3 Company growth-related activities that can be life (and tax) changing

Sales and use tax compliance can impact financing events, M&A activities and technology platform integration projects more than many businesses may realize

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Growth strategy can vary widely among companies and industries. The catalyst to growth, or in some cases the outcome of growth, is an influx of new funding, intellectual or physical property, or technical capability resulting from financing events, mergers and acquisitions, and even changes or upgrades to technology platforms.

During these dynamic change events, tax compliance often takes a backseat to other priorities. But it shouldn't. Company growth can vastly change your sales tax nexus footprint (the obligation to collect sales tax in a state based on sales activities in that state). Having a reliable, scalable plan in place to deal with any new tax obligations that result from these changes is imperative to avoid any lapses in compliance that could come back on you.

Read on for key insights and best practices from leading industry experts on why managing change is imperative for growing businesses and how sales tax management factors into this process.

"We've been on both sides of these transactions and seen many instances where sales tax exposure is the single biggest obstacle to overcome. It makes sense to buyers to be cautious because, even in a pure asset sale, the buyer may bear the burden of any past sales tax exposure. It's very important for a company looking to sell, or even just seeking outside funding, to make sure they're on top of potential exposure."

- Andrew Johnson, CPA, Managing Partner, Peisner Johnson & Company LLP

Financing Events

Companies need capital to grow. But backing a venture is a big decision – a risky one – and investors don't fund deals without first doing their homework. For any financing event, public or private, investors not only look closely at how you plan to grow the business but also how you are managing it now. This includes tax compliance and audit histories.
The impact of sales tax on company valuation is often underestimated. But that can be detrimental, warns financial consultant and strategist Lisa Serwin. If there is a funding round, company sale, or IPO, being clean and consistent and having an auditable record is of the utmost importance. Poor sales tax management practices or unfavorable audit outcomes can impact valuation, jeopardize funding or even nullify deals.

High visibility events like funding rounds and IPOs can also bring your business to the attention of state auditors looking to draw in more tax dollars. Companies with a higher profile and higher revenues tend to be chosen for audits more often warns Shane Ratigan, a tax attorney and compliance manager for Avalara. Several states have nexus discovery units within their revenue departments that scour public information to find companies that are not compliant with their states' laws. The more you "stand out from the crowd" among other businesses, the more likely they are to pay attention to your situation.

"In some cases, an acquiring company requires the seller to provide a 'tax clearance certificate' or its equivalent from states where the target company is doing business. Certain states may also require buyers and sellers to give notice of a sale of the company."

- Andrew Johnson, CPA, Managing Partner, Peisner Johnson & Company LLP

A phase of rapid growth can quickly change your tax profile. To avoid frequent reassessments of tax risk or worse, missing it altogether, it's imperative to have a tax compliance plan that grows with your business. The plan should soberly address where you are likely to grow next and address those tax responsibilities up front.

Mergers and Acquisitions

A good M&A strategy is important for growth, but from an operational standpoint, it can present challenges. After the deal is inked and the excitement wanes, you're now faced with bringing together one or more organizations that, while aligned in some areas of the business, may not be in others.

It's a concern that keeps company executives up at night, according to Deloitte. A recent survey by the global advisory firm found that problems with business integration was the number one worry following an M&A transaction. That's not surprising given that 75% of acquisitions performed below expectations following a merger.[1]

The meshing together of people, assets, systems and processes can be lengthy and complicated. Between due diligence, integration, accounting/financial reporting, and post-acquisition compliance, who has time for the minutia of sales tax? Not finance, operations and IT; they're focused elsewhere. Yet, many of the reasons for acquiring a business – more market share, a broader product mix, even physical property – are common tax liability triggers. During the integration process, it can be easy to overlook new or different tax obligations, such as nexus, jurisdictional rate changes or product taxability rules. This can lead to over or undercharging sales tax and raise red flags with auditors.

Additionally, the target company may have been carrying tax attributes on its books or ongoing tax audits that could transfer to the new organization. If these

[1] Deloitte

aren't properly identified and managed as part of the due diligence during the deal, they could cause compliance problems later.

Technology platform changes, consolidations or upgrades

During periods of growth or change, it's good practice for CFOs or controllers to dive deeper into how compliance is being managed, identify vulnerabilities, and look for new or better ways to operationalize or optimize the business. This could mean re-evaluating your financial systems and filling any gaps with new solutions or functionality that can advance these objectives. For example, Accenture found that companies that take the time to properly integrate systems following a merger reduce costs of key business functions by as much as 40 percent.[2]

CPA Firms routinely advise clients to automate sales tax during systems integrations to reduce compliance costs and audit risk. Failure to properly integrate systems may prevent the company from "speaking with one voice" on the taxability of the same or similar products and services in a merger of equals. While it's understandable that differences may exist early on in the process, such discrepancies are harder to explain or defend over time.

Having sales tax automated in your ERP, ecommerce system or other financial application ensures that you're able to keep up with your compliance obligations as your business grows or changes. Cloud applications like Avalara that integrate easily with your existing systems help protect against lost or spotty data resulting from a platform change, upgrade or consolidation. They can also help unite valuable transaction and tax data from disparate systems and processes that so that your financial team isn't delayed in closing the books and forced to pay costly penalties.

Changes to sales tax rates and rules are often done last minute or with minimal notice, so it's not always easy to know when they happen or how they affect you. If you are having to make these updates manually in several different systems or server locations, it's a lot harder to ensure consistency and timeliness, which could impact sales and customer service. Avalara's automated, cloud-based tax solutions make those updates and changes in real-time and push that data to all your systems simultaneously so you don't risk these errors or oversights happening.

[2] Accenture

Get ready to grow with Avalara

If you're company is growing, it's highly likely that you'll be engaged in one or more of these change events. When that happens, your attention and resources will be strained and focused elsewhere – not on sales tax. So don't wait. Implement an automated sales tax compliance solution like Avalara now so that when the inevitable happens, you're ready. You may even find that confidence in your tax compliance is one of the most valuable assets to come out of the deal.

Your accounting team may try to avoid exposing their own mistakes or might simply overlook errors. Auditing yourself is like editing your own book. It's difficult to be objective when you're so close to the process. But even if you don't employ outside expertise, conducting an internal audit is worth the effort and will likely pay off in reduced penalties down the road.

Something to consider: If you choose to handle the audit yourself, at the very least consider getting a tax representative to bounce questions off of. Just like most things in life, what you don't know can hurt you.

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