

Drop Shipments

Drop shipments present a very unique problem in identifying the taxpayer subject to the state and in what state the taxpayer is subject to tax. A "drop shipment" means the direct delivery of tangible personal property to a purchaser in Michigan by a person who has sold the property to another person not licensed in Michigan but possessing a resale or exemption certificate or other written evidence of exemption authorized by another state, for resale to the Michigan purchaser. (MCL 205.54k(2)) A sale at retail includes a drop shipment. (MCL 205.54k(4))

The sale of tangible personal property that is part of a drop shipment is exempt from the sales tax if the taxpayer complies with the following: (MCL 205.54k(1))

For each transaction for which an exemption is claimed under subsection (1), the taxpayer shall provide, but not more frequently than annually, any information required by the board under the streamlined sales and use tax agreement in addition to the following information in a form prescribed by the department to the department: (MCL 205.54k(3))

(a) The name, address, and, if readily available, the federal taxpayer identification number of the person to whom the property is sold for resale. (MCL 205.54k(3)(a))

(b) The name, address, and, if readily available, the federal taxpayer identification number of the person to whom the property is shipped in Michigan. (MCL 205.54k(3)(b))

Administrative Guidance

The Michigan Department of Treasury issued Revenue Administrative Bulletin 2002-10 (RAB 02-10) on March 28, 2002. RAB 02-10 replaces RAB 1988-34. The Michigan Department of Treasury has established the following guidelines for the taxability of drop shipments as defined in Acts 41 and 42 of the Public Acts of 1986, being MCL 205.54k and 205.94i of the Sales and Use Tax Acts, respectively. These guidelines are effective March 17, 1986.

Drop Shipment Defined

A drop shipment (or third party sale) is a transaction where a retailer seller accepts an order from an end purchaser/consumer, places this order with a third party, and directs the third party to ship the tangible personal property directly to the end purchaser/consumer.

Examples

The following examples illustrate the applicability of sales and use taxes to various drop shipment transactions.

Example 1:

Company A = Michigan Company
Company B = Out-of-state seller
Person C = Michigan purchaser/consumer

Company B takes the order, collects the money and has Company A drop-ship to Person C. If Company B has a Michigan sales tax license, the tax is collected and remitted by B on that order from C. [Sales Tax Act, MCL 205.52(l)]

If Company B is not registered with the Michigan Department of Treasury due to lack of nexus, Person C shall be liable for the 6% use tax on the purchase as if it were any other purchase from out-of-state. [Use Tax Act, MCL 205.97]

If Company B is not required to be licensed to collect sales tax in Michigan, and it presents Company A with a valid sale for resale exemption certificate, Company A may be relieved of responsibility for the tax on that transaction, provided the following requirements are met:

1. Company A retains this certificate for their records [MCL 205.67, Section 17], and
2. Company A supplies the Department of Treasury with an annual information list or computer tapes containing the following:
3. The name, address and, if readily available, the federal taxpayer identification number of the out-of-state seller.
4. The name, address and, if readily available, the federal taxpayer identification number of the person to whom the tangible personal property is shipped in Michigan.

Example 2:

Company A = Michigan Company
Company B = Michigan Seller
Person C = Out-of-state consumer

This is a sale in interstate commerce. No tax is due to Michigan if the Michigan company ships to the out-of-state consumer. [Specific Sales and Use Tax Rules, 1979 AC, R 205.91]

Example 3:

Company A = Out-of-state company
Company B = Out-of-state seller
Person C = Michigan purchaser/consumer

If Company B is not registered in Michigan for sales and use tax collection, and no Michigan tax is charged on the transaction, Person C shall be liable for the 6% use tax on the purchase. [Sales Tax Act, MCL 205.52(l); Use Tax Act, MCL 205.97]

Example 4:

Company A = Out-of-state company
Company B = Michigan seller
Person C = Michigan purchaser/consumer

If Company B is responsible for the billing and collecting of the purchase price, it is responsible for the collection and remittance of sales tax. *Beitzel v Dep't of Treasury*, 2 Mich App 311 (1966).

If Company B takes the order for Company A, and Company A handles the billings and collections; it is considered a sale in interstate commerce. If Company A is not registered to collect and remit sales tax to Michigan, the 6% use tax shall be due from Person C. If Company B is acting as an authorized agent for Company A, then Company A shall be determined to have nexus in Michigan and shall be registered for sales and use tax collection and remittance. [*E C Cords v Dep't of Revenue*, SBTA Docket No. 573; *W E Phillips v Dep't of Revenue*, SBTA Docket No. 381]

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