

AR

THE AUDIT REPORT



ARTICLE TOPICS
ANOTHER YEAR ENDS!
CLOSING THE GAP
WHAT'S EXEMPT?



Another Year Ends

Thank You for Another Amazing Year at Tax Management Associates! | By Chip Cooke

It's hard to believe, but another year is ending at Tax Management Associates. This has been a diverse year at TMA, with big moves throughout the company. Even in a down economy, TMA has gone from 110 employees in January to 132 in November - an uptick of 22 new faces to join the team - with the expectation of more to join in 2011.

W.L. (Bubba) Ricketts Retirement

TMA has also had some departures this year, including the retirement of long-time Tennessee sales lead W.L. (Bubba) Ricketts. Bubba will continue to work with TMA on a contract basis, so you will still see him around the state, but he has earned a much deserved rest in his retirement. Bubba started with TMA on November 1, 1996 and since that time has touched thousands of lives within the property tax community. He was instrumental in signing eighty-four (84) of the ninety-five (95) counties in Tennessee and assisted in starting TMA's Nashville and Chattanooga offices.

Those who have worked with Bubba know him as thoughtful, knowledgeable and well-versed in tangible personal property taxation. Although Bubba will still participate in certain events throughout the state, he will be missed

“Even in a down economy, TMA has gone from 110 employees in January to 132 in November, an uptick of 22 new faces to join the team.”

as a full-time TMA employee. Best wishes to Bubba in his retirement.

Special Projects Division Growth

TMA's Special Projects Division may have seen TMA's biggest percentage increase in business this year, with

many successful discovery initiatives, outsourcing programs in two (2) states and the continuation of TMA's Principal Residence Exemption (Homestead) program at the Michigan Department of Treasury.

TMA's Discovery Division, led by Jessica Hadlock, has had one of the most successful years in the division's history. To date, Jessica's teams have completed, or are in process of completing programs for thirty-seven (37) clients in (6) states. These programs have added over 20,000 taxable businesses to the rolls - an average 10% increase. These businesses equate to over \$1.2 billion in additional taxable value. With several high profile clients signed for 2011, Discovery's growth next year is all but assured.

Sarah Diehl, leader of TMA's Outsourcing programs, has had an equally good year with the successful completion of programs at three client locations. Durham County and

Orange County in North Carolina and Gwinnett County in Georgia have all completed their programs and are on tap to start the listing process anew in January 2011. Listing administration outsourcing has become a popular topic among those in the tax community as our clients try more creative ways to reduce cost and staff efforts in the personal property process. TMA expects more clients to exercise this option as we strive to perfect this difficult and time-consuming process.

Kathy Boyea and TMA's PRE program for the Michigan Department of Treasury continued its good work in 2010 with more value created for the state. In four (4) years, TMA has examined over 6.5 million parcels across fifty-five (55) counties for improper PRE filings.

TMA's Audit Division Additions

By now, you have already heard of new staff additions, including new North Carolina / Georgia Area Manager Chip Bourgeault and new sales and marketing member Kirk Boone, PPS from the North Carolina Department of Revenue. 2011 is shaping up to be one of the best in TMA's audit history with work signed in Indiana, North Carolina, Georgia, Alabama, Tennessee, Florida, and Connecticut. As the economy continues to struggle, we are also seeing opportunities in states that did not previously rely on audits for equity and uniformity. Until revenues to state and local governments rebound, jurisdiction leaders will continue to check every self-assessed tax for accuracy and completeness. As TMA has now completed over

140,000 similar audits, we will continue to be a leader in that respect.

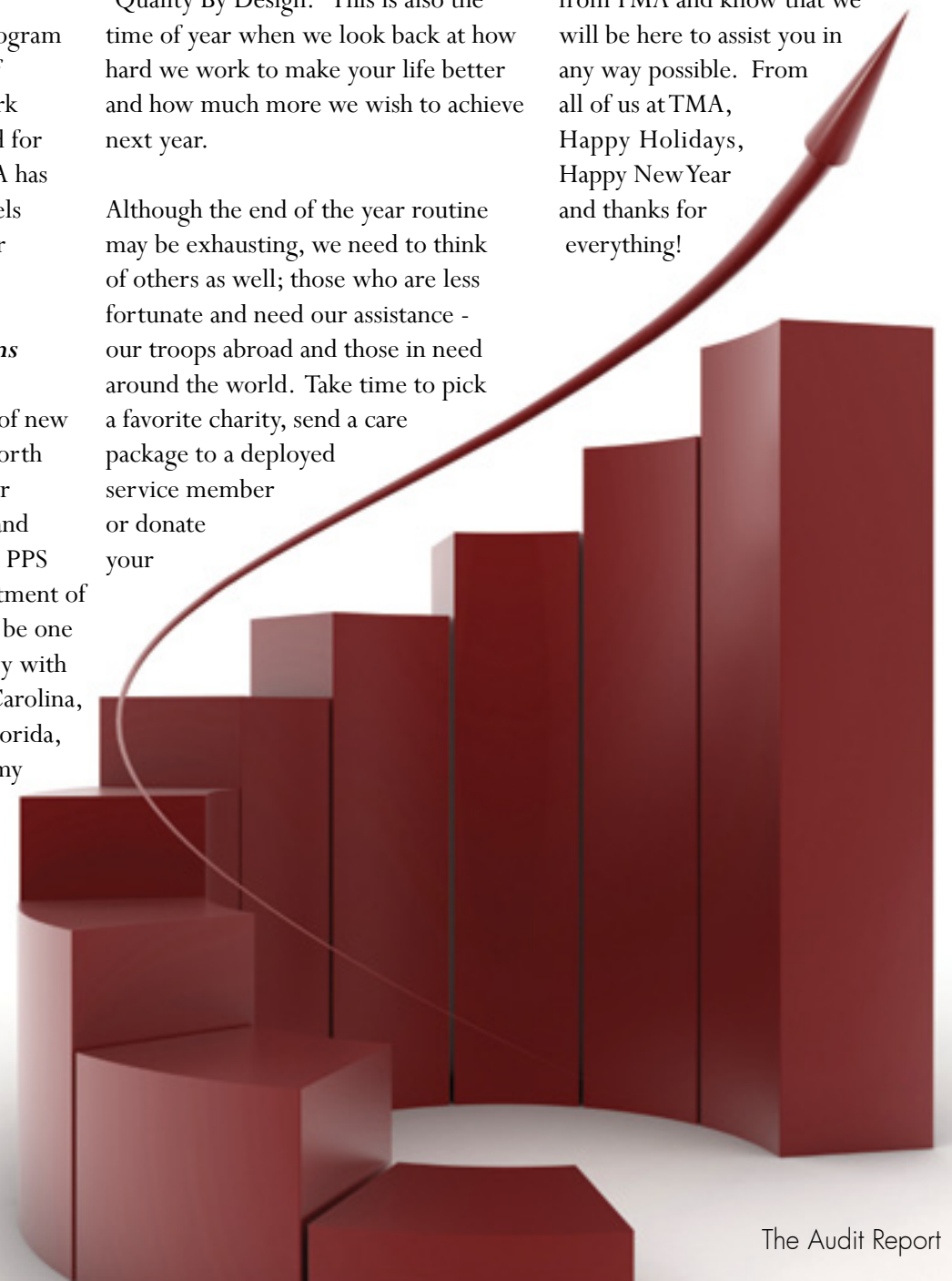
Holiday Wishes and the New Year

This is the time of year when we try to do our best in thanking all our wonderful clients, partners and friends. The end of the year brings reflection on all the things we have done well and all those that need attention. We are the first to admit we are not perfect, but we are always striving towards our motto: "Quality By Design." This is also the time of year when we look back at how hard we work to make your life better and how much more we wish to achieve next year.

Although the end of the year routine may be exhausting, we need to think of others as well; those who are less fortunate and need our assistance - our troops abroad and those in need around the world. Take time to pick a favorite charity, send a care package to a deployed service member or donate your

time to an aid organization, but most of all, make a difference in some small way to show how much you care.

In the new year, TMA will be continuing its service to all of our clients, and starting services for new jurisdictions. In our 32nd year, we strive toward even higher levels of service across all aspects of our company and will continue to lean on you for advice and feedback on how to make that goal possible. Be on the lookout for new creative solutions from TMA and know that we will be here to assist you in any way possible. From all of us at TMA, Happy Holidays, Happy New Year and thanks for everything!



To learn more about any of TMA's services, visit www.tma1.com or contact us at 1-800-951-5350



Closing the Gap

How TMA Helps Clients Right the Fiscal Ship | By Chip Cooke

It's everywhere you look these days. The nation is awash in red ink as the recession continues to batter state and local government budgets. For the past three years we have watched as revenues from income tax, sales tax and property tax have declined throughout our client base. Pressure to eliminate items from client budgets has resulted in staff declines, early retirements, eliminated programs and stalled capital projects. With few exceptions, this downturn has become the new normal.

While there have been some promising trends in the stock market in 2010, consumer confidence remains weak, and those with disposable income continue to sit on the sidelines, watching for some sign that the worst is over. This reluctance to spend is draining sources of revenue for governments, forcing budgets to be slashed and resources to be stretched too thin. This is the problem our clients are facing - when there is nothing left to cut, what are your options? The answer,

as TMA has suggested, is to ensure that every existing tax is administered to the fullest potential.

For over thirty (30) years, TMA has been a leader in the state and local

“Quite frankly, this is a job we take seriously. To date, TMA has created almost \$800 million in additional tax dollars for our clients across the country.”

government space, and increasingly we find ourselves in the role of revenue enhancement - maximizing dollars to government through existing resources. This means finding everything that is taxable and ensuring that individuals and businesses pay their fair share. Quite frankly, this is a job we take

seriously. To date, TMA has created almost \$800 million in additional tax dollars for our clients across the country. These tax dollars have come with the addition of almost \$36 billion in unreported additional property tax value from various sources, including business personal property tax audits, discovery of non-listing businesses and denied homestead applications. The best part about this tax value is that it often creates continuing annual revenue for our clients.

From a philosophical perspective, these service lines make even more sense. Imagine the dilemma of community elected leaders who need to provide services to their constituents. Those constituents agree to fund these services through taxes that are approved at both the state and local levels. But what happens when the taxes are only assessed and collected at 50% of their allowable level? Of course, the quality of the services is sacrificed.

It's unfortunate, isn't it? But there are a number of factors that contribute to these lower than anticipated revenue levels, especially when dealing with self assessed taxes, where the problem can persist indefinitely if not addressed with specific policies and procedures. A self-assessed tax by its very nature is voluntary - not voluntary in that you may choose not to participate, but voluntary in that the information supplied is freely given by the taxpayer. That information may or may not be accurate, and the duty to determine truthfulness in listing becomes the responsibility of the taxing jurisdiction. So what happens when staff is lost through budget cuts and other revenue shortfalls? The ability to ensure accurate listings becomes even harder and revenues continue to drop. These decreased revenues lead to decreased staff, eliminating compliance efforts and decreasing revenues even further - the tax system essentially begins to eat itself.

So the question becomes, how do we close the gap and stop the cycle? The answer is fairly obvious - the jurisdiction has to collect everything it is legally owed in order to remain funded at the highest level possible. There are a few options jurisdictions have to accomplish this. They may shift staff from other responsibilities to compliance efforts. This could mean having real estate appraisers double as compliance personnel, or moving personnel from other departments to the tax office for a limited time. However, these options are not ideal and the jurisdiction may not have the resources in place to adequately train staff to perform these functions. Because of this problem, compliance efforts often fall to the wayside.

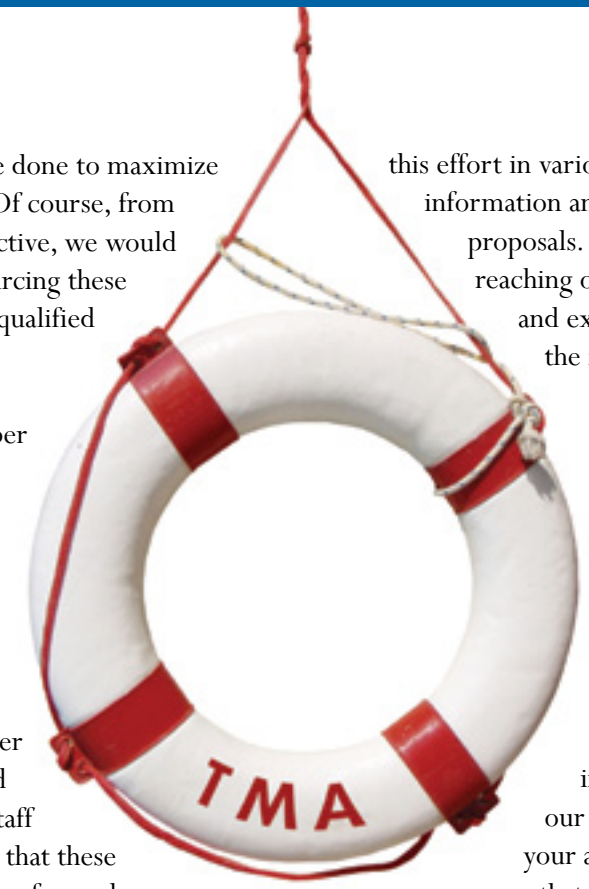
So what can be done to maximize compliance? Of course, from TMA's perspective, we would suggest outsourcing these functions to a qualified third party. Outsourcing carries a number of benefits, including, but not limited to cost, training, scalability and experience. The costs are inherently lower than hiring and training new staff due to the fact that these programs are performed on a limited basis - usually from three to five years in nature. A staff hire, on the other hand, will incur cost until the employee is terminated, quits, or retires - often carrying additional costs in terms of associated pensions. A qualified third party will already be trained in the field of compliance and will bring its own policies and procedures as best practices for the client. The third party is more readily scalable and may add or decrease staff as necessary to reach the client's objectives. Finally, the third party is often more experienced in these matters, and in the case of TMA, may bring decades of experience and training to bear.

Until the economy recovers and revenues begin to flow into state and local government again, it is imperative that tax offices across the country become more aggressive in their approach to verification of existing taxes. We are already seeing

this effort in various requests for information and requests for proposals. States are reaching out to contractors and experts across the field of taxation looking for comprehensive solutions in revenue enhancement. As TMA responds to these requests, we return the same information to our clients - know your available taxes, ensure that everyone who is supposed to list with your office is doing so, and verify that the listing is accurate.

As budgets are already stretched, even projects with positive ROI are hard to fund initially. TMA can assist in that effort by suggesting alternative forms of payment, including revenue sharing and enterprise fund arrangements. With these arrangements, the client may realize the full benefit of the program now, instead of waiting for budget requests that never materialize. Let TMA assist your jurisdiction by showing the many solutions we have to create stop gap funding.

For more details, visit our website www.tma1.com or contact a TMA representative at 1-800-951-5350.



For more information, please visit www.tma1.com or contact a TMA representative at 1-800-951-5350





What's Exempt?

Assessing and Taxing Inventory | By Kirk Boone

The assessment and taxation of inventory is anything but uniform throughout the United States. One of the most confusing aspects of inventory taxability and exemption is that the accountant's definition of inventory often differs from a government's definition of inventory for property tax purposes.

For example, in North Carolina, inventory held for sale during the regular course of business by manufacturers, wholesalers, retailers and contractors is exempt. Since fuel used in the manufacturing process is not held for sale, it is taxable. To the accountant, fuel is a supply item that is considered inventory and may frequently be omitted from the annual listing process if the only known rule is, "Inventory is exempt in North Carolina."

For those of you reading this in states that tax inventory, I'll share with you that it has not been easy for North

Carolina to exempt it. State law governs the uniform property tax laws in North Carolina, but the state itself receives no property tax revenue. From the late 1980s through the early 1990s, North Carolina phased out inventory taxation in an attempt to draw more businesses to the state. State government assured county governments that not only would we see a rush of new businesses to our state, meaning more tax revenue, but the state would also reimburse local governments for the revenue loss due to inventory exemption. Everybody wins, right? But after a few years of the state distributing about \$200 million to the local governments, and as soon as the state hit a tight budget, the friendly agreement between state and local governments was "renegotiated." The state repealed the law granting the reimbursement, and it left a bad taste in the mouths of the local governments. I'm sure there are similar stories in other states.

Whether or not you are in a state that taxes inventory, the arguments are still there: "I didn't list it because it's inventory;" "That should be taxed as inventory which gives it a lower tax rate;" and "They don't do it that way in other states." It is helpful to hear how courts decide cases, which may give guidance as to how it would be decided in your state.

Take, for example, an inventory property tax case that went to the highest court in the state that hears only property tax cases, the North Carolina Property Tax Commission, where I spent 18 years serving as a staff member. The case was appealed up to the North Carolina Court of Appeals, which upheld the lower court's decision. The case involves the argument of a manufacturer who has equipment they no longer use, and instead they hold it for sale, becoming exempt inventory. What do you think? After reviewing, I welcome your comments and questions about inventory in your own state. My contact information is at the bottom of this page.

To read both decisions at the Property Tax Commission and Court of Appeals, which goes into great detail, please visit our website at www.tma1.com and look under the articles in the lower right hand corner.

The North Carolina Court of Appeals in their review of the Property Tax Commission's decision in favor of the County wrote, in part:

Taxpayer, Cone Mills Corporation,

is engaged in a variety of business activities in North Carolina, including the manufacture of textiles. Taxpayer's sales of textile products generate annual gross revenues in the range of \$500 million to \$750 million. In November 1988, taxpayer closed one of its plants, and the textile manufacturing equipment and machinery, which was no longer in use at the plant, was sold by the taxpayer.

On 21 March 1990, the Guilford County Board of Equalization and Review denied taxpayer's request to classify the personal property as inventory and imposed an ad valorem tax on the sale of the property. Taxpayer appealed to the Property Tax Commission, which affirmed the decision of the Guilford County Board of Equalization and Review. Taxpayer appealed.

According to N.C. Gen. Stat. § 105-274:

(a) All property, real and personal, within the jurisdiction of the State shall be subject to taxation unless it is:

(1) Excluded from the tax base by a statute of statewide application enacted under the classification power accorded the General Assembly by Article V, 5 2 (2), of the North Carolina Constitution, or

(2) Exempted from taxation by the constitution or by a statute of statewide application enacted under the authority granted the General Assembly by Article V § 2 (3), of the North Carolina Constitution.

N.C. Gen. Stat. § 105-275(34) designates inventories "owned by retail and wholesale merchants" as a special

class of property which "shall not be listed, appraised, assessed, or taxed." Inventories are defined as "goods held for sale in the regular course of business by manufacturers, retail and wholesale merchants, and contractors." N.C. Gen. Stat. § 105-273(8a).

Wholesale merchant is defined as a taxpayer who is regularly engaged in the sale of tangible personal property, acquired by a means other than manufacture, processing, or producing by the merchant, to other retail or wholesale merchants for resale or to manufacturers for use as ingredient or component parts of articles being manufactured for sale.

N.C. Gen. Stat. § 105-273(19)

Taxpayer argues that because it sells its used machinery and equipment from time to time the sale of its machinery and equipment meets all the requirements set forth above and is therefore excluded from taxation. We do not agree.

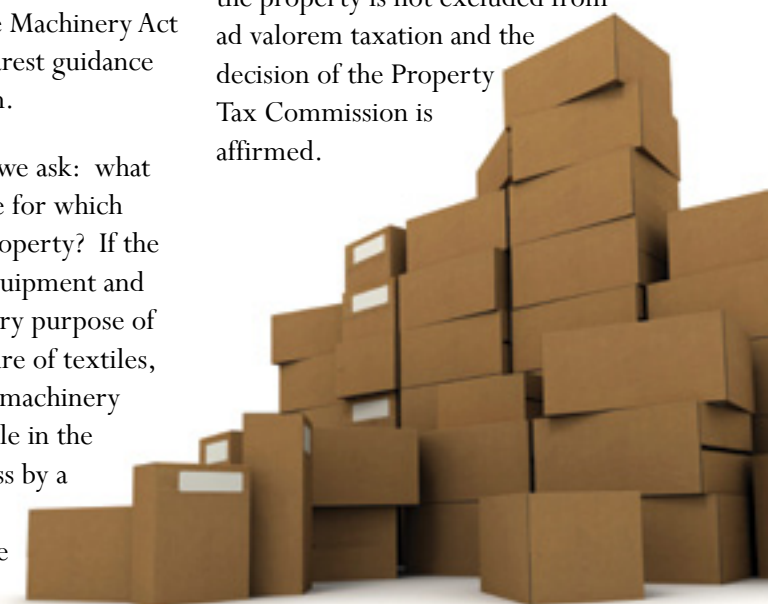
The dispositive question on appeal is whether the taxpayer is a wholesale merchant of inventories as defined by N.C. Stat. § 105-273 (8a) and (19). The statutory language of the Machinery Act provides us with the clearest guidance in resolving this question.

To resolve this question we ask: what was the primary purpose for which taxpayer acquired the property? If the taxpayer acquired the equipment and machinery for the primary purpose of using it in the manufacture of textiles, then the equipment and machinery are not goods held for sale in the regular course of business by a wholesale merchant. If the taxpayer acquired the

property for the primary purpose of resale, then the property would be excluded from ad valorem taxation.

Taxpayer admits that the primary purpose for which it purchased the machinery and equipment was for use in its manufacture of textiles. Only when the taxpayer no longer used the machinery and equipment in its textile business did taxpayer offer it for sale. Taxpayer's annual revenues generated from the sale of used equipment and machinery totaled approximately \$200,000, whereas taxpayer's annual gross revenues from the manufacture of textiles totaled approximately \$500 million.

After reviewing the whole record, we conclude that the Property Tax Commission's decision was supported by substantial evidence. Taxpayer acquired the property primarily for use in its manufacture of textiles and only held the goods for sale after the property was no longer useful in taxpayer's textile business. The equipment and machinery at issue were not inventory held for sale in the regular course of business by a wholesale merchant. Consequently, the property is not excluded from ad valorem taxation and the decision of the Property Tax Commission is affirmed.



If you have any questions or comments about this article, please contact Kirk Boone at 1-800-951-5350

Look to us...
We're here to help.



Address:

Corporate Office
2225 Coronation Blvd.
Charlotte, NC 28227

Contact Information:

Toll Free: 800.951.5350
Telephone: 704.847.1234
Fax Number: 704.708.8400

About Tax Management Associates:

For the past 30 years, Tax Management Associates, Inc. (TMA) has been in the business of assisting state and local taxing officials in their day to day duties of administering ad valorem taxation.

Audit | Discovery | Outsourcing | Special Projects

www.tma1.com