Optimizing Tax Jurisdiction Assignments to Reduce Cost and Meet Compliance

Minimizing Compliance Issues and Improving Customer Relationships
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ABSTRACT

THE PRESSURES OF TODAY’S HIGHLY COMPETITIVE, NON-REGULATED COMMUNICATIONS MARKETPLACE MANDATE ONGOING INNOVATION AND THE ADOPTION OF THE MOST EFFECTIVE NEW TECHNOLOGIES IN ORDER TO SUCCEED. DESPITE IMPROVEMENTS, CONTINUED INEFFECTIVENESS IN THE ASSIGNMENT OF TAX JURISDICTIONS AT THE STATE AND LOCAL LEVEL ARE REDUCING THE PROFITABILITY OF MANY TELECOMMUNICATIONS FIRMS. ASSIGNING INCORRECT JURISDICTIONS TO CUSTOMER ACCOUNTS CAN LEAD TO BOTH COMPLIANCE ISSUES AND PENALTIES; WHILE ASSIGNING INACCURATE LOCATIONS TO FIXED ASSETS CAN LEAD TO HIGHER, SOMETIMES DUPLICATIVE, PROPERTY TAX PAYMENTS.

DEVELOPMENTS IN LOCATION ASSIGNMENT TECHNOLOGY NOW ALLOW TELECOMMUNICATIONS COMPANIES TO ACHIEVE GREATER PRECISION IN THE ASSIGNMENT OF TAX DISTRICTS, BOTH FOR THEIR CUSTOMERS AND FOR CORPORATE ASSETS. ADOPTING A NEW AND MORE ROBUST SYSTEM TO CORRECTLY ASSIGN TAX JURISDICTIONS CAN ENHANCE OPERATIONAL EFFICIENCY, REDUCE TAXES, AND ELIMINATE PENALTIES AND COMPLIANCE ISSUES, YIELDING STRONGER BOTTOM LINE PERFORMANCE FOR TELECOMMUNICATIONS COMPANIES.

THIS WHITE PAPER PROVIDES AN ANALYSIS OF THE CHALLENGES FACING TELECOMMUNICATIONS COMPANIES IN ASSIGNING ACCURATE TAX JURISDICTIONS, FOLLOWED BY A SYNOPSIS OF RECENT ADVANCES IN LOCATION INTELLIGENCE TECHNOLOGY AND HOW THESE ADVANCES CAN IMPROVE CORPORATE PERFORMANCE.
Problems with Typical Tax Assignment Systems

The accurate assignment of tax districts is critical to effective tax management in the telecommunications industry. Unfortunately, many tax departments are forced to handle this challenging task with minimal staffing and limited budgets, using outdated tax software and arduous manual processes to research and comply with the filing requirements of over 10,000 state and local taxing jurisdictions.

These outmoded tax management systems are inherently inefficient and prone to errors. Tax directors are faced with the need to research literally thousands of state and local taxing jurisdictions to keep up with the constantly changing rates and jurisdiction boundaries. Incorrect tax assignments can lead to audit exposure and penalties for incorrect filings. This is particularly true for telecommunications firms, which are often the target of auditors and consumer watchdog groups. Inaccurate tax filings also cause corporations to run the risk of duplicate taxation from multiple taxing entities. Even worse, errors in customer billing can harm vital customer relationships, in some cases even raising the risk of class-action lawsuits.

Source of the Tax Assignment Problem

At the root of the problem is the lack of a unified, nationwide system for designating tax jurisdictions. Simply put, each state has a system of its own. In some states, for example, local tax jurisdictions are formed along county or municipal boundaries. Other states create special districts as the basic method of assigning property taxes or “mill rates” based on a variety of more granular levels such as school, fire, metropolitan and public utility districts, hospital, drainage, and more. To further complicate matters, many of these tax districts overlap. The significance of this fragmentation becomes clearer as one considers property taxes today: according to the Council on State Taxation, “Over the last 100 years, the property tax has gradually shifted from a tax generally imposed at the state level (accounting for 43% of state revenue in the early 1900s), to circumstances today where 98% of the property tax is imposed at the local level—accounting for over 70% of revenues for local governments.”

Sales and use tax assignments are also problematic. ZIP Codes are often used, but they are designed for delivering mail, not for assigning taxes. In many cases, they do not align accurately with tax jurisdictions.

Property Tax Challenges Vary State to State

Complicating the issue is the fact that these special tax districts across the nation do not follow any traditional norm or standard. In Louisiana, for example, the state bases many tax districts on Police Jury Wards that are no longer even identified as Minor Civil Divisions by the U.S. Census Bureau. In Idaho, on the other hand, county taxing districts have created over 3,000 tax code areas, with each county developing its own numbering scheme for identification. As these two examples make clear, the wide variation in systems across states makes correlating tax jurisdictions to their corresponding districts virtually impossible from a macro level.

Louisiana is an extreme example of the property tax challenge, with multiple types of special districts creating a labyrinth of different jurisdictions authorized to collect taxes for road maintenance, parks, fire districts and other improvement projects. Each district determines their own mill rate based on a single point within the Parish, with potentially up to 20 districts residing in one single location.
Boundary Changes Shift Sales and Use Assignments

Constantly changing municipal boundaries make the identification of the correct tax jurisdictions even more challenging for the corporate tax director. Far from remaining static, state and local tax boundaries frequently change as a result of incorporations, annexations, mergers, consolidations, dissolution or addition of tax districts, and new mandates. In fact, of the approximately 19,000 incorporated municipalities in the United States, approximately 25 percent change their boundaries every year. Manually keeping track of this fluid target is an extremely challenging task for tax departments—and error prone.

Special Issues Facing Telecom Industry

Tax jurisdiction assignment issues are the bane of all corporate tax managers, creating ongoing uncertainty and the risk of audits and penalties. Nowhere, however, are these issues more challenging than in the telecommunications industry, where tax directors are faced with unique situations on a variety of fronts, including property tax and sales and usage taxes.

Property Tax Challenges

First, most telecommunications firms need to assign appropriate tax jurisdictions to many properties without street addresses: e.g., cell towers or underground cables. Further complicating matters is that fact that many of these assets also cross numerous tax jurisdictions—e.g., network cables running through several communities or even crossing state lines—and taxes must be apportioned appropriately across all districts. Calculating the miles and miles of these sometimes confused networks is largely a manual process that is time-consuming and often inaccurate. Managing this tax jurisdiction minefield threatens to overwhelm traditional communications tax departments. The challenge is all the more daunting with the advent of a changing array of fixed and wireless technology that delivers communications and data, graphics and television, at ever-increasing speed and convenience to consumers across geographies and tax jurisdictions.

The Complexities of Customer Sales and Use Tax

Equally challenging for telecommunications is the accurate assignment of customer sales and use taxes. With the rapid spread of wireless technology, most telecommunications companies are governed by the Mobile Telecommunications Sourcing Act (MTSA), which requires that sales and use taxes be assigned according to customer’s primary point of use, whether business or personal. Traditionally, this assignment has been made according to the customer’s billing ZIP Code. However, as discussed below, ZIP Codes—even ZIP+4—are not accurate surrogates for tax districts. A more precise system is needed to reduce errors so customers are neither over- nor under-charged for sales and use taxes.

Maintaining Competitive Advantage

A third issue facing telecommunications companies is the need to ensure accurate tax assignments as the industry migrates from traditional communications toward digital products and data. New product offerings often defy traditional tax categorization, and communications companies risk being assigned a sales tax rate that may be inaccurate or higher than a competitor’s rate. Accurate location intelligence is the best way to avoid the risk of operating at a competitive disadvantage.
Components of a Comprehensive Location Intelligence System

Telecommunications companies need a location intelligence mechanism that can provide truly accurate assignment of tax jurisdictions. Within the last decade, the advent of GIS data has given firms the ability to pinpoint the locations of properties without physical addresses. Recent advances in the availability and accuracy of tax boundary data have also helped to move the needle in a positive direction. Today’s most advanced location intelligence systems combine address data with both GIS and boundary data to create a complete and accurate picture of tax jurisdictions, generating accurate results and significant cost savings.

ZIP Codes: Only Part of the Picture

Traditionally, telecommunications (and other) companies have utilized ZIP Code-based tax software products to identify tax districts. While seemingly simple to use, ZIP Codes have inherent characteristics and limitations that consistently cause ongoing and expensive problems for tax jurisdiction assignments.

ZIP Codes were established for use by the United States Postal Service and are designed to meet their unique needs. They were never intended to align with tax districts—and in many cases, they align quite poorly. For example, many ZIP Codes are so large they encompass multiple counties, municipalities, or unincorporated areas. In addition, ZIP Codes actually cross municipally assigned boundaries about 30 percent of the time—and cross special taxing districts even more frequently. An additional issue is that ZIP Codes are in a constant state of flux, with 25% of ZIP +4 codes changing in a given year. Using ZIP Codes as the sole means of identifying the tax district of a customer or a company asset can therefore be misleading, introducing a significant error rate. Combined with the data sources outlined below, however, ZIP Codes can be an important starting point for location assignment.

DATA QUALITY: THE FOUNDATION OF SUCCESSFUL GEOCODING

Ensuring data quality is critical to the design of any location intelligence system—if the initial address data is not accurate, the resulting geocode will not be accurate, either. Quality assurance is built into a robust system such as GeoTAX® Enterprise Tax Management. Quality checking begins at the outset, with all addresses checked and validated before geocodes are assigned, assuring that the resulting codes are, in fact, accurate. Validation and “double-checks” continue throughout the geocoding process, yielding precise, reliable location intelligence.
GIS Data: A Critical Tool for Accurate Location Assignment

Today’s sophisticated GPS tools and geographic information system (GIS) applications go well beyond ZIP + 4® methodologies to assist in the accurate assessment of jurisdiction boundaries. With GIS data, telecommunications providers are able to identify latitudinal and longitudinal coordinates for any location, enabling them to assign remote assets to the correct tax district. This provides obvious benefits over the use of ZIP Codes alone. For example, both tax districts and customer addresses can now be identified by using the “common language” of GIS data, greatly increasing the likelihood of an accurate tax assignment.

GIS data has limitations, however. Specifically, because many telecommunications companies routinely expand their service territory by acquisition, they often find themselves in a situation where they are relying on disparate systems to track their assets in various locales. As a result, geocoding information may not be available for all company assets. Therefore, it is important to utilize GIS data as a component of a more comprehensive location intelligence system.

Boundary Data: A Vital Piece of the Puzzle

Parcel boundary data allows telecommunications companies to assign accurate tax codes to fixed assets that cross multiple properties and may or may not have physical street addresses, such as wire centers, cell towers and linear assets. Boundary data has become widely available—data is now available for more than 129 million parcels. Public land survey data is also now readily available for township, section and range boundary information in most western states, while very current municipal boundary data is available nationwide. Even deeply granular property tax boundary information is available for sixteen states: Arkansas, Idaho, Indiana, Kentucky Louisiana, Michigan, Mississippi, New Jersey, New Mexico, Ohio, Oklahoma, Texas, Utah, Washington, Wisconsin and Wyoming. Property tax data for more states is also currently in development. The use of this increasingly detailed boundary data has become an important part of today’s most comprehensive location intelligence systems, supplementing GIS and ZIP Code data to optimize results.

Combining the Puzzle Pieces: A New Standard in Location Intelligence

Modern location intelligence provides a new methodology that uses geography to solve myriad location-based business problems. Today’s state-of-the-art systems combine ZIP Code information, geocoding, boundary data, and spatial analysis to develop and map rich sets of data for use in such far-ranging activities as customer profiling, disaster preparedness, risk management, coverage locators, network prequalification, and regulatory reporting.

Location intelligence is particularly well suited to solving the tax assignment issues facing the communications industry. Location intelligence combines the multiple layers of geographic data described above to provide a more in-depth understanding of a physical location, utilizing ZIP Code, GIS, and boundary data to assign accurate geographic locations. By bringing street address-level precision to county, municipality and special district tax assignments, location intelligence can provide truly reliable location information, allowing for the correct assignment of tax jurisdictions.

GeoTAX® Enterprise Tax Management: A Comprehensive Solution

The GeoTAX® Enterprise Tax Management solution from Pitney Bowes is an excellent example of a state-of-the-art location intelligence system. GeoTAX® was designed specifically to address the unique challenges in accurate tax jurisdiction assignment. GeoTAX® maintains an ongoing national research program to ensure that all location decisions are based on accurate, up-to-date jurisdictional boundary information down to the municipal, school, and special tax district level. The software system is fully integrated, allowing telecommunications firms to assign location information as needed to customer address files—and, by basing location assignment on a robust combination of location intelligence factors rather than relying solely on ZIP Code information, it provides a new level of accuracy in these applications. In fact, with all data sources updated monthly, the currency of the data is unequaled in the industry.
Benefits of the GeoTAX® System

State-of-the-art location intelligence systems such as GeoTAX® provide significant benefits for telecommunications companies, allowing tax directors to:

• Generate more accurate franchise assignments based on service area
• Create accurate tax returns for fixed assets, including linear property such as cable, fiber, or transmission lines
• Correctly assign taxes to customer primary point of use, avoiding stiff penalties

Simply put, GeoTAX® utilizes the latest location intelligence technology to provide telecommunications firms with truly accurate tax jurisdiction assignments. Adopting an up-to-date location intelligence system such as GeoTAX® provides tax directors with an effective way to limit audit risk, improve compliance, and maintain strong customer relations.

References

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