REGULATORY & TAX

Sales & Use Tax: Definitions May Vary By Jurisdiction

By Diane L. Yetter

Since each state—and in some cases, locality—administers its own tax, definitions may differ by jurisdiction. It is imperative to review the particular jurisdiction’s definitions and exemptions as they relate to your business. An incorrect interpretation may result in liability to your business.

Sales Tax is defined as a tax on the sale, transfer, or exchange of a taxable item or service. The Sales Tax generally applies on the sale to the end user or ultimate consumer. The Sales Tax is generally added to the sales price and is charged to the purchaser. Sales Tax in its truest definition applies only to intrastate sales where the seller and the customer are located in the same state. Sales Taxes are considered “trust taxes” where the seller collects the tax from the customer and remits the collected tax to the appropriate taxing jurisdiction.

There are different types of sales taxes imposed by the states. Some states are Seller Privilege Tax states while others are Consumer Tax states. This determines who is primarily liable for the payment of the tax. In Seller Privilege Tax states, the seller is primarily liable for the tax. The seller must pay the tax whether or not the tax is collected from the purchaser. The tax is generally imposed on the privilege of doing business in the state. Since the tax is not required to be passed on to the purchaser, it is not required to be separately stated on the invoice. However, most sellers do show the tax on the invoice. Under audit, the state can only collect the tax from the seller. California and Arizona are two of the Seller Privilege Tax states.

In Consumer Tax states, the tax is imposed on the buyer with responsibility for collection by the seller. The seller is still required to remit the tax even if it is not collected from the buyer, but it is usually easier to recover the tax from the buyer. The tax is generally imposed on the privilege of using or consuming the products or services purchased. Under audit, the state can collect the tax from either the seller or the purchaser. New York and Ohio are two of the Consumer Tax states.

Gross Receipts Taxes are a type of sales tax. The tax is a percentage of the total dollar amount of the transaction. This includes gross receipts from sideline operations such as occasional sales or sales outside the regular course of business. As a general rule, there are very few deductions allowed under a gross receipts tax structure. In most gross receipts tax states, many services are subject to tax that are not taxed in states that impose a sales tax. Hawaii and New Mexico are two of the Gross Receipts Tax states.

Complementary to the sales tax is the use tax. Use tax is defined as a tax on the storage, use, or consumption of a taxable item or service on which no sales tax has been paid. The use tax does not apply if the sales tax was charged. The use tax applies to purchases made outside the taxing jurisdiction but used within the state. The use tax also applies to items purchased exempt from tax which are subsequently used in a taxable manner. There are two types of use taxes—Consumer Use Tax and Vendor/Retailer Use Tax.

Consumer Use Tax is a tax on the purchaser and is self-assessed by the purchaser on
taxable items purchased where the vendor did not collect either a sales or vendor use tax. The purchaser remits this tax directly to the taxing jurisdiction. This is what most people think of when they talk about “use tax”.

Vendor or Retailer Use Tax applies to sales made by a vendor to a customer located outside the vendor’s state or sales in interstate commerce if the vendor is registered in the state of delivery. Many people also consider this sales tax. However, it is important to make the distinction as differences can exist between the sales tax and the retailer use tax in relation to who has the liability for the tax, the sourcing of the tax and the tax rate. For example, in Illinois the sales tax is an origin tax and can include local taxes. However, the use tax is sourced to the customer delivery location and there is no local use tax that is required to be collected by the seller. Only in the city of Chicago is there a local use tax.

A sale is defined as any transfer of title or possession, exchange or barter, conditional or otherwise, in any manner by any means whatsoever of tangible personal property for consideration. The imposition of tax is determined upon the passage of ultimate ownership or title or possession of tangible personal property or a taxable service. A transfer of title is an indication that ownership has been transferred. A transfer of title does not require that possession has also occurred. Thus, a sale has occurred when the “right to use” the property has changed hands. An actual change in possession need not occur. A transfer of possession is a transfer of control over a piece of property. A transfer of possession, temporary or permanent, may result in a sale. A lease involves a transfer of possession but not of title. Most states include both transfers of title and possession in its definition of sale. Illinois does not. Illinois only includes transfer of title in its definition. Therefore, true leases are not subject to Illinois sales or use tax.

Barter transactions are included in the definition of sale. Therefore, it is important to determine if a non-cash transaction has a sales tax implication. If either side of the barter transaction would be taxable if it had been a cash transaction, a value of
the item must be determined. Generally, the person obtaining the taxable item owes consumer’s use tax on the taxable value. Before the item is deemed taxable, all possible exemptions should be evaluated, including occasional sale.

Use is defined as the storage, use or consumption of taxable property or services and includes the exercise of any right or power incident to the ownership of the property. Louisiana defines use as “the exercise of any right or power over such property incident to ownership, including distribution.” Nebraska defines use as “the exercise of any right or power over tangible personal property incident to the ownership or possession of that tangible personal property.”

Some states do not include storage in their definition of use. This generally will exclude from taxation property temporarily stored within the jurisdiction for shipment and use in another state. This is commonly referred to as “temporary storage exclusion.”

Use includes the conversion of property purchased exempt from sales tax that is used in a taxable manner. This includes samples, donations and converted inventory. Most states impose the tax on the cost of property. Therefore, for items removed

### ACCOUNTS PAYABLE MANAGER’S CASE STUDIES

#### TOP BRASS TAKES A SHINE TO AP

**Challenge:** The top management at a mid-sized wholesale and retail firm had little awareness or appreciation of the impact its AP department had on the company’s bottom line.

**Action:** The AP Manager set out to change that perception. She began by tracking statistics on invoice discounts taken as a percentage of those available. She also looked for opportunities to expand available discounts and was able to recommend opportunities that resulted in five new discount agreements. Finally, she tracked the number of invoices processed in the department and was able to demonstrate there had been an increased workload in the department without a corresponding increase in headcount.

**Result:** By showing these statistics to senior management, the AP manager was able to make them aware of the contributions being made by her department and staff.

#### OH, WHAT A RELIEF WORKFLOW IS!

**Challenge:** Struggling with a slow-moving invoice process, the AP manager of a research firm wanted to initiate a scanning and workflow system to accelerate invoice processing time and eliminate the time and cost of shipping documents to a centralized processing center.

**Action:** The firm, after reviewing a number of software providers, implemented Kofax imaging and workflow solutions for accounts payable that automated the processing of approximately 300,000 invoices and other accounts payable-related documents it received annually.

**Results:** Now, invoice images and data are routed to an Oracle repository for easy access. By capturing and transforming the paper invoices into digitized information as the invoices enter an enterprise, the company has streamlined the entire accounts payable process from end-to-end. They quickly realized an ROI through reduced errors, faster processing times, and improved cash management.

The overall solution improved data accuracy, accelerated the processing of multilingual invoices, and significantly reduced the cost of manual tasks. The new system provides scan-to-archive capabilities by scanning documents and creating digital images. It extracts data for retrieval purposes, and delivers the images and associated data to a variety of repositories and applications. This has significantly reduced retrieval costs while improving regulatory and compliance efforts.
from inventory that are self manufactured, the material cost is generally the basis subject to tax.

Some states define the tax basis on these items as manufactured costs, and a few states impose tax on the retail selling price. Before assuming the tax is due, verify that no other exemption would apply.

Editor’s Note: Diane L. Yetter CPA, MST, is president of YETTER™ (www.yettertax.com), a sales tax services firm. Yetter is a strategist, advisor, speaker, author, and expert witness in the field of sales and use tax. She is also a member of IOFM’s Editorial Advisory Board.

Special Invoices
CONTINUED FROM PAGE 1

“Sometimes pay alone status is determined by the nature of the payments. For example, many companies choose to pay utility bills individually to avoid application errors that could result in cut-off notices,” says Miller.

Work to Minimize Pay Alone Invoices

These types of invoices generate additional work for AP. And since AP is often charged with “doing more with less,” improving processes even incrementally can help meet that goal. While there is not one single solution, there are a number of techniques that Miller offers to ease the burden:

Or perhaps a vendor will request pay alone status. If the vendor is paid infrequently, the request is not likely to cause too much difficulty. But if the vendor is paid frequently, the amount of time and effort devoted to accommodating the request can be significant.

Other times, the pay alone request is the result of remittance issues—the vendor wants to establish a one-to-one relationship between invoice and payment to ease the cash application side. “The pay alone status may be requested simply because there is a lack of understanding about what pay alone entails,” says Miller.

Congratulations to the AP Professionals Who Have Achieved Certification in the IOMA/TAPN Accounts Payable Certification Program in June.

In June, the following AP professionals took the IOMA/TAPN one-day certification program and exam and earned an Accredited Payables Specialist (APS) certification (for key AP staff), or an Accredited Payables Manager (APM) certification (for AP department heads). Congratulations to the graduates!

Advance Auto Parts
Joseph Priore, APM

Autoliv
Angela Kennedy, APS
Michele Owens, APS

Cancer Treatment Centers of America
Arlene Corpus, APM

Cardinal Health
Tammy Martinez, APM
Beth Murillo, APM
Kathy Sardano, APM
Edwina Zamora, APM

Cardinal Health Fss West
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For more information on the certification program, please contact Andrew Fitzpatrick at 203-889-4977, e-mail andrew.fitzpatrick@iofmonline.org, or view our online video at www.iofm.com/certification/accounts-payable.