’s your money, we get it back!”**
- Identify & Recover Overpayment of Sales/Use Tax
 - What is sales tax vs. use tax
 - Applies to purchases/spend
 - Refund is recovered from the respective state
 - Refund filed directly with the state or through the vendor
- No risk upfront for clients (30% contingency fee)
- Why do companies overpay sales/use tax?
 - Not aware of exemption on items purchases
 - May be aware of the exemption but client does not review each invoice
 - CLA has identified a unique exempt position





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Where Do We Find Refunds

- Technology
 - Software development
 - **Includes R&D** and “production”
 - All hardware & software used to develop software can be considered manufacturing
- AG
 - **R&D**
 - Growing
 - Processing
- Construction
 - Mining
 - Self Manufactured materials
- Trucking, Airlines (T&L)



Process

- Initial 1-2 day feasibility analysis – Prefer to be on site
 - Fixed Asset Listing
 - Trial Balance
 - A/P Detail for selected accounts
 - Invoices (Paper, electronic or on-line)
- Compile refund claims with required support (on site or remote)
- Submit refund claims to respective state or by vendor
- Follow up with State
- Training for client team handling sales tax
 - Help claim the appropriate exemption going forward
 - Boutique firms don't do this
- CLA Model
 - Flexible (Across Industries), Efficient (leveraged), Scale able (\$1 million to \$170 billion)





Exemption Certificate Management

Joe Solana & Matt Corley

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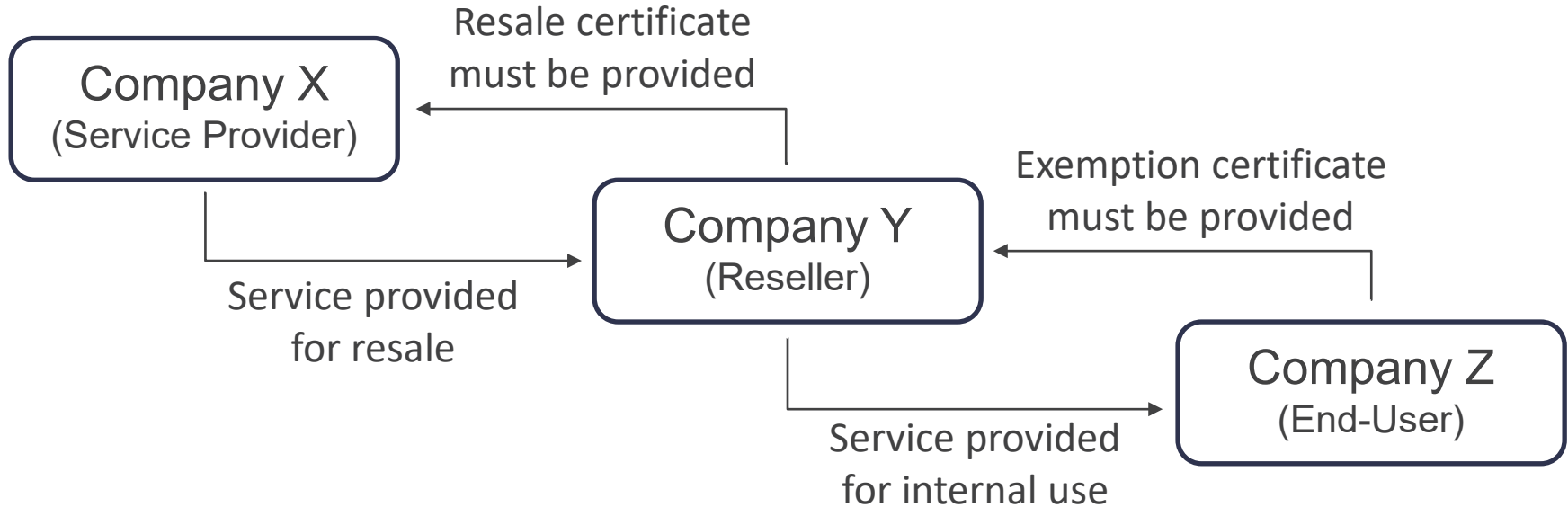
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You may ask yourself... How Does an Exemption Certificate apply to my Manufacturing Operation?

- An exemption is a lawful reduction of the amount of income that would otherwise be taxed.
- An Exemption Certificate is an official document that grants an individual or organization special permissions from paying taxes assessed on the services they provide.
- Exemptions can apply to any consumer in the chain of transactions, from the Service Provider all the way down to the End-User.



Chain of Responsibility Flow Chart for Providers



Customer Exemption Process

- Customer Exemptions (Sales Transactions) – *Full-Service Option*
 - Develop annual exemption campaign with you and your team
 - Customer Distribution List
 - Personalized emails to customers
 - Cadence of email communications with customers
 - Utilize 3rd party CERTifyTax software application to store customer forms under a separate client specific partition
 - CLA or client will send out all communications to customer (agreed upon during project scope)
 - CLA or the client interacts directly with the customer to address all questions, guidance, missing forms, etc. (agreed upon during project scope)
 - CLA provides good faith testing for all forms provided
 - All forms whether complete or incomplete are indexed and stored in CERTifyTax for audit trail
 - For redundancy, forms are also stored in the client's folder on the CLA network
 - Reporting is provided to client on an agreed upon cadence to provide visibility on progress
 - CLA provides client with the tax types to be shut off and/or exemption codes to be used by their billing ops team to apply to respective customer record
 - If CLA manages the billing instance for the client (SureTax) then CLA will update the customer record with the client's authorization
 - Provide clients with training of CERTifyTax self-generated reports for tax audit support purposes



Customer Exemption Process (continued)

- Customer Exemptions (Sales Transactions) – *Partial Option*
 - Client provides CLA with the customer exemption forms to review and ensure they meet good faith standard requirements
 - CLA provides a response back to the client and will also provide applicable tax types to be shut off if requested by client
 - All forms are stored within the client's folder on the CLA network



Common Exempt Customers

Business/Residential Customers

- Federal Government
- State Government
- Local Government
- Eligible Foreign Diplomats
- Indian Tribe Reservation
- **Reseller**
- Lifeline
- Senior Citizen

Non-Profit Customers

- Non-Profit Charitable
- Non-Profit Educational
- Non-Profit Hospital
- Non-Profit Mental Health Agency
- Non-Profit Religious Organization
- Non-Profit Residential Care Organization
- Non-Profit Social Service Agency
- Non-Profit Veterans Organization



What is the risk of not collecting and maintaining proper exemption certificates from your customers?

- What happens if you get audited?
- Who is held liable for the outstanding tax?
- Can you back date exemption certificates?

Claiming Exemptions – A How to Guide

1. Federal Communications Commission (FCC) / Universal Services Administrative Company (USAC) Registration
2. Secretary of State (SOS) Qualification
3. Department of Revenue (DOR) Registrations
4. Actively Remit to the required jurisdiction(s)
5. Provide Documentation to Service Provider(s)



What is the risk of not maintaining and providing the appropriate exemption certificates to your service provider?

- Do you pay taxes to both the state and your vendor?
- What if your certificate expires?
- How far back is your vendor willing to go back and issue credits?

Common Certificates and Forms

The applicability and use of each will vary based the jurisdiction and exemptible taxes.

- State issued certificates
- Official state issued forms
- Streamlined/Multi-Jurisdictional forms
- CLA drafted client specific exemption packages



Thanks for Attending!

Muthu Periakaruppan

Nick Sowden

Joe Solana

Matt Corley



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