

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 11-64**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

The application of the Tennessee sales and use tax to sales for resale of [PRODUCTS].

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the Department by the taxpayer. The rulings herein are binding upon the Department and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time. Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling; and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

FACTS

[TAXPAYER'S NAME] (the "Taxpayer") is a manufacturer of [PRODUCTS]. The Taxpayer has customers both within and outside of Tennessee. [PRODUCTS] may be made of [MATERIALS]. [REDACTED]. The Taxpayer also is a wholesaler of [PRODUCTS]. In no instance does the Taxpayer actually install any of its products.

The Taxpayer has two basic channels of distribution. First, products may be sold to a contractor-dealer who then either resells the products in its capacity as a dealer or installs the products for its own customers in its capacity as a contractor. It is usually unknown at the time of the sale if the contractor-dealer will resell or install the products. Alternatively, products may be sold to dealers who in turn resell the products to end purchasers who install the products themselves in their own homes or businesses. The dealer may also resell the products to a contractor-dealer who then either resells the products or installs the products for its own customers. The end purchasers are in some instances nonprofit entities. However, the Taxpayer frequently will not know who the end purchaser is.

The Taxpayer is periodically asked to drop ship products to locations specified by its customers. The Taxpayer currently makes nontaxable sales in Tennessee only upon receipt of a Tennessee resale exemption certificate.

QUESTIONS

1. Can the Taxpayer accept a Tennessee resale certificate from an out-of-state customer who is registered for sales and use tax purposes in Tennessee?

Ruling: Yes. The Taxpayer may accept a Tennessee resale certificate or a fully completed Streamlined Sales and Use Tax Certificate of Exemption, which must include a Tennessee exemption number, from an out-of-state customer who is registered for sales and use tax purposes in Tennessee.

2. For Tennessee sales and use tax purposes, can the Taxpayer make an exempt sale under a Tennessee resale certificate if the Taxpayer drop ships its product on behalf of a purchaser who is a dealer to the dealer's customer?

Ruling: Yes. If a registered dealer purchases products from the Taxpayer under a Tennessee resale certificate or a fully completed Streamlined Sales and Use Tax Certificate of Exemption, which must include a Tennessee exemption number, and has the Taxpayer drop ship the products to the registered dealer's customer in Tennessee, then the sale by the Taxpayer to the dealer is exempt from the Tennessee sales and use tax as a sale for resale.

3. For Tennessee sales and use tax purposes, can the Taxpayer make an exempt sale under a Tennessee resale certificate if the Taxpayer drop ships its product on behalf of a purchaser who is a contractor-dealer to a job site for use by the purchaser as a contractor?

Ruling: No. If a contractor-dealer purchases products from the Taxpayer and has the Taxpayer drop ship the products to a job site in Tennessee for use by the contractor-dealer as a contractor, then the sale is not exempt from the Tennessee sales and use tax.

4. Do the analyses for Questions #2 and #3 change if the Taxpayer's product is drop shipped to the dealer's customer that is a nonprofit entity?

Ruling: No. The analyses for Questions #2 and #3 remain the same, regardless of whether the product is drop shipped to the dealer's customer that is a nonprofit entity.

ANALYSIS

Retail sales of tangible personal property and specifically enumerated services in Tennessee are subject to sales and use tax under TENN. CODE ANN. § 67-6-101 *et seq.*, unless specifically exempted from taxation. TENN. CODE ANN. § 67-6-102(78) (2011) defines a “retail sale” as any “sale, lease, or rental for any purpose other than for resale, sublease, or subrent.” The term “sale” is defined under the Tennessee sales and use tax laws in part as “any transfer of title or possession, or both, exchange, barter, lease or rental, conditional or otherwise, in any manner or by any means whatsoever of tangible personal property for a consideration.”¹ TENN. CODE ANN. § 67-6-102(80)(A).

Tennessee generally imposes use tax on the purchase price of tangible personal property when the property is not sold but is used, consumed, distributed, or stored for use or consumption in Tennessee. TENN. CODE ANN. § 67-6-203(a) (2011). Additionally, TENN. CODE ANN. § 67-6-209(b) (2011) imposes the use tax on a contractor or subcontractor who uses tangible personal property in the performance of the contract, regardless of who holds title to such property, or to fulfill contract or subcontract obligations, unless such property has been previously subjected to a sales or use tax, and the tax due thereon has been paid.

A contractor-dealer is a person who is “engaged in the business of erecting, building or otherwise improving, altering and repairing real property for others” (*i.e.*, acting as a contractor) but is also “engaged in the business of selling building materials and supplies to other contractors, consumers, and users” (*i.e.*, acting as a dealer). TENN. COMP. R. & REG. 1320-5-1-.08(1) (1984). Generally, a contractor-dealer may purchase items on a resale certificate but must pay tax for items withdrawn from inventory for use as a contractor. TENN. COMP. R. & REG. 1320-5-1-.08(1) and (2); *Security Fire Prot. Co. v. Huddleston*, 138 S.W.3d 829 (Tenn. Ct. App. 2003).

1. *Resale certificate from an out-of-state customer*

The Taxpayer may accept a Tennessee resale certificate or a fully completed Streamlined Sales and Use Tax Certificate of Exemption, which must include a Tennessee exemption number, from an out-of-state customer who is registered for sales tax in Tennessee.

TENN. CODE ANN. § 67-6-102(77)(A) requires that all “sales for resale” be in strict compliance with the rules and regulations promulgated by the Commissioner of Revenue.² TENN. COMP. R. & REGS. 1320-5-1-.68(1) (2008) states that for Tennessee sales and use tax purposes, a dealer must require a resale certificate from a purchaser in order to make an exempt sale for resale of tangible personal property or taxable services in Tennessee. This rule applies to purchasers who are duly registered under the provisions of the Retailers’ Sales Tax Act. There is no restriction in the rule that limits the use of Tennessee resale certificates to Tennessee purchasers only. In order to purchase under a Tennessee resale certificate, a dealer only need be registered for sales

¹ TENN. CODE ANN. § 67-6-102(91)(A) defines “tangible personal property” as “personal property that can be seen, weighed, measured, felt, or touched.”

² A “sale for resale” is defined in pertinent part as “the sale of the property, services, or taxable item intended for subsequent resale by the purchaser.” TENN. CODE ANN. § 67-6-102(77)(A).

tax in Tennessee, not located in Tennessee. Alternatively, the Taxpayer may present a fully completed Streamlined Sales and Use Tax Certificate of Exemption, which must include a Tennessee exemption number, in lieu of a certificate of resale.

Therefore, if the Taxpayer's customer is registered for Tennessee sales/use taxes and presents a valid Tennessee resale certificate or fully completed Streamlined Sales and Use Tax Certificate of Exemption, which must include a Tennessee exemption number, the Taxpayer may accept the certificate and make a tax-exempt sale under the certificate, regardless of where the customer is located.

2. *Drop shipment to customer of purchaser who is a dealer*

If a registered dealer purchases products from the Taxpayer under a Tennessee resale certificate or a fully completed Streamlined Sales and Use Tax Certificate of Exemption, which must include a Tennessee exemption number, and has the Taxpayer drop ship the products to the dealer's customer in Tennessee, then the sale by the Taxpayer to the dealer is exempt from the Tennessee sales and use tax as a sale for resale.

Retail sales of tangible personal property and specifically enumerated services in Tennessee are subject to sales and use tax under TENN. CODE ANN. § 67-6-101 *et seq.* TENN. CODE ANN. § 67-6-102(78) defines a "retail sale" as any "sale, lease, or rental for any purpose *other than for resale*, sublease, or subrent." (Emphasis added.) Thus, a sale for resale is not a taxable sale under the Tennessee sales and use tax laws.

A "sale for resale" is defined as "the sale of the property, services, or taxable item intended for subsequent resale by the purchaser" and is required to be in strict compliance with the sales and use tax rules and regulations. TENN. CODE ANN. § 67-6-102(77). TENN. COMP. R. & REGS. 1320-5-1-.62(1) (1974) defines "sales for resale" as "those whereby a supplier of materials, supplies, equipment and services makes such tangible personal property or services available to legitimate dealers actually selling such property or services as such." TENN. COMP. R. & REGS. 1320-5-1-.68 requires that all sales for resale be supported by a valid Tennessee resale certificate.³ If a sale qualifies under the above definitions and conditions as a sale for resale, it is such regardless of whether the products are delivered to the registered dealer-purchaser or whether the products are drop shipped to the dealer's customer. A drop shipment is the shipment of goods from a manufacturer or other supplier directly to the customer of an intermediate seller.

³ TENN. COMP. R. & REGS. 1320-5-1-.29 (1974) provides that if an out-of-state vendor makes purchases for resale from a Tennessee dealer, the vendor can provide a valid foreign certificate of resale showing that it is an out-of-state dealer that would be entitled to purchase the property on a Tennessee resale certificate if it were a Tennessee dealer. TENN. COMP. R. & REGS. 1320-5-1-.96 (1974) further provides that if an out-of-state vendor has the Tennessee dealer act as its agent by drop shipping the purchased items to its Tennessee customer, then the sale is subject to the sales and use tax. However, these rules do not apply to out-of-state vendors that are registered in Tennessee for sales and use tax purposes and which present a valid Tennessee resale certificate.

⁴ Note, however, that it is the responsibility of the Tennessee registered dealer to collect Tennessee sales and use tax when the dealer resells the products to the end users.

The Taxpayer sells its products to registered dealers, who in turn resell the products to the end users. The sales' status as sales for resale does not change even when the Taxpayer drop ships the products directly to the end user. Provided that the dealer is registered for Tennessee sales and use tax purposes and presents the Taxpayer with a valid Tennessee resale certificate or fully completed Streamlined Sales and Use Tax Certificate of Exemption, which must include a Tennessee exemption number, the sale is exempt from the Tennessee sales and use tax as a sale for resale.⁴

3. *Drop shipment to job site of a purchaser who is a contractor-dealer*

If a contractor-dealer purchases products from the Taxpayer and has the Taxpayer drop ship the products to a job site in Tennessee for use by the contractor-dealer as a contractor, then the sale is a taxable retail sale under the Tennessee sales and use tax laws.

Generally, a supplier may make tax-free sales to a contractor-dealer under a resale certificate. TENN. COMP. R. & REGS. 1320-5-1-.08(1) provides that contractors who use materials and supplies, but who also sell at retail materials and supplies, may purchase the materials and supplies under a valid Tennessee resale certificate. However, if the materials and supplies purchased by the contractor-dealer are to be delivered to a job site for use by the contractor-dealer, or are to be tagged or marked for a particular job being performed by the contractor-dealer, then the supplier of the materials and supplies must collect sales and use tax. TENN. COMP. R. & REGS. 1320-5-1-.08(3).

Therefore, sales to contractor-dealers that are tagged or marked for a particular job intended to be performed by the contractor-dealer, or are delivered to the contractor-dealer's job site for use by the contractor-dealer, cannot be purchased tax-exempt with a resale certificate. The taxpayer must collect applicable sales or use tax on those sales.

4. *Nonprofit end user*

The analyses above for Questions #2 and #3 remain the same, regardless of whether the product is drop shipped to the dealer's customer that is a nonprofit entity.

TENN. CODE ANN. § 67-6-202(a) (2011) states that "[f]or the exercise of the privilege of engaging in the business of selling tangible personal property at retail in this state, a tax is levied on the sales price of *each item* or article of tangible personal property *when sold* at retail in this state." (Emphasis added.) Thus, the taxable event occurs at the time an item is sold by the Taxpayer; subsequent transactions will have no effect on the taxability of the Taxpayer's sale.

As explained in the response to Question #2, if a dealer purchases products from the Taxpayer under a Tennessee resale certificate and has the Taxpayer drop ship the products to the dealer's customer in Tennessee, then the sale to the dealer is exempt from the Tennessee sales and use tax as a sale for resale. The fact that the dealer's own customer may be a nonprofit entity does not change the exempt status of the Taxpayer's sale.

As explained in the response to Question #3, if a contractor-dealer purchases products from the Taxpayer and has the Taxpayer drop ship the products to a job site in Tennessee for use by the contractor-dealer as a contractor, then the sale is a taxable retail sale to the contractor under the

Tennessee sales and use tax laws. The fact that the contractor-dealer's own customer may be a nonprofit entity does not affect the taxability of the Taxpayer's sale to the contractor-dealer who is acting as a contractor.

Consequently, the Taxpayer's tax liability and tax collection responsibilities for Tennessee sales and use tax purposes are unaffected by whether the product sold by the Taxpayer ultimately becomes affixed to real property or remains tangible personal property upon installation.

Elizabeth Henderson
Tax Counsel

APPROVED: Richard H. Roberts
Commissioner of Revenue

DATE: November 21, 2011