Blueprint for Success: Sales Tax Essentials for Construction & Real Property

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On-Demand Webinar

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Overview

Overview

- The discussion of the tax treatment of real property transactions must be looked at from a number of different perspectives.
  - For contractors: Should you try to minimize tax costs or are they just pass through?
    - Should you be providing tax advice to property owners?
  - For property owners: Do you know what exemptions could apply? You'll want to know what you should be negotiating with the contractor before the contractor starts the bid process.
- Contractors and property owners both need to pay attention to the structure of the contract.

Overview (cont.)

- Tax staff from both the Property Owner and the Contractor should be involved with:
  - Contract structure
  - What's covered under the contract
  - Tax clauses
  - Flow-through exemptions

New York Ruling on Sales Tax Refund for Concrete

- A New York appeals court ruled against a company claiming eligibility for sales tax refunds on concrete purchases.
- The company argued that its purchases of concrete were for a nontaxable service provided by the seller that would also provide "the installation of capital improvements to real property, rather than a taxable delivery of concrete."
- The appeals court upheld a previous ruling and affirmed that the transactions were retail sales of personal property.
- The appeals court said that if the concrete had been purchased in conjunction with the installation, instead of individually, it would have been exempt from sales tax.
- In this case, the invoices reflected purchases of concrete rather than installation services.
- Having documentation properly prepared at the time of transaction will provide a clearer picture of intention and a much more robust defense if questioned in audit as states look at invoices as the proof of the transaction.
- (Matter of M&Y Devs. Inc. v Tax Appeals Trib. of the State of N.Y., 2022 NY Slip Op 04600, July 14, 2022)

Real Property vs. Tangible Personal Property

- Real property includes buildings, land, and many items incorporated into the buildings and land.
- Generally, real property includes fixtures that cannot be removed without destroying either the fixtures or the real property.
- Examples of real property include carpet that is glued down, plumbing systems, insulation materials, and electrical systems.
- It should be noted that the term "fixtures" can take on various meanings and in some states, such as California, can be deemed tangible property for which a retail sale situation can be challenged if/when a contract or related quote is not clear.
- In most states, the contractor is the deemed consumer of materials incorporated into real property and incurs the tax.

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Real Property vs. Tangible Personal Property (cont.)

- Most states include in their regulations lists of items which they consider tangible personal property when sold by a contractor.
- Tangible personal property includes window treatments, most appliances, window air conditioners, tacked down carpet, and other items that can be removed without damage to the structure.

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Real Property vs. Tangible Personal Property (cont.)

- Tangible personal property is typically movable and not affixed to the land.
- Controversies arise with respect to fixtures and leasehold improvements.
- Even where machinery and equipment is embedded in or bolted to a concrete floor, the state may assert that the property is tangible personal property subject to sales tax.
- Sales of tangible property are taxed on the sale transaction to the property owner.

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Grass Seed and Erosion Control Blankets Exempt as Construction and Building Materials in Colorado

- The Colorado DOR issued a private letter ruling discussing the taxability of sales of grass seed, erosion control blankets and fertilizer to a construction contractor.
- Per the letter ruling, sales of grass seed and erosion control blankets are exempt from sales tax as construction and building materials if the sales are made to a construction contractor who provides an exempt certificate to the seller for installation in property owned by an exempt entity. Sales of fertilizer are not exempt from sales tax as construction and building materials.
- The phrase "construction and building materials" is not defined in a Colorado statute or rule. The letter ruling notes that the Court of Appeals has explained that the plain meaning of the phrase "construction and building materials" suggests that the materials must lose their identity and become a permanent part of the realty.

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Grass Seed and Erosion Control Blankets Exempt as Construction and Building Materials in Colorado (cont.)

- The DOR states that landscape construction generally involves altering the land to make it visibly functional. Landscaped areas are constructed using components such as grass seed and erosion control blankets that become a permanent part of the realty, similar to wood or metal.
- Therefore, sales of grass seed and erosion control blankets are exempt from sales tax as construction and building materials when purchased by a contractor for installation at an exempt or governmental organization.
- Landscape construction does not generally include regular maintenance of the landscaped areas – such as applying fertilizer – after construction.
- Since fertilizer does not contribute to landscape construction but rather landscape maintenance, fertilizer does not qualify for the exemption on construction and building materials.
- (PLR 23-001, Colorado Department of Revenue, January 13, 2023)

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The Tax Treatment of Different Contract Types

Construction Contracts

- The key elements of a contract to consider when doing tax planning are: scope of project, contract price, and tax responsibility.
- A contract should clearly delineate what work is to be performed and what materials will be procured and installed to meet the contract's requirements.
- For a tax professional to determine the application of taxes to the contract, the scope of the project must be specific, detailed, and not exceedingly technical.

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Construction Contracts (cont.)

- A well-written contract indicates the tax responsibilities of both the contractor and the customer.
- Contractors are often responsible for paying tax on the items they install and convert into real property.
- Therefore, it is important that contractors that wish to pass along the cost of the tax to their customers estimate these tax costs and include them in the original bid or quoting process and in the final contract price.
- Conversely, tax reductions that result in cost savings by the contractor should be passed on to the property owner.

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Construction Contracts (cont.)

- From a customer perspective, the customer should include and engage their tax personnel in the process during the bidding stage and communications with the contractor(s).
- Depending on the type of project and/or location, there may be tax planning opportunities that need to be considered.
- In some situations, exemptions or credits may require pre-approval by state or local agencies.
- There may also be situations where the customer needs to procure and act as purchaser for materials and equipment in order to be eligible for exemptions or credits. Identifying exemption or credit opportunities after-the-fact generally results in no savings when related to construction contracts.

Construction Contracts (cont.)

- The customer should never assume that a contractor is fluent with all tax planning opportunities related to their specific project.
- To ensure a consistent bidding process, all contractors involved should be providing their quotes with a consistent fact pattern.
- It is not uncommon for a contractor's bid to be immediately excluded from the selection process due to a 6-8% pricing difference caused by inclusion of sales tax that may not have been included in other bids.
- It is also in the contractor's benefit to be alert to tax planning opportunities that may apply to projects and/or discuss the topic with their potential customer during the bidding process.

Types of Construction Contracts

- Lump sum contract – a contract that does not distinguish between the charges for materials and the charges for labor.
- Separated contract – a contract that separates the charges for labor and materials. Typically, separated contracts are either cost-plus contracts or time-and-materials contracts.

Tax Treatment of Construction Contracts

- Sales tax is generally imposed on the "ultimate consumer." The ultimate consumer is usually the last person to purchase and use the item.
- In the construction or improvement of real property, the contractor usually is considered the ultimate consumer of the tangible personal property incorporated into the realty.
- The contractor is selling real estate or an improvement to real estate and this is generally not subject to sales and use tax.
- When the tax burden is on the contractor, the contractor may pass the cost of the tax on to the purchaser as part of the contract price but is not allowed to display the tax as an add-on tax when the tax burden is on the contractor as the purchaser.

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Tax Treatment of Construction Contracts (cont.)

- In some states, for time and material contracts where materials are separately stated from the labor (e.g., Florida, Texas), a contractor may be considered a retailer of the materials and can purchase the items that become components of the realty for resale.
- In some states, if the contractor is providing a taxable service, such as taxable real property remodeling, the contractor can purchase the items that are incorporated into the realty for resale.
- In both cases, sales tax must then be charged on the <u>selling</u> price of the taxable materials.

Tax Treatment of Construction Contracts (cont.)

- Indiana
  - In a lump sum contract, the contractor must pay either sales or use tax on purchases of construction materials.
  - In a time and materials contract, the contractor's purchases of construction materials are exempt, but tax must be collected on the sale of those materials. Labor is exempt.

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Tax Treatment of Construction Contracts (cont.)

- Contractors are considered consumers when they purchase items of tangible personal property that is used or consumed in their construction activity even if it isn't incorporated into the real property.
- Sales or use tax should be paid on the purchase of these items when they are purchased such as cleaning supplies, administrative items and marketing materials.
- Additionally, all equipment used by the contractor is taxable.

Items Purchased by Property Owner for Installation

- Taxpayers who purchase items for incorporation into real property and hire a contractor to perform the labor are considered the consumer of the items purchased.
- Sales or use tax should be paid on the purchase of these items by the property owner.
- The separately contracted labor for installation may be taxable depending on the state and the nature of the installation.

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Real Property Repairs and Maintenance

- A few states tax real property repairs and remodeling.
- Some states distinguish between real property repairs and maintenance.
- In Texas, real property maintenance is exempt. The maintenance must be scheduled and periodic (34 TAC §3.357). However, real property repairs are taxable.
- Some states also tax commercial real property repairs but not residential real property repairs.

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Real Property Repairs and Maintenance (cont.)

- Texas
  - A contractor's labor charges for new construction of real property and for residential real property repair, remodeling, or restoration are exempt.
  - A contractor's labor charges for nonresidential real property repair, remodeling, or restoration and real property services are taxable.

Remodeling

- Many construction contracts include both new construction and remodeling. In some states, remodeling is a taxable service.
- It is important for the contractor to delineate between the new construction and remodeling in the contract amount.
- If this is not possible, the contract should have some form of recordkeeping to separate out the remodeling from the new construction to prevent the entire contract amount being subject to tax.
- Some states will allow a percentage to be used to determine the taxable portion of the contract amount.

Special Circumstances

Government & Exempt Entity Contracts

- There is significant confusion among contractors concerning their liability for sales and use tax on materials used or incorporated in government or exempt entity contracts.
- Because in construction contracts the legal incidence of the tax is often on the contractor, it is important to understand the contractual relationship between the contractor and the government/exempt entity and the legal incidence of the tax rather than just the economic incidence of the tax.
- Just because the tax amount may be included in the contract price and thus the government or exempt entity may bear an economic burden of taxation, the legal incidence may still be with the contractor and therefore, legally imposed by the state.

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Government & Exempt Entity Contracts (cont.)

- Some states may provide for an exemption to pass through to a contractor performing a government contract. However, in other cases, only direct sales to the government are exempt from sales and use taxes.
- When engaged in a "government" contract, it is important to distinguish the difference between federal, state and local government as well as other exempt entity contracts. There may be situations where a flow-through exemption is applicable for one and not the other.

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Government & Exempt Entity Contracts (cont.)

- States distinguish between government contracts related to real property and those related to supply contracts. It is important to evaluate whether you are engaging in a real property or supply contract.
- In general, if items are purchased that are directly resold to the government without incorporation into real property, the resale exemption should apply to the items when purchased by the contractor and then the government's exemption would apply on the transaction between the contractor and the government.

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Government & Exempt Entity Contracts (cont)

- SST Disclosed Practice 9 addresses exemptions and exemption documentation. A specific portion addresses sales to contractors for use on contracts with exempt organization
- 9.2.L. – Sales to Construction Contractors for sales of construction materials incorporated into real property construction activities for the specified organizations. This does not include sales for resale.
- 9.2.M. – Sales to third parties who are providing services or performing contracts not related to real property.

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Federal Contractor Required to Pay Washington Use Tax on Design and Engineering Costs Associated with Government Contract

- The Court of Appeals of Washington determined that Alstom Power Inc. was required to pay Washington use tax for a turbine rehabilitation project.
- Alstom contracted with the federal government to complete turbine rehabilitation work.
- Alstom subcontracted with one of its affiliates to design, engineer and manufacture the turbine components.
- The Washington Board of Tax Appeals (Board) determined that Alstom owed Washington use tax on the design and engineering costs because those costs were part of the value of the turbine components.
- The Court of Appeals stated that under Washington tax law, because federal contractors may not impose sales tax on the federal government, federal contractors are required to pay use tax on the value of the materials and tangible personal property used for the government contract.

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Federal Contractor Required to Pay Washington Use Tax on Design and Engineering Costs Associated with Government Contract (cont.)

- Per the court's opinion, Alstom essentially purchased the turbine components from its subcontractors, paying for both the raw materials and the design and engineering work.
- Because Alstom purchased and incorporated turbine components into the turbines, they became the "articles used" for the project.
- Washington tax law dictates that Alstom must pay use tax on a value equivalent to a retail selling price, which like any purchased product, would necessarily include the costs to design and engineer the components.
- (Alstom Power Inc. v. Washington, Wash. Ct. App., Div. 2, No. 56476-9-II, March 28, 2023)

Customer Purchased Materials

- In the case of a statutorily exempt entity, the purchase of these materials directly by the customer may be a way to exempt the materials otherwise subject to tax. Several states have provided such an exemption
- In the Minnesota Tax Court case, *Stretar Masonry Co., Inc v. Commissioner of Revenue*, the Minnesota Supreme Court found building materials for use in constructing public buildings were exempt from sales and use tax because the construction contractor was acting as a purchasing agent for Wright and Morrison counties.

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State Tax Treatments for Flow-Through Exemptions

- Minnesota
  - In Minnesota, exempt entities may designate contractors as their purchasing agent in order to make exempt purchases for use on a construction contract.
  - To qualify for the purchasing agent exemption, the construction contract cannot be a lump-sum contract or a similar type of contract with a guaranteed maximum price covering both materials and labor, and if the materials purchased are used to construct buildings or facilities, the buildings or facilities must be used principally by the exempt entity.

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State Tax Treatments for Flow-Through Exemptions (cont.)

- Minnesota (cont.)
  - In addition, exempt entities may only appoint a contractor as its purchasing agent if the exempt entity initially advertises for separate bids for material and labor, only accepts one bid without accepting both bids, and separate contracts are issued for the accepted bids for materials and labor.
  - The terms of the contract must be in a written contract and stipulate that the contractor has been appointed as purchasing agent, that the exempt entity takes title to all materials at point of delivery and the exempt entity has risk of loss for all materials and responsibility for defective materials.
  - All appointed contractors much provide notification to all suppliers that it is the exempt entity's obligation to pay for the materials and all purchase orders must clearly reflect the agency relationship between contractor and exempt entity.
  - Subcontracts can also qualify if they comply with similar provisions.
  - (Revenue Notice No. 17-10, Minnesota Department of Revenue, December 4, 2017)

State Tax Treatments for Flow-Through Exemptions (cont.)

- In *Kern-Limerick, Inc. v. Scurlock*, contractors' purchases of machinery in Arkansas for use in building a military building for the federal government were found to be exempt because the contractors were designated purchasing agents of the federal government and title of the purchased items passed directly to the federal government from the vendor.

State Tax Treatments for Flow-Through Exemptions (cont.)

- In Illinois, exempt entities that have been issued a sales tax exemption identification number are granted flow through exemptions on contractors' purchases. The exempt entity must supply its exemption certificate to the contractor who will then supply this same certificate to its suppliers to satisfy the exemption documentation requirements to the supplier.
- (86 Ill. Adm. Code 130.2075)

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State Tax Treatments for Flow-Through Exemptions (cont.)

- In order for an exemption for a governmental or exempt entity to flow through to the contractor in Alabama, the contractor must be appointed as a purchasing agent.
- Form ST:PAA-1, Purchasing Agent Appointment will allow an exempt entity to appoint a purchasing agent to act on their behalf when making tax-exempt purchases.
- A contractor may also use this form to appoint subcontractors to make tax-exempt purchases on behalf of the exempt entity.
- *(Rule 810-6-3-.69.02, Alabama Department of Revenue, effective January 5, 2010)*

State Tax Treatments for Flow-Through Exemptions (cont.)

- States including North Carolina, North Dakota, Tennessee and Washington do not allow flow through exemptions for any type of exempt agency.
- Other states may allow the flow through exemption for some but not all types of exempt organizations.
  - MI allows for charitable and religious organizations but not for governmental, educational or tribal organizations.
  - WI allows for charitable, religious, educational, tribal and local government organizations but not for any federal or state governmental agencies.

Idaho Issues New Exemption Certificate for Real Property Contractors

- Idaho has issued a new sales tax exemption certificate for real property contractors who work on projects that qualify for exemption. These can include
  - Agricultural Irrigation
  - Data Center
  - Production Equipment
  - Pollution Control
  - Qualified Clean Room or qualified semiconductor
  - Installation in a nontaxing state
- The new certificate – Form ST-103C – can be downloaded at https://tax.idaho.gov/taxes/sales-use/ under "Forms & Instructions."
- Contractors who make improvements to real property should use the new Form ST-103C instead of Form ST-101.
- (Press Release, Idaho State Tax Commission, September 1, 2022)

Rate Increases During Term of Contract

- Due to the nature of construction contract taxation, many states provide a "grandfather rate" provision such that if there is a rate increase during the term of a fixed fee contact entered into prior to the rate increase, the contractor is eligible to pay the prior rate for a period of time.
- In Illinois, property delivered to a construction contractor after the effective date of a rate change for use in a binding construction contract entered into before the rate change is taxed at the rate in effect before the increase, provided the contractor is legally unable to shift the burden of the rate increase to the customer.
- (86 Ill. Adm. Code 130.101(a)(2); 86 Ill. Adm. Code 150.115(b))

Rate Increases During Term of Contract (cont.)

- In Oklahoma, contractors who purchase taxable materials, supplies, and equipment to comply with their contractual obligations subsequent to entering into a contract can use the tax rate effective at the time the contract was initially entered into. This is accomplished through a refund system. Purchases are made at the current tax rate and the contractor has the option to file for a claim for refund. The deadline to apply for the refund is by when the contractor has satisfied its obligation or two years from the date on which the contract was entered into, whichever occurs first.
- (OK Rule 710:65-13-70)

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Rate Increases During Term of Contract (cont.)

- For construction contractors entering into lump-sum or fixed fee contracts, language should be incorporated into the contract to allow for reimbursement of increased tax costs related to tax rate increase situations that exceed a specified contract threshold.
- Customers should request that this clause also permit for refunds if there is a tax rate decrease.

Rental of Equipment with Operator

- The tax treatment of a transaction can vary depending on rental of equipment vs. rental of equipment with an operator.
- Rentals of equipment with an operator are often classified as a service rather than a rental
- To qualify, control and operation of the equipment must remain with the provider

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Washington Amends Lease and Rental Excise Tax Rule for Certain Construction Scenarios

- The Washington DOR has made amendments to the state's excise tax rule on leases or rentals of TPP to clarify its policies regarding charges for specific construction services.
- The rule revision clarifies the distinctions between charges for the rental of concrete pumping equipment with an operator.
- In Washington, equipment rentals without an operator and leases of operated equipment are generally subject to the retailing B&O tax. In certain scenarios, when services are eligible for resale, the wholesaling B&O tax may apply.
- The rule revision provides several examples.

Washington Amends Lease and Rental Excise Tax Rule for Certain Construction Scenarios (cont.)

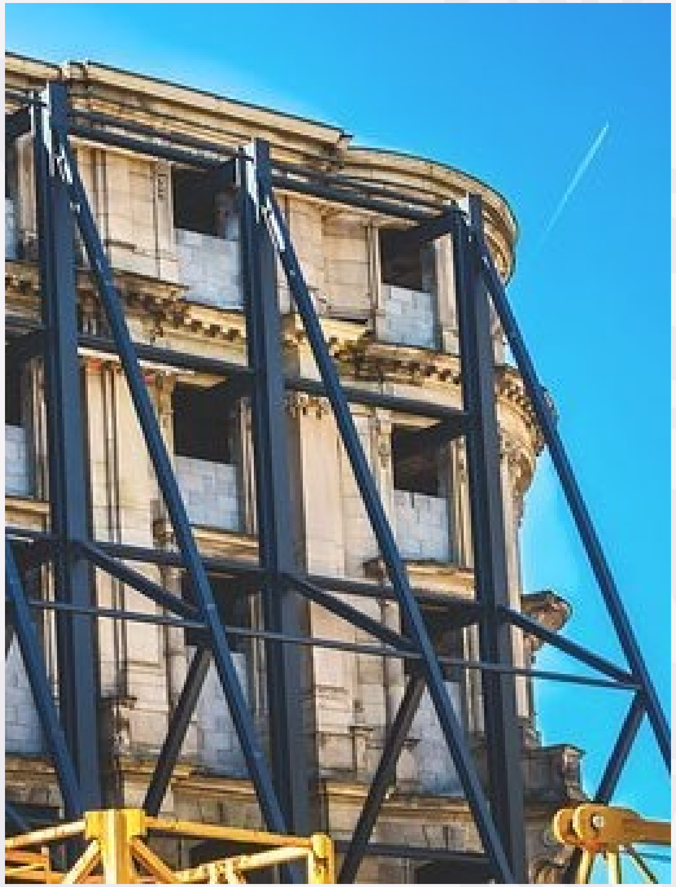
- Example 1: A prime contractor hires a concrete pumping company to pump premixed concrete. The concrete pumping company operates its own equipment but does not provide the concrete mix. The stand-alone concrete pumping services are classified as a rental of equipment with an operator. The charges are subject to retailing B&O tax and retail sales tax.
- Example 2: A subcontractor is hired by a prime contractor to pave a parking lot. The subcontractor uses its own equipment. The prime contractor provides the subcontractor with a reseller permit. The subcontractor's activity is classified as a construction service and not "rental of equipment with an operator." The charges are subject to wholesaling B&O tax, as construction services are eligible for resale.
- (WAC 458-20-211, Washington Department of Revenue, effective April 23, 2021)

New York Capital Improvement Rules

- In New York, capital improvements are not considered taxable sales. However, the contractor or whoever purchases tangible personal property that is added to or incorporated into real property by a capital improvement is subject to tax when purchased.
- The sales tax paid on the purchase price of the materials by a contractor can be passed through as part of the cost of the project but should not be separately stated as tax
- The customer must issue a Certificate of Capital Improvement to the contractor in order to exempt the purchase of the capital improvement contract of an addition or improvement to real property
- Capital improvements can be commercial or residential property

New York Capital Improvement Rules (cont.)

- Capital Improvement definition - An addition or alteration to real property which:
  - substantially adds to the value of the real property or appreciably prolongs its useful life;
  - becomes part of the real property or is permanently affixed to it so that removal would cause material damage to the property or article itself; and
  - is intended to become a permanent installation.



New York Capital Improvement Rules (cont.)

- Leasehold Improvements
  - Additions or alternations to leased property made by or for a tenant may not qualify as a capital improvement
  - If the lease agreement requires that the lessee return the property to its original condition or if the leasehold improvements do not transfer to the property owner, then these will be considered taxable repair or installation

Hawaii Subcontract Deduction

- In Hawaii, payments by a contractor (prime contractor) to another contractor or specialty contractor qualify for the subcontract deduction if:
  - The prime contractor and subcontractor or specialty contractor are licensed under the GET (general excise tax) law;
  - The name and general excise number of the subcontractor or specialty contractor and the amounts paid are listed on the prime contractor's GET return
  - The amounts are paid to a subcontractor or specialty contractor who is:
    - A contractor, as defined in section 237-6, HRS
    - A specialty contractor, duly licensed by the DCCA pursuant to section 444-9, HRS; or
    - A specialty contractor who is not licensed by the DCCA pursuant to section 444-9, HRS, but who performs contracting activities on federal military installations and nowhere else in Hawaii.
- (Hawaii DOT Announcement No. 99-25)

Special Tax Planning Opportunities

Enterprise Zones

- Many states provide for additional exemptions for projects located in Enterprise Zones.
- In some jurisdictions, the exemptions are very broad while in others they are restricted.
- Pre-approval eligibility requirements are also common and may be required.

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Enterprise Zones (cont.)

- New York contractors may claim a credit or refund for tax paid on qualifying materials incorporated into an Empire Zone. There are over fifty Empire Zones in New York.
- Qualified exempt purchases include building materials used in constructing, expanding, or rehabilitating industrial or commercial real property in a zone. Credits or refunds of sales and use taxes paid are available from the state and may be available from local jurisdictions in some cases.
- The person eligible to claim a refund or credit is whoever, under the tax law, has the liability for payment of the sales tax due on purchases of tangible personal property, whether it is the tenant/property owner or the contractor.
- Note: The Empire Zone program is closed to new entrants.

Moveable Property

- Because contractors are liable for tax on all equipment used in construction projects, contractors who operate in numerous states face the burden of multistate taxation.
- Not all states have a temporary storage exemption. This poses special problems for construction contractors.

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Moveable Property (cont.)

- For example, if a construction contractor is located in State A and buys a piece of equipment from a vendor located in State A, but takes possession of the equipment in State B, if there is no temporary storage exemption in State B, the contractor must pay State B's tax on the equipment.
- When the contractor moves the equipment to State A, the contractor will owe tax to State A on the depreciated value of the equipment, and a credit may be allowed for tax paid originally paid.
- As the equipment is used in various states, the contractor must pay close attention to what depreciation method each jurisdiction uses so that tax is correctly assessed.

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Cross Border Implications

- The North Carolina Court of Appeals ruled that TPP procured outside the state, such as building components, is subject to use tax when it becomes part of a building or structure in NC.
- Materials are not exempt despite being moved into the state in a different form than in which they were first purchased (e.g. assembling materials into trusses, columns, purlins, and metal panels).
- The Court also clarified that even if materials were bought, stored, and transformed into building components outside the state, incorporating these materials into buildings constructed in NC constituted "use" and subjects them to use tax.
- *(Morton Buildings, Inc. v. Tolson*, No. COA04-1053, August 2, 2005)

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Overall Tax Planning

- Sales and use tax planning is only one aspect of tax planning for construction projects.
- From a property owner's perspective, it is important to evaluate all tax aspects and the various different contract structures to determine the most advantageous structure.
- Classification of items as real property may result in sales tax benefits but result in property tax assessments or incur a longer depreciation period for income tax purposes.

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Overall Tax Planning (cont.)

- When dealing with projects that involve multi-state suppliers, it is important to ensure that the method of obtaining materials related to an exempt project does not jeopardize the exemption.
- For example, if an exempt project is located in State A, but the contractor picks up materials in State B to transport back to State A for use, it is possible that State B will not honor the exemption. If the items were shipped to the job site by the supplier, the exemption would apply.
- SST Disclosed Practice #9 does provide guidance for cross border situations

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Overall Tax Planning (cont.)

- Sales and use tax minimization usually occurs if property is classified as real property. However, in some situations, sales tax exemptions may be lost if the property is classified as real rather than personal property.
- This is especially true in relation to machinery and equipment and these types of contracts should be evaluated.
- In addition, if the machinery is purchased and installed by the contractor the exemption may be lost as some jurisdictions limit the exemption to direct purchases by the manufacturer.

Audit Considerations

Audit Considerations

- Construction contractors are prime targets for sales and use tax audits.
- States may audit the entire operations for the audit period, or they may audit specific projects on a stand-alone basis.

Audit Considerations (cont.)

- Although auditors typically will review all purchases and sales, auditors pay close attention to the taxability and use of construction equipment.
- For this reason, and because construction equipment is a high-cost area of operations, it is important that construction contractors take special care and maintain supporting documentation when determining the taxability of such equipment.
- Make sure to document what materials were incorporated into the building vs. what materials were used/consumed.

Audit Considerations (cont.)

- Contractors who do work for government or other exempt entities will be required to provide all exemption documentation to support exempt purchases.
- Contractors who also operate as retailers need to maintain appropriate records distinguishing purchases for resale and purchases for incorporation into real property.
- Because audits are likely, construction contractors should ensure that the construction contract includes specific information about responsibility for taxes and access to the project site for audit tour purposes when needed to resolve an issue.

Audit Considerations (cont.)

- There is a benefit to require the customer and contractor to meet on the front end of a project and discuss the taxability of the project components and provide applicable training to personnel that will be involved with invoicing and compliance processes.
- Development of a tax matrix that both parties agree upon is also recommended and many times becomes a component of the contract for reimbursement or indemnification situations.

Other Real Property Transactions

Property Managers

- Property managers deal with maintenance and janitorial services, lease agreements and build outs.
- Build out/leasehold improvements
  - If the lessee pays an up-front cost for the build out, then it qualifies as construction
  - The landlord may need to charge sales tax on this transaction if they are deemed the contractor in certain states
  - In Texas, the repair or remodeling of nonresidential or commercial real property is a taxable service

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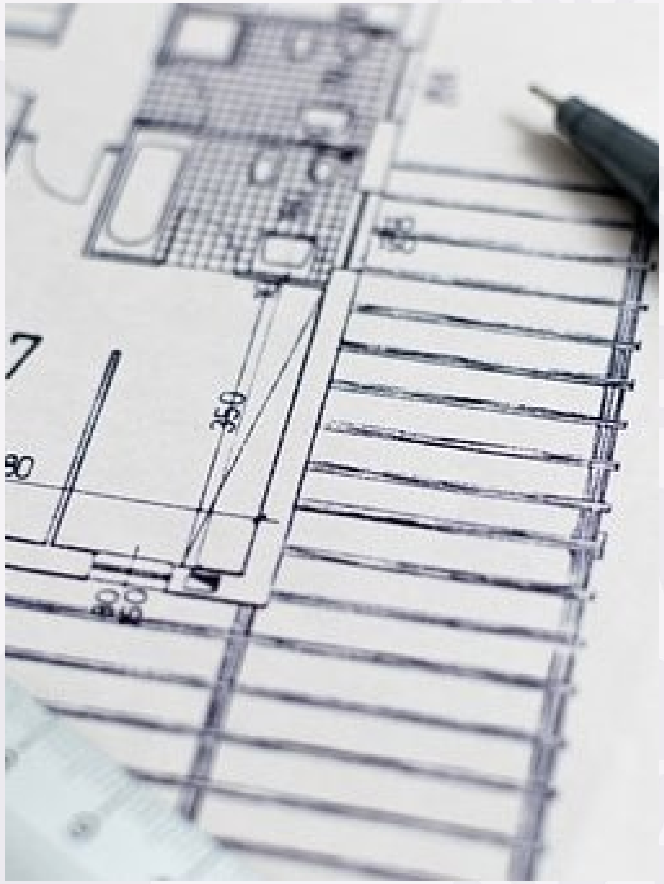
Property Managers

- Real Property Repairs
  - If the property manager charges for repairs and parts and they are the "seller" they are required to be registered retailers and charge tax according to rules in the property state.
- Janitorial Services
  - In states that tax janitorial services, if the property manager is the provider, tax should be charged on the service.
  - If a third party provides the service, rules can vary as to whether a resale certificate should be issued by the property manager.

Architects

- Usually, an architect’s services are non-taxable. Delivering the original blueprints is usually not taxable.
- Copies of blueprints are often considered a taxable sale of tangible personal property.



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Interior Designers

- Interior designers often procure items, mark them up and sell them to their customers. In this instance, they are considered retailers and are required to collect and remit sales tax on the sale of these items.
- "Custom" items such as draperies and window coverings are taxable tangible personal property even if the labor is separately stated.

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Carpeting

- States may have different tax treatments for carpeting depending on how it is installed into the real property – glued down vs. tacked down.
- Illinois has issued *Informational Bulletin FY 2000-18, Illinois Department of Revenue, May 1, 2000* regarding the installation method of carpet:
  - Carpet that is sold installed by using tacks, staples, or tacking strips is treated in the same manner as carpet that is sold installed by gluing it down. All of these methods of installation are considered permanent installations of personal property into real estate.
  - Previously if carpet was sold and installed by using tacks, staples, or tacking strips, you were responsible for collecting and paying Retailers' Occupation Tax on the selling price of the carpet.

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Impact of South Dakota v. Wayfair

Impact of South Dakota v. Wayfair

- For contractors, generally there is a bigger focus on nexus now, but if you are going on-site in a state, you have physical nexus in that state and the economic nexus thresholds are irrelevant.
- If you are a supplier to contractors, you need to keep track of where you are drop shipping, which can create nexus issues.

Impact of South Dakota v. Wayfair (cont.)

- For purchasers, it is more important than ever to review the tax charged by suppliers.
- In states where the tax is on the contractor, the customer still does not owe use tax. But contractors may not know the rules if they are from another state.
- Very few purchasers have a formal regular process of reviewing tax paid to vendors.
- In many cases, the tax department does a review of transactions identified for use tax accrual but no review at all of invoices where the vendor charges tax.
- Monitor for vendors that you buy exempt items from to make sure you've issued the right exemption certificates to them .

Impact of South Dakota v. Wayfair (cont.)

- Review or implement a vendor tax validation process.
- If you're using a managed compliance rate, review to see if vendors are charging you tax.
- As more suppliers start charging tax, the opportunity for reverse audits will increase. This is an area of opportunity for refunds.

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Resources

- Remote Seller Nexus Chart: https://www.salestaxinstitute.com/resources/remote-seller-nexus-chart
- Remote Seller Resources page: https://www.salestaxinstitute.com/resources/remote-seller-resources

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Questions & Comments

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- Join the Sales Tax Institute's Linked In group, exclusively for Sales Tax Institute course attendees!

  https://www.linkedin.com/groups/12048069

- Post questions, ideas, practical suggestions and news updates that you think will be relevant to other Sales Tax Institute alumni.
- We will be moderating the group and we will remove inappropriate content posts so that this stays as a resource for our students to help them develop their sales tax expertise and ask questions.

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- Webinars on-demand – New courses now available!
  - NEW! Use Tax Accrual for Automated and Manual Processes
  - NEW! Software, Digital Goods, NFTs and Digital Currency: What You Need to Know for Sales Tax
  - Registration Deep-Dive
  - Compliance Deep Dive
  - Sales Tax 101
  - Administering the Sales Tax Function
  - Drop Shipments: What Are They and What's New Post-Wayfair?
  - Great Exemption Adventure
  - Sales Tax Challenges with Services – Freshly Updated!
  - Starting a New Business or Initiative: What You Need to Know for Sales Tax
  - Audit Empowerment: Techniques and Tips to Pass Your Next Audit
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Use Tax Accrual for Automated and Manual Processes

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March 29, 2023

Diane L. Yetter

- Strategist, advisor, speaker, and author
- President of YETTER
- Founder of the Sales Tax Institute
- Testified before Senate Finance Committee
- Accounting Today's 100 Most Influential People in Accounting for 8 times between 2011 and 2022
- Woman Business Owner of the Year 2020

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Introduction

Consumer's Use Tax

- "Use" : the **storage, use or consumption** of **taxable** property or services and includes the **exercise of any right or power** incident to the ownership of the property
- Use Tax
  - Complementary to sales tax and does not apply if sales tax charged
  - Applies to purchases made outside the taxing jurisdiction but used within the state
  - Also applies to items purchased exempt from tax, but subsequently used in a taxable manner

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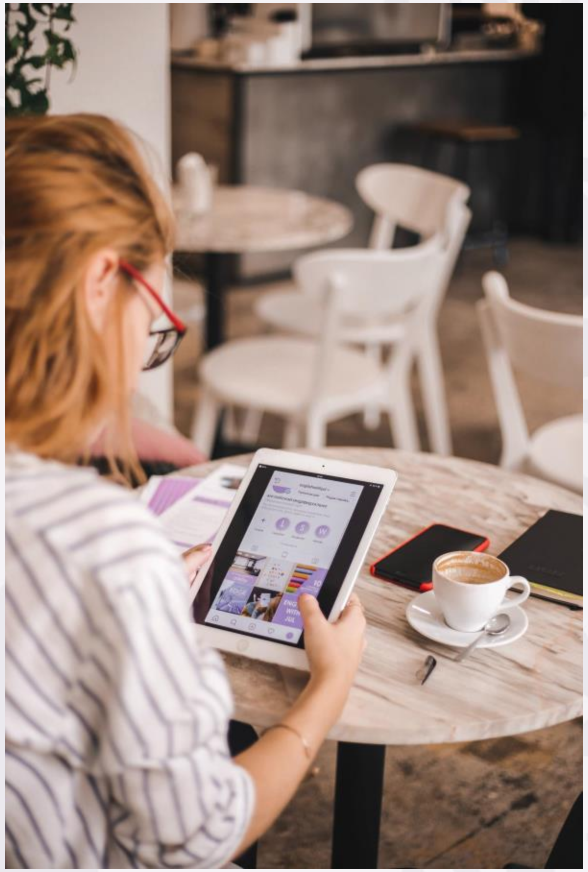
Consumer’s Use Tax

- Purchases of taxable property where the seller did not collect sales or seller’s use tax are subject to consumer’s use tax
  - The determination of the correct local rate to apply generally follows the seller’s use tax rules
  - However, in some states, if the seller and purchaser are located in the same state, special rules may apply
  - In some instances, the tax is imposed on the seller and if the purchaser did not provide an exemption certificate to the seller, the purchaser does not owe the consumer’s use tax. This is very state specific and the particular rules must be reviewed in detail.



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NC Supreme Court Rules Against Sales and Use Tax Distinction in Wisconsin Taxpayer's Appeal

- The Supreme Court of North Carolina ruled to uphold a sales tax assessment against a Wisconsin based printer, rejecting the taxpayer's argument that they could not be subject to sales tax under the 1944 U.S. Supreme Court decision *McLeod v. J.E. Dilworth Co*.
- The *McLeod* ruling created a clear distinction between sales tax and a use tax in interstate commerce, defining sales of goods that occurred outside of a state that were delivered into the state via common carrier as out of state sales that could not be subject to sales tax under the Commerce Clause.
- In a companion case, *General Trading Co. v. State Tax Comm'n*, the court clarified that a use tax could be required to be collected in similar circumstances, as the tax was on the in-state consumer's use of the product rather than on the out of state sales.

NC Supreme Court Rules Against Sales and Use Tax Distinction in Wisconsin Taxpayer's Appeal (cont.)

- The printer argued they delivered their sales from out of state to a common carrier, and because the assessment on the business was for sales tax, the assessment was invalid under *McLeod*.
- The Court determined that more recent rulings - *Complete Auto Transit v. Brady* (1977) and *Wayfair v. South Dakota* (2018) – contradicted the 1944 rulings and overruled their precedent.
- The state's decision also clarified that, because both the state's sales and use tax are based on the destination at which the purchaser takes ownership of the property sold, the imposition of sales rather than use tax on out of state sellers fulfilled *Complete Auto*'s four-part test.
- (Quad Graphics Inc. v. North Carolina Department of Revenue, 407A21-1, North Carolina Supreme Court, Dec 16, 2022)

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Use Tax Determination Process

Challenges with Use Tax Determination

- Items in question are unknown
- Ship-from information missing
- Location of where items will be used is unknown
- Tracking and documentation of who paid taxes and when
- Record maintenance and audit readiness
- Manual tax determination in purchasing or payables departments is dependent on non-tax professionals making decisions
- Employee turnover and limited training resources contribute to the problem

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What is Purchased?

- Tangible Personal Property – can be perceived by the senses: see/feel/smell
- Intangible Personal Property – patents, copyrights, contracts, some digital items
- Real property – land, buildings, fixtures, and structures that are permanently affixed to real property
- Services – generally defined as occupation/function of performing an activity to satisfy a public demand
  - Services may include transfer of tangible personal property
  - What is the *true object* of the transaction?

Use Tax Base

- The value of the items that are subject to sales or use tax
- Generally defined as the total amount of the sales price, without any deduction for the cost of the goods sold, interest paid, other expenses or transportation
- Taxable and Non-Taxable components must be separately-stated or the entire cost becomes subject to tax. There are a few exceptions to this rule if the taxable component is incidental to the non-taxable portion.

Measuring Use Tax

- Use tax base on self-consumed property purchased exempt from tax can be based on:
  - Material cost - only the value of raw materials at purchased cost.
  - Inventory or standard cost (raw cost) - the direct cost of placing the property into inventory.
  - Full retail or fair market value - the price at which the property is sold to your customers.
- States vary on which value they use in measuring the cost price. This must be researched for each state.

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Measuring Use Tax (cont.)

- Based on an annual survey of state tax departments conducted by Healy & Schadewald:
  - 21 states use the raw material cost (e.g. Colorado, Illinois)
  - 9 states use the full inventory cost (e.g. Arizona, Florida)
  - 4 states use the full inventory cost or raw material cost (e.g. Kentucky, Maine)
  - 10 states use the retail price (e.g. Massachusetts, Washington)

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Use Tax Base

- The tax base may be adjusted for exemptions, exclusions, or deductions that are determined by specific statutory authority
- Exclusions could include:
  - Discounts
  - Trade-ins
  - Freight and transportation charges (freight out),
  - Installation
  - Interest, finance or carrying charges
  - Refunds and returns
  - Other taxes and licenses

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Possible Tax Exemptions

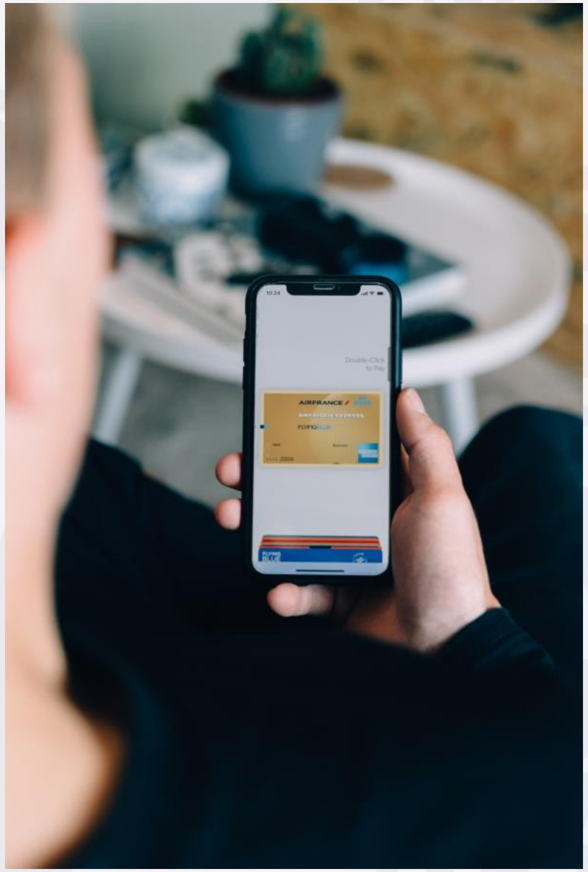
- Usage Based Exemptions
  - Resale
  - Manufacturing
  - Pollution Control
  - Research & Development
  - Agriculture
  - Enterprise Zones
  - Incentives
  - Temporary Storage

Nebraska Provides Guidance on Use Tax

- The Nebraska DOR released guidance on the handling of use tax in the state, specifically noting the following exempt situations:
  - When property from a taxable transaction was first used for its intended purpose in another state (does not apply to motor vehicles, motorboats, or airplanes)
  - When property from a taxable transaction is only stored temporarily in the state
  - When building materials are taken from inventory to a construction product outside the state
  - When purchases are made from "commissaries, base exchanges, ships' stores, or voluntary, unincorporated organizations of personnel of any branch of the Armed Forces of the U. S. by any person authorized to make these purchases.
  - (Nebraska Use Tax Information Guide, Issued March 2021)

Direct Pay

- Most states authorize direct pay authorities
- May be restricted as to who can qualify
- Benefits
  - Delay tax payment until use occurs
  - Minimize tax payments on temp storage in different location than use
  - Control over taxability determination
- Risks
  - Full responsibility for use tax payment
  - Likely regular audits



Converted Inventory

- Use includes the conversion of property purchased exempt from sales tax that is used in a taxable manner.
- This includes samples, donations and converted inventory for self use.

When Use Occurs

- Use tax applies when “use” in the state occurs
- Withdrawal from inventory can be deemed the “use” even if goods are subsequently shipped out of state
  - Contractor/Retailers – Morton Building Cases
  - Donations - YAMAHA CORPORATION OF AMERICA, Plaintiff and Respondent, v. STATE BOARD OF EQUALIZATION (1999)
  - Service Providers

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California Taxpayer Liable for Use Tax on Repair Parts Used for Out-of-State Customers

- California held that a taxpayer under audit was liable for use tax on parts used to repair equipment in California as part of optional lump-sum maintenance contracts for out-of-state customers.
- The taxpayer purchased repair parts without paying sales tax. The taxpayer stored the repair parts in its California facility until it withdrew the parts from resale inventory to perform repairs.
- The taxpayer's customers would ship equipment needing repair to the taxpayer's California facility. After performing the repairs, the taxpayer would ship the equipment back to the customers.
- The taxpayer argued that it was not the consumer of the repair parts and that the parts were consumed by the customer when the repaired equipment was used for its intended purpose.

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California Taxpayer Liable for Use Tax on Repair Parts Used for Out-of-State Customers (cont.)

- The state relied on two state regulations pertaining to optional warranties/maintenance contracts to determine that the taxpayer is the consumer of the parts and materials furnished and therefore liable for use tax on the repair parts.
- The state found that the property was not used solely outside the state since the repairs, which are taxable use, occurred in California.
- The taxpayer was liable for a negligence penalty in addition to the tax due since it had failed to correct similar errors identified in prior audits.
- (In the Matter of the Appeal of Olympus Am. Inc., 2023-OTA-087 (Cal. OTA Dec. 20, 2022)

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Vendor Tax Validation

- Vendors charge tax where they have nexus – not necessarily where the customer has nexus
- Risk of incorrect tax being charged as more vendors are required to register post-Wayfair.
  - Lack of certificate – Vendors may be charging tax because you didn't previously give them a certificate.
  - Uncertainty of taxability
- When a vendor has charged tax on the transaction, the seller should validate that the tax is correct
  - Jurisdiction Validation – has the vendor taxed the correct jurisdiction?
  - Taxability Validation – is the item subject to tax in the jurisdiction where it is delivered and used?
  - Rate Validation – if the item is taxable, did the vendor use the right rate based on the item and jurisdiction?

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Vendor Tax Validation (cont.)

- Implementing Corrective Actions
  - Enter the vendor tax in the voucher header in the AP system
  - Be sure to issue exemption certificates when applicable
  - Communicate timely with vendor so they can fix the problems
  - If you short pay, be sure to send communication with reasons and documentation
  - If you file a refund claim, provide all necessary documentation and do it timely

Determination of Correct Rate

- The location of use typically is the jurisdiction that drives the tax rate
- Purchase and use in an origin tax state results in tax due at the suppliers location
- Purchases for use in a home rule locality could result in buyer’s obligation to accrue only the local tax

Procurement Processes

Procurement Payment Methods

- In addition to traditional Accounts Payable processes, there are a number of alternative processes that businesses use
- Some of these create additional challenges with use tax determination due to lack of integration or human review
- Tax professionals should coordinate with Payables professionals to minimize tax risks

Procurement Card Transactions (P-Card)

- Corporate credit cards used to purchase goods without completing a purchase order
- Allows companies to make high-volume low-cost purchases while reducing the cost of processing purchase orders and checks

Procurement Card Transactions (P-Card)

- P-Card Use Tax Issues
  - Sales tax information needs to be retained for state audit purposes
  - Determining when and where sale took place
  - Ascertain whether sales tax was collected by vendor
  - Maintaining detailed transaction records to determine what was purchased

Procurement Card Taxability Issues

- Programs can be established to minimize tax implications
- Examples of Authorized Uses:
  - Local vendors who collect tax
  - Taxable-only transactions
  - Exempt-only transactions
  - Expense purchases
  - Asset purchases
  - Travel & Entertainment

E-Procurement

- The E-Procurement model is essentially an online store where approved items and negotiated pricing make it easy for any employee of a purchasing company to purchase items (e.g. office supplies).
- It reduces how much work the Procurement Department needs to do.
- Examples of E-Procurement providers are SAP Ariba and Coupa.

E-Procurement

- One of the use tax challenges with E-Procurement is that the products are onboarded by the E-Procurement provider in conjunction with the suppliers, which means that product categories are not necessarily something that the buyer can control.

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Evaluated Receipts Settlement

- Evaluated Receipts Settlement (ERS) is a payment method designed to eliminate the need for a supplier to provide an invoice to the customer
- ERS payments are calculated based on the quantity received by the customer times the unit price on the purchase order
- In an ERS transaction, the vendor does not issue an invoice.
- The customer must determine the tax to be paid to the vendor

Evaluated Receipts Settlement

- For companies using an ERS process, it is vital that purchasers know the vendor’s tax nexus profile.
- Purchasers should maintain the taxability jurisdictions of the supplier
  - Purchasers need to be able to calculate the correct amount of sales tax on goods received as if they were the vendor.

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Evaluated Receipts Settlement

- Once the tax is calculated, the purchaser should remit the sales tax to the vendor for states where the vendor is registered as the vendor is liable to remit the tax to the state
- Note that purchasers should not remit sales tax to the vendor for jurisdictions where the vendor is not registered to collect and remit sales tax. In these cases, the purchaser must accrue and pay use tax on the taxable purchases.
- Regular review of vendor nexus profile should occur

Evaluated Receipts Settlement

- Accounts Payable processes must be able to differentiate between registered and non registered vendors by state of delivery
- Posting rules must be able to appropriately post the vendor remitted tax to the vendor payable account but accrued use tax to the tax payable account

Evaluated Receipts Settlement

- When negotiating ERS with vendors, be sure to consider the following points:
  - Direct Pay Status – if the buyer has direct pay authority this will make ERS much easier as tax does not have to be paid to the vendor
  - Vendor Registered States – ensure there is a regular process to obtain updated information from the vendor including local registration

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Evaluated Receipts Settlement

- When negotiating ERS with vendors be sure to consider the following points (cont.):
  - Vendor Tax Rates – be sure the vendor provides all physical ship from locations and also indicates these on the delivery documentation
  - Exemption Notification – provide all exemption certificates that could apply in advance and in a timely manner as they change

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Automated Data Feeds

- Many AP departments are working with vendors to receive data files in lieu of individual invoices in order to minimize data entry time and errors
- These data feeds typically are used for high volume vendors
- These vendors could represent transactions that are not sales tax relevant transactions such as telecommunication, travel and benefits or high volume transactions like office supplies

Automated Data Feeds

- The AP department needs to ensure that key data elements needed to determine taxability are included in automated data feeds
  - Line level data from invoices, not just the total purchase amount
  - Information related to the items purchased such as material numbers or material groups
  - Tax codes and the amount of tax charged should be included for each transaction
  - Ancillary or header items like freight need to be identified separately

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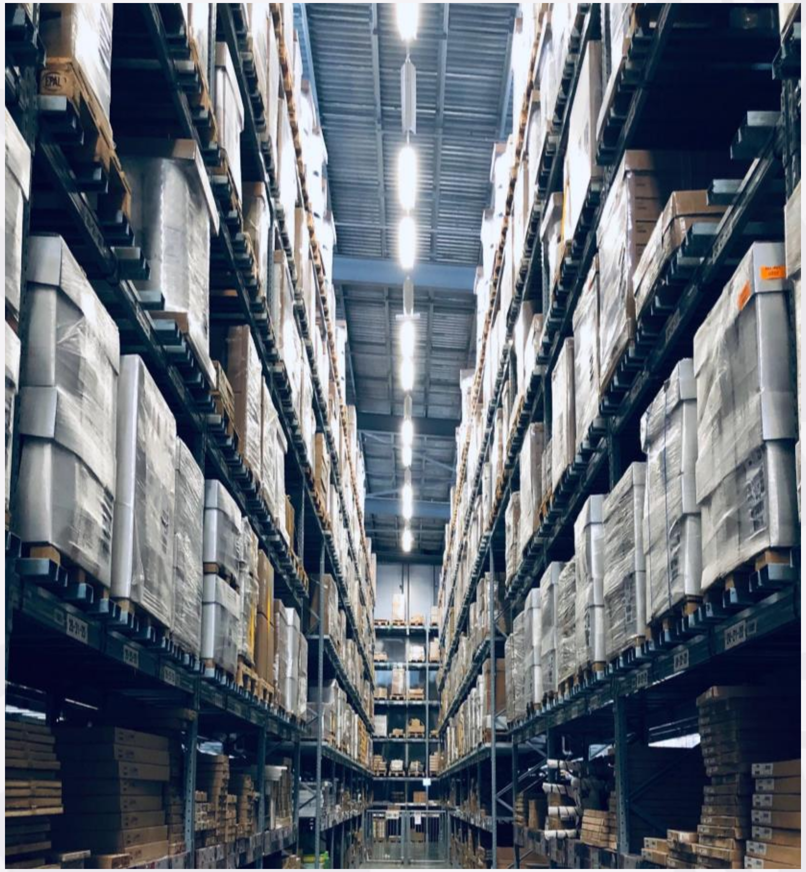
Use Tax Challenges

Procurement Taxability Determination

- Determination of taxability on purchases can be based on various parameters and can vary based on the type of transaction.
  - Product Identification
  - Product Class
  - Account Number
  - Asset/Project Number
  - Cost Center
  - Usage Indicator



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Procurement Taxability Determination

- Expense Purchases - item master taxability can be based on:
  - Item number
  - Location of use
  - Nature of use

Procurement Taxability Determination

- Non-Stock Purchases
  - Lack of item identification
  - Non-standard identification
  - Cost Center/ Profit Center and GL Account can help in making the determination of what the item is and its taxability determination.

Procurement Taxability Determination

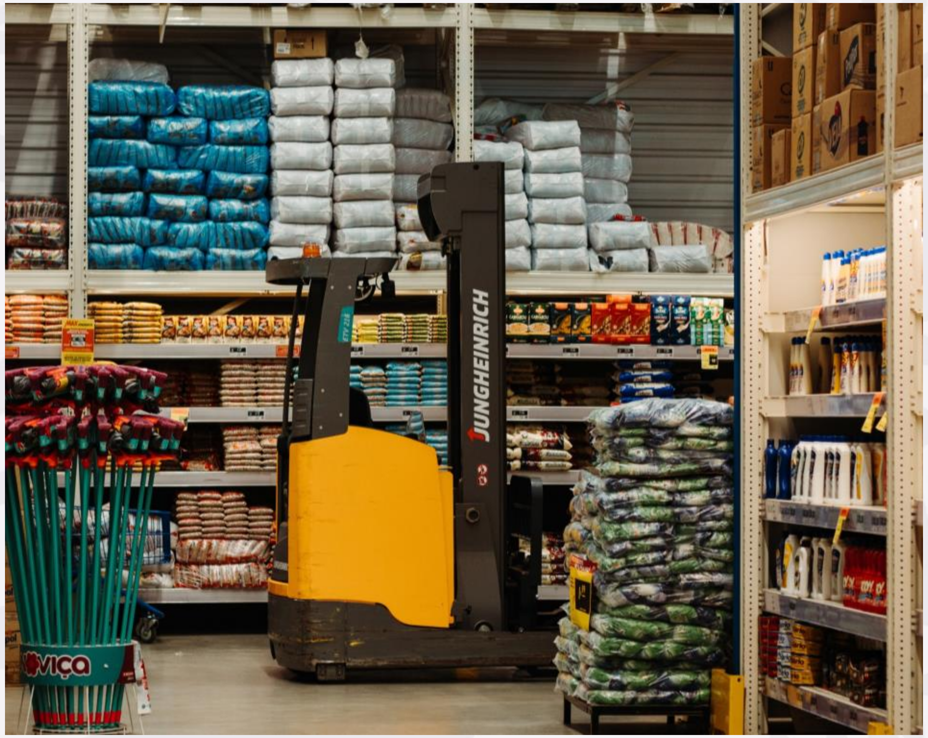
- Asset Purchases
  - Project vs. Item taxability could vary
  - Nature of item
  - Use of item
  - Bundling of contracts

Procurement Taxability Determination

- Digital Goods
  - Classification of Digital Goods
  - User location
  - Value allocation
  - Bundling with services or tangible goods

Procurement Taxability Determination

- Movable Goods
  - Tax paid on original purchase documentation
  - Value at time of move
  - Credit for tax paid
  - Differing taxability
- Temporary Storage Items
  - Claiming temporary storage exemption
  - Documenting duration and any use



Audit Activity

State Audit Activity

- Post-Covid we are seeing audit activity increase
- Consumer's Use Tax is being questioned even on remote seller audits
- Penalties are being assessed more aggressively for non-compliance.
- Subsequent audits without corrective actions are being assessed higher penalties or automatic penalties.

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How States Target Possible Audits

- Nexus inquiries
- Late filed returns
- Large refund request
- Large fluctuations in tax liabilities reported
- Audits of your partners
- Audits of Direct Pay Percentage Allocations
- Recurring compliance issues

NO USE TAX REMITTED

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Audit Defense Best Practices

- Indicate vendor tax amounts on payable transaction after validation
- Accrue use tax on purchases on which no tax was paid
- Don’t pay tax to a supplier when it wasn’t charged – including local taxes
- Post use tax accrual to a separate GL account from sales tax collected
- Timely issue exemption certificates to suppliers as well as documentation for any short payments of tax
- Maintain documentation on tax status and tax payments on goods movement transactions
- Determine correct value of converted assets for use tax
- Understand what constitutes use vs sale

Use Tax Automation Tools

Key Components of Any Solution

- Taxability Determination
- Vendor Tax Validation
- Rate Determination
- Tax calculation
- Tax Accrual
- Transaction Detail Reporting

Data Elements for Use Tax Determination

Sample Data Elements that can help with Tax Determination

- Vendor Name/Code
- Product/SKU
- Material Group
- GL Account
- Cost Center
- Plant Number
- Line of Business
- Asset Number
- Project Number
- Usage Indicator
- Purchasing Agent
- Vendor Type (inventory, supply, etc.)

Automated Solutions for Use Tax Determination

- Automated Tax Systems
  - Most sophisticated option
  - Will limit the risk of errors
  - Aim for about 80% accuracy
  - Consistent decisions are driven by automated generalizations
  - Will likely need to create tax matrices
- Evaluate the cost
- Real time and Batch options for integration
- Evaluation of Tax Software Functionality and Partners

Automation and Compliance Alternatives

- Manual review and identification
  - Selective Vendor Accrual
  - Selective GL Account Accrual
- Create Excel Spreadsheet or copies of invoices put to side or in digital file
- Mark vendor invoices with a stamp or the use tax accrual account

Automation and Compliance Alternatives

- Managed Compliance Agreements
  - In lieu of specific transaction evaluation for use tax
  - Determine a use tax accrual rate based on a sample review to report use tax
  - To limit risks, participate in state approved program
  - State sets up specific guidelines
  - Taxpayer or third party performs the audit work
  - State reviews the taxpayer's work
  - Could be used with an automated solution

Automation and Compliance Alternatives

- Simplified Automated Process
  - Involve Purchasing to indicate taxable or exempt on PO
  - AP inputs a simple code on AP Invoice
    - 0=Taxable and tax charged
    - 1=Taxable and no tax charged
    - 2=Exempt and no tax charged
    - 3=Exempt and tax charged
  - Tax department accrues tax on all coded “1” and files refund claims on all “3”

ERP Accounts Payable Solution

- Most ERP systems have some sort of tax functionality
- Depending on your needs, this could be sufficient
- Typically rely on AP Staff to make taxable/exempt determination and select the correct tax code
- Likely requires maintenance of tax rates within the ERP in order for tax calculation and accrual to post

Automated Tax Engine Solutions

- Batch vs. Interactive (real-time) options
- External “bolt-on” solution to ERP/AP system
- Includes tax rates including effective dates
- Includes special rate rules like max taxes in most cases
- More sophisticated solutions include taxability rules

Automated Tax Engine Solutions

- Allow mapping of data elements to create tax rules
- Some solutions allow “if-then” rules to allow for assumptions when data is unavailable

Procurement Card Use Tax Solutions

- Use Tax Accrual Percentages
  - Similar to Managed Compliance Agreement
  - In lieu of actual determination, use test to determine percentage for accrual
  - Update based on business and law changes

Procurement Card Use Tax Solutions

- Automated Use Tax Integrated with Reconciliation
  - "Tax Included" Check Box
  - Jurisdiction assigned to card holder or cost center
  - Taxability based on "usage code" input by card holder
  - Generate extract file and process in tax solution in a batch process
  - Typically only used for invoices without tax since can't adjust the tax amount

Automated Solutions Third Party Vendors – Tax Calculation Engines

- AccurateTax - www.accuratetax.com
- Avalara - www.avalara.com
- Ryan – www.ryan.com
- Sovos – www.sovos.com
- Thomson Reuters/OneSource - https://tax.thomsonreuters.com/en/corporation-solutions/indirect-tax
- Vertex - www.vertexinc.com
- Wolters Kluwer/CCH – https://www.wolterskluwer.com/en/solutions/tax-accounting-us/sales-tax-software

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Tips for Success

Key Components of a Project

- Have a defined project plan with goals and objectives
- Include a broad project team (Accounts Payable, Purchasing, Master Data, Finance, Tax, Fixed Assets team, ERP)
- Develop comprehensive requirements and definitions
- Be open to creative solutions and change
- Develop and conduct thorough testing

Pay Now or Pay MORE Later

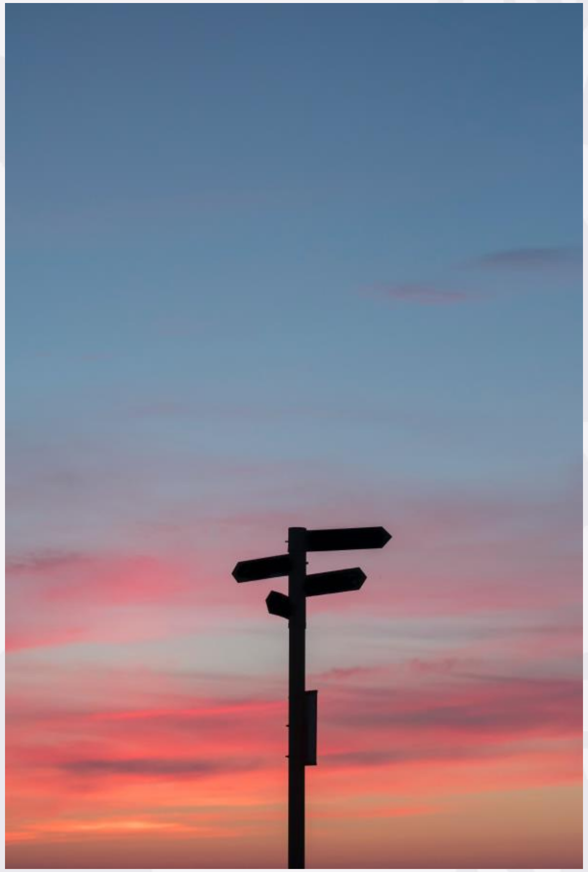
- Don't just guess, ask questions
  - What is being purchased?
  - Who requested the purchase?
  - How will it be used?
  - Where will it be used?
  - Is there an exemption certificate on file?

Helpful Hints

- Involve Purchasing or Requisitioner to put good description on PO or Req
- Add a "usage" indicator on the PO to help identify functional area (Manufacturing, R&D; Quality Control)
- Identification of tax amounts by GL account number
- "Use tax paid" stamp or GL coding for invoices where use tax is accrued
- Separately enter vendor charged tax in ERP

Helpful Hints

- Develop tax matrices that all team members can refer to.
- Consider use tax training for other departments so they clearly understand the process.



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Process Changes to Implement Post-Wayfair

- Buyers should have a formal regular process of reviewing tax paid to vendors.
- Review or implement a vendor tax validation process.
- If you're using a managed compliance rate, review to see if vendors are charging you tax.
- Monitor for vendors that you buy exempt items from to make sure you've issued the right exemption certificates to them.

Process Changes to Implement Post-Wayfair

- As more suppliers start charging tax, the opportunity for reverse audits will increase. This is an area of opportunity for refunds.
- Vendors may be charging tax but not the way you need them to. Situations may arise where you don’t want to be charged tax but would rather accrue and pay use tax.

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Summary

- Relying on the state to determine use tax due during audit is no longer accepted.
- When tax decisions are made accurately:
  - The company saves money
  - Vendors are more satisfied
  - There is less impact to resources
  - Audits do not result in large tax liabilities
  - Penalties and interest are minimized
- Automation can increase accuracy at different levels depending on sophistication of solution

Questions & Comments

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