

Drop shipments occur when a retailer takes an order and directs a wholesaler to ship the product directly to the customer. The wholesaler invoices the retailer, who in turn invoices the customer. When the wholesaler is registered to collect sales and use taxes in the purchaser's state, they may be required to collect these taxes from either the customer or the retailer. However, depending on the facts and circumstances, such as location and nexus status for all parties involved, how property is delivered, and how the title to property passes, the responsibility and requirement to charge and collect sales tax can change.

To highlight a few of the differences of the requirements under drop shipment arrangements, below are a few examples of the differing state rules:

California:

Drop shipments involve two sales: a “true retailer” contracts to sell tangible personal property to a consumer, and the true retailer then contracts to purchase that property from a supplier - instructing the supplier to ship the property directly to the consumer. The supplier is the drop shipper. A drop shipper engaged in business in California is considered the retailer. The retailer has the responsibility for collecting the tax and bears the burden of proving that a sale is exempt. Thus, the supplier must either collect tax or obtain exemption documentation.¹ An out-of-state retailer that is registered in California for sales or use tax must collect and remit tax on sales to California residents. However, if the out-of-state retailer is not registered, the supplier is required to report and submit any tax. The supplier should charge tax based on the retail amount of the transaction, and may choose to seek reimbursement from the in-state consumer.²

Out-of-State, Unregistered Retailer, In-State Supplier Example:

A California consumer orders and pays for a doghouse from ABC Supplies (ABC), an out-of-state retailer who is not registered to collect and pay California sales or use tax. ABC buys the doghouse from XYZ, a California retailer, and directs it to deliver the doghouse to the California consumer. XYZ delivers the doghouse directly to the California consumer on behalf of ABC.

Result:

XYZ is the drop shipper and is liable for the sales tax due on the transaction because ABC is not registered to collect tax in California.³

Note that these rules change if a marketplace facilitator is involved.

¹ Cal. Rev. & Tax. Code § 6007; Cal. Rev. & Tax. Code § 6091; Cal. Code Regs. tit. 18, § 1706(b).

² California Tax Publication 121 (an invoice cannot call this “California tax” or “California sales tax,” but may say “California tax paid to California drop shipper”); California Tax Publication 73.

³ California Tax Publication 121.

Florida:

Drop shipments involve three transactions: (1) the sale for resale between the supplier and the retailer, (2) the sale from the retailer to the consumer, and (3) the shipment from the supplier to the consumer.⁴

Out-of-State Retailer, In-State Supplier Example:

Consumer C, located in Florida, places an order with Company B for 100 widgets. Company B is an out-of-state retailer not registered in Florida. Company B purchases 100 widgets from Company A, a supplier located in Florida. Company A ships the widgets directly to Consumer C in Florida.⁵

Result:

Company A is required to collect sales tax on the sale to Company B because Florida does not accept out-of-state resale exemption certificates. Company B may not collect sales tax on the sale to Consumer C because it is not registered in Florida. Consumer C is required to remit use tax on the purchase.

Out-of-state Retailer, Registered Out-of-state Supplier Example:

The taxpayer is an out-of-state supplier with no physical presence in the state, but who has registered in Florida as a non-resident dealer. The taxpayer makes sales to Company A, an out-of-state retailer not registered in Florida. The taxpayer ships the goods directly to Company A's customers in Florida by common carrier.

⁴ Florida Technical Assistance Advisement 15A-020 (Dec. 7, 2015); Florida Technical Assistance Advisement 07A-043 (Nov. 8, 2007).

⁵ Florida Technical Assistance Advisement 15A-020 (Dec. 7, 2015); Florida Technical Assistance Advisement 07A-043 (Nov. 8, 2007); Florida Technical Assistance Advisement 86A-29 (Dec. 26, 1986) (if the purchaser is not sufficiently present in Florida to be required to register and collect tax, the ultimate customer would have a use tax liability); Fla. Admin. Code Ann. R.

Florida:

Result:

The taxpayer is not liable for sales tax on its sales to Company A because the transactions do not fall within the jurisdiction of Florida's sales and use tax laws. The taxpayer should retain documentation proving that the sales take place outside of Florida's jurisdiction and that delivery is made via common carrier. Any consumer in Florida is required to remit use tax on the purchase price of the property.⁶

Note that if the retailer is unregistered and located out-of-state, Florida applies different rules to suppliers depending on whether they are Florida manufacturers. If a supplier that is a Florida manufacturer drop ships merchandise to an unregistered out-of-state retailer's customer in Florida, the supplier is required to collect tax on its sale of the merchandise to the retailer. If a supplier that is not a Florida manufacturer drop ships merchandise to a Florida customer on behalf of an unregistered out-of-state retailer, the supplier is only required to collect tax from the Florida customer if: (1) the supplier delivers the goods from a Florida facility; (2) the supplier delivers the goods in its own or leased vehicles; or (3) the payment terms are COD.⁷

New York:

Drop shipments involve three transactions: (1) the sale for resale between the supplier and the retailer, (2) the sale from the retailer to the consumer, and (3) the shipment from the supplier to the consumer.⁸

In-State Retailer, Out-of-State Supplier Example:

Consumer C, located in New York, places an order with Company B for 100 widgets. Company B is a retailer located in New York. Company B purchases 100 widgets from Company A, an out-of-state supplier, and provides Company A with a completed Form ST-120. Company A ships the widgets directly to Consumer C in New York.

Result:

The sale by Company A to Company B is exempt from sales tax as a sale for resale.⁹

⁶ Florida Technical Assistance Advisement 15A-020 (Dec. 7, 2015); Florida Technical Assistance Advisement 83A-074R (Feb. 18, 1984), superseding Florida Technical Assistance Advisement 83A-074 (Nov. 29, 1983), (the purchaser is selling the materials in Florida, and accordingly should provide the vendor with a resale certificate, register as a dealer, and collect Florida tax, unless Florida does not have nexus over the purchaser, in which case the customer is required to remit use tax on the property); Florida Technical Assistance Advisement 09A-010 (March 2, 2009) (taxpayer registered as out-of-state Florida dealer not required to collect sales tax on items drop shipped to nonresident buyers' customers in Florida when nonresident buyers had no Florida nexus and were not registered in state); Florida Technical Assistance Advisement 86A-29 (Dec. 26, 1986) (if the purchaser is not sufficiently present in Florida to be required to register and collect tax, the ultimate customer would have a use tax liability.)

⁷ Florida Technical Assistance Advisement 94A-060 (Nov. 17, 1994); Florida Technical Assistance Advisement 00A-044 (Aug. 3, 2000); Florida Technical Assistance Advisement 09A-010 (March 2, 2009).

⁸ New York TB-ST-190.

⁹ New York TB-ST-190.

New York:

Out-of-State Retailer, Out-of-State Supplier Example:

Consumer C, located in New York, places an order with Company B for 100 widgets. Company B is an out-of state retailer that meets the requirements of a “qualified out-of-state purchaser”. Company B purchases 100 widgets from Company A, an out-of-state supplier, and provides Company A with a completed Form FT-120. Company A ships the widgets directly to Consumer C in New York.

Result:

The sale by Company A to Company B is exempt from sales tax as a sale for resale. New York has not addressed the tax liability for the sale from Company B to Consumer C, however it likely can be concluded that unless an exemption applies, Company B would charge sales tax to Consumer C so long as Company B has nexus in New York State.¹⁰

Note that a qualified out-of-state purchaser is a purchaser that is not registered or required to be registered with the department; registered with or located only in another jurisdiction; and that is purchasing items for resale that will be delivered either to the purchaser's customer or unaffiliated fulfillment services provider located in New York; or the purchaser in New York but resold from an out-of-state business.¹¹

¹⁰ New York TB-ST-190.

¹¹ New York TB-ST-190; see also New York TSB-A-00(20)S (April 25, 2000); New York TSB-M-98(3)S (June 5, 1998); New York TSB-A-92(3)S (Jan. 30, 1992).

Texas:

Drop shipments involve three transactions: (1) the sale for resale between the supplier and the retailer, (2) the sale from the retailer to the consumer, and (3) the shipment from the supplier to the consumer.¹²

In-State Retailer, Out-of-State Supplier Example:

Consumer C places an order with Company B for 100 widgets. Company B is engaged in business in Texas. Company B purchases 100 widgets from Company A, an out-of-state supplier, and provides Company A with a completed resale certificate. Company A ships the widgets directly to Consumer C in Texas.

Result:

Company A has met its legal responsibility in terms of sales and use tax on the sale by collecting the completed resale certificate. Company B is required to collect and remit Texas sales tax on its sale to Consumer C.¹³

Out-of-State Retailer, Out-of-State Supplier Example:

Consumer C places an order with Company B for 100 widgets. Company B is not engaged in business in Texas. Company B purchases 100 widgets from Company A, an out-of-state supplier, and provides Company A with a completed resale certificate. Company A ships the widgets directly to Consumer C in Texas.

Result:

Company A has met its legal responsibility in terms of sales and use tax on the sale by collecting the completed resale certificate. Company B is not required to collect and remit Texas sales tax on its sale to Consumer C because it is not engaged in business in Texas. Consumer C is required to remit the use tax on the purchase directly to the state of Texas.¹⁴

If you have not reviewed your sales tax requirements recently or have any questions, please reach out to our office.

This article is a summary of the laws and regulations in effect at the time of publication, and changes may have occurred to the laws and applicable regulations since writing. Conflicts between the text of this article and the law will be based on law.

¹² Texas Comptroller's Letter No. 200203857L (March 13, 2002); Texas Comptroller's Letter No. 200002088L (Feb. 29, 2000).

¹³ Texas Comptroller's Letter No. 200002088L (Feb. 29, 2000); Tex. Admin. Code tit. 34, § 3.286(k)(2)

¹⁴ Texas Comptroller's Letter No. 200002088L (Feb. 29, 2000); Tex. Admin. Code tit. 34, § 3.286(k)(2)