

# How to *prepare* for a Texas Sales Tax Audit



**The key to surviving a sales tax audit is documentation.** In Texas, you are considered guilty (taxable) until proven innocent (non-taxable), and for many types of exempt sales, the only acceptable documentation is a resale or exemption certificate, a contract, or another supporting document. Keeping thorough, organized records will make the audit process much smoother.

Here's how to prepare.

- Establish Procedures:** Ideally, you have procedures in place that look at the sales tax consequences of all sales and purchase transactions.
- Purchases:** If tax was not paid, determine why:

## NON-TAXABLE TRANSACTION

The most common reason is a **purchase for resale**. In that case, you don't need supporting documentation, but you must ensure that 100% of the items on all invoices are indeed for resale. In other situations, a contract or additional documentation may be required.

## TAXABLE TRANSACTION NOT TAXED

The transaction was taxable, but the vendor did not charge sales tax. In that case, you should accrue and remit **"use tax"** and report the amounts on your next sales tax return as a taxable purchase.

- Sales:** Verify that tax collection is correct:
  - Ensure proper taxable amounts, factoring in **discounts, rebates, and trade-ins**.
  - Confirm the **correct local sales tax rate** (up to 8.25%).
  - If tax was not collected, you should receive a **resale/agricultural/exemption certificate** that is fully completed and signed. You only need one certificate per customer.

**Tip:** One of the most productive things you can do prior to an audit is to **collect missing certificates**. You never know when a customer will go out of business or disappear.



Suspect prior tax exposure? **A Voluntary Disclosure Agreement (VDA) allows you to report and pay up to four years of back taxes anonymously** in exchange for a waiver of all penalties and interest, along with forgiveness for prior periods.



Don't just stop at the checklist.  
Schedule a call with our **SALT Specialist**.

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# How to *Survive* a Texas Sales Tax Audit



Once the audit begins, understanding the process helps reduce stress.

- Notification:** You'll receive a letter stating you've been selected and requesting a **completed questionnaire**.
- Entrance Conference:** A brief **phone call** may be scheduled for the auditor to understand your business, accounting procedures, and any other relevant history.
- First Visit & Confirmation Letter:** The auditor will schedule a **formal first visit**, establish the audit period (typically the **previous 42 months**), and issue a "confirmation letter" requesting specific documents. The requested documentation typically includes financial records, tax documents, and other detailed materials.

## EXAMPLES OF REQUESTED DOCUMENTATION

### FINANCIAL RECORDS

- Bank Statements
- Financial Statements
- General Ledgers

### TAX DOCUMENTS

- Sales Tax Returns
- Supporting Workpapers
- Chart of Accounts

### DETAILED MATERIALS

- Exemption/Resale
- Certificates
- Invoices
- Contracts
- Deal Jackets

- Providing Documentation:** Once you submit the requested documents, the auditor will focus on specific invoices or vendors they believe are taxable, and may ask for supporting documentation or explanations for any disputed items.
- Reconciliation:** In addition to reviewing specific items, the auditor will perform a reconciliation of your books and records against your sales tax returns to ensure they match.

*For example, if your sales tax return reports less tax than what is recorded in your sales tax payable account, the auditor will ask for an explanation—and if a valid reason isn't provided, additional tax may be assessed.*

- Ongoing Communication:** You will continue exchanging documentation and explanations with the auditor until the review is complete, **even if you still disagree with some of the findings**.

## RESPONSIBILITY REMINDER



You are responsible for sales tax on both purchases (even if the vendor didn't charge it) and sales (even if you didn't collect it). While you have the legal right to recover sales tax from customers, this may not always be practical. **When in doubt, the safest approach is to collect the tax.**

## COMMONLY OVERLOOKED TAXABLE PURCHASES:

- Cleaning Services
- Software
- SAAS
- Data Processing Services
- Web Hosting
- Subscription-based Online Tools

# How to *protest* a Texas Sales Tax Audit



Once the auditor completes their fieldwork, you'll move into the **exit and protest process**. Here's how it works:

- ❑ **Exit Conference:** After the fieldwork is finished, you and the auditor will have a (virtual) **exit conference** to review the audit. The audit is then submitted for processing.
- ❑ **Request IARC:** At the exit conference, you can request an **Independent Audit Review Conference (IARC)**. This involves a non-Audit Division Comptroller employee joining to bring a fresh perspective and try to resolve any disagreements. A report with recommended changes will be issued afterward.

↪ Note: IARCs rarely favor taxpayers, so most businesses do not use this option.

- ❑ **Receive Notification of Audit Results:** About six weeks later, you'll receive the official Notification of Audit Results. You will have 60 days to pay or protest.
  - If you protest, you do not have to pay until the appeals process is complete, which can take months or years. **Interest will continue to accrue on the amount due.**
  - You may choose to pay all or part of the assessment at any time.
  - Payment plans and settlement agreements are also options.

The **appeal process** typically works like this:

- An appeals officer issues a **Reply Letter** in response to your protest.
- You respond, and the officer replies again.
- If still unresolved, you can escalate to an **Administrative Law Judge (ALJ)**.
- ALJ hearings can be virtual, in person, or via written submission. They have their own procedural rules.
- If you disagree with the ALJ's ruling, the next step is **district court**, which concludes the administrative appeals process.

## COMMONLY TOPICS FOR PROTEST:

- An exemption certificate was obtained **after the audit ended**.
- Additional documentation was obtained to support your position.
- A legal dispute exists with the Comptroller over tax interpretation of the law.
- The auditor misunderstood the transaction in question.
- Your vendor or customer was audited and already paid the tax.
- Your vendor or customer voluntarily corrected an error and paid the tax.



Don't wait until an audit notice arrives. Start preparing your records today. Review your sales and purchase transactions for compliance, organize all resale and exemption certificates, and consider consulting a tax professional if you suspect prior exposures or complex issues.

**An audit assessment isn't the final word.  
Strategize with our SALT Specialist.**

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