

# **ELECTRONIC COMMERCE**

## **A Report of the Steering Committee**

### *Task Force on EDI Audit and Legal Issues for Tax Administration*

**January 2005**

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## **Acknowledgment**

A special acknowledgment is due to Stanley R. Arnold, Commissioner of the New Hampshire Department of Revenue Administration for 14 years. He retired in 2002 after 20 years of service with the agency. Mr. Arnold also served as Chair of the Task Force on EDI Audit and Legal Issues for Tax Administration for eight years. His tireless and thoughtful work on this publication was one of his final acts of service to the tax community.

## Foreword

The Task Force on EDI Audit and Legal Issues for Tax Administration (Task Force) was formed to coordinate efforts between the business community and tax administrators in analyzing and addressing the issues posed by electronic commerce and related business processes. The Task Force comprises representatives of the Council On State Taxation (COST), Institute for Professionals in Taxation (IPT), Tax Executives Institute (TEI), Multistate Tax Commission (MTC), and Federation of Tax Administrators (FTA). This report is the eighth in a series of Task Force reports on issues related to electronic commerce, emerging business processes and tax administration. (See Appendix 3 for other reports in the series.)

The Task Force formed a working group to examine the tax administration and compliance issues associated with business-to-business electronic commerce. This report provides a basic overview of electronic commerce in its most general applications and discusses what taxpayers and state tax administrators need to consider when addressing electronic commerce and tax compliance. The report also provides an overview of previous Task Force publications and examines how electronic commerce processes may affect the guidance and recommendations offered in the original reports.

The Steering Committee wishes to acknowledge the contributions of all individuals who devoted their time and effort in developing and refining this report. A complete list of participants can be found in Appendix 2.

Stanley R. Arnold, Steering Committee Chair  
Commissioner, New Hampshire Department of Revenue Administration (retired)

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# **ELECTRONIC COMMERCE**

## **A Report of the Steering Committee Task Force on EDI Audit and Legal Issues for Tax Administration**

### **Introduction**

Electronic commerce (e-Commerce) has allowed companies to transact business in an efficient, automated fashion as never before, using the Internet. But while e-Commerce has provided unprecedented opportunities to businesses and consumers, e-Commerce's rapid—and continuing—evolution has posed unique challenges to tax administrators. The challenge was captured in the title of a feature article in the kickoff issue of *Line56's E-Business Journal*, Summer 2002, "Who's in Charge of E-Business?" The answer, of course, is no one. The responsibility has fallen to tax administrators to sort out, as best we can during this exciting yet chaotic new era, the complex issues of compliance, recordkeeping and even taxation.

The Task Force on EDI Audit and Legal Issues for Tax Administration is concerned that businesses and state revenue departments have not paid sufficient attention to how e-Commerce affects tax administration and tax compliance.

Paul Higgins, the editor of *Line56's E-Business Journal*, points out in a study conducted by the magazine that two-thirds of respondents had reorganized their e-Business structure within the past year and one-third within the past six months. The question that comes to mind is, "Were the tax folks involved in all these reorganizations?" Too often, we fear, the answer has been "no."

Ever-newer tools, procedures and systems constantly replace the software and other technology driving e-Commerce. Again, a corporate information technology department may not consult the corporate tax department when these upgrades are made, to the detriment of tax compliance and recordkeeping.

Currently, little guidance is available from federal and state policymakers on the actual taxation of e-Commerce transactions. Despite these challenges, tax administrators must fully comprehend how businesses are, or are not, accomplishing recordkeeping and subsequently must apply that knowledge to audit and compliance activities. While e-Commerce continues to change and grow, the need for tax compliance remains.

The Task Force believes it is critical that taxpayers and tax administrators consider certain issues now, while e-Commerce is still developing, and wrote this "White Paper" to assist in that process. The introduction provides an overview of the mechanics and processes of e-Commerce, while the second half of the paper reviews previous Task Force publications and updates each vis-à-vis e-Commerce. Tax administration and compliance issues are discussed in detail within these reviews. Recommendations are

offered concerning the actions of taxpayers, tax administration agencies and software and Internet service providers. It is our hope that the recommendations and the report will be helpful in addressing tax administration and compliance issues in a fashion that meets the needs of all parties.

Readers interested in more information about Business-to-Business (B2B) e-Commerce should go to <http://www.line56.com/>. This is one of the most authoritative sites on the Internet dedicated to B2B e-Commerce. The site has a subscription service, but there is a wealth of information on the free pages. To gain a visual understanding of the many aspects of a complete B2B e-Commerce system, download the free poster series at [www.line56.com/articles/ebiz\\_ecosys\\_index.asp](http://www.line56.com/articles/ebiz_ecosys_index.asp).

## **Business-to-Business e-Commerce and the Digital Marketplace**

The Internet was developed by the U.S. Department of Defense to test the feasibility of connecting computing devices. In 1969, there were four connected computers; in 1984, 1,000; and by mid-1995, 6.6 million. Today, terms like vertical portals, net infrastructure and B2B are part of the daily vocabulary of businesses large and small—the virtual marketplace has emerged as a fast-growing offspring of the Internet.

Rapid developments in e-Commerce and its terminology make it impossible to write a paper that will remain technologically current for any period of time. By the time a paper can be produced, models discussed will have evolved into new forms. Nonetheless, the broad outlines of e-Commerce remain sufficiently stable to allow a discussion of major models and considerations for state and local tax administration.

**e-Commerce** is generally described as businesses and consumers using the Internet to exchange information and buy and sell goods and services. It offers solutions to a variety of market-related problems, including:

- commerce fragmented by geography,
- a preponderance of complex interactions between businesses that are labor- and information-intensive, and
- supply chains bloated with excess inventory because of an inability to foresee and plan for the right products.

Electronic exchanges may take place through **digital marketplaces** (also known as net markets, hubs, virtual markets, and butterfly markets), which are Internet or Web-based trading hubs that bring together sellers and buyers. Purchasing also may take place through a company's own internal procurement Web site, where approved sellers display their items or catalogues.

Digital marketplaces can be created and hosted (maintained) by either of the parties (buyer or seller) involved in the trading or by a third party who may charge for this service. The beauty of digital marketplaces is that their use and setup is entirely flexible.

Key examples of digital marketplaces include:

- A commercial, third-party host provides procurement services to a specific set of suppliers and their customers, for a fee.
- A franchise or trade association provides online procurement services to its members, thereby aggregating their orders from approved suppliers.
- A new market maker offers online information and services to a specific industry, replacing existing distribution channels.
- A large distributor automates processes among several buyers, suppliers or manufacturers.

Digital marketplaces raise revenue through advertising, commissions and lead referrals. Some marketplaces receive a transaction fee from participants.

Digital marketplaces are an increasingly important model for modern businesses. Corporate leaders are attracted to their ability to extend customer reach and enhance customer service; simplify the exchange of business-related information; preserve proprietary procedures, relationships and pricing; and aggregate buying power among independent companies, divisions and partners. Tax authorities may face difficulties in performing their compliance tasks when businesses adopt a digital marketplace model, but they should recognize that businesses are making the change for compelling business reasons.

## Types of Digital Marketplaces

**Digital marketplaces** may be oriented toward sellers, buyers or both, and may be based on several business models.

A marketplace that brings both buyers and sellers together, and was not created to benefit one or the other, is considered a business-to-business (B2B) exchange market. The role of the B2B market is to improve the functioning of the marketplace by improving the availability of information and reducing transaction costs, thus allowing the laws of supply and demand to determine the optimal process between sellers and buyers. B2B exchange markets are typically owned by entities independent of any seller or buyer group. They require a real-time, bid-ask matching process, market-wide price determination, as well as a settlement and clearing mechanism. B2B exchanges create significant value in market sectors where demand and prices are volatile. These exchanges allow businesses to manage excess supply and peak-load demand.

Models may fall into either of these categories:

- **Vertical Marketplaces** – a focus on a single industry by providing new distribution channels for raw materials, secondary inventory and supplies.

- **Horizontal Marketplaces or e-Business Portals** – hosted by third parties to provide online buying and selling to a set of identified clients. The value to buyers is the aggregated buying power.

They may also be divided into these two types of models:

1. **Sell-centric markets** exist for the economic benefit of their supplier members. “Sell-centric” markets are formed by one or several large sellers hoping to draw smaller, fragmented buyers. When virtual or Web-based, they create efficient, aggregated distribution channels and provide easier access to untapped buyer groups.
2. **Buy-centric markets** are essentially online procurement portals that exist for the economic benefit of the purchaser. Typically they are formed when a few large customers join forces to purchase from a variety of sellers. They provide an efficient mechanism for aggregating the buying power of otherwise fragmented buyers to achieve improved procurement advantages (i.e., better price, greater access to products, etc.).

In this **procurement marketplace**, Web-based procurement technology, or e-Procurement, replaces expensive proprietary networks and electronic data interchange (EDI). A company will establish a procurement marketplace to connect employees directly with suppliers. This streamlines the procurement process and reduces purchasing costs across departments and business units. Buyers interested in maximizing savings will use procurement software and procurement Web sites and ftp sites. There are two basic types of e-Procurement:

- a. **Production (Direct Spend)** – The procurement of production items such as raw materials that are scheduled by production runs and driven by specific design-specifications.
- b. **Nonproduction (Indirect Spend or Operating Resources)** – The procurement of operating resources such as office supplies and commercial services which normally require approval and are catalogue-driven.

While Digital Marketplaces are in common use today, they still face challenges that may add complexity to the problem of “designing tax into the process”:

- The business models are relatively new and may evolve rapidly.
- Application software and platforms being used are immature.
- There are difficulties with integrating existing customer management, procurement and enterprise applications with digital market solutions.
- Digital marketplaces affect existing customer and supplier relationships (and many tax laws were written specifically for the old model relationships).
- Digital marketplaces affect an organization’s logistics.

- Digital marketplaces cross international boundaries, creating foreign exchange issues.

## Considerations When Selecting e-Commerce Technology

While businesses can choose from many kinds of custom or packaged software when selecting their e-Commerce technology, they should keep in mind that the technology must do more than create a transaction. It must also provide a history of details to permit the appropriate determination of tax and to permit an audit of those determinations.

Remember, *the client still has ultimate responsibility for the integrity of its data*, even if the hosting is provided externally. Businesses need to make sure that their new software, Web sites and portals give full access to taxing authorities, who will need very specific data and data trails that may not be otherwise required by the transaction. For a detailed discussion of data management from a tax administration perspective, please see Appendix 1.

Businesses can include tools in their e-Commerce software and systems to ease the task of determining tax compliance. These include:

- The use of ID codes, if the records are complex and related to a variety of transactions;
- Tools that make it possible to determine the integrity of archival records; and
- A system that permits efficient sampling.

For a detailed discussion of business technology and tax-related recordkeeping, please see “What is the B2B Impact on Auditing Electronic Records?” on page 9.

Because every business is unique, packaged applications often fail to provide the level of support that enterprises need “out of the box.” When corporations purchase end-to-end applications, they should be prepared to spend a significant amount of time and money writing custom code to make enterprise applications work with each other and share common data sources—even across enterprise boundaries. Otherwise, a tax audit trail and data for compliance cannot be seamlessly generated.

Given this need, many companies are moving toward **Enterprise Resource Planning (ERP)** systems, which can integrate numerous systems and processes, including financial accounting and reporting, procurement, inventory management, personnel management, and even production management.

There are other options that will support an integrated system and process. Some businesses want to turn to traditional software, which can be purchased together with installation. Some traditional software can be tightly integrated with an ERP, such as Ariba, 12, etc. A business may choose to turn to a commercial host or e-Procurement Service Providers such as CovisInt or Xchain. Or a business can go directly to a portal

site (QuestLink, Intraware) or purchase the tools to create its own proprietary Intranet/Extranet solution (Attunity, CommerceQuest).

## **Third-Party Hosts**

The rapid growth in commercial, third-party hosting services deserves special attention because of its impact on e-Commerce. Third-party hosts, or application service providers (ASPs), are businesses that offer virtual access to software applications and related services via Internet Web or ftp sites. ASPs are quickly becoming an important alternative, not only for smaller companies and individuals with small technology budgets, but also for larger companies that have the option of owning an in-house system.

With third-party application hosting:

- The programs and data are installed and maintained by the ASP's professional information technology staff at its hosting facilities;
- The ASP and its technology staff build and maintain the computing infrastructure hardware, software, and networking;
- Applications are available to anyone who has been cleared for access, within the organization or outside contractors;
- Employees and contractors can access the application from anywhere: home, airports, hotels, or remote offices; and
- The entire system, including software, hardware, networking and services, is subject to a predictable monthly fee.

## **The Impact of B2B Electronic Commerce Processes on Previous Task Force Issues**

The Task Force has issued seven reports since 1996 examining issues related to the impact of various electronic business processes on tax administration. The reports consider the viewpoint of taxpayers as well as state tax administrators. Given the fast pace of technological advancement, each document must be updated to reflect technological changes and the significant increase in B2B activity.

### ***1. Model Recordkeeping and Retention Regulation, March 1996***

The Model Recordkeeping and Retention Regulation (Model Regulation) governs taxpayer retention of books and records, particularly electronically generated and retained records, for tax administration purposes. To date, Alabama, Arizona, Arkansas, California Board of Equalization, Connecticut, Florida, Georgia, Illinois, Iowa, Maryland, Michigan, New Hampshire, New Jersey, New Mexico, New York City, North

Dakota, South Carolina and Utah have adopted the model regulation in whole or in large part.

During the creation of the Model Regulation, the Task Force recognized that new electronic business processes would continue to develop. The intent was to word the Model Regulation in such a way that changes would not be required whenever new technology was developed. Wording was chosen, wherever possible, that would be consistent with the ultimate objective of ensuring appropriate tax compliance, while taking into account emerging business processes in the information age.

At the time the Model Regulation was developed, electronic data interchange (EDI) was one of the processes about which state tax administrators had concerns, especially as to whether sufficient data would be available to provide adequate records. For purposes of the Model Regulation, EDI was defined as “the computer-to-computer exchange of business transactions in a standardized structured electronic format.” However, the document stated that the Model Regulation was “designed to cover not only the retention of records created using EDI technology, but also the retention and access to records generated through other electronic means and maintained by taxpayers in various computerized accounting systems.”

Given this definition, one could consider B2B e-Commerce as a more sophisticated and faster form of EDI. In fact, e-Commerce is more streamlined than the more traditional EDI transactions. EDI transactions are usually based on a legal agreement between two distinct businesses with direct involvement between the two parties as to how the data is to be configured and determining the timing of EDI transactions. EDI transactions ordinarily require that the data processing departments for each party manage the data layout and transmission. Internet transactions also require an agreement with regard to data format. However standards have been set for multiple users, they tend to be set up in advance, and they are largely transparent to the user.

However it is labeled, B2B e-Commerce clearly fits the Model Regulation's approach to compliance. B2B is simply another electronic business process, an exchange of business information, which is ordinarily recorded in the financial accounting and other computer systems of the businesses involved in the transaction. Appropriate recordkeeping for state tax administration purposes is necessary for B2B transactions, just as it would be for any other business transactions.

***Data Requirements.*** Section 3.1 of the Model Regulation states:

A taxpayer shall maintain all records that are necessary to a determination of the correct tax liability under [*insert appropriate citations to state tax statutes*]. All required records must be made available on request by the [*state taxing authority*] or its authorized representatives as provided for in [*insert appropriate citations to state tax statutes*]. Such records shall include, but not be necessarily limited to:

[*Insert elements of state law which require certain records to be retained (e.g., books of account, invoices, sales receipts), or specific tax elements or transactions (e.g., credits, exemptions etc.) for which particular records may be required.*]

Section 3.1 is the key to the Model Regulation. Records necessary to a determination of the correct tax liability must be available to the state taxing authority, whether electronic or paper. The Regulation specifies that: “Where a taxpayer uses electronic data interchange processes and technology, the level of record detail, in combination with other records related to the transactions, must be equivalent to that contained in an acceptable paper record.” (Section 4.2.1.) “The taxpayer may capture the information necessary to satisfy section 4.2.1 at any level within the accounting system and need not retain the original EDI transaction records provided the audit trail, authenticity, and integrity of the retained records can be established.” (Section 4.2.2.)

***Storage and Maintenance.*** Adequate storage and maintenance of taxpayer records are critical to the ability to sustain documentation for business transactions. Given the multitude of process changes that may occur as a taxpayer begins utilizing e-Commerce, issues surrounding storage of records may be overlooked. Also, companies may make an incorrect assumption that their third-party system providers will store all necessary records.

Sections 5 and 6 of the Model Recordkeeping Regulation address the specifics of records storage and maintenance. Section 5 refers the taxpayer to the National Archives and Record Administration (NARA) standards for guidance on the maintenance of electronic records, and states that the “taxpayer’s computer hardware or software shall accommodate the extraction and conversion of retained machine-sensible records.”

Section 6 describes four possibilities for which the state taxing authority can be provided access to machine sensible records:

- 6.2.1 The taxpayer may arrange to provide the [*state taxing authority*] with the hardware, software and personnel resources to access the machine sensible records.
- 6.2.2 The taxpayer may arrange for a third party to provide the hardware, software and personnel resources necessary to access the machine-sensible records.
- 6.2.3 The taxpayer may convert the machine-sensible records to a standard record format specified by the [*state taxing authority*], including copies of files, on a magnetic medium that is agreed to by the [*state taxing authority*].
- 6.2.4 The taxpayer and the [*state taxing authority*] may agree on other means of providing access to the machine-sensible records.

Taxpayers utilizing integrated accounting systems (such as ERP systems) need to ensure that built-in functionality, such as cross-reference tables, are also stored with the appropriate period data. When utilizing integrated or enterprise systems it may become necessary to have a separate data warehouse to properly store and access historical data for tax purposes. Maintenance of not only ERP/host data but also tax systems data is necessary.

***Third-Party or Host Providers.*** In cases where there is a third-party or host provider for accounting or e-Commerce systems or data, the taxpayer must ensure that all records are available for an auditor. This should be addressed in the contract with the provider, along

with a provision that the records will be returned to the taxpayer should the provider go bankrupt or cease operating the business. Section 7.2 of the Model Regulation states, “A taxpayer may contract with a third party to provide custodial or management services of the records. Such a contract shall not relieve the taxpayer of its responsibilities under this regulation.” While the regulation specifically addresses storage, the taxpayer needs to ensure that any third-party provider who either generates or maintains records for the taxpayer will provide appropriate storage and access to those records. Taxpayers must also be diligent when changing service providers to ensure consistency and continuing maintenance of both old and new records for the appropriate statutory period.

## ***2. Auditing Electronic Data, January 1997***

The Task Force produced a white paper on Auditing Electronic Data to identify the issues involved in a tax audit when electronic records are used and to assess alternative approaches to the audit of such records. Changes in the business environment since the publication of this paper mainly relate to an increase in the business processes that are performed electronically. Although the original paper does not require major modifications, the Task Force believes that clarification of certain areas is needed.

The main topics addressed in the paper relate to the electronic tax audit, system integrity audit, access to all appropriate data, confidential information, hardware and software issues, data dictionary of desired elements, and sampling guidelines. The original paper concluded that the primary objective of the tax audit does not change if all or a part of the taxpayer’s records are in electronic form. However, it did emphasize that, “In an electronic recordkeeping environment, more weight must be given to the internal controls installed to support the tax accrual and reporting systems.”<sup>1</sup> Similarly, in B2B environments greater emphasis may need to be placed on the internal controls safeguarding the business processes.

### **What is the B2B Impact on Auditing Electronic Records?**

The primary objective of the tax audit does not change because all or part of the taxpayer’s records are in electronic form. As a taxpayer moves more and more business operations into an electronic environment, the electronic audit moves closer to becoming the only tax audit program versus being a component of the tax audit program. While the addition of B2B may move the audit closer to a complete electronic audit, it should not change the overall focus of the audit program.

The reliability of internal controls is the foundation for determining the scope of the tax audit, whether examining paper or electronic records. While many of the basic internal control functions are similar in both systems, the introduction of electronic records introduces new and expanded internal controls into the equation. The 1997 paper reviewed certain functions, including: access authorization or security codes, system access and data access logs, regular review of these logs, preservation and security of

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<sup>1</sup> Auditing Electronic Data: A Report of the Steering Committee Task Force on EDI Audit and Legal Issues for Tax Administration (January 1997), p. 3-4.

data integrity of archival records for the statutory period, and the existence of a formal security policy or applicable procedures manual.

A System Integrity Audit (SIA) may be undertaken to determine a level of confidence in the various electronic processes in place. The use of B2B will bring another electronic process into the mix for review purposes. This should not have a significant impact on the methodologies necessary to perform audits of electronic business processes. The issues and concerns should not be significantly different regardless of the electronic business process in place.

In today's environment of ever-changing technologies, a taxpayer may have multiple systems in place for various functions and for conversion from one system to another (e.g., legacy systems to ERP). It is the taxpayer's responsibility to maintain these records for use by the taxing authorities. Maintenance and access to these records is addressed within the Model Recordkeeping and Retention Regulation (Model Regulation) as discussed earlier in this paper. Other laws or regulations may exist in states that have not adopted the Model Regulation. Regardless of the type or number of systems in place, it is still necessary to have a methodology of providing access to these records and ensuring that sufficient detail is retained to support the determination for tax compliance.

Access to all appropriate data is an important piece of the original paper and needs reinforcing as it relates to the use of B2B. Records and data relevant to the determination of a correct tax liability must be made available to taxing authorities. As stated in Section 7.2 of the Model Regulation, using a third party does not relieve a taxpayer of responsibility to provide access to electronic records regardless of the type of electronic business process utilized.

The remaining sections of the paper relating to confidential information, hardware and software issues, data dictionary of desired elements, and sampling guidelines should not be affected by e-Commerce.

### **Recommendations**

It is the taxpayer's responsibility to ensure that the appropriate records are maintained. A third party or host may be relied upon for record maintenance or retention. The taxpayer and third party may wish to enter into an agreement regarding record retention and audit support to identify the responsibilities of each party. A number of items should be considered and addressed when entering into these agreements, including:

- Who will be responsible for making taxability decisions?
- Who will be responsible for tax rate updates?
- How will records be retained and for how long?
- How will records be provided to the user and in what time increments (daily, weekly, monthly, etc.)?
- Who owns the records?
- How will access to the records be provided?

- Who bears the cost of providing the data?
- How will system integrity be verified?
- What will be available to verify that the data provided is complete and accurate?
- What timeframes should apply for providing the data for use in an audit?
- How often will periodic reviews of the host site be performed and access provided regarding the results of these reviews?

### **Additional Recommendations**

***Electronic Catalogues.*** When a taxpayer uses electronic catalogues, whether maintained by the taxpayer or a third party, the description of each item and its related identifier must be maintained. This may be accomplished by having the description captured within each individual line item or through references to the electronic catalogues. When catalogue references are utilized, the catalogues must be retained. The dates the catalogues were in use and a method of matching the catalogue reference numbers to the actual item descriptions must be available. When a taxpayer maintains the catalogues, it is the taxpayer's responsibility to ensure the information is available. When a third party maintains the catalogues, the access and retention of this information should be addressed by the agreement between the two parties.

***Identifying Codes.*** When creating a system or designing a record retention policy, a taxpayer will find it beneficial to have a coding system or other method available to identify the various electronic commerce initiatives in use. Codes for paper, EDI, procurement cards, ERS (evaluated receipts settlement), B2B, etc., may be beneficial for retention and future audits. The use of codes to identify types of transactions may assist in the audit process by allowing for the segregation of the various distinct business processes. This may be necessary due to the potential differences in the business processes associated with electronic commerce transactions, especially if significant volume exists for a particular business process. As in any other business process, if codes are used to identify items in an electronic record, the codes and code definitions need to be maintained as they existed during the period that the records are retained. Changes to codes or code definitions must be documented and retained or problems will arise in making determinations relating to the proper tax treatment of transactions. This is true whether the taxpayer or a third party maintains the records.

***Hosting Multiple Companies.*** When a third party is used and a number of companies are represented on the site, it is important that a unique identifier be created for each company. This identifier will assist in retrieving records from the site and will also help to ensure that one company's records are not inadvertently provided to another company on the site. It would also be beneficial for the third party to create a standard file format for the information captured by the site to provide to the various companies represented.

Appendix 1 of this paper contains an outline of steps a taxpayer may use in identifying data sources, and data retention and management issues.

### ***3. Procurement Cards and Tax Compliance: Bridging the Gap, June 1997***

The use of procurement cards in purchasing goods and services can reduce the costs associated with such purchases. Procurement cards can also raise certain tax compliance and administration issues for both taxpayers and tax administration agencies. For this reason, the Task Force developed a white paper with four objectives in mind: (1) Improve the understanding of procurement card programs and their operations. (2) Identify and analyze the tax administration and compliance issues associated with such programs. (3) Review steps that taxpayers and state tax agencies have taken to address these issues. (4) Recommend certain actions to taxpayers, tax administration agencies, vendors/suppliers and procurement card issuers that will help them address the administration and compliance issues in a fashion which meets the needs of all parties.

Changes in the business environment since the paper was published relate to the increase in business conducted in an electronic environment. In general, the original paper does not require major updates or changes, but the Task Force determined that certain areas need additional clarification when procurement cards are used in the B2B environment.

#### **What is the B2B Impact on Procurement Cards?**

In the most basic analysis, a procurement card program replaces the various steps in the traditional purchasing process, including purchase orders, invoices and receipts. However, in a B2B environment, purchase orders and receipts may be transferred between the parties. With the exception of some additional documentation that is not traditionally provided for in a typical procurement card program, the operations and mechanics of a procurement card program does not really change in the B2B environment.

As described in the original paper, the primary tax compliance and administration issue with respect to the use of procurement cards is “whether the information provided to card users on the periodic statement from the card issuer regarding purchases made with procurement cards is sufficient to document that the correct amount of state and local sales or use tax was collected on the transaction at the time of sale.” This concern will continue in the B2B environment. It is imperative that the businesses using procurement cards determine the proper methodology for maintaining documentation that details the proper tax has either been paid to the vendor or accrued and paid to the appropriate tax jurisdiction. This requires that the procurement card user maintain a system that allows for reconciliation between procurement card payments and the detailed records that support those payments (e.g., provide a detail trail from the vendor to the procurement card custodian to the final procurement card payment). In addition, all records with respect to B2B transactions should be stored according to the Model Recordkeeping and Retention Regulation. Maintaining proper documentation will assist the procurement cardholders in minimizing overpayment of taxes on transactions associated with e-Commerce, in general, and B2B transactions in particular.

In the original paper, the tax compliance issues revolved around the amount of detailed information that was captured on the periodic statement from the card issuer. When the

information was insufficient to determine the correct tax liability, the taxpayer was required to maintain the transaction-level paper records generated at the time of sale. When the periodic statement contained sufficient detail, the transaction-level paper records were not required under the Model Regulation. In the B2B e-Commerce environment, it is possible that the detailed transaction information captured within the software is not only sufficient for determining taxability but also may provide useful information for other business purposes.

When a procurement card is used to purchase an item over the Internet, the electronic invoice from the vendor will normally provide the required detail to track the purchase from the vendor to the procurement card statement. In this instance, either the vendor will charge sales tax or, if no nexus exists, the purchaser will accrue and remit use tax to the appropriate taxing jurisdiction. It will be important to establish the proper documentation process in order to determine where, in the purchasing and accounting process, tax is calculated and to ensure this information is integrated into the company's accounting software.

### **Recommendations**

It is important to remember that all interested parties—card users, vendors/suppliers, tax administration agencies, and card issuers—should work together to develop approaches that ensure sufficient detail is retained for tax administration purposes. As businesses continue to move toward electronic business processes, the opportunity exists for companies to capture and retain all procurement card information necessary for tax administration purposes.

Procurement card users must develop well-defined procedures and internal controls that address the tax administration requirements and reduce audit exposure. Vendors/suppliers should work with card issuers and users to ensure complete and accurate information is available in a usable format. In addition, vendors/suppliers should become properly registered in states where nexus exists. Card issuers are the ultimate provider of information to card users and should ensure that all information required for tax administration purposes will be available to card users. State taxing authorities have an obligation to define record retention standards and develop appropriate audit approaches and procedures for the review of procurement card transactions.

The original paper concluded: “As a final matter, however, all parties recognize that what we have today is not what we will have tomorrow or the day after. As the use of procurement cards matures and the technology of procurement cards improves, all stakeholders should establish a goal of ensuring that, over the long term, procurement card transactions are like any other and that the detailed information required for tax administration and other business purposes is readily available.”

#### ***4. Evaluated Receipts Settlement (ERS) and Tax Compliance, Sept. 1998***

Evaluated Receipts Settlement (ERS) is a business process between trading partners that conduct commerce without invoices. In an ERS transaction, the supplier ships goods based upon an Advance Shipping Notice (ASN), and the purchaser, upon receipt, confirms the existence of a corresponding purchase order or contract, verifies the identity and quantity of the goods, and then pays the supplier. ERS allows a business to streamline its purchasing and payment process, which results in reduced costs, reduced errors and elimination of unneeded activities. In addition, ERS results in more timely communication of information between trading partners, which results in better supplier relationships. The ERS white paper is an educational document that outlines the issues associated with ERS and discusses options for taxpayers and taxing authorities to ensure the necessary documentation is available for tax compliance and tax audits.

Similar to the Procurement Card process, ERS processes do not change significantly in a B2B environment. There may be additional parties involved in the ERS process due to B2B and there may be changes to how vendor information is maintained. In the early years of the B2B boom, a number of authorities predicted the demise of ERS. That has not been the case and ERS has been successfully integrated into many B2B systems. There continue to be a number of tax issues created by the use of ERS. The following is a summary of those issues and the questions that both taxpayer and taxing authority need to consider.

Issues common to electronic data interchange (EDI) and ERS follow:

1. Is there a sufficient audit trail to ensure proper regulatory compliance?
2. What access to these electronic or computer records will be given to the taxing authorities?
3. Are there adequate internal controls to ensure the integrity of the data?
4. Are hard copies available to support refund claims?

Issues unique to ERS include:

1. Since there are no invoices generated by a supplier, what will be accepted as a valid receipt of sales taxes paid by the purchaser directly to the supplier?
2. Traditionally, the obligation to calculate and remit sales tax is imposed on the supplier. Since the supplier no longer has complete control over the tax calculation function, this becomes more complicated. How will the tax authorities cope with this changing environment? How will the supplier be able to document that the correct tax was paid? How will the purchaser and supplier maintain nexus coordination so the purchaser calculates tax only in jurisdictions where the supplier is registered? In origin-based states, how will the purchaser know where the order originated? How will sales versus use tax be calculated appropriately?
3. ERS creates accounting and auditing issues different from those posed by conventional systems. Validating internal and inventory controls, no sales

- invoices, and a different method of purchasing and payment provide new challenges for taxing authorities. How will they deal with these challenges?
4. There may be discrepancies such as freight, price, or quantity adjustments that affect the sales tax base. What will be available and acceptable to validate these changes from the original purchase order (goods order)?
  5. Local taxes and home rule taxes may differ from state laws. How can these differences be addressed in an ERS system? Alabama, Arizona, California, Colorado, Illinois, Louisiana and others have different local tax rules that may be different from their state tax rules. This issue needs to be considered when using ERS.
  6. Since a sales invoice may not be created involving an ERS transaction, what will be acceptable proof to support a claim for refund?
  7. Many states' laws require that sales and use tax are separately stated. In the absence of an invoice, can this legal requirement be met by other documentation? What forms of documentation will be available and acceptable to meet this requirement?
  8. With additional parties in a B2B ERS environment, issues related to internal controls need to be addressed by the parties and states.

#### **ERS - Tax Calculation/Verification**

1. In ERS, the purchaser must calculate tax as if the supplier were issuing an invoice. This can only happen if significant programming and system enhancements are installed as a transition from a traditional accounts payable environment. Some third-party sales tax software products may be able to accommodate the complexities related to determining tax on ERS transactions. Others will not. Since the purchaser must calculate tax as if it were the supplier, an ongoing relationship between the two parties is necessary.
2. Purchaser should not remit tax to the supplier for jurisdictions where the supplier is not authorized to collect taxes. In these situations, the purchaser must accrue and pay the use tax on taxable purchases. Many states do not authorize direct pay. Therefore, purchaser should not assume that it can pay all the taxes directly to the tax authorities as use tax. Also, the supplier may turn to the purchaser for payment of tax at a later date and double taxation may occur.
3. To accurately calculate the sales tax that the supplier would charge, the purchaser must set up taxability matrices simulating the tax authority of each supplier. It is important for the tax departments of both supplier and purchaser to communicate regarding the jurisdictions where supplier is registered.
4. ERS transactions will be processed first through the taxability matrices simulating the supplier's tax authorities on the purchaser's system to calculate the tax "charged" by the supplier. Tax should **not** be established as a tax accrual, since the tax is not being paid by the purchaser to the state. The purchaser will need to set up procedures to include the tax calculated with the payment of the ERS transaction.

5. If no tax was calculated through the taxability matrices either because the supplier is not registered in the delivery state or because the ERS transaction is exempt, then the ERS transaction is processed through the use tax accrual process. A procedure may be written such that if after passing through the taxability matrices the ERS transaction is determined to be exempt, no pass to the accrual tables is necessary.
6. Since the order may include the tax amount, the purchaser may wish to have an interface to the order system to read the supplier taxability tables to calculate the tax for inclusion on the order system.
7. Because tax rates differ in some jurisdictions between sales and use tax, appropriate address information should be maintained to determine the correct tax type. This information includes the ship from, ship to and order acceptance locations for both the supplier and purchaser.
8. In the B2B environment, additional tax issues arise related to who will be responsible for the tax calculation and the maintenance of the data elements. If an exchange is used, the purchaser may not have access to the information necessary to determine the amount of tax to be paid to the supplier. Another issue is who will be responsible for making taxability determinations and maintenance of the detailed records needed under audits.

#### **Potential Solutions to ERS Issues**

Steps that can be taken to address the ERS issues include the following:

1. Whenever possible, master service agreements, master contracts, trading partner agreements or other similar agreements should be formalized. Items that should be addressed in these agreements are, taxability of goods, discount terms, supplier's sales tax registration numbers, calculation and payment of sales tax, and agreement by both parties to cooperate in the event of a tax audit. In a B2B environment, additional items that need to be addressed include listing who is responsible for handling all the sales tax calculation processes, noting where the records will be maintained and determining how long the records will be retained.
2. The parties should agree to work together on audit issues, and should make available to each other any and all necessary records or documents as requested by taxing authorities. This may be more important and more frequently needed in an invoiceless environment.
3. The parties should work together to ensure that the taxes are calculated, sourced, and remitted correctly. Issues such as taxability, sourcing for local taxes, and timing for remittance should be thoroughly documented and agreed upon.
4. Trading partners should archive all pertinent electronic data and retain for audit purposes in the same manner as paper records. It is suggested that the following electronic records be archived and retained pursuant to taxing authorities statutes:
  - a. **Electronic Purchase Orders** – Including purchase order number, supplier name, description of goods, quantity, price, discount terms, taxability of item, freight, tax, and account coding.

- b. **Electronic Goods Receipt Data (Receiving Report)** – Including goods receipt reference number (receiving report number), date of receipt, supplier name, quantity received, description of goods, bill of lading or packing slip number, purchase order number, and contract number.
  - c. **Electronic Price Lists** – Including all updates, changes, dates, etc. to support pricing on the purchase order.
  - d. **Tax Calculation Data** – Including historical tax rate tables, matrices, and related data.
5. States with limited or no direct pay authority should consider broadening or implementing direct pay authority statutes to accommodate taxpayers utilizing ERS and other advanced electronic processes. This would shift the tax compliance burden to the party that possesses the requisite information. The payment information generated and captured by the purchaser is more precise; therefore, the compliance level increases. Implementation of direct pay authority will require major law changes in some taxing jurisdictions.
  6. Maintain documentation of the procedures used to enter the information pertaining to the ERS transactions into the accounting system and be prepared to explain them to the taxing authorities.
  7. Consider the use of “tax only” summaries or invoices to be sent by suppliers to purchasers to address valid receipt concerns. In the event the supplier provides “tax only” invoices, the purchaser will need enough detail to be able to trace the taxes back to the applicable transaction/payment in the purchaser’s system to document for audit purposes and verify for accuracy.
  8. Another possibility is for taxing authorities to recognize purchase orders as an “in lieu” invoice, consider ANSI X12 transaction set 856 generated by the supplier as an “in lieu” invoice, or some combination of the purchase order and transaction set 856 as an “in lieu” invoice.
  9. Some purchasers send a monthly tax summary or statement to their suppliers. Purchasers who send a monthly statement to a supplier, summarizing sales taxes paid to state taxing authorities, may be relieved of their tax liability in some jurisdictions. Other taxing authorities may not accept this premise and may require additional documentation.
  10. In the event the purchaser will be calculating sales and use taxes to pay the supplier, the supplier will need to provide the purchaser with the appropriate list of taxing jurisdictions, and their respective registration numbers, where the supplier is qualified and registered to collect sales and use taxes. Without such information, the purchaser will need to remit the appropriate taxes directly to the taxing authority. This ensures that the purchaser does not make a voluntary payment of taxes to the supplier for a jurisdiction where the supplier is not able to remit such taxes.

### **Recommendations**

Use of ERS in a B2B environment creates the same issues as a traditional ERS process. However, given that there are typically additional parties to the transaction, full

cooperation between all the parties is necessary. Coordination of record retention, record location, and system functionality and tax information maintenance is critical. Internal controls are also of concern as an unrelated party may be the primary party handling the sales and use tax issues.

### ***5. Sales and Use Tax Compliance Agreements, March 2000***

Sales and Use Tax Compliance Agreements (SUTCAs) are up-front agreements between a taxpayer and tax authority that detail the manner in which the taxpayer is to calculate and report tax on its purchases and the manner in which tax compliance is to be evaluated on audit. SUTCAs are known by a variety of names, including managed compliance agreements, effective use tax rate agreements, formulary sales and use tax agreements, negotiated rate agreements, alternative use tax payment methods, and simplified procedure agreements.

The Sales and Use Tax Compliance Agreements report explores the operation of the SUTCA and outlines the perceived benefits and costs associated with them. The report also reviews the major elements likely to be present in a SUTCA and discusses a number of issues that are likely to affect the operation of a SUTCA, and, therefore, ought to be considered in arriving at an agreement. Finally, the report concludes by reviewing activities that need to be undertaken in evaluating a SUTCA at the conclusion of its term.

#### **What is the B2B Impact on SUTCAs?**

B2B transactions may be different from traditional purchases relating to tax compliance and accounting practices. Since this is a new and evolving business process, the taxpayer and taxing authority may wish to consider whether B2B transactions should be included in the scope of the SUTCA or whether a separate effective tax rate or taxable ratio should be calculated.

Several matters should be evaluated in making this decision. Perhaps the most important aspect of this decision is the consistency of purchasing practices within the taxpayer's B2B environment. While expansion in the number of transactions using B2B should not cause any unmanageable problems, the change in mix of products purchased under B2B may. A significant change in the mix of taxable and exempt purchases and qualifying and non-qualifying direct pay purchases will require an adjustment in the rate or ratio calculated. If this is in a constant state of flux, it may be difficult to create an effective rate or taxable ratio that is representative of the business activity over a period of time and that does not require constant monitoring and adjusting.

Another major question is whether the taxing authority has sufficient knowledge of the subject to feel comfortable including B2B transactions in the SUTCA. With this being a new emerging technology, taxing authorities may not have begun auditing the periods where B2B has been used and may have limited experience in dealing with this business practice. The taxpayer should work with the taxing authorities to educate them about B2B and explain how this business process is integrated into the company's purchasing and accounting systems. A better understanding of the company's B2B process may

allow the taxing authority to gain sufficient comfort to include B2B transactions in the SUTCA.

Once these hurdles are crossed, the tax authority will need to determine if the taxpayer has utilized B2B processes long enough in a stable pattern to have sufficient history to develop a base period that accurately reflects the taxpayer's purchasing patterns. This base period will be analyzed and used to formulate the effective tax rate or taxable ratio. If the answer to this is no, it may be prudent to leave the B2B transactions out of the SUTCA until a stable base period exists. If the answer is yes, then the following items will need to be addressed: (1) Does sufficient information exist in the B2B records to make a determination of proper tax treatment? (2) If a taxing authority requires the use of direct pay to enter into a SUTCA, do the taxpayer's B2B purchases qualify for direct pay treatment? (3) If there is a mix of qualifying and non-qualifying purchases, can the taxpayer's system or the third-party host manage the tax compliance issues related to the different transactions? (4) Does the taxpayer or third-party host maintain detailed electronic records necessary for the tax authority to develop a base period, calculate the effective tax rate or taxable ratio, conduct verifications, and establish a new base rate?

### **Recommendations**

Regardless of the questions that exist regarding B2B and SUTCAs, the concepts and techniques for including B2B transactions within a SUTCA should not be substantially different from the methods identified for other types of transactions. The taxpayer and tax authority should work together to develop an understanding of the B2B processes and how they may affect development of the SUTCA. It cannot be stressed enough that the taxpayer must maintain detailed records necessary for the tax authority to develop a base period, calculate the effective tax rate or taxable ratio, conduct verifications and establish a new base rate. Once the outstanding issues surrounding a taxpayer's use of B2B are settled, there should be nothing that would prohibit the inclusion of B2B transactions in the SUTCA.

## **6. *Model Direct Payment Permit Regulation, June 2000***

Direct pay is an authority granted by a tax jurisdiction that generally allows the holder of a direct payment permit to purchase otherwise taxable goods and services without payment of tax to the supplier at the time of purchase. The holder of the direct payment permit then timely reviews its purchases, makes a determination of taxability, then reports and pays the applicable tax due directly to the tax jurisdiction. Direct pay was originally designed to overcome the tax complexities in situations where the taxability of a transaction could not be easily determined at the time of purchase. In today's environment, however, with the increased volume of activities in interstate commerce and the application of new technologies to purchasing practices, some members of the business community would like to see direct pay authority expanded to allow more taxpayers to better administer their tax compliance activities and accommodate new electronic business processes. In response, the Task Force developed a Model Direct Payment Permit Regulation (Model Regulation), which focuses on the business process of a taxpayer when a tax jurisdiction considers whether to grant direct pay authority.

### **What is the B2B Impact on the Model Direct Payment Permit Regulation?**

Advancements in technology have allowed businesses to streamline their purchasing and payment processes, but have increased the administrative work of complying with state and local tax laws. Some large multistate businesses view direct pay authority as a valuable tool in automating their accounts payable function and managing their tax compliance responsibility. Direct pay allows businesses to handle EDI transactions more efficiently, makes ERS transactions much more straightforward and auditable, and facilitates the use of SUTCAs. The increased use of B2B processes only emphasizes the need for an expansion and simplification of direct pay authority within all states.

Within the Model Regulation, it is important to note that the applicant is required to demonstrate its ability to comply with the sales and use tax laws and reporting and payment requirements of the taxing authority. The applicant must also provide a description of the accounting system(s) to be used and demonstrate that the accounting system(s) will reflect the proper amount of tax due. All records must be maintained and made available to the taxing authority upon request. Failure to comply with the provisions of the Model Regulation may result in revocation of the direct payment permit by the taxing authority.

### **Recommendations**

As stated in the original Task Force report, taxpayers and tax jurisdictions should work together to establish tax compliance procedures that ease the tax administration process. Therefore, simplified, consistent rules for direct pay authorization should be considered by all taxing jurisdictions. Taxing jurisdictions should consider following the Model Direct Payment Permit Regulation when implementing or expanding a direct pay program. Taxpayers should make use of available opportunities to work with the appropriate legislative bodies and revenue departments to ensure that they have an understanding of business concerns and needs to have consistent and logical direct payment provisions among all states and the potential benefits that could be derived from such.

## ***7. Sampling for Sales and Use Tax Compliance, December 2002***

Sampling is used when transactions are so voluminous that it is not feasible for an auditor to examine every transaction. The volume of transactions during a typical compliance review is growing as taxpayers' business activities increase. Both taxpayers and taxing authorities seek sampling methods that will be effective, efficient and equitable in determining sales and use tax compliance at a reasonable cost.

Although most states employ sampling in some form, the sampling methodologies vary from state to state. However, in many instances the typical steps involved in a compliance examination, especially when sampling is used, will remain constant. Both taxpayers and taxing authorities agree that a better understanding of state practices with respect to sales and use tax compliance and sampling practices is needed.

In response, the Task Force developed the sampling white paper to (1) provide an introduction to the applications of sampling in tax and nontax environments; (2) identify

the typical steps involved in the compliance review when sampling is used; (3) review supplemental issues that may arise from the use of sampling; (4) educate taxpayers and taxing authorities on the various sampling methodologies used by the states; and (5) provide a common language that taxpayers and taxing authorities may use to facilitate discussions.

### **What is the B2B e-Commerce Impact on Sampling Practices?**

As stated above, sampling is important to the tax administration process when transactions are so voluminous that it is not feasible for an auditor to examine every transaction. Sampling may be performed on paper records, electronic records, or a mix of the two. The move to B2B processes does not change the primary focus of the tax audit, which is to verify that a taxpayer has properly determined and paid its tax liability. Accounting records that are maintained electronically will allow the tax auditor to streamline the sampling process and will generally result in audit efficiencies.

As stated in the original paper, “When the population is available electronically, besides the obvious ability of the computer to handle very large populations or to sort and manipulate data, it is easier to do the following:

- Analyze the population for its completeness or suitability for sampling
- Refine the population by removing extraneous accounting records not relevant to the compliance review
- Stratify, or divide the population into segments (strata)
- Correspond random numbers to actual business documents
- Manage information obtained in the examination of the sample units
- Evaluate the sample using objective statistical formulas
- Obtain information about the population, including total amounts, record counts, and other statistical data (such as a mean, median and standard deviation of amounts to be sampled)”

### **Recommendations**

The Sampling white paper was developed solely as an educational document for taxpayers and tax administration agencies and made no recommendations on sampling methods or strategies. Rather, the paper provided a detailed look at the typical steps involved in a compliance review when sampling was utilized. It is important to remember that each taxing authority develops its own policies on acceptable sampling practices, and businesses are encouraged to gain a better understanding of the sampling practices and methodologies employed by individual taxing authorities.

## **Summary**

Electronic commerce is here to stay. It is also the most rapidly changing aspect of tax administration and compliance. This means that taxpayers must remain aware of all of the many issues surrounding electronic commerce. It falls on each company's tax

department to stay abreast of changes within their company that may affect their ability to comply with the tax laws and to document that compliance.

Tax administration agencies need to understand the difficulty faced by corporate tax departments in staying abreast of these rapid changes and work cooperatively to minimize problems. The task force experience is that taxpayers are working very hard to master these issues and to comply with individual state tax laws. They ask only that agencies work with them to resolve all of the various issues raised in this paper.

## **Appendix 1**

### **Data Management and Retention Issues**

The following is a suggested outline of issues:

#### **1. Identify All Data Sources**

- Who created it?
- What systems were utilized?
  - Mainframe/legacy
  - ERP – SAP, Peoplesoft, Oracle, etc.
  - Web Solutions
  - B2B – Commerce One, Ariba, Oracle, etc.
  - P-Card
- What PC applications were utilized (Excel, Word, Access, Lotus Notes, etc.)?
- Where is the supporting detail information stored?
- How long is the supporting detail information retained?
- What common link is there to the original transaction?
  - Purchase Order number
  - Work order number
  - Project description
  - P-Card transaction number
  - Bill of lading

#### **2. After Identifying the Data, What is Next?**

- Determine what is considered “tax data” and identify record retention requirements and communicate to staff
- Develop an automated tool to capture non-transactional information
- Set up a methodology to ensure that transactional level data from all legacy systems and any new systems is captured in a standard format. This might be accomplished via a data warehouse
  - Define the fields that are required from each system
  - Establish a corporate policy to ensure the data is captured, retained and tested for accuracy

#### **3. Potential Benefits**

- Critical Tax Staff data will be readily available to facilitate planning, compliance and audit requirements
- Best reporting practices can be identified and implemented across all systems
- A standard file format for all systems will assist in the retrieval and processing of the data. While this may not be possible within the systems themselves, it may be possible to create separate audit files as long as a proper audit trail is available to verify that the information is accurate and complete

## **Appendix 2**

### **Persons Contributing to This Report**

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## **Appendix 3**

### **Summary of Other Task Force Reports**

***Model Recordkeeping and Retention Regulation*** is intended to govern taxpayer retention of books and records, particularly electronically generated and retained records, for tax administration purposes. To date, *Alabama, Arizona, Arkansas, California State Board of Equalization, Connecticut, Florida, Georgia, Illinois, Iowa, Maryland, Michigan, New Hampshire, New Jersey, New Mexico, New York City, North Dakota, South Carolina* and *Utah* have adopted the model regulation in whole or in part.

***Auditing Electronic Data*** provides an overview of the basic framework of the tax audit and examines various issues related to auditing in an electronic environment.

***Procurement Cards and Tax Compliance: Bridging the Gap*** discusses use tax compliance issues associated with corporate procurement cards and examines alternative methods of achieving the appropriate compliance.

***Evaluated Receipts Settlement (ERS) and Tax Compliance*** focuses on understanding the ERS process and identifying potential solutions that would be helpful in addressing the audit and recordkeeping issues created by the use of ERS.

***Model Direct Payment Permit Regulation*** examines the issues involved in the use of “direct pay” permits, a procedure through which certain purchasers are allowed to pay use tax on their purchases directly to the state tax administration agency, rather than to a retailer. The report also contains a model regulation to govern direct pay authority and a survey of state direct pay authority statutes and use.

***Sales and Use Tax Compliance Agreements (SUTCAs)*** are agreements between taxing agencies and taxpayers that specify an agreed-upon method for calculating and remitting tax on specified purchases, and which identify alternative reporting methodologies, best practices, and recommendations for taxpayers and tax agencies to follow when entering into these agreements. This report includes a summary of state practices with respect to sales and use tax compliance agreements.

***Sampling for Sales and Use Tax Compliance*** examines the typical steps involved in a compliance examination, especially when sampling is used. The report also reviews supplemental issues that may arise from the use of sampling, provides a summary of the various sampling methodologies used by the states, and provides a common language that taxpayers and taxing authorities may use to facilitate discussions.

Editor’s Note: All reports are available from the Federation of Tax Administrators’ Web site <http://www.taxadmin.org>.