



HOW TO CONDUCT A REVERSE SALES AND USE TAX AUDIT TO MITIGATE RISKS AND IMPROVE COMPLIANCE

**UNCOVERING ISSUES EARLY HELPS AVOID
COSTLY ERRORS THAT CAN STRAIN
RESOURCES AND RELATIONSHIPS**

SPEAKERS



Larry Mellon

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Sandra Schaper

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Global Indirect Tax, ResMed



Bill Loew

Executive Vice President
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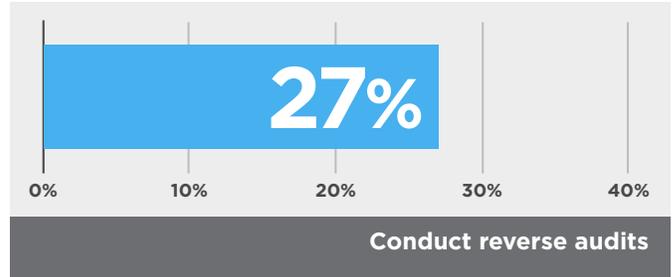
AS STATE AND LOCAL TAX JURISDICTIONS CONTINUE TO EXPAND their definitions of nexus, companies are at a greater risk than ever before of failing to comply with sales and use tax reporting requirements where they do business.

One of the best ways to mitigate a sales and use tax audit is to conduct an audit in reverse. This can reveal issues with sales and use tax reporting that companies might otherwise overlook.

“A reverse audit facilitates the identification of items and transactions in which a company may have underpaid or overpaid sales and use taxes,” said Larry Mellon, Tax Manager, Vertex, Inc., during a recent Vertex-sponsored CFO webcast.

“While many people associate reverse audits with uncovering underpayments to limit exposure, there are other benefits of this exercise. There is an opportunity to determine what has been overpaid, and then explore the need for a solution,” Mellon added.

“Reverse audits can result in refunds, but that isn’t the only reason to perform one. They can also ensure compliance and enhance the reputation of



Source: live webcast audience poll, 3/24

the internal tax department, which is something that is often overlooked,” Mellon pointed out.

Despite these benefits, less than one-third (27%) of webcast attendees indicated that their organizations conduct reverse audits.



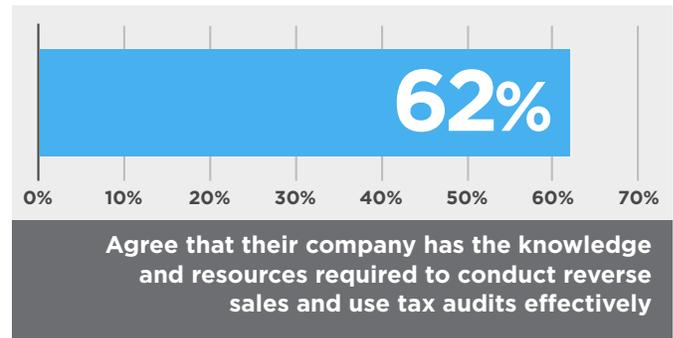
PREPARING AND CONDUCTING A REVERSE AUDIT

On a positive note, many organizations are prepared for a reverse audit. A poll of webcast attendees indicated that nearly two-thirds (62%) are confident that their company has the knowledge and resources required to conduct reverse sales and use tax audits effectively.

Mellon outlined the steps for a preliminary assessment of your audit capabilities, which includes asking key questions such as:

- Does the system calculate proper tax?
- How easily can data be retrieved?
- What is the quality of the data?
- What web-based applications are utilized?
- What are the security concerns?
- How much time needs to be invested?
- Is data available electronically?
- Are invoices imaged and retrievable in bulk?

As you assess your company's ability to comply with sales and use tax regulations, it is important to evaluate internal and external resources needed to work on a reverse audit, Mellon remarked. The tax department should be on board. While accounts payable should not be the decision maker for tax decisions, they, along with purchasing and supply chain functions, should be given the tools and knowledge necessary to ensure that taxes are calculated and paid correctly.



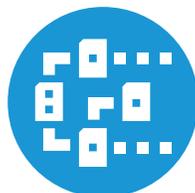
Source: live webcast audience poll, 3/24

“An external resource could be needed if your team is understaffed or lacks the expertise to be able to provide the information,” Mellon said. “In addition, some organizations want to engage an external resource because they have more advanced knowledge of the tax laws in various jurisdictions and can act as a buffer.”

As organizations consider the costs of reverse sales audits, Mellon suggests choosing a short period of time or small area of the business to get a sense of the return on the investment.

Timing is also critical, Mellon noted. He said the statute of limitations is a key consideration in planning.

Following the audit, organizations want to look at the vendors and purchases where sales tax was charged incorrectly.



BUILDING A COMPELLING BUSINESS CASE

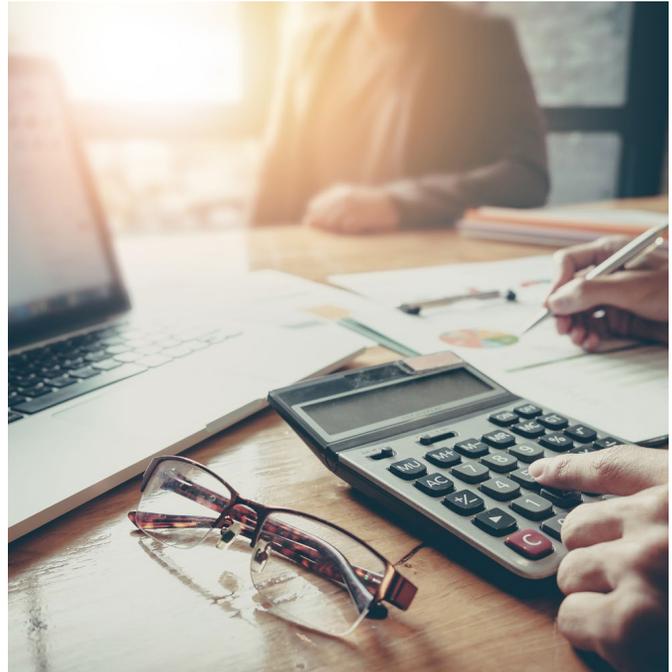
Following Mellon’s presentation, the webcast transitioned to a panel discussion on building a business case for a reverse audit. Panelist Bill Loew, Executive Vice President, Miles Consulting Group, noted that sales and use taxes average close to 10% nationwide.

“You don’t have to look too far to determine whether or not 10% of gross receipts are a material number for you or whether 10% of your annual capital equipment spend could be a material number for your business,” Loew said. “If your business happens to be a service business where you’re not collecting sales and use tax on your revenue, 10% of your parts or materials or other tangible personal property that are used to perform your services is typically a material number for you as well.”

Panelist Sandra Schaper, Senior Manager, Global Indirect Tax, ResMed, said a compelling case to leadership can be made by talking about collecting all taxes properly. “If you’re not collecting the tax, your company still owes it as the seller of the property or taxable service. That’s a very compelling reason to conduct a reverse audit.”

Schaper noted the need for a strong manager at a high level for a reverse audit to be successful. Commitment of technical resources is also critical, she noted. “It could be someone in-house with operational experience, but most likely you need to look for an external tax resource.”

Collaboration between external and internal resources is crucial, Loew noted. “It is important to have an internal liaison that can get things



done for the external consultant, such as arrange meetings and set up the internal resources.”

Schaper pointed to the risk of not being compliant. “You have a high risk of being selected for an audit if you’re sending invoices out and the taxes are not calculated correctly.”

The result can be undercollection or overcollection of taxes, Schaper noted, which can strain customer relationships. “Charging incorrect taxes can affect the customer experience and that in turn impacts your days receivables outstanding.”

Finally, reverse audits can identify areas for process improvement, Loew concluded. “Poor processes can cause errors. But the takeaway and the process improvement that occurs as a result of one of these projects and exercises is invaluable to the organization.”

CONCLUSION

A reverse sales and use tax audit is a critical component of any organization's efforts to mitigate risk, ensure compliance and foster positive customer relationships. While many organizations approach the process with the expectation of uncovering underpayments, a reverse audit also reveals overpayments and poor processes that can put your company at risk.

SOME KEY TAKEAWAYS INCLUDE:

- Preparing your company for a reverse sales and use tax audit involves evaluating internal and external resources to ensure that the process is accurate with minimal disruption.
- Sales and use tax rates average nearly 10% nationwide, making it imperative to perform reverse sales audits to reduce errors before they happen and negatively impact the bottom line.
- Successful companies apply lessons learned from a reverse audit to identify concrete steps their finance team can take to mitigate risks of an actual sales and use tax audit.