
NOTICE 07-03
Sales and Use Taxation of Third-Party Drop Shipment
Office of Policy & Research --- June 13, 2007

2007 House Bill 2171 amends Kansas law to allow a drop shipper to honor a resale exemption certificate from an out-of-state seller that is not registered as a retailer with the department. This changes how Kansas sales and use taxes apply to certain drop shipments on and after July 1, 2007.

For purposes here, a drop shipment is a sale in which a seller accepts an order for merchandise, places the order with a third party such as a manufacturer or wholesaler, and directs the third party to ship the merchandise to a Kansas address. The third-party manufacturer or wholesaler is the "drop shipper." Some sellers and drop shippers that are located outside Kansas are registered to collect Kansas retailers' sales or use tax, while others are not.

(a) Drop shipment scenarios whose tax treatment is unchanged. When a seller is a registered Kansas retailer, it is required to charge and collect Kansas tax on the taxable sale of merchandise that it directs to be drop shipped to a Kansas address. The "ship to address" determines which local tax to charge in addition to state tax. This destination-based sourcing requirement applies even when the seller accepts an order from a customer that is located outside Kansas. If the sale is exempt, the seller should secure a Kansas exemption certificate from its customer. The seller should always have a resale exemption certificate containing its Kansas registration number on file with the drop shipper, regardless of whether the sale is taxable or exempt.

A seller that is not registered as a Kansas retailer should not bill Kansas or any other state's sales or use tax on merchandise that it has drop shipped to a Kansas address. Whenever tax is not billed on a taxable drop shipment, the consumer is required to self report and remit Kansas consumers' use tax on the purchase price of the merchandise, which includes any shipping charges that are billed as part of the sale. If the consumer is a contractor, professional, retail store, or other entity located in Kansas either temporarily or permanently, this is done by registering with the department for Kansas consumers' use tax purposes and self reporting consumers' use tax on these types of taxable transactions. Individual Kansans may self report the consumers' use tax that they owe on their individual income tax return. (*See Line 18 of the K-40, Kansas Individual Income Tax Return.*)

(b) Drop shipment scenarios whose tax treatment is changed by HB 2171. Beginning July 1, 2007, a drop shipper that is a registered Kansas retailer may honor a resale exemption certificate from an out-of-state seller that is not registered with the department as a Kansas retailer. A drop shipper may honor a seller's resale exemption certificate from the seller's home state or a multi-jurisdictional exemption certificate, such as the Kansas Form ST-28M or the MTC's Uniform Sales & Use Tax Certificate-Multijurisdiction. There is no longer a requirement that a seller's multi-jurisdictional exemption certificate contain a Kansas registration number. As with any untaxed purchase, the Kansas consumer is required to self report and remit Kansas consumers' use tax on the purchase price unless the purchase is otherwise exempt. In the unlikely event that the seller cannot provide a resale exemption certificate because it is not registered as a retailer in any state, a drop shipper that is a registered with Kansas is required to charge Kansas tax to the seller for the merchandise being drop shipped to Kansas.

HB 2171 repeals the prior law that made a drop shipper that was registered with Kansas a "deemed retailer" that was responsible for charging Kansas retailers' sales or use tax on the estimated retail selling price of the merchandise being drop shipping if the seller did not hold a Kansas retailers' registration number and the sale was not otherwise exempt. This notice takes effect on July 1, 2007 and revokes and supersedes all previous department of revenue notices, revenue rulings, private letter rulings, and other advice regarding drop shipments.