

## Anatomy of a Sales Tax VDA: Organizing and strategizing a multi-state Sales Tax Voluntary compliance project

By Raymond Chang, CPA

(Part 2 of 3)

*In part one of this series, we examined the initial steps in tackling a comprehensive review of a client's potential exposures to sales tax requirements to states in which they have conducted business. Here, we look into the results of our initial analysis and "fill in the gaps" to lay the groundwork for executing voluntary disclosure agreements with applicable states.*



From our deep-dive into our client's sales order process, we discovered some notable issues, all of which would create some complications in executing the voluntary disclosure (VDA) process to remedy the state sales tax exposures. These issues included:

1. Computer system did not provide for a dedicated section or field as it relates to customer exemption information – such information were being kept in an ancillary field in each customer's account.
2. Some customers exempt from sales tax were missing their required certificate or exemption information entirely. Yet the sale went through as nontaxable.

Our walkthrough made it clear that our client needed to update their customers' exemption information and certificates on files and upgrade their system to capture and retain them. This is not only a necessary step for the process at hand, but it will also ensure records are being entered and maintained in a way that will facilitate future process reviews. However, it's a tall order. There were many customers and deliveries are made across the United States. How can the team best tackle and sort out such an extensive database?

Our initial thought was to go with a typical "Sales by Customer" approach. But this might not yield sufficient coverage by state. A "Sales by State" approach would be more thorough, but it might result in their customers getting contacted more than once as we worked from state to state in this multi-state project – something we wanted to avoid. The client's IT department ended

up running sales reports in a variety of ways to maintain the advantages of each approach. This process required a member of the team to have sufficient knowledge of Excel's advanced database functionalities – a resource we'd recommend for all companies who are going through a similar process.

After compiling and analyzing four years of sales data, our client discovered that their sales data was very disaggregated. The data turned up with duplicate customers with different names that were actually the same customer, and customers with similar names who were actually separate legal entities for sales tax purposes. A comprehensive review had to be done by hand to ensure the database was clean and usable.

### Setting the Stage for the first VDA

Armed with the new and improved sales report, we now needed a way to look at customers' delivery landscape so that the "Sales by Customers" report would also be able to indicate how much shipments were made to each state. To do this, we provided our client with a template allowing them to summarize sales totals by customer and by state. In this template, customers were listed in rows and ship-to states were in columns. This template was designed around

the “Uniform Sales & Use Tax Exemption/Resale Certificate” or the multi-jurisdiction certificate where the participating states would accept this certificate in lieu of their own state specific certificate.

Once the client completed the template, we then matched up the results to the company’s Nexus footprint and then prioritized the states by total sales dollars. We called them “Tier I, II and III” states based on their total sales dollars. Tier I states would represent the greatest exposure, and thus the greatest priority.

For each of these states we then helped our client by quarterbacking their VDA and compliance initiative. We also referred them to a few high-end sales tax filing servicers such as Avalara and Vertex to further assist in the process. The main purpose of using these services—besides compiling monthly sales data and preparing the monthly filings and submissions—is that they would also provide a repository for storing all the resale certificates of our client’s customers. Essentially, they would serve as an additional layer to our client’s sales order and reporting process, similar to what ADP or Paychex does for payroll.

As it turned out, Texas was one of the Tier I states. As Texas was also the state that required the greatest level of detail (by invoice) in its VDA submission package, it was selected to be the first VDA. As we began the process to execute the first VDA with Texas, we used this state to also serve as a model to learn all of the issues and gaps that could arise as the client reviewed and updated their resale certificates and retention system.

*In the final piece of this three-part series, we will walk through the specific steps of executing the first VDA process with the state of Texas. We will also investigate the lessons learned through this first process and explore how to broaden the process to all necessary states.*

### **About Raymond Chang, CPA**

As a Senior Audit Manager with more than 15 years of industry experience, Raymond’s practice focuses on providing assurance and advisory services to privately-and publicly-held clients in the middle market. He is particularly skilled at working with companies in the manufacturing, distribution and real estate sectors.

Highly analytical, Raymond is skilled at analyzing extensive data and identifying areas for improvement. He enjoys working with clients to find solutions to their problems and advises them in all aspects of business and financial management, including operational and internal control matters and financing. He is involved in the planning and supervision of various corporate, partnership and individual tax returns.

Raymond is a member of the Chinese American Society of CPAs and an active member of the firm’s Best Practices and CPE committees. He often takes a leadership role in many of the firm’s training and staff development programs. Raymond graduated from St. John’s University with a Bachelor of Science degree in Accounting. Raymond can be reached at [rchang@mwellp.com](mailto:rchang@mwellp.com).

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