Use Tax Compliance Teleconference

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Dave Hobley, Masco Corp.
david_hobley@mascohq.com

I. Use Tax Determinations – Systems And Methods

A. Legacy systems

1) Self-developed (often Excel- or Access query-based)

2) Labor-intensive, in order to maintain and update tax matrices and rates

3) Error-prone (system changes frequently develop at a lag with changes to business)

4) System knowledge often disappears when the SME leaves

B. Direct pay agreements

1) Benefits

a) Tax determination, calculation and reporting are 100% under your control

b) Accuracy <u>should</u> increase

i. Vendor errors are minimized or eliminated

ii. Incremental taxes are minimized

- Taxes are paid directly to the jurisdiction where use occurs, as opposed to the seller's location or some other trans-shipment point

2) Challenges

a) Compliance shifts to the purchaser

b) Visibility is heightened

i) Taxes paid are “uncloaked”

ii) Number of audits may increase due to higher amounts of tax reported

c) All tax errors are internal now

3) Single-rate programs

a) Can be formal or informal

b) Statistical sampling of purchases for selected accounts used to generate initial rate

c) Rate is tested periodically for validation, and necessary adjustments are made to rate

d) Generally operate in conjunction with direct pay agreements

e) Simplifies tax reporting

f) Fewer states are pursuing these agreements

C. Expert systems

1) Automation can bring significant efficiencies to determination, calculation and reporting process

2) Tax software vendors offer wide variety of products and services

3) Every project stage is important

a) Kickoff to selection

i. Conduct/confirm needs-based analysis

- Persuasive business case is critical to success

- Increase compliance accuracy and reduce costs

- Simplify audits

- Free up scarce staff hours to apply to more proactive, value-added pursuits

ii. Beware of "scope creep"

b) Audition multiple vendors

i. Though there are many similarities among software packages, each vendor has a different range of products and services

ii. Don't put too much value on testimonials from "satisfied customers" – Your facts (and results) may vary significantly

c) Evaluate and select

4) Installation to implementation

a) Define – What you want it to do

b) Design – How it will do what you want it to do

c) Build – Nuts and bolts

d) Test – Run real-world transactions to see where adjustments need to be made in order to fine-tune software operation

e) Implement – Operate, monitor and maintain

5) Operation

a) Training is critical

i. Example: ERP implementation inadvertently defaulted all customers to "taxable" in customer master

ii. Rather than fixing problem in customer master, order entry was granted authority to override tax field

iii. Mayhem ensued

b) Automation is not the end of continuous improvement practices

II. Audit Strategies

A. Before the audit begins

1) Attempt audit pre-elimination/minimization

a) Ask the auditor of state REALLY wants to audit you (Hint: This only works when your point is convincing, e.g. the last time they wound up writing you a check)

b) Consider a managed or desk audit

i. Are the resources available?

ii. Can you meet their requirements/requests for data and documentation?

2) Narrow or widen the audit's scope

a) Example: Auditor reviewed material purchases (not reviewed in previous audits) and uncovered significant exposure item – "brush cleaner"

b) Example: One IN auditor wants to audit 2004-05, but not 2006

3) Know your strengths and weaknesses

a) Demonstrating highly defined and/or automated processes with robust controls helps establish the auditor's confidence and trust

i. Good example: Significant refund claim went from discovery to approval and payment in less than two years (single issue, favorable facts, excellent documentation, experienced auditor)

ii. Bad example: Significant audit assessment under appeal is in Year 4 (single issue, favorable facts, bad recordkeeping, weak auditor)

b) Document descriptions can be misleading, so anticipate questions and have your answers ready

i. Example: Invoice used the term "belt cleaner" (T), but it actually was a solvent used in stain (E)

B. During the audit

1) Get to know your auditor

a) Be sincere – Make a good faith attempt to develop a rapport

i. You don't want him on *your* company softball team, but you might play on *his*

b) It's not personal; he/she has a job to do and so do you

2) Explain your company's rules

a) Single point of contact

b) Visitor status

c) Data and document policies

3) Set expectations

a) Establish timeline and milestones

b) Establish accountability for both parties

4) Request progress reports and discuss questioned transactions proactively

5) If you cannot come to an agreement with the auditor on contested items, determine whether you will utilize informal pre-assessment forums in an effort to reach consensus

III. Post-Op (After The Assessment Has Been Issued)

A. Do you agree with the audit findings?

B. If not, will you appeal?

1) Cost/benefit calculation

a) Litigation costs

b) Opportunity cost of appeal (staff hours)

2) If yes, on which items?

3) Is counsel required?

C. Reach out to peers for help, advice, recommendations

1) COST forums, IPT members, etc.

D. Refund claims

1) Overpayment review should be a default procedure when an audit is announced

2) What happens if you uncover an overpayment and you are not under audit?

a) File a claim anyway?

b) Reduce reported amount on return?

c) Law of unintended consequences

i. TN refund claim story