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Home > Sales Tax Information > Sales Tax Questions > Sales Tax Exemptions

Sales Tax Exemptions

Issues and Documentation

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If you are making sales of taxable property, you are required to register to collect sales tax in any **state** in which you maintain a substantial physical presence. If you then make a sale in a **state** where you have registered, you are required to collect sales tax on any order delivered to that **state** unless a valid exemption is applied - applicable to the purchasing entity or the nature of item sold.

- [Common Types of Exemptions:](#)
- [Exemptions for Resellers:](#)
- [Exemptions for Drop Shipments:](#)
- [Exemptions For Manufacturers \(or Purchasers of Raw Materials\):](#)
- [Proving an Exemption - The Purchaser's Responsibility:](#)
- [Exemption Documentation Requirements:](#)
- [Exemption Expiration Dates:](#)
- [What is the difference between a Resale Certificate and Tax Exempt Certificate?](#)
- [Sales Tax Exemptions Assistance and Other Resources:](#)

Common Types of Exemptions:

Type of Good: Necessity goods including foods, medicines and clothing are often exempt from sales tax (or sometimes taxed at a lower rate). In addition, items such as services, real property, and intangibles such as digital goods may be statutorily exempt. These types of exemptions do not require any form of exemption documentation.

Type of Use for Goods Sold: If goods purchased are to be resold in the same form in which they are purchased they may qualify for a resale exemption. Alternately, if goods are processed (or incorporated into other goods) prior to resale, they too can be exempt from sales tax. Additional use exemptions are often available in certain industries including agriculture, manufacturing or industrial processing.

Type of Purchaser: Goods that are sold to the federal government cannot be taxed. Similar exemptions are also often available to **state** and local governments and agencies - as well as non-profit organizations or other recognized charitable, religious or educational groups.

[Back to top](#)

Exemptions for Resellers:

The most common exemption is a resale exemption. Goods purchased to be resold in the same form in which they are purchased qualify for a resale exemption (which removes the requirement to pay sales tax) assuming that the reseller is licensed and can provide a resale certificate (for the ship-to **state**). When that reseller later sells the goods, they are required to collect sales tax on the full selling price of the product. Once a seller has registered to collect sales tax, and has received a sales tax registration number, that number can be used to complete a resale certificate which can then be provided to suppliers. **States** that allow for resale exemptions either accept a **state** issued resale certificate or, in some cases, a multi-**state** certificate. Multi-**State** Sales Tax Exemption Certificates can be accessed at [MTC](#). Many **states** also allow "blanket" resale certificates for wholesalers who deal largely in resale transactions, often to regular clients who may make numerous and/or repeat purchases throughout the year. Basically a blanket certificate is a document kept on file which applies to multiple purchases from a single customer. Resellers must however be aware that there are certain limitations associated with the use of resale certificates:

- A business which is registered for sales and use tax can use a resale certificate only when the merchandise being purchased is to be resold by the business.
- A business cannot use a resale certificate to purchase merchandise if that merchandise is used or consumed by the purchaser in any manner without being resold. If you purchase items for resale (and the supplier did not charge you sales tax), and then later consume those items or use in providing a service, as the end consumer you owe tax on that purchase. In this situation, the tax would be submitted as use tax.
- A resale certificate may not be signed by a purchaser who does not know at the time of purchase whether the item will be resold or used for some other purpose.

[Back to top](#)

Exemptions for Drop Shipments:

Generally, if a seller has nexus in a **state** and has registered to collect sales tax, they are required to collect sales tax on all taxable sales delivered into that **state**. Drop ship transactions (see also [Drop Ship](#) section) differ somewhat in that the purchase by the retailer (from the product supplier/shipper) is in effect a purchase for resale - which is normally exempt from sales tax. However, drop ship taxation often becomes more complicated, as often the retailer is not registered in the ship-to **state** but the supplier/shipper is. In such cases, the supplier/shipper is obligated to collect tax from the retailer on the drop ship transaction unless the retailer can provide valid exemption documentation that is deemed acceptable by the ship-to **state**. (See [Drop Shipment](#) section for additional details.)

[Back to top](#)

Exemptions For Manufacturers (or Purchasers of Raw Materials):

If you purchase materials for incorporation into an end product (or other processing) prior to resale, you may be viewed as a manufacturer or processor rather than a reseller - and qualify for exemptions as such. In some **states**, machinery and equipment used in the manufacturing process is also exempt from tax. In this case, the manufacturer would issue an exemption certificate to their suppliers when they purchase qualifying items claiming the manufacturing exemption. For exemption certificates, forms, rules and procedures vary by **state** and within a **state** by the type of exemption. It is very important to review and evaluate the rules that apply for the type of exemption being claimed to be sure the appropriate documentation is used.

[Back to top](#)

Proving an Exemption - The Purchaser's Responsibility:

In order to qualify for a tax exemption, it is the purchaser's responsibility to adequately prove that they meet the exemption requirements for that purchase - generally in the form of an exemption certificate which meets that **state's** requirements. The retailer must retain (and file) a copy of the purchaser's exemption documentation to substantiate the exemption as without the documentation, the sale is deemed taxable.

[Back to top](#)

Exemption Documentation Requirements:

Generally, assuming that the purchaser has provided acceptable documentation, the seller is relieved of their legal obligation to collect sales tax on the transaction - assuming that the documentation is accepted in good faith and with the belief that the purchaser is entitled to the exemption. However, it is important to note that **states** having differing requirements regarding exemption documentation. Some **states** provide specific forms while others may simply require that certain information be included in the submitted exemption document. Regardless of the **state** and its particular requirements, it is recommended that the retailer always ensure that the following information is included in the exemption documentation:

- the type of exemption being claimed
- the names and addresses of both the purchaser and seller involved in the transaction
- a description of the goods being purchased
- the purchaser's tax registration number or business license (as appropriate)
- a **statement** that if the purchaser uses the items in a taxable manner that they will be responsible for the use tax
- a signature of the purchaser (or their agent or employee) and the date signed

Some **states** also offer on-line services to enable sellers to validate resale permits and/or exemption numbers - in order to ensure that they are dealing with registered vendors. At this time there are only a few **states** which require online validation and will assess liability if the seller has not performed the validation. In terms of a best practice, for the **states** that do require the validation, this should be performed. In other **states**, in addition to ensuring that all suggested data is captured (per list above) the format of the number, the type of exemption claimed and the form completed should be validated to ensure the seller is protected in case of audit.

[Back to top](#)

Exemption Expiration Dates:

In terms of expiration dates they can vary between the types of certificates. It is more common for expiration dates on exempt organization exemption certificates but between all the **states**, there are many different rules. Therefore, a best practice is to update all your exemption certificates every three to five years.

[Back to top](#)

What is the difference between a Resale Certificate and Tax Exempt Certificate?

The difference between a resale certificate and tax exempt certificate is the reason for the exemption. Companies that qualify for a resale certificate are eligible to purchase items that they buy either as ingredient or component parts of what they are selling or items that they resell in their purchased condition. For example, a department store can issue a resale certificate to a clothing manufacturer for sweaters that they purchase and plan to resell. A manufacturer of bread can purchase flour for resale as they are incorporating flour into the bread that they will resell to a store to sell. A resale certificate cannot be used to purchase other types of items exempt from sales tax that don't qualify for this purpose. An exemption certificate is issued either because the entity qualifies for an exemption or the use of the item qualifies for an exemption. For example, in many **states**, hospitals are considered exempt organizations. If an exemption

exists for these types of organizations in a given **state**, they are issued an exemption status and will need to issue an exemption certificate to their suppliers to exempt the sales tax.

[Back to top](#)

Sales Tax Exemptions Assistance and Other Resources:

If you require assistance regarding sales tax issues, **YETTER** is available to provide a broad range of services. Please call [Diane Yetter](#) at 312-701-1800 to discuss your requirements. The Sales Tax Institute also offers classes which review sales tax basics - through to advanced issues and best practices.

See the [CURRENT list of all Sales Tax Institute Online Courses & Webinars - Including Puerto Rico VAT Reform](#).

Are you a multi-**state** company with a SALES TAX EXEMPTION question that we have not yet covered here - or in our Sales Tax Archives (below)? If so - [Submit it here](#).

[Back to top](#)

Sales Tax Questions - Sales Tax Exemptions

Filter by topic or industry using the dropdown menus, or use the search field to filter by search term.

Topic Industry [reset](#) Search

Question/Topic	Date
If we have no nexus in state must we request resale or exemption certificate from our customer?	2015-04-29
What is correct process for sales tax registration, collection and exemption certificates?	2015-04-29
What are the requirements for a "digital signature" on a tax exempt form to purchase product online?	2015-01-05
If developing a sales and use tax exemption certificate program, what is estimate of average cost/account and time/account to obtain and file documents?	2013-11-05
When selling services to companies and organizations that are (or claim) to be non-profits are we required to charge sales tax?	2013-06-10
Can we use our IL exemption Tax ID number in the state of RI for Drop shipments? We are not registered and do not have nexus in RI.	2012-04-18
I'd like to purchase items for resale in my store, but vendor will not accept resale certificate. Is that legal? If I am charged sales tax on resale items, can I deduct from taxes?	2012-03-04
We are a manufacturer and deal in agricultural, fuel and retail products. Agriculture and fuel items are exempt from sales tax, but does that extend to transportation equipment?	2012-02-19
We are verifying seller permits and/or exemption numbers to ensure that we are dealing with registered vendors. If states offer online validation, is that a good practice?	2012-02-03
We sell computer hardware and software to schools. Are we required to charge sales tax when a school purchases something?	2012-02-02
Does the GA Department of Revenue send out resale certificates showing the expiration date?	2012-02-01
We are based in NC and perform work in several other states. All work is on federal projects - none are private. Do we have a responsibility regarding sales tax?	2012-01-13
Does a plumber pay sales tax on labor? My mom's beauty shop pays no sales tax on her labor. Is my situation the same?	2011-12-22
What resale certificate does a contractor use for the resale of materials and service?	2011-12-19
We sell t-shirts and screen printing. One customer uses them for promotion and sells some of them. He says promotional companies are tax exempt. Is that true?	2011-12-14
What is the difference between a Resale Certificate and Tax Exempt Certificate? (We are establishing a procedure for tax exemption certificate management.)	2011-10-18
I have an e-commerce website and suppliers are asking for Multi-State Sales Tax exemption forms. Do I need to obtain a Sales Tax Number or Certificate of Authority from each state?	2011-08-26
I am based in MA and sell to other states. I have a new NJ client. The P.O. and billing come from NJ but they want delivery to MA. Is order subject to MA tax?	2011-02-04
We are a not for profit organization. We plan to print our magazine in MA because the editor lives there and would like to have a sales tax certificate of exemption. How do we go about it?	2010-11-04
NH based bakery delivers product to ME and MA customers, both retail and wholesale. Are we required to collect sales tax for deliveries in those states?	2010-09-06

[Return to Sales Tax Question Home](#) — or [Back to top of Sales Tax Exemptions page](#)

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