



Lease tax automation eliminates daily damage control

Gordon Flesch Company strengthens tax management through automation

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About Gordon Flesch Company

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Complexity and confidence

Would your tax department rather handle damage control or take control?

The question crops up frequently in the leasing industry, where complexity infiltrates every stage of the leasing lifecycle. "So many challenges arise each day that we have to deal with," reports Diane Parisi, finance and tax manager for Gordon Flesch Company (GFC), a family-owned office equipment leasing business founded in 1956. Parisi ticks off a long list of complex issues related to origination, customer moves, services, upgrades, down payments, home-rule requirements, exemption certificates, and end-of-term options.

Addressing these challenges in a manual fashion — with the heavy involvement of order entry professionals who do not possess deep tax expertise — required GFC's tax department to engage in significant damage control. And, it ultimately drove the company to invest in an automated solution, a combination of Vertex® Indirect Tax for Leasing and Vertex partner Odessa Technologies' LeaseWave, an Internet-based lease management system.¹

Today, Parisi reports that GFC's tax department is very happy to have shed its damage-control role in favor of a firm sense of being in control of daily tax challenges. "There really is no comparison," Parisi says. "We went from a completely manual process, where individuals lacking deep tax expertise had to make difficult decisions, to a centralized, consistent, and controlled setting. We definitely prefer being in control. I think we all know that damage control is not really a fun place to be."

Many tax departments in the leasing industry continue to operate in that mode. GFC's experience offers instructive guidance on this point. The company's experience, as well as the subsequent sections in this paper, cover the following:

- Contending with a rash of common leasing tax challenges
- Implementing an automated solution, supported by training and consulting
- Reaping the benefits of taking control of tax-management challenges



3 keys to implementation success

GFC encountered typical bumps in the road during its implementation phase of Vertex® Indirect Tax for Leasing and Vertex partner Odessa Technologies' LeaseWave. These minor issues included data migration from a legacy system, previous data errors that existed in the old system, and the testing and data validation challenges that crop up in all software implementations. Parisi also deems the implementation a success and cites the following factors as key enablers of this success:

1. **Training:** GFC tax professionals attended Vertex training sessions prior to the implementation. The knowledge they gained from that experience, Parisi says, helped the company “plan our implementation better.”
2. **Consulting:** Parisi describes the Vertex consultants who assisted with the implementation as “very, very knowledgeable and extremely easy to work with.” She adds, “We got them involved a little bit late in our project. Get Vertex Consulting involved early.”
3. **Networking:** GFC tax professionals have compared notes with tax professionals in other leasing companies — at industry-specific meetings during Vertex Exchange and through ongoing participation in the user community. “Get involved in the Vertex user community,” Parisi adds. “Talking to people and sharing your experiences helps make you feel more confident that you’re doing things correctly.”

A new lease on tax complexity's many forms

Tax professionals in the leasing industry face so many challenges on a daily basis because multiple elements in leasing transactions determine taxability. Unlike a simple sale, there are two main components: the asset being leased and the lease itself. Additionally, customers may want to finance ancillary charges, such as freight, installation, or upfront sales tax. Applying the correct tax is no simple matter.

That's why tax departments are staffed with tax professionals who are trained in the intricacies of tax law. As long as they are in control, the process tends to run smoothly. The problem is that, in many leasing companies, the people making these tax decisions are not tax professionals. Order entry clerks are in the unfortunate position of needing to apply the correct tax to a transaction, without having the knowledge or systems to do so reliably. As a result, errors are made. A customer may be charged too much tax, which leads to dissatisfaction. Or, the customer may be charged too little tax, which makes the relevant tax jurisdiction unhappy.

Most tax departments do their very best to provide the order entry clerks with the information they need by providing tax tables, training, and assistance. However, there are many variables that hinder this effort. “Prior to investing in tax automation, all of our tax transactions were handled manually,” Parisi reports. “And much of that work was processed by our order entry department. Essentially, we were taking people who really didn't know how to deal with tax and asking them to step into a tax role and make a lot of decisions that determined whether or not the sales tax was correct on the customer invoice.”

Tax departments in the leasing industry typically encounter other common challenges, including:

- + **Taxing the assets:** Many leases are booked with multiple assets, which customers often use in different ways. Tax professionals need to determine if the assets included in the lease are subject to tax and how to track the varying taxability. For example, a manufacturer may use multifunction copiers in the office, as well as in the manufacturing process. In the first case, the asset is taxable, but in the second, it is not. Having a completed exemption certificate is only part of the story. Understanding the tax law well enough to know whether the exemption is valid is another matter.
- + **Ancillary charges:** Some customers prefer to finance all related ancillary charges, such as software, freight, installation, consulting, usage fees, upfront sales taxes, and a variety of other services. Most of these items have a different tax treatment than the related equipment.
- + **Services:** Equipment leases often include a maintenance agreement. A computer equipment lease may include IT services, such as consulting or cloud computing. Many times, the customer does not know the pricing breakdown between the equipment and the service component. Additionally, the taxability of the various transactions may result in different tax treatments.
- + **Taxing the lease:** Once taxability of the assets and any related fees have been determined, the tax on the lease must be determined: Is the tax on the stream

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Finance and Tax Manager,
Gordon Flesch Company, Inc.

of payments, upfront on the cost of the equipment, or upfront on the stream of payments? Each jurisdiction may treat the taxability of varying asset types (e.g., equipment, services, etc.) and each lease type (e.g., fair market value [FMV], conditional sales agreement, etc.) differently. Additionally, rules and rates are always subject to change.

- + **Asset moves:** A customer with multiple locations may move equipment among those locations. Jurisdictions treat leases differently, so the taxability evaluation performed when the lease was booked often needs to be repeated to determine if additional tax is due. For example, if equipment on an FMV lease is moved from Illinois to Ohio, the lessor needs to calculate and remit upfront tax on the remaining stream of payments.
- + **Equipment upgrades:** Customers routinely upgrade their equipment before the original lease term concludes. Sometimes, the equipment is returned and sold back to the vendor and sometimes it is rolled over to a new lease. This raises additional tax questions that must be addressed: Is the refinance balance of the returned equipment subject to sales tax? For equipment that remains on lease, is there a change in the tax treatment?
- + **End-of-term options:** Customers have many choices at the end of a lease term — returning the equipment, purchasing the equipment, or extending the lease — and each option requires different tax treatments.

Seeking an alternative to damage control

GFC contended with the challenges described above as well as several others, including the complications that arise when a leasing company has offices and business in a home rule state (in GFC’s case, Illinois). The company also routinely handles lease upgrades, through which changes with tax implications — such as rolling the equipment into a new lease — are made before the original equipment lease reaches full term.

As is the case in many leasing companies, GFC tax professionals were often thrust into damage-control roles to address these challenges. GFC’s tax department also invested significant time and effort to avoid getting to this state before investing in tax automation. The tax team developed an intricate matrix for order entry professionals to refer to figure out how to book leases.

The matrix included as many considerations and factors as possible, including how transactions should be handled in specific tax jurisdictions, sales tax codes, the application of sales tax (e.g., upfront or on the stream of payments), and much more.

“We really relied on the order entry individuals to follow that matrix and to pick the correct system settings so that they would charge the appropriate tax on the appropriate transactions,” Parisi notes. “This matrix required constant research, monitoring, and maintenance — along with constant communications to the individuals who were booking the leases.”

While GFC’s previous leasing system had some built-in sales tax rules, they were designed at the portfolio level. To effectively manage all the different tax scenarios, the tax department was forced to create multiple portfolios. “That created another set of operational issues,” Parisi continues, “because the portfolio rules were set at the

About Vertex® Indirect Tax for Leasing

Vertex® Indirect Tax for Leasing (Vertex Leasing) is designed for the leasing industry. It integrates with Lease Management software to automatically apply the correct tax for the transaction. Vertex Leasing determines where a transaction is taxed, what assets are taxed, how the lease is taxed, how much tax is charged. Vertex Leasing provides tax system processing for each phase of the leasing/rental business process, from origination to invoicing to disposition. While business processes vary by lessor, the system was designed to provide any host financial program comprehensive tax information to make a decision on further tax processing. Tax information includes product taxability, tax basis, and tax rates.

state level. And a state is either taxable or non-taxable.” That lack of granularity created problems when GFC encountered situations with nuanced tax implications — such as the bundling of services, a home-rule issue, end-of-term extensions, exemption certificates (all of which were handled manually), and much more — that required a detailed level of data, insight, and decision-making that the matrix and portfolio of scenarios did not provide. With regard to the manual management of exemption certificates, Parisi says, “We weren’t tracking the reason for the exemption, which created a whole other slew of issues.” There was at least one other significant matter. “We didn’t really have a good way to get information out of this system so that we could get our sales tax returns filed,” Parisi adds. “It required sort of a dump-the-data-out-of-the-system approach, which required a couple hours of manipulation each month — and the hope that all of the information was correct.” This created reporting difficulties and posed a potential audit risk.

For all of these reasons, GFC decided to make a change.

Training, consulting, and implementing

GFC purchased a combination of Odessa LeaseWave and Vertex® Indirect Tax for Leasing. One of the primary intentions of this investment was for the tax department to ensure that the correct tax is automatically applied to every transaction. While tax rules and rates must be updated regularly, GFC’s tax department did not want to be burdened with manually researching this data and then translating into a format that order entry professionals could understand. Vertex Leasing includes leasing-specific tax rules for countries across the globe. These rules and rates are updated monthly.

Parisi indicates that GFC is very happy with the return on this investment. “Overall, Vertex really has made us so much more confident that we’re being compliant and that we’re not going to encounter all of the issues we previously dealt with.” And she credits the training and consulting offerings for helping her team manage the implementation process.

GFC tax professionals attended a Vertex training session roughly one month before the implementation. The purpose was to gain knowledge of the application to help eliminate implementation hiccups and reduce implementation costs. Part of the motivation for this education, Parisi notes, was the fact that the Vertex implementation coincided with several other system implementations and upgrades.

The GFC team also attended a two-day add-on training class dedicated to the lease-specific elements of the system. “Our thought was that since we have internal tax expertise, we should learn as much as possible about the system so that we can manage a good chunk of the implementation ourselves to save a few dollars,” she says. “Once we were in the training sessions, we thought it seemed very intuitive and easy to navigate.”

Parisi credits the training event for being hands-on and including the lease-specific instruction. “As a result of developing a better understanding of the technology, we were able to plan our implementation better. And it helped us gain a better understanding of how the interface between Odessa and Vertex works.” She also credits Vertex®

About Vertex

Vertex, Inc. is a leading tax software and services provider that empowers global commerce. The company's mission is to connect customers and partners across all industries to deliver the world's most trusted tax solutions for businesses to grow with confidence. Vertex provides cloud-based and on-premise solutions that can be tailored to specific industries for every major line of indirect tax, including sales and consumer use, value added, and payroll. Headquartered in North America, and with offices in South America and Europe, Vertex is a privately held company that employs over 1,000 professionals and serves companies across the globe.

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Consulting Services (“very, very knowledgeable and easy to work with”), which assisted on the implementation as well as the experience of attending Vertex Exchange,² the annual customer conference, where her tax professionals huddled with peers in other leasing-company tax departments to compare notes. “Most leasing companies wrestle with similar types of tax issues” Parisi says. “So it was really great to get to know other people who were using the system and have the opportunity to bounce some ideas off of each other.”

The tax-management confidence Parisi describes marks one of several benefits GFC had gained from automation investment.

Other benefits include relying on fewer people to manage the application of tax rules to leases, freeing up order entry professionals to focus on what they do best (booking leases), automatic tracking of exemption certificates, spending less time researching tax rules changes (now handled automatically in the new system), and churning out accurate reports in a timely fashion.

The confidence also extends to audit issues. “We now have a good system in place to audit transactions because we can get the information out of Vertex so much more easily,” Parisi reports. “When we do find a hiccup in a process, we tend to catch it earlier and we use that to train our people to avoid those issues in the future. So, we’re not reacting anymore. We’re taking more of a proactive approach to things.”

That leaves the entire company feeling more confident. “The biggest thing for us is really that the tax department is now in control,” Parisi concludes. “We’re not relying on multiple individuals to make decisions anymore. That change has resulted in more consistency and fewer errors.”

Conclusion

The root cause of the tax issues identified in this paper is typically a combination of data accuracy and data transparency. Because many leasing systems do not have automatic tax rule updates, every new rule or modification to a rule has to be made manually. The opportunity for error is high and when the rules are not up to date, and therefore the tax assessed is potentially not accurate, the door is left open for audit scrutiny.

Automated transaction tax software provides numerous benefits as a core part of an organization's operational efficiency plan — from both a business and technology perspective. Implementing tax automation enables the tax department to put an end to damage control and gives it full control of the tax process.

Endnotes

1. <http://www.vertexinc.com/partners/software-integration-partners/odessa-technologies>
2. <http://www.vertexinc.com/vertex-exchange>

North America
King of Prussia, PA, USA

Latin America
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