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The term *sales tax* means different things to different people. Your definition may be narrow or broad, but in the world of tax compliance today, sales and use taxes practically include *any* type of *transactional* tax, fee or surcharge. Accurately calculating the amount of sales or use tax owed, and accurately determining the party to which it is owed, is not as simple as it may appear at first glance. The factors affecting the calculation and filing of a sales and use tax include the following:

- Nexus determination
- Situs determination
- Taxing jurisdiction
- Profit or non-profit status of the entity from which you are collecting the tax
- Other special tax status situations, such as agricultural exemptions
- Special “tax holidays”
- Taxability status of the product or service
- “Bucketing” decisions
- Summarization decisions
- Forms decisions

- Minimum and maximum taxes

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particular about not paying more than they must. In extreme cases of mistaken tax collection, they back up their claims with individual and class action law suits. As the entity calculating, collecting and forwarding taxes to government jurisdictions, businesses are caught in the middle of both of those sets of expectations.

Once all of the above variables are accounted for, accurate and timely tax collection and payment involves the completion and filing of forms. With approximately 10,000 different taxing jurisdictions in the United States, keeping track of and filing the correct, latest-version forms for the correct amounts is a daunting task. Even with that, the taxation cycle is not complete once a form is filed and payment sent. The ability to track and reproduce the data-gathering and decision-making process that went on behind the scenes to fill out the form is a vital step. And with the broadening implications of Sarbanes-Oxley regulations, having a transparent, accessible audit trail is more important than ever.

FORMS LIBRARY

VS. COMPLIANCE ENGINE

A reproducible, auditable trail is the major difference between form filing software and true sales and use tax compliance software. A compliance engine gathers other information from the transaction in addition to revenue. For example, it pulls multi-faceted data to make complex situs decisions. Where the transaction takes place determines who gets the taxes, but defining that spot is not as simple as it may sound. If a consumer who lives in New York City orders goods from a company in California, which has the goods shipped from a warehouse in New Mexico, determining situs for taxation purposes becomes a multi-step process that also must take into account nexus data.

As more companies market and deliver goods and services through multiple

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~~Employed common carriers for delivery.~~

The standard invoice provided that customers could inspect the delivered merchandise and request replacements from the taxpayer. Any claim for damages in transit was made by the taxpayer against the carrier, implying that title continued to be held by the taxpayer. The taxpayer also failed to establish that its customers had already paid sales or use taxes on some of the sales in question.

The taxpayer's argument that it did not have substantial nexus with Wyoming for sales tax purposes was rejected. The taxpayer could not establish that its salesmen did not travel to Wyoming. Further, at all pertinent times, the taxpayer voluntarily held a Wyoming sales tax license and thus was authorized to collect taxes on behalf of Wyoming, which it did on some occasions. When it voluntarily applied for the license, the taxpayer established substantial nexus with the state and subjected itself to the requirements of Wyoming sales tax statutes. In effect, attempting to conscientiously fulfill tax jurisdiction requirements is part of what got this taxpayer in hot water.

As of May 1, nineteen states had filed petitions to initiate compliance with the guidelines of the Streamlined Sales Tax (SST) initiative. While SST appears to be poised for real-world implementation in the fall of 2005, recent introduction of a two-tiered membership with varying levels of compliance means the sales and use tax picture won't be much clarified, simplified or indeed "streamlined" for quite some time. Even full enactment of the SST will not completely eliminate the complexity of situs and nexus decisions.

Compliance software also takes into account what the product is and how it will be used. Durable medical goods, for example, are taxed differently depending upon where they are sold, who is buying them, and how

they will be used. The granularities of such decisions at times seem to defy common

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agement services for the defibrillators are also exempt. However, when the defibrillators are not purchased by or on behalf of an individual, tax is imposed on the defibrillators and on charges for the services, even if the charges for services are separately stated on invoices.

IMPROVING

THE AUDIT TRAIL

As tax rate and taxability decisions grow more complex rather than simpler, regulatory demands for transparency and auditability grow more intense. To provide the transparent, valid audit trails businesses need to maintain and prove compliance, their software must provide documentation for all of the decisions for every variable made along the way (even for things such as who will be using that defibrillator), so that any single transaction can be back-tracked, checked and verified. A sophisticated compliance engine can give a unified data set that integrates with all of their tax collection, calculation and payment steps rather than having audit trails separate from bookkeeping.

In addition to providing a verifiable audit trail, a compliance engine can also reduce chances of human error and system error. This is particularly important when a business' accounting isn't centralized and/or it has information coming in from a variety of locations. Multi-user, multi-site accounting systems are becoming more and more the norm as corporations acquire and move subsidiaries about. Absence, however, does not mitigate compliance needs. A compliance engine, however, can eliminate individual decision making at each location and allow the business to review records for any part of any transaction, no matter where it originated and ended.

A forms engine is a library of editable forms. While a forms engine saves time by

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a compliance engine and a forms engine appear similar — both end up with a filled out form — a compliance engine works on several levels, with the filled out forms being just the end result.

Every accounting system has its own way of storing, interpreting, and using data. A compliance engine is set up to seamlessly integrate with a company's existing system, no matter what its current workflow. For example, a compliance engine will calculate the business' taxes based on the "gross up" scenario if that is how it has done so historically. Some sales tracking systems are only location based or ZIP-code based, which may or may not match the business' work processes already in use. As with any type of program, to save time and effort, the software should be adaptable enough to work in the organization's system, and not expect the existing system to adapt to the software.

If the company has been bought, sold or has purchased another company, it may be having even bigger accounting integration issues. Calculating business taxes due for multiple sites is not made any easier by lack of software compatibility. Fortunately, a compliance engine is usually versatile enough to collect and use data from disparate sources that are using different software packages.

Whatever the business' starting configuration, the end result of a forms compliance system is really three layers of processing and tracking. It starts at the file level, dissecting a business' current files to sort and store (what's known as "bucketing") the data in such a way that the form will understand the information provided. Then, given the business' nexus and filing history, the compliance engine selects, calculates and places the information into the forms. With software at this level,

individual variations and interpretations are taken into account as well as the rote

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a million-dollar form, helping ensure both are completed and filed accurately.

Throughout that process, decisions that drive the calculations are being made on many levels. This is where a traceable audit trail becomes critically important. When an auditor looks at what the business filed and tries to reconcile it with the data, it should have a readily reproducible trail documenting how the data was used and how the forms and regulations have been interpreted for every decision that has been made. The better the integration of change analysis into the software, the more effective and efficient auditing from any number to any number can become.

Compliance technology should be designed to take into account the available transaction and calculation information, and the existing (and future) processes, as well as the forms, as diagrammed on page 70. When a business has software that works in the compliance zone overlap, then it has the audit trail of information. It can reconstruct any transaction to support the numbers on the forms. It has situs, nexus and all other transaction information to support any calculation. Any number on any form is no longer just a number — it's a representation of a detailed account of the transaction.

When to choose a compliance engine instead of a forms library.

If a business' needs are quite simple and straightforward, a simple forms library is probably sufficient. However, if the business has two or more of the circumstances below, a compliance engine is probably the safer choice:

- Multiple nexuses,
- Multiples situses,

- Multiple locations

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unavailable IT resources,

- A nexus in Georgia, California, New Mexico, Alabama, Louisiana, Florida, Colorado or Texas,

- A history of one or more past audits.

The functionality checklist at the bottom of page 70 can be used to determine if a business' needs will be best met by a forms library or a compliance engine.

Compliance software has another stress-reducing benefit. A forms engine calculates and reports a business' taxes due at pre-set intervals appropriate for the taxes it should pay. It will calculate taxes due for the month or quarter, but does not keep a running tab. A compliance engine, however, often shows the tax liability in real time, where the business doesn't have to wait for a monthly or quarterly report to know where it stands on taxes owed.

Compliance is often less expensive and less stressful than an audit. And it can be easier too.

The following example is a life lesson on picking software carefully and making sure the results can be easily checked. An officer of a New York company that retails sales of shirts, suits and accessories was a person responsible for the collection and payment of New York sales and use taxes on behalf of the company. Even though he did not have direct responsibility for keeping the books and filing tax returns, he was

directly responsible for the operation and oversight of the department that

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footed and cross-footed with every transaction for every form. That intensive, real-time auditability of the numbers, along with the adaptive cross-checks that ensure form-filing accuracy, gives a level of compliance that will make it less likely that a business will be audited. If the business ever is audited, however, information should be readily available. A compliance engine is effectively in a constant state of readiness to respond to internal or external audit requests.

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Technology

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