



# K A N S A S

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## **NOTICE 03-04** **NEW "DESTINATION-BASED" SOURCING RULES FOR RETAILERS' SALES AND COMPENSATING USE TAX**

In 2003 House Bill 2005, the Kansas Legislature adopted legislation intended to bring Kansas sales and use tax laws into conformity with the Streamlined Sales and Use Tax Agreement (Agreement) requirements. This Agreement is a product of the Streamlined Sales Tax Project (SSTP), a cooperative effort among several States and the business community, which responds to the concerns of merchants about the difficulties in dealing with different States' sales tax laws, and to State and local government concerns about loss of revenues from remote retail sales by mail-order, telephone and the Internet. The SSTP seeks to "level the playing field" between in-state and out-of-state merchants regarding collection of sales and use tax on retail sales to customers in the taxing State. The SSTP's goal is to make administration of different States' sales and use tax laws more uniform, efficient, and less burdensome on retailers. The SSTP seeks to encourage multi-state merchants to voluntarily register to collect and remit use tax on sales to customers in States where they may not have any physical presence or legal obligation to collect and remit use tax. More information on the SSTP, as well as the text of the Agreement, are available at the following website: [www.streamlinedsalestax.org](http://www.streamlinedsalestax.org).

The Agreement contains certain uniformity provisions that States must adopt in order to be eligible to join. The Agreement takes effect once at least 10 States with at least 20% of the total population of States imposing sales tax have made the necessary statutory changes to meet the uniformity requirements. With the adoption of 2003 House Bill 2005, Kansas has amended its sales tax laws to conform to the uniformity requirements in the Agreement, and should be in a position to seek membership in the Agreement. These changes take effect on July 1, 2003.

The most significant changes to Kansas sales tax law required by the Agreement are the sourcing rules. They are found at Sections 1, and 15 through 19, of 2003 House Bill 2005. Beginning July 1, 2003, retailers must use these new "destination-based" sourcing rules to correctly identify the local sales tax to charge on a retail sales transaction. Under prior law, sales were generally sourced to the retailer's business location, for purposes of determining the local sales tax due. Thus, the local sales tax in effect at the retailer's business location applied to the transaction. This is an "origin-based" sourcing rule. Under the new "destination-based" sourcing rules, sales generally are sourced to the location where the purchaser receives the item sold. Retailers who ship or deliver sold items to their customers' locations will be required to collect the local sales tax in effect where delivery is made.

### **General Destination-Based Sourcing Rules**

2003 House Bill 2005 requires use of "destination-based" sourcing rules to determine the applicable local sales or use tax on a given sales transaction, subject to certain exceptions. These sourcing rules apply, regardless of whether the taxable item sold is characterized as tangible personal property or a service.

(1) Under the "destination-based" sourcing rules, the sale is "sourced" to the retailer's business location if the buyer receives the merchandise there.

(2) If the retailer delivers or ships the merchandise to the buyer (or the buyer's donee), the sale is "sourced" to location where the buyer (or donee) receives the merchandise, and the local sales tax applicable at the buyer's (or donee's) location applies and should be collected by the retailer. Note: The term "received" or "receipt," for purposes of the sourcing rules, means: (a) taking possession of tangible personal property; or (b) making first use of services. The terms "receive" and "receipt" do not include possession by a shipping company on behalf of the purchaser.

(3) If neither (1) nor (2) apply, then the sale is sourced to the location indicated by an address for the purchaser that is available from the business records of the seller maintained in the ordinary course of the seller's business.

(4) If neither (1), (2) nor (3) apply, then the sale is sourced to the address of the buyer obtained during consummation of the sale, and can include the address of the buyer's payment instrument (check, credit card or money order).

(5) If (1), (2), (3) or (4) do not apply, or the retailer has insufficient information to determine whether (1), (2), (3) or (4) should apply, then by default, the "origin-based" sourcing rule applies. The sale is sourced to the address from which the merchandise (tangible personal property) was shipped, computer software delivered electronically was first available for transmission by the seller, or from which the taxable service was provided.

**Examples:**

A Hays resident purchases a camera from a store in Salina and takes possession of the camera at the store. The retailer should collect the local sales tax applicable to the Salina store location.

A rural Lincoln County resident purchases a couch from a furniture store in Salina and requests that the furniture store deliver the couch to the buyer's address. The retailer should collect the local sales tax applicable to the buyer's address in rural Lincoln County.

**Gifts**

When the product is not received by the purchaser at the seller's location, if the purchaser has given the seller instructions to ship or deliver the product to a donee of the purchaser, then the sale is sourced to the donee's address furnished by the purchaser.

**Example:**

A Russell resident purchases a computer from a Wichita business as a gift for a student attending college in Hays, and requests that the business ship the computer to the student's address in Hays. The student is the purchaser's "donee," so the local sales tax applicable at the donee's address, Hays, applies.

**Receipt by Shipping Company on Behalf of Purchaser**

Receipt by a shipping company on behalf of a purchaser is not considered "received" for purposes of the sourcing rules.

**Example:**

A law firm in Hutchinson orders office supplies from an office supply company in Overland Park and requests that the office supply company deliver the order to Jones Shipping Company, which the law firm has requested to ship the order to the law firm's Hutchinson address. In this situation, receipt by Jones Shipping Company is not considered "receipt" by the purchaser, for purposes of applying the sourcing rules. Since rules (1) and (2) do not apply, in that the buyer did not receive the order at the seller's location and the seller did not ship or deliver the order to the buyer, rule (3) applies: the sale should be sourced to the address of the buyer shown on the seller's business records. If the seller's business records do not contain an address for the buyer, then rule (4) would apply, and the seller should source the sale to the address of the buyer shown on the buyer's payment instrument. If there is no address on the payment instrument for the buyer, then rule (5) would apply, and the sale would be sourced to the seller's location.

## Out-Of-State Sales

If the retailer sells merchandise that is to be shipped or delivered to the purchaser out-of-state, then the sale is considered to occur out-of-state, and no Kansas retailer's sales tax is due. The out-of-state purchaser may owe compensating use tax in the state where the purchaser is located.

### ***Example:***

A South Dakota resident places a telephone order for office supplies from an office supply business in Lawrence, Kansas requesting that the order be shipped to South Dakota. This is considered out-of-state sales and Kansas retailer's sales tax is not due. The South Dakota purchaser may owe compensating use tax to the state of South Dakota.

## Sourcing of Services

Effective July 1, 2003, the "destination-based" sourcing rules will apply to all retail sales of taxable services, as well as sales of tangible personal property. This means that the sale of a taxable service is sourced to the location where the purchaser of the services makes first use of those services. In many situations, this is the location where the taxable services are performed.

### ***Examples:***

A rural Jefferson County resident brings his car to a mechanic in Topeka for repairs. The car repairs are performed at the mechanic's shop in Topeka, and the consumer picks the car up at the shop location. The mechanic should collect state sales tax and the local sales tax in effect at Topeka on the repair charges. If the mechanic had performed the repairs at the consumer's residence, then the mechanic should collect state sales tax and the local sales tax in effect at the consumer's rural Jefferson County address.

The air conditioning system goes out in a law office and a repairman is called to fix the system. The repair charges are sourced to the law office location where the repairs are performed.

## Change to Sourcing Rules for Construction/Contractor Work

Before July 1, 2003, retail sales involving the furnishing of services taxable under subsections (p), (q) and (r) of K.S.A. 79-3603 (installing, repairing, servicing, altering or maintaining tangible personal property not being held for sale in the regular course of business; service or maintenance contracts on such property) pursuant to a contract were sourced to the location where the services were performed only if the contract price exceeded \$10,000 per contract. See K.S.A. 2002 Supp. 12-191. If the contract price were \$10,000 or less, the sale of taxable services was sourced to the contractor's place of business. Under the new sourcing rules that take effect on July 1, 2003, such services are sourced under the "destination based" rules, that is, the location where the services are received by the purchaser, i.e., the location where the purchaser makes first use of the services. This often will be the same location as where services are performed.

### ***Examples:***

A building contractor enters into a remodeling contract with the owner for a commercial building located in Olathe, Kansas for a contract price of \$100,000. The remodeling contract labor services are sourced to the commercial building location where those services are performed, and received by the buyer. The local sales tax in effect at the Olathe building address applies.

A Lawrence roofing contractor enters into a roof repair contract for \$5,000 with the owner of a commercial building located in Topeka, Kansas. The repair services are sourced to the commercial building address where the services are performed, and received by the buyer. The local sales tax in effect at the purchaser's Topeka building address applies.

## **Exceptions to General “Destination-Based” Sourcing Rules**

Certain items are excepted out of the “destination-based” sourcing rules. These are: sales of watercraft, modular homes, manufactured homes or mobile homes, and the sale of motor vehicles, trailers, semitrailers or aircraft that do not qualify as “transportation equipment” (defined below). These sales remain sourced to the retailer’s business location under the previously existing “origin-based” sourcing rule. For sales or leases and rentals of qualifying transportation equipment, the general “destination-based” sourcing rule applies.

### ***Example:***

A consumer residing in Junction City purchases a motor vehicle from a dealer in Manhattan. Because motor vehicle sales (other than “transportation equipment” defined below) are excepted from the new “destination-based” sourcing rules, the old sourcing rules applicable to motor vehicle sales prior to July 1, 2003 will continue in effect. The dealer will collect the state and local sales tax applicable to the dealer’s location in Manhattan (combined rate of 7.3%). Note: When the consumer registers the vehicle with the County Treasurer, the consumer will owe to the County Treasurer as local use tax the difference between the Manhattan local sales tax rate and the Junction City local sales tax rate (2.25% Junction City rate less 2% Manhattan rate equals .25%) on the purchase price.

### **• Transportation Equipment**

In general, “transportation equipment” includes railroad locomotives and railcars, trucks, buses and aircraft utilized for carriage of persons or property in interstate commerce. “Transportation equipment” is specifically defined, for purposes of the sourcing rules, to include any of the following:

(1) locomotives and railcars that are utilized for the carriage of persons or property in interstate commerce;

(2) trucks and truck-tractors with a Gross Vehicle Weight Rating (GVWR) of 10,001 pounds or greater, trailers, semi-trailers, or passenger buses that are: (a) registered through the International Registration Plan; and (b) operated under authority of a carrier authorized and certified by the U.S. Department of Transportation or another federal authority to engage in the carriage of persons or property in interstate commerce;

(3) aircraft operated by air carriers authorized and certificated by the U.S. Department of Transportation or another federal or a foreign authority to engage in the carriage of persons or property in interstate or foreign commerce;

(4) containers designed for use on and component parts attached or secured on any of the above items of transportation equipment.

The general “destination-based” sourcing rules apply to the retail sale, including the lease or rental, of qualifying transportation equipment.

Special sourcing rules exist for certain categories of sales.

### **• Leases or Rentals of Tangible Personal Property (except for motor vehicles, trailers, semi-trailers or aircraft that do not qualify as transportation equipment)**

For leases or rentals of tangible personal property (other than motor vehicles, trailers, semi-trailers, or aircraft that do not qualify as “transportation equipment”) in which periodic payments are made, the first lease payment is sourced under the general “destination-based” sourcing rules, as described above. The payments after the first payment are sourced to the primary property location. For leases with only one payment, the sale is sourced under the general “destination-based” rules.

### ***Examples:***

A consumer enters an equipment rental business and rents a lawn mower for a day, picking up the mower at the business and paying for the mower at that time. The rental is sourced to the business premises, and the local sales tax in effect at that location applies.

A consumer rents a tent for an outdoor party in the consumer’s back yard. The equipment rental business delivers the tent to the consumer. The rental is sourced to the consumer’s location, and the local sales tax in effect at that location applies.

A Cottonwood Falls resident enters into a one-year lease as lessee of computer equipment with rental payments due monthly. The lessor's business location is in Hutchinson. The consumer picks up the computer equipment from the lessor's business in Hutchinson. The computer equipment will be located at the consumer's residence in Cottonwood Falls during the term of the lease. Because the lessee first took possession of the computer equipment at the lessor's business premises, the first lease payment is sourced to that location, and the local sales tax in effect at Hutchinson will apply to that payment. However, subsequent lease payments will be sourced to the consumer's location, and local sales tax in effect in Cottonwood Falls will apply to those lease payments. Had the lessor shipped the computer equipment to the consumer's location, the first lease payment (as well as the subsequent lease payments) would have been sourced to the consumer's location in Cottonwood Falls.

- **Leases of Motor Vehicles, Trailers, Semi-trailers, or Aircraft Not Qualifying as "Transportation Equipment"**

For leases or rentals of motor vehicles, trailers, semi-trailers, or aircraft not considered "transportation equipment":

(a) when recurring periodic payments are involved, those payments are sourced to the primary property location, which is the address for the property provided by the lessee that is available to the lessor from the lessor's business records. This should be the registered address for the vehicle. Intermittent use of the property at different locations will not alter the primary property location.

(b) when recurring periodic payments are not involved, the lease or rental payment is sourced in accordance with general "destination-based" sourcing rules.

***Examples:***

An Emporia resident, the lessee, leases a new car from a car dealer located in Wichita, the lessor, for a term of 3 years, with monthly lease payments due. The lease payments are sourced to the "primary property location," which is the address that the lessee furnishes to the lessor as the location of the vehicle. This should be same as the location where the vehicle is registered, the consumer's Emporia address. The local sales tax in effect at the "primary property location" of the leased vehicle, Emporia, applies to each of the lease payments. The lessor should collect and remit the state and local sales tax in effect at Emporia on the lease payments. During the term of the lease, if the lessee of the vehicle moves to another location and registers the vehicle at that new location, the lease payments due after the move will be sourced to the new location, for purposes of calculating the applicable local sales taxes on the lease payments.

A Council Grove resident rents a trailer from a rental business in Manhattan and takes possession of the trailer at the rental business location in Manhattan. The rental period is 45 days, for a lump sum rental payment of \$250. The rental business should collect state sales tax at the 5.3% rate and local sales tax at the rate in effect for the Manhattan address of the business on the rental proceeds of \$250. If the rental business delivered the trailer to the consumer's Council Grove address, the rental business should collect the state sales tax, and the local sales tax in effect at Council Grove, instead of the local sales tax in effect in Manhattan.

- **Multiple Points of Use Certificate**

When a business purchasing computer software that will be delivered electronically knows that the computer software will be concurrently available for use in more than one taxing jurisdiction, the purchaser must give to the seller a multiple points of use (MPU) exemption certificate disclosing this fact. Once the seller receives the MPU exemption certificate from the purchaser, the seller is relieved of the obligation to collect or remit sales or use tax, and the purchaser assumes that obligation on a direct pay basis. The purchaser using an MPU exemption certificate may use any reasonable, consistent and uniform method for apportioning the local sales or use tax among the taxing jurisdictions where the computer software can be concurrently used.

***Example:***

An accounting firm with its headquarters located in Lawrence also has branch offices in Topeka and Olathe. The accounting firm purchases prewritten computer software from a software vendor located in Salina for \$5,000, and the prewritten computer software is delivered electronically to all of the offices of the accounting firm. The books and records of the accounting firm reasonably support an apportionment of the local sales tax

on the purchase of the prewritten computer software among the locations where the prewritten computer software is being used as follows: ½ to Lawrence, ¼ to Olathe and ¼ to Topeka. The accounting firm gives the software vendor an MPU exemption certificate. The accounting firm then assumes the obligation to report and remit state and local sales tax on this transaction to the department as follows: state sales tax at the rate of 5.3% on the \$5,000 total purchase price, plus the local sales tax applicable at the Lawrence location on ½ of the purchase price (\$2,500), plus the local sales tax applicable to the Topeka location on ¼ of the purchase price (\$1,250), plus the local sales tax applicable to the Olathe location on ¼ of the purchase price (\$1,250).

- **Direct Mail Sourcing Rules**

For a direct mailing to addresses in several locations, the purchaser of the mailing must give to the printer the information showing the multiple jurisdictions to which the mailing is to be delivered, or a “direct mail form.” If the printer receives the delivery information from the purchaser, then the printer shall bill and collect the tax from the purchaser according to the delivery information provided by the purchaser. If the printer receives a “direct mail form” from the purchaser, then the printer is relieved of the obligation to collect sales or use tax, and the purchaser assumes the obligation to directly remit the state and local sales tax applicable in the appropriate taxing jurisdictions, based on the mailing addresses for the flyers. If the purchaser of the mailing does not have a direct pay permit and does not provide the printer a direct mail form or the delivery information, then the printer should collect from the purchaser on the price of the direct mailing the state and local sales tax in effect at the address from which the mailing was shipped.

***Example:***

A business located in Hays, Kansas purchases a direct mailing of advertising flyers from a printer located in Hutchinson, Kansas. The flyers are to be mailed from Hutchinson to the business’s customers located at various addresses in Kansas and surrounding states. The business provides the mailing addresses of its customers to the printer. The printer should bill the purchasing business for local sales taxes (in addition to the state sales tax) applicable to the mailing, based on the addresses to which the flyers were mailed. If 500 flyers were mailed to Great Bend, the local sales tax would be due on the price of those 500 flyers at the rate in effect at Great Bend. If 200 more flyers were mailed to Larned, the local sales tax would be due on the price of those 200 flyers at the rate in effect at Larned.

Same situation as above, except the purchasing business gives the printer a “direct mail form,” indicating that the purchaser will assume the obligation to pay and remit the applicable tax on a direct pay basis. Having received a direct mail form from the purchaser, the printer is then relieved of the obligation to collect and remit sales tax on the direct mailing. The purchaser is then obligated to remit directly the state and local sales tax applicable to the mailing, based on the addresses to which the mailing was delivered.

Same situation as above, except the purchasing business fails to provide to the printer a direct mail form, the information showing the jurisdictions to which the direct mail is delivered, or a direct pay permit. In that situation, the printer must bill the purchaser for state and local sales tax at the rate applicable to the location from which the flyers were shipped, Hutchinson, Kansas.

- **Telecommunications Sourcing Rules**

Telecommunications service has its own sourcing rules. Telecommunications sourcing is the same as under current Kansas law. This means that telecommunications sales are generally sourced to the customer’s billing address. These rules are consistent with the federal Mobile Telecommunications Sourcing Act, adopted in Kansas last year.