

Audit Manual

Chapter 2

PREPARING AND COMPLETING AUDITS

Business Tax and Fee Division
*California Department of Tax
and Fee Administration*

This is an advisory publication providing direction to staff administering the Sales and Use Tax Law and Regulations. Although this material is revised periodically, the most current material may be contained in other resources including Operations Memoranda and Policy Memoranda. Please contact any California Department of Tax and Fee Administration office if there are concerns regarding any section of this publication.

December 2021

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PREPARING AND COMPLETING AUDITS 0200.00

INTRODUCTION 0201.00

CENTRALIZED REVENUE OPPORTUNITY SYSTEM (CROS) 0201.01

The audit team uses the Centralized Revenue Opportunity System (CROS), the California Department of Tax and Fee Administration (CDTFA) mainframe computer system, to prepare, complete, and process audits. In all other parts of the Audit Manual, CROS will be referred to as “the system.”

CUSTOMER SPRINGBOARD DEFINED 0201.03

The Customer springboard provides a high-level summary of the Customer and its associated accounts. This springboard also provides an overview of the financial activities for each account. A Customer may not always have an Account, but is merely a Customer in the system. This is the case with a CPA, Trustee, Assignor, etc., because they do not sell tangible personal property.

ACCOUNT SPRINGBOARD DEFINED 0201.05

The Account springboard allows auditors to view account details such as account balance, account number, filing frequency, commence date, impact indicators, 1099K data, registration information, open Tasks, pending credit balances and additional details. Auditors should perform a review of the various tabs on the Account springboard to determine if any issues need to be addressed in the audit.

AUDIT SPRINGBOARD DEFINED 0201.06

The Audit springboard allows auditors to work an audit Case through its various stages from creation to completion. Most audit activities can be initiated or accessed via the Audit springboard. This springboard stores audit information and provides a place to create, review, work, and approve audit credits and assessments.

The Audit springboard provides methods for:

- Attaching electronic documents (for example, Microsoft Excel, Word, forms, e-mails, custom letters, and pdf documents) created by the auditor, the customer, or a third party;
- Creating summary, lead and penalty schedules to process audit findings;
- Posting the deficiency or credit, through the schedules created, in the system;
- Documenting the audit process, via CRM Notes;
- Documenting the stages of the audit;
- Automatically notifying other system users that an audit has been completed or is in process;
- Managing waivers of limitations and other Tasks; and
- Creating audit letters.

PRELIMINARY AUDIT RESULTS LETTER DEFINED**0201.07**

A Preliminary Audit Results Letter communicates to the taxpayer the auditor's preliminary findings and recommendations after completion of an audit, field billing order (FBO), or re-audit, prior to review. The Preliminary Audit Results Letter can be sent only when the audit is in one of the following stages: "Prepare Audit Package," "Prepare Reaudit Package" and "Audit Supervisor Review." Auditors must provide the taxpayer a Preliminary Audit Results Letter, along with the Audit Working Papers (AWP), when recommending an increase or decrease of the reported tax owed.

FINAL AUDIT RESULTS LETTER DEFINED**0201.08**

A Final Audit Results Letter is sent to the taxpayer after the audit, reaudit or FBO has been reviewed and is ready to be Posted and Billed or when the audit has been reviewed and staged to "Audit Principal Review" to start the ten-day process to contact the Audit Principal to discuss the audit items in disagreement. The audit reviewer, audit supervisor or Audit Principal or their designee will send the Final Audit Results Letter after they review the audit, FBO, or reaudit. The Final Audit Results Letter can be sent only when the audit is in one of the following stages: "Audit Review," "Audit Principal Review," "Reaudit Supervisor Review," "Reaudit Review" or "Reaudit Audit Principal Review." The Final Audit Results Letter is neither a Notice of Determination nor a Notice of Refund. The CDTFA will separately issue a Notice of Determination or a Notice of Refund, when applicable.

FIELD BILLING ORDER (FBO) DEFINED**0201.09**

The CDTFA uses a field billing order (FBO) to recommend an additional tax liability or refund using procedures other than those used in a regular audit. An FBO is not an audit report and does not change the audit status of the account. The most common uses of an FBO are when one period of an audit is nearing its statute date and the auditor is unable to obtain a waiver for that period or when the auditor is addressing a claim for refund, but a full audit is not warranted. It can also be used when an entire three-year period is not appropriate for a deficiency or a credit. For further details and examples, see 0213.01.

NO OPINION WARRANTED (NOW) DEFINED**0201.11**

When an auditor recommends an account that has been selected for audit requires no further review, they will issue a No Opinion Warranted (NOW) recommendation. A NOW is not an audit, as the auditor may not have examined all of the transactions of a business. Generally, if a routine audit results in a NOW, the auditor does not prepare any additional audit working papers, comments, or other written information. Refer to section 0208.00 for more information on a NOW recommendation.

OFFICE WAIVER DEFINED**0201.12**

An office waiver is a disclaimer of opinion that provides a method of reporting a conclusion that an audit is not warranted, and the CDTFA will close the audit assignment. Generally, a supervisor may recommend an office waiver and stage the audit Case in the system accordingly. Conducting an office waiver removes an account from the list of active accounts eligible for audit for the length of the period waived. An office waiver is normally used to keep related accounts on the same audit cycle.

NOTE: An audit can only be staged to "Completed-Office Waiver" from the "Pre-Planning stage". If the auditor needs to complete an office waiver and the audit stage is "Perform Audit", the audit must be staged back to the "Pre-Planning" stage to stage it to "Completed-Office Waiver."

AUDIT CASE NOTES DEFINED

0201.14

Auditors must enter notes in CRM Notes to document all taxpayer contacts, auditor actions or requests, taxpayer’s or taxpayer’s representative’s responses, waiver requests, the date and name of the party along with method of delivery for AWP, reason for any lost periods, and significant events that occur during the course of an audit assignment. Auditors must add CRM Notes to the Audit springboard, as the actions occur, to document a timeline of events during the audit. The system will keep track of the date and time the auditor enters the notes. Notes cannot be back dated. It is important to enter Notes as they occur, rather than all at one time, for correct tracking of actions taken.

If team members are unable to access the system or for any reason, they should enter comments as soon as possible and should start the note with the actual date (i.e. XX/XX/XXXX) of the related comment.

If notes are exported for the taxpayer, auditors can exclude system-generated notes which are under “Added” type. Team members should ensure comments are professional and appropriate.

CANCELED AUDIT STAGE DEFINED

0201.15

An audit in the “Canceled” stage is an audit created in error. For example, an audit supervisor intends to create an audit for an account, but accidentally creates an audit on the wrong account, they must stage the audit created in error, to the “Canceled” stage.

Also, when an audit is not currently warranted but may be in the future, cancelling the audit leaves the account eligible if an audit is later deemed warranted for any three-year period.

An audit should be cancelled only when no contact was made with the taxpayer and no records were reviewed. If any work is done by the auditor, a NOW should be used instead of cancelling the audit.

CASE DEFINED

0201.16

A Case is a type of Task that can be created within an audit Case. The types of Cases found within an audit Case are Audit Disagreement, Audit Evasion (Fraud) Memo, Audit Plan, Audit Survey, Information/Document Request, Memorandum of Potential Tax Liability, California Nexus, Prior Audit Percentage, and Waiver of Limitations. Different Cases in the system have different configurations to meet the needs of each specific type of work assignment. Some are created by the system and some are manually created using the Task tab under Forms.

TASK DEFINED

0201.17

A Task is a Case or Work Item for which one or more actions are required. In some instances, a Task may need to be completed and confirmed in the system by the assignee but in other instances it is a request to someone else, to complete a Task, (e.g., account maintenance).

There are three different categories of Tasks.

Taxpayer Forms	Supporting Functions	Lead
Waiver of Limitations	Add Note to Related Audits	Memorandum of Tax Liability
Information/Document Request	Date of Knowledge Review Related Audit	California Nexus
Audit Plan	Audit Split	Create Related Audits
Prior Audit Percentage	District Reallocation Request	
Fraud Memo	Local Reallocation Request	
Audit Disagreement Case		

WORK ITEM DEFINED**0201.18**

A Work Item is a type of Task that allows the user to create, assign, and track an assignment in the system. Registration and account maintenance are two of the most common Work Items used by auditors. Work Items are found under the Task tab at the Customer, Account or Audit level. Depending on the springboard, there are different types of Work Items.

In the **Customer springboard**, you will find the following Work Items for audits:

- Jeopardy Determination Request
- CSB Work Items, (used in the case of bankruptcy)
- Request Account Maintenance

In the **Account springboard**, you will find the following Work Items:

- External Agency Tracking (EATs)
- Jeopardy Determination Request
- Generic Compliance Work Item (used only if there is no other applicable Work Item)
- CSB Work Items, (used in the case of bankruptcy)
- Request Account Maintenance
- Request Site Maintenance

In the **Audit springboard**, you will find the following Work Items:

- Audit Case Assistance
- CAS Consultation
- Change Request
- Cooperative Audit-Audit Verification
- Request for FTI

Auditors must always be mindful of what springboard they are in when making requests for Work Items. Some Work Items will only be shown in the Customer or Account springboard, therefore, it may be necessary to make the Work Item request at one of those levels. Ensure that any request that is made at the Customer level applies to **all** the Accounts the Customer has. Otherwise, the request should be made at the Account or Audit level.

The difference between a Work Item and a Case is that a Case has multiple stages to get it to completion, while a Work Item is a “Complete” and “Confirm” assignment, with no stages to get it to completion. They are both located under the Task tab.

IMPORTANCE OF PROMPT COMPLETION OF AUDITS**0201.21**

The audit team must promptly complete all audit assignments and must give priority to reaudits and claims for refund so that CDTFA may timely clear petition and refund cases. The audit team must also give priority to “legal” audits (bankruptcies, probates, and assignments) to allow CDTFA sufficient time to meet statutory requirements of claims.

VERIFYING AND UPDATING ACCOUNT INFORMATION**0202.00****GENERAL****0202.01**

Auditors must verify that the taxpayer's Customer and Account information are current. The CDTFA encourages auditors to inform the taxpayer of our Online Services portal, which is available for them to sign into our system and update their Customer and Account information. However, if the taxpayer is unable to update information online, auditors must notify the compliance team to update the information or assist the taxpayer themselves.

Verifying Taxpayer Contact Information

When auditors are in contact with a taxpayer, whether in person, over the telephone, or via email, they should request any updated phone numbers, email addresses, and business and mailing addresses for contact purposes. Telephone and email records in the system must be current and accurate in order to reach our taxpayers timely.

The accuracy of telephone, email and physical addresses in the system should be verified by doing the following:

- Request updated contact information from taxpayers and verify it against current system records.
- Using a Work Item in the system, request an update of the records when there is any change. The Work Item is completed at the Account or Customer springboard level, depending on the item being updated.

Verifying Taxpayer Registration Information

When an audit is assigned, auditors are responsible for ensuring the **entire** account is up to date. It is imperative that CDTFA has current and accurate account information and auditors are in the best position to obtain this information. Auditors must verify the system contains accurate registration information. For accounts registered as corporations, partnerships, or limited liability companies (LLCs), auditors must also verify contact information in the system for corporate officers, partners, and LLC members, under "Links" in the Customer springboard.

Auditors should encourage the taxpayer to make all changes to their account using Online Services. If necessary, auditors can assist the taxpayer using the "View Support ID" function in the system or obtain assistance from a compliance team member. The compliance team will make the necessary changes to a taxpayer's account only if the taxpayer needs assistance. However, auditors are responsible for verifying the taxpayer's information and notifying the compliance team of any updates in the taxpayer's information. Auditors must notify the compliance team of the following changes:

- Business entity type
- Taxpayer's mailing or business address
- NAICS code
- DBA
- Partners in a partnership
- Corporate officers
- Any other change to the taxpayer's registration information in the system, including, but not limited to, IDs, Names, Addresses, Contacts, Links, Sites and Bank Information. All these items are located under the Registration tab on the Customer springboard.

Auditors will send a “Request Account Maintenance” Work Item in the system to notify the compliance team of the update. Auditors must subscribe to the Work Item so they are notified when the update is completed. The Work Item must include detailed notes indicating the requested change. Information in the Work Item must include the following:

- A short explanation regarding the updated information, along with the effective date of the change. In the case of an NAICS code correction, provide a short and accurate description of the taxpayer’s primary business activity.
- The auditor’s name and telephone number.
- The site number, for example, 00001 or 00002 (Customer springboard, Registration, Sites) with documents supporting the update.

In the case of a change in partners, auditors must attach evidence supporting the date of the change (for example, addendum to the partnership agreement, letter of withdrawal, Statement of Dissociation, etc.) to the Customer springboard and the Audit springboard, CRM, Attachments.

After the compliance team updates the account information, auditors must verify the update is accurate. This should be done after receiving the system’s notification that the Work Item is completed.

CDTFA-1296, ACCOUNT UPDATE INFORMATION

0202.03

Auditors must complete form CDTFA-1296, *Account Update Information*, for each audit report, including Field Billing Orders and NOWs, except for audits of Fortune 500 businesses (www.fortune.com/fortune500/). Auditors must complete form CDTFA-1296 during the course of field work and before the exit conference with the taxpayer and/or representative. Auditors must complete the form and may not mail or hand the form CDTFA-1296 to the taxpayer for completion. Auditors must not obtain information to complete the form from the CDTFA file or permit application. Detailed completion of form CDTFA-1296 can assist in determining responsible person liability, when needed. Upon completion of form CDTFA-1296, a copy of it, along with proof of tax reimbursement, any documents used to verify changes in corporate officer(s) or LLC member(s), and other documents, as explained below, should be attached in both the Account and Audit springboards.

If the updates in the CDTFA-1296 are required to be completed prior to the posting and billing of the audit, auditors must create a “Request Account Maintenance” Work Item. The “owner” of the Work Item should be left blank. Auditors should make themselves a subscriber to the Work Item. Auditors must then email their supervisor (or create a bookmark for their supervisor, depending on office policy) letting them know the Work Item should be routed by the audit supervisor to the Compliance Principal for immediate assignment. If the CDTFA-1296 does not require immediate attention, auditors will still create the “Request Account Maintenance” Work Item, but no email or bookmark is required. After the CDTFA-1296 is attached in the system, it can be destroyed.

Updating Information for Corporate Officer or LLC Member

When completing form CDTFA-1296, *Account Update Information*, auditors must verify the corporate officers' or LLC members' name(s) and contact information in the system. If there is a change of corporate officers or LLC members, auditors must attach a copy of the documents used to verify the information in the Customer springboard, Registration, Links, and create a "Request Account Maintenance" Work Item detailing the specific request. A copy of the documents should also be attached in the Audit springboard, CRM Attachments.

Documents used to verify an officer or member change include, but are not limited to, the following:

- Validated copies of pertinent forms filed with the Secretary of State (SOS). Validated copies are the forms available from the SOS website. See SOS website below. This includes the Statement of Information (SI and SI-Complete).
- A copy of the corporate minutes stating a change of officers.
- A signed letter from the corporation or LLC, preferably on corporate or LLC letterhead, authorizing the corporation or LLC requester to make such changes and documenting the officer or member change.
- A copy of the bill of sale showing a transfer of the corporate stock to the new officer(s).
- Secretary of State information obtained from the publicly available information on <https://businesssearch.sos.ca.gov/>.

Other Information

Form CDTFA-1296 allows auditors to record information regarding a taxpayer's bank accounts, merchant account (credit card processor), accounts receivable, notes receivable, and suppliers. If available, copies of bank statements should be included with the CDTFA-1296 in the system as an Attachment.

This form also allows auditors to indicate whether a taxpayer includes or adds sales tax reimbursement to the sales price of tangible personal property. Examples of the taxpayer's records illustrating that the taxpayer includes or adds sales tax reimbursement to the sales price of tangible personal property include, but are not limited to:

- copies of sales invoice(s),
- cash register receipts,
- internet information, and
- point-of-sale documentation.

Auditors must include the above documents with form CDTFA-1296 in the system as an Attachment. If the taxpayer makes any statements regarding payment of liability (for example, a statement indicating that the taxpayer is unable to pay the entire liability at once but can pay it over the next four months), auditors should document this information in CRM Notes on the Account springboard.

In the case of automobile or mobile home dealers, auditors should include on form CDTFA-1296 the value and location of all non-disbursed escrow accounts established for funds received from buyers as whole or partial payment for mobile homes.

In bankruptcy cases, auditors must also include the following comments on the CDTFA-1296:

- Type of Bankruptcy filed, such as Chapter 7, 11, 13.
- Petition date (the date the bankruptcy was filed).
- Bar date (or the last day to file a claim), Case Number, and Court of Jurisdiction.
- Names of the corporate officers responsible for the business during the period of liability and those in charge when the audit is completed. This is relevant for bankruptcy cases and helps in establishing responsible party liability.

SITE

0202.05

A tax area code (TAC) for each “verified” address (site) entered into the system will be automatically created. Auditors must verify the site address is accurate for each registered site. Auditors must notify the compliance team or Local Revenue Branch (LRB) through a “Request Site Maintenance” Work Item if any update is necessary.

Field office team members should only update an address if it is in the exact same TAC, for instance, changing only a suite number generally will be in the same TAC. If the address change would result in a different TAC, a “Request Site Maintenance” Work Item **must** be created. When the Work Item is created, auditors must not select an owner, but should select themselves as a subscriber so they are notified when the Work Item is completed. A “Request Site Maintenance” Work Item without an owner will be worked by LRB.

See AM section 0212.13 regarding changes in tax area code (TAC) during the audit period due to incorporation, annexation, or relocation.

NORTH AMERICAN INDUSTRY CLASSIFICATION SYSTEM (NAICS) CODE 0202.07

The North American Industry Classification System (NAICS) code may be viewed from the Customer springboard, Registration, Activity Codes. Auditors must check the NAICS code(s) for accuracy for all registered sites.

When a significant change in the business activity of an active account has occurred before or during the audit period or if the NAICS code is incorrect, auditors must notify the compliance team through a “Request Account Maintenance” or a “Request Site Maintenance” Work Item. These changes can be done by field office team members and do not require LRB assistance.

Sales and Use Tax and Special Taxes accounts are populated with a six-digit NAICS code. It is the taxpayer’s primary business activity, not what the taxpayer sells, that predominantly determines the taxpayer’s NAICS code. The primary business activity is the main activity from which the business generates the majority of its revenue and incurs most of its costs. The primary business activity may not be directly related to a taxable activity.

Auditors must verify that the taxpayer’s NAICS code accurately identifies the taxpayer’s primary business activity by looking up the code in the CDTFA NAICS Code Generator. The first two digits of the NAICS code represent the Industry Sector. The Generator provides the Class Description for the Sector Code. The Sector Code and the Class Description must accurately identify the taxpayer’s primary business activity.

Special comments are required for the following types of business:

- Grocery Store — Beer, wine, liquor, meat, or produce departments (see AM Chapter 9, Grocers).
- Restaurant — Beer, wine, liquor, drive-in, and extent and type of take-outs (see AM Chapter 8, Bars and Restaurants).
- Construction Contractor — Lump-sum/time and material/cost-plus contracts, subcontracts, and over-the-counter sales (see AM Chapter 12, Construction Contractors).

VERIFICATION OF TAXPAYER’S LEGAL NAME

0202.09

Auditors must verify the accuracy of the taxpayer’s legal name. The Notice of Determination will be invalid if it is issued to the wrong person. Auditors must ensure that the correct name is populated in the system even if it is different than the name in which the permit was issued.

If there is any change to the taxpayer’s name or address in CDTFA’s records, auditors must immediately notify the compliance team through a “Request Account Maintenance” Work Item. **The Audit Results Letters must not be generated in the system until the registration information is confirmed and updated.**

Auditors must compare the information in the system (Account springboard, Registration, Summary) with information from the areas listed below to make sure that they are consistent and accurate.

- Secretary of State website (for businesses that need to be registered)
- CDTFA-80RU, *Record Update*
- CDTFA-1296, *Account Update Information*
- CDTFA-392, *Power of Attorney*
- Federal Income Tax returns in audit working papers
- ABC License, if applicable
- Any DBA filed with the city or county (DBAs can be issued by the city or the county and it will depend on where the business is located as to which one auditors should contact.)

WHERE PROPRIETOR’S NAME IS IN DOUBT

0202.11

If there is no question as to the identity of the owner, but only a question as to the correct name, auditors must ensure the correct name appears on the Audit Results Letters. Auditors must immediately create a “Request Account Maintenance” Work Item for the compliance team that includes detailed instructions with the updated name and effective date of the change. The Audit Results Letters cannot be generated until the registration information is updated. Examples of what to include in the Work Item:

Old name: California Glass Company, Inc.

Correct name: California Glass Company, Ltd.,

or

Old name: J. O. Smith

Correct name: Oliver Smith

WHERE PRECISE OWNERSHIP IS UNKNOWN

0202.13

If it is impossible to determine the identity of the owner, auditors should ascertain the name and permit number of all possible or probable owners and enter that information into CRM Notes. Auditors should ensure the “Private” box on the Note is **not** checked which will allow the note to show on other springboards. When precise ownership is unknown, the use of a dual determination should be considered. See section 0209.00 for more information about dual determinations.

SOLE PROPRIETORS

0202.15

Auditors must verify that the owner’s name and the fictitious business name, if any, are accurate in the system prior to generating the Audit Results Letters and Notice of Determination.

MARRIED CO-OWNERSHIP

0202.17

For accounts registered as a married co-ownership, auditors must verify that the name of both spouses are accurate in the system prior to generating the Audit Results Letters and Notice of Determination.

Example: John F. and Mary G. Smith

PARTNERSHIP ACCOUNTS

0202.19

To inform general partners of their partnership’s tax liability, the audit team members must send a Notice of Determination to **all** known general partners and their representatives on the **same day**. This procedure also applies to closed-out/ceased accounts. Furthermore, the CDTFA team members must send a separate Notice of Determination addressed to the partnership entity.

For closed-out partnership accounts, the audit team members must verify that the registration information for the partnership and for all partners is accurate at the time of close-out. If there is any update, auditors must create a “Request Account Maintenance” Work Item for the compliance team and follow up to ensure the updates are done timely and accurately before the Audit Results Letters and the Notice of Determination are sent out.

General Partnership:

Auditors must verify the accuracy of the name of the partnership in the system prior to generating the Audit Results Letters and Notices of Determination. If the account is not registered in the partnership name (for example, a partnership name was not provided at the time of registration), auditors must create a “Request Account Maintenance” Work Item for the compliance team and follow up to ensure the updates are done timely and accurately and the proper links are created in the system. (Timely means prior to the audit being Posted & Billed).

PARTNERSHIP ACCOUNTS

(CONT.) 0202.19

Limited Partnership:

Unlike general partnerships, all limited partnerships (and limited liability partnerships) are required to register with the Secretary of State (SOS). Auditors must verify that the limited partnership’s name, as registered with the SOS, is accurate in the system prior to generating the Audit Results Letters and Notices of Determination. If there is any update, auditors must create a “Request Account Maintenance” Work Item for the compliance team and follow up to ensure the updates are done timely and accurately. Because each limited partnership must have at least one general partner’s name, it is imperative that the general partner(s) and all names of the limited partner(s) be entered in CRM Notes in the system and noted whether they are a general or limited partner.

For example:

“Limited Partnership. John L. Ritter, general partner, and Robert M. Kyle, limited partner.”

LIMITED LIABILITY COMPANIES

0202.21

Auditors must verify the accuracy of the name of the limited liability company in the system prior to generating the Audit Results Letters and Notice of Determination. The name of each limited liability company must be followed by the letters “LLC.”

CORPORATIONS

0202.23

If a corporation operates under a fictitious business name, auditors must verify both the corporate name and the fictitious business name are accurate in the system prior to generating the Audit Results Letters and Notice of Determination. Auditors must ascertain the correct corporate designation, such as Company; Co.; Company, Inc.; Co., Inc.; Inc.; Incorporated; or Ltd., since many corporations have names which are identical except for a difference in such designations. List the names of the primary officers of the corporation in CRM Notes.

Dual determinations may be issued against a corporation and its corporate officers, shareholders, or other responsible persons. See AM section 0209.00 for further information on dual determinations.

PRIVATE TRUSTS

0202.25

Auditors must verify the names of the trustees, in addition to the name under which the business is operated, are accurate in the system prior to generating the Audit Results Letters and Notices of Determination. Do not include the names of the beneficiaries.

JOINT VENTURES

0202.27

Auditors must verify the name of each party to a joint venture, in addition to the name under which the venture is being conducted, is accurate in the system prior to generating the Audit Results Letters and Notices of Determination.

SURNAME CHANGES

0202.29

If a person who operated a business changes their surname and continues to operate the business as a sole proprietor, auditors must verify that the Account and Customer names are correctly displayed in the system and on the Audit Results Letters and Notices of Determination as follows:

ACCOUNT NAME	Robin Hood Tearoom
CUSTOMER NAME	Robin Smith, formerly Robin Jones

DECEASED TAXPAYER (PROBATE CASES)**0202.31**

If the audit covers the operations of a decedent, auditors must verify that the Account and Customer names are displayed in the system and on the Audit Results Letters and Notice of Determination.

If the account is closed out/ceased, due to the taxpayer's death, the names should be displayed as follows:

ACCOUNT NAME	Acme Electrical Works
CUSTOMER NAME	John Smith, deceased

If the audit covers operations **subsequent** to the date of death and a personal representative or administrator is operating the business only to close out the business (not to purchase additional inventory for the continuation of the business) the Account and Customer names should be displayed in the system and on the Audit Results Letters and Notice of Determination as follows:

ACCOUNT NAME	Acme Electrical Works
CUSTOMER NAME	Estate of John Smith, deceased Peter Jones, Executor

The Account and Customer names should be shown in this manner whether or not the personal representative (executor, administrator, etc.) has obtained a new permit.

If a deceased taxpayer's business is operated during the audit period after the taxpayer's death, and will be a going concern, the executor, administrator, or personal representative must apply for a seller's permit with CDTFA. In this case, the audit period must be changed to end on the close-out/cease date of the decedent's death. Two audit cases, Audit Results Letters and Notices of Determination are required, one for the period prior to the death of the original Customer and one for the period when the business is operated by the decedent's personal representative, under their own permit.

BANKRUPTCY CASES**0202.35**

When auditors are made aware a Customer has filed for bankruptcy, they need to determine as much information as possible. Generally, auditors can get the information by asking the Customer for a copy of the bankruptcy petition.

Auditors are required to obtain the following information:

- Type of bankruptcy, (Chapter 7, 11 or 13)
- Petition Date
- Bar Date
- Case number
- Court of jurisdiction

Auditors must obtain the bankruptcy claims bar date so an audit can be billed with sufficient lead time to permit the Collection Support Bureau (CSB) team members to timely file a proof of claim. CSB team members need at least two weeks prior to a claims bar date to process and file a proof of claim.

If audit team members are contemplating an audit after a bankruptcy case is filed and the audit period is pre-petition, or pre-confirmation (Chapter 11 cases), auditors must contact the bankruptcy team in CSB to determine whether the bankruptcy case affects the liability not yet billed, prior to investing time in an audit.

Auditors must periodically communicate with CSB regarding the status of the audit. Auditors should ensure they are aware of the important deadlines for the bankruptcy and check with CSB at least two weeks prior to each of the deadlines to ensure CSB is aware of any new information auditors may have obtained. If there are problems or delays in the completion of the audit, communication should take place as early as possible to ensure that all required steps to preserve CDTFA's claim are taken by both the Audit team and CSB.

In all cases of bankruptcy where an audit is to be conducted or is in process, but is not yet completed, the audit information is indicated in the system on the Audit springboard. For example, the audit period and whether the Account is active or closed out/ceased. Once completed, the audit information will be transmitted promptly to CSB, via a bookmark or email, to establish proper controls for the timely filing of a proof of claim.

Auditors are only required to enter the information regarding the bankruptcy, such as Petition Date, Case Number, Bankruptcy Type, Jurisdiction and Bar Date, in CRM Notes, but not to enter the Indicator into the system. If auditors are unsure of what is needed, they should seek assistance from the compliance team in their office.

The only bankruptcy case that requires a new seller's permit is a Chapter 7, asset case. Chapter 7, no asset and Chapters 11 and 13 do not require a new seller's permit. In a Chapter 7, no asset case, there must not be any further sales made and the Customer must be closed out/ceased. With Chapters 11 and 13, the Customer will continue with the same seller's permit.

For the period during which the business was operated by the debtor, auditors must verify that the Account and Customer names are displayed in the system and on the Audit Results Letters, and Notices of Determination in the same manner as though the taxpayer was not a debtor.

The Account and Customer names should appear in the system and on the Audit Results Letters and Notices of Determination as follows:

ACCOUNT NAME	Elite Restaurant
CUSTOMER NAME	Estate of John Smith, debtor

For a chapter 7, asset case, the Customer's account must be closed/ceased and the trustee assigned must obtain a seller's permit to make the final sales. If the trustee is already a Customer in the system, the compliance team members must link that Customer to the debtor's account as a trustee.

For the period during which the business is operated by a trustee, the trustee's Customer name should appear in the system and on the Audit Results Letters, and Notices of Determination as follows:

CUSTOMER NAME	Peter Jones, Trustee
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If a taxpayer operates a business during the audit period after filing a bankruptcy petition, two audit cases, Audit Results Letters and Notices of Determination are required, one for the period prior to bankruptcy and one for the period when the business is operated by the trustee or business, owner under the jurisdiction of the court. The audit supervisor shall determine whether it is beneficial to continue with an audit on a pre-petition liability. If the potential amount is immaterial, the audit supervisor can change the audit period to exclude the pre-petition portion of the audit.

ASSIGNMENTS FOR THE BENEFITS OF CREDITORS**0202.37**

For periods during which the business is operated by an assignor, the assignor's Account and Customer names should appear in the system and on the Audit Results Letters and Notices of Determination as though no assignment had been made. For the periods during which the business is operated by the **assignee**, the Account and Customer name should appear in the system as follows:

ACCOUNT NAME	Best Bakery
CUSTOMER NAME	Peter Jones, Assignee for John Smith

Receivership 0202.39

If a court has appointed a receiver, auditors must verify that the Account and Customer names are displayed in the system and on the Audit Results Letters and Notice of Determination as it was prior to the receivership. However, the name and firm name for periods operated by the **receiver** should appear in the system and on the Audit Results Letters and Notice of Determination as follows:

ACCOUNT NAME	Alaska Fur Store
CUSTOMER NAME	John Jones, Receiver for Peter Smith

MAILING ADDRESS**0202.41**

The taxpayer's current mailing address is displayed on the Customer springboard, Registration, Addresses. To ensure proper notification to the taxpayer in the event of a liability or refund, auditors must verify the mailing address is up to date. Auditors must notify the compliance team to update the taxpayer's mailing address if it has changed.

This is accomplished by adding a Work Item under the Task tab in either the Customer springboard (Request Account Maintenance) or on the Account springboard (Request Account Maintenance or Request Site Maintenance). Auditors should also include a CRM Note at the Customer or Account level and on the Audit springboard.

When a Notice of Determination is to be issued close to the statute date or on a closed-out/ceased account (and if the taxpayer's correct address is uncertain, or there is information of a possible alternate address), the Notice of Determination will be mailed to the last address of record received from the taxpayer. In addition, the Notice of Determination will be mailed to any other address believed to be the taxpayer's correct address. Site addresses are located on the Customer springboard, Registration, Sites.

CHANGE IN OWNERSHIP**0202.43**

If there is a change of ownership during the audit period and CDTFA has no record of such change (for example, the incorporation of a sole proprietorship), auditors should encourage the Customer to use the Online Services portal on CDTFA's public website. If the Customer is hesitant to use Online Services, auditors should assist the Customer, using View Support ID. If the Customer is unable to use Online Services, auditors must prepare a form CDTFA-406, *Closeout Worksheet*, and immediately forward (office policy should be followed as a Work Item or email process, as both methods are acceptable) the completed CDTFA-406 to the compliance team. Generally, auditors should not prepare a CDTFA-406 just for the addition or deletion of partners since Revised Uniform Partnership Act (RUPA) allows for the continuation of a partnership entity in most circumstances.

CHANGE IN OWNERSHIP

(CONT.) 0202.43

However, if the partnership agreement stipulates dissolution of the partnership when a partner is added or dropped, then auditors must prepare CDTFA-406 to add or remove partners. The taxpayer must be advised of the closeout of the permit and the need for the application for a new permit. See Compliance Policy and Procedures Manual, Chapter 6, “Closeouts and Clearances,” for instructions on how to prepare the CDTFA-406.

Auditors are responsible for verifying the address and documenting the type of ownership in the Verification Comments, and for ensuring that CDTFA’s records on the account are updated.

CHANGE IN OWNERSHIP - NO ADDITIONAL LIABILITY DISCLOSED 0202.45

When an audit discloses no additional liability but indicates changes of ownership have occurred in the operation of a continuing business, auditors **must** complete a No Opinion Warranted (NOW) case in the system.

- Under the original permit number if the business is no longer operating, or
- Under the ownership currently operating the business.

Auditors will make a comment in CRM Notes in a similar manner as the following example:

This audit includes the operations of the following ownerships:

- John Doe, Sole Proprietorship Period 3/1/wwww to 2/28/xxxx
- John Doe and Robert Doe, Partners Period 3/1/xxxx to 2/28/yyyy
- Doe Corporation Period 3/1/yyyy to 1/31/zzzz

Issuance of permits on an “issue and cancel” basis should not be done. A seller’s permit must be issued for each owner (sole proprietor, partnership, corporation, etc.) that made sales during the audit period. Each owner is a separate person under the Sales and Use Tax Law.

CHANGE OF OWNERSHIP - ADDITIONAL LIABILITY DISCLOSED 0202.47

If the audit discloses additional liability for any one of the ownerships, auditors must prepare a separate audit case for each “person” for the additional tax (Person is defined in RTC § 6005). This issue is best described in Audit Manual section 0202.45 where a sole proprietor changed to a partnership and then changed to a corporation. Appropriate cross-references should be made in the system and commented on in the Verification Comments. Auditors must include CRM Notes in each audit regarding the operations of any entities audited which did not obtain permits but have no additional liability.

AUDITS OF MORE THAN ONE LOCATION 0202.50

To keep all related accounts on a consistent basis for audit selection purposes, all related sales and use tax accounts are generally audited simultaneously for the same period. However, processing of a completed audit should not be delayed while audits of related accounts are in process. Related accounts are those that are under the same Customer.

Auditors should take care when listing an Account as “related” in the system. Even though two separate corporations have the exact same officers, if they do not have the same corporate number, they are not “related.” In this instance, this would not be entered in the Account’s CRM Notes, but rather, it may be considered an audit lead if the initial audit findings result in a deficiency and they are similar types of businesses.

CDTFA-523, TAX RETURN AND/OR ACCOUNT ADJUSTMENT NOTICE

0203.00

GENERAL

0203.01

There are situations that may require returns to be moved and/or adjusted for periods in the audit. CDTFA-523, *Tax Return and/or Account Adjustment Notice*, is used to clear or establish delinquencies, to adjust returns, payments, or tax between accounts and/or reporting periods, and to transfer information between accounts. The CDTFA-523 should be sent to the Return Analysis Unit (RAU) at the following email:

BTFD.RAUElectronicMaintenanceRequests@cdtfa.ca.gov

Information on preparation and submission of the CDTFA-523 is provided in detail below.

REASONS FOR PREPARING CDTFA-523

0203.03

There are many circumstances that may require the preparation of Form CDTFA-523. For example, at the beginning of the audit, the auditor is made aware the taxpayer has incorporated. In that instance, auditors will need to ensure the taxpayer gets a new seller's permit. After determining whether a new permit is required, some of the returns may need to be moved to the newly established account. The list below provides illustrative examples of some of the types of situations that may require auditors to prepare Form CDTFA-523. The list is not meant to be all inclusive, but merely illustrates the common types of situations encountered by an auditor, requiring preparation of the form.

For the following changes, auditors must create a "Request Account Maintenance" or "Request Site Maintenance" Work Item in the system. Auditors must make themselves a subscriber so they will be notified when the change is complete. The request must be very specific and provide as much detail as possible. The CDTFA-523 is no longer required for these types of changes.

- (a) Change of start or close-out dates.
- (b) Requests for "Did Not Operate" (DNO) clearances.
- (c) Requests to apply payments to audit periods.

The following changes reported on **Form CDTFA-523 will be sent to the RAU** via email with the CDTFA-523 attached to the email and attached to the Account in the system.

- (a) All requests to transfer returns between periods and/or accounts.
- (b) Requests to apply a payment to a specific period.
- (c) Requests to apply a partial payment or return to a specific period/account.
- (d) Requests to split revenue between a specific period/account.

Changes which cannot be made to Existing Accounts

Certain changes may not be made to an existing account either manually or on-line:

- (a) Incorporation of an account or formation of a limited liability company.
- (b) Change of ownership type after taxpayer has filed the first return, such as from individual to partnership.

Each of the situations above requires closeout/ceasing of the existing permit and issuance of a new permit. It is best to encourage the taxpayer to accomplish this through Online Services. If the taxpayer has difficulty using Online Services, a CDTFA team member can assist them with the close-out/cease and new permit processes using View Support ID. Otherwise, a form CDTFA-406 will be required.

PREPARATION OF FORM CDTFA-523 TO MOVE RETURNS

0203.05

Although a new seller's permit, when necessary, must be obtained prior to posting and billing, a Form CDTFA-523 to move payments between accounts does not have to be processed prior to processing or posting and billing the audit in certain situations. These situations are expanded on below.

In order to process/post and bill an audit prior to Form CDTFA-523 being processed, a new seller's permit must be obtained for the new entity and the start date of the new Customer should be the effective date of the ownership change. If the taxpayer obtains the new seller's permit through Online Services, auditors must verify that the start date of the new permit is correct for the new Customer. Oftentimes, the start date will need to be adjusted by compliance team members, especially in cases when the taxpayer has been operating under a different legal entity for a long period of time. A verification of the close-out/cease date of the old account must also be verified. The new account should be placed on the same reporting basis as the old account. A "Stop Delinquency Notice" needs to be placed on the new account to ensure delinquency notices are not issued.

The Transcript of Returns for the old account will be used to input reported taxable measure for the CDTFA-523 process. The old account number and old case identification number (ID) on the transcript of returns should be replaced with the new account number and case ID. Auditors must indicate in the Verification Comments (Miscellaneous) specifying that Form CDTFA-523 has been prepared to move the returns. The comment must include a reference to the periods being moved and the account numbers involved. Auditors must save a copy of Form CDTFA-523 which should be attached in the Account springboard, CRM, Attachments. Auditors must document this in the Audit CRM Notes on the date the Form CDTFA-523 was submitted.

A Form CDTFA-523 **must** still be processed and the returns moved **prior** to the billing of the audit if:

- The taxpayer is in bankruptcy during the audit period.
- The audit involves application of a fraud penalty.
- Credits exist on any of the returns filed under the old account and these credits need to be applied when the audit is billed.

INFORMATION FOR PREPARATION OF FORM CDTFA-523**0203.07**

Auditors will prepare Form CDTFA-523 for each account. For the situations noted in AM section 0203.03, the form will be sent to the RAU. Auditors should send this form to the RAU via email as soon as possible to expedite the required change. Auditors must save a copy of Form CDTFA-523 and attach it in the Account springboard, CRM, Attachments. The form should also be attached in the Audit springboard and a CRM Note entered stating that the email was sent to RAU.

Auditors may also email other routine RAU maintenance requests, which include Form CDTFA-523, to the email group: BTFD.RAUElectronicMaintenanceRequests@cdtfa.ca.gov.

Auditors must include the Customer/Account number and the reason for the request in the email subject line to aid in the distribution of the emails. If a specific request needs to be expedited, auditors must add "RUSH" in the subject line and provide a brief reason for the rush in the email.

If only section 1 is to be completed, auditors must enter the full account number, the taxpayer's name, and reporting basis.

If sections 1 and 2 are to be completed, both sections must contain the business and tax area codes. See AM section 0202.07 for information on NAICS codes.

Following are general instructions for each section:

- SECTIONS 1 & 2: When two accounts are involved, section 1 is used for the account from which a transfer or adjustment is made. Section 2 is used for the account to which a transfer or adjustment is made.
- SECTION 3: This section is used to transfer entire returns or prepayments from one account to another.
- SECTION 4: Not used by the field auditor.
- SECTION 5: Not used by the field auditor.
- SECTION 6: This section is used to transfer a fractional period erroneously included in a return or prepayment from an incorrect account to the correct account.
- SECTION 7 & 7B: For Headquarters' use only.
- SECTION 8: This section is for explanations of adjustments made in sections 1 to 7B.

CONVERTED RETURNS**0203.09**

Converted returns (returns converted from the old system to the new system) cannot be moved and/or adjusted unless the returns(s) that were converted into the new system are manually reversed, then rekeyed in the system as a native return for the correct period. The audit team must send a request to RAU to request converted returns be reversed and rekeyed. If RAU will make the move/adjustment to the return(s), the CDTFA-523 should be sent at the same time so both tasks will be worked together.

AUDIT SPRINGBOARD	0204.00
GENERAL	0204.01
As previously discussed, the Audit springboard is used to stage the audit from creation through completion and contains frequently-used tabs, sub-tabs, hyperlinks, and related information.	
PROGRAM DEFINED	0204.03
The Program reflects the tax or fee program being audited.	
TYPE DEFINED	0204.05
The Type is the description of the type of assignment (that is, audit or FBO) for the Case.	
STAGE DEFINED	0204.07
The Stage refers to the various stages of an audit, reaudit or FBO which includes, but is not limited to, “Created”, “Pre-Planning”, “Perform Audit”, “Prepare Audit Package”, “Audit Review”, and “Posted & Billed”.	
STATUS DEFINED	0204.09
The status of a Case shows the current status of the Case, such as “In Progress”, “Sup Review”, “Audit Review”, “PA Review” and “Posted”.	
LEAD AUDITOR DEFINED	0204.11
The lead auditor displayed on the Audit springboard is the lead auditor assigned to the audit. More than one auditor may be assigned to an audit Case. Additional auditors will be added to the audit Case’s timesheet on the Time tab.	
CASE ID DEFINED	0204.13
The Case ID number is a unique identifier for an audit or FBO.	
EXTERNAL ID DEFINED	0204.15
The External ID is the case ID number given to cases that were previously outside of the system (generated in the old system). The External ID is strictly used to document the case number of audit/reaudit/FBO generated in the old system.	
ASSIGNED DATE DEFINED	0204.17
The Assigned Date is the date the audit was assigned to the lead auditor.	
AUDIT BEGIN/END DEFINED	0204.19
The Audit Begin/End date is the date the Audit is staged to “Perform Audit” for the “begin” date. For the “end” date, it is either when the audit is staged to Review or, in the case of a NOW, when the NOW is staged to the “Completed” stage.	
AUDIT PERIODS DEFINED	0204.21
The Audit Periods lists the periods being audited. Note that with the system, the dates shown, including the “begin” date, will show the last day of the period/quarter.	
POSTING PERIOD DEFINED	0204.23
Once the audit is complete, the Posting Period is the final date of the audit period.	

FIRST STATUTE DATE DEFINED**0204.25**

The First Statute Date displays the end date of the first expiring period. Because this date is not always accurate in the system, auditors should also **review the statute of limitations dates** under Attributes to ensure no periods are expiring before the First Statute Date listed.

ACCOUNT INDICATOR(S) DEFINED**0204.27**

Indicators are alerts, or “flags,” placed on a Customer, Account, or Period. An indicator can:

- Provide additional relevant information about the record in context; or
- Affect the results of a process for the record in context (for example, a Stop Mail indicator stops mail from being sent).

The indicator either provides relevant information or indicates that an action is currently happening (or not happening) within the system. There are two basic types of indicators: information indicators and action indicators.

RECENT NOTES DEFINED**0204.29**

The Recent Notes section displays the three most recent notes for the Customer, Account or Audit for the Customer.

AUDIT TAB DEFINED**0204.31**

Under the Audit tab on the Audit springboard, the associated sub-tabs are displayed. The following information is displayed from the Audit tab:

- **Periods:** A list of all financial periods included in the audit, including tax/fee, penalty, interest, other, credit, and current balance. If periods are grayed out, then periods were removed from the audit Case.
- **Working Papers:** A list of all lead schedules, penalty schedules and the summary schedule.
- **Postings:** A list of all audit postings, i.e., tax, penalty, interest, and any credit, once a Summary Lead Schedule is created. The posting date for tax, interest, and penalty and the posting date in the top section of the audit Case should match the end of the audit period to ensure amounts are billed in the proper period.
- **Prepayments:** A list of any pre-payments associated with the audit.
- **Vouchers:** A list of any vouchers associated with the audit. These are produced monthly and sent to the taxpayer showing the current balance due.
- **Attributes:** This is the area that is required to be completed by auditors for every audit and FBO. It includes the field office that conducts the audit, the taxpayer’s activities, the taxpayer’s representative information, and converted audit hours from the old system (if applicable). It also includes a check box for the audit team to indicate the audit is a managed audit and all the questions previously found on the 414A page 3, as to whether a taxpayer has 50 or more employees; if the auditor checked for cigarette indicia; if the taxpayer sells televisions, computers, etc.; if the taxpayer sells lead acid batteries; if the taxpayer sells tires; if the taxpayer sells cigarettes; if the taxpayer is a distributor of cannabis; if the taxpayer sells alternative fuels; if there are any related accounts; and if they have an underground storage tank.

The second tab under attributes is the Statute of Limitations tab. This lists all the periods in the audit and shows the Statute Date and Expire Date which will later be on the waiver of limitations, if obtained.

- **History:** A list of any audit history. Values displayed in bold text indicate the item was changed.

CRM TAB DEFINED

0204.33

The CRM Tab is used to add/view notes, letters, and attachments. It can be used to add indicators, cross references, and information. It can also be used to access/view the Online Services settings for the Customer or Account. The CRM tab displays the following sub-tabs:

- A list of notes, including all user-entered and system-generated notes is displayed on the **Notes** sub-tab. The user is able to view, add, edit, filter, and export notes.
- A list of indicators placed on a Customer, Account, or Period is displayed on the **Indicators** sub-tab, depending on which springboard is being viewed.
- A list of audit letters generated, sent, or invalidated is displayed on the Letters sub-tab. The **Letters** sub-tab allows the user to view, add, issue, or reissue letters.
- A list of cross references (informational links that can be added between different items in the system) is displayed on the **Cross Reference** sub-tab.
- A list of attachments related to the audit is found on the **Attachments** sub-tab. The user is able to add, download, filter, and attach documents here. All prior versions of attachments will be retained in the system. Different versions can be sorted and viewed by date.
- A list of each action that took place in the system (for example, an address was added or a Case was closed) is displayed on the **Information** sub-tab.

TASK TAB DEFINED

0204.35

The Task tab provides the ability to view/create Tasks such as Cases and Work Items. The Task tab displays the following sub-tabs:

- A list of different types of Cases that can be created such as a Waiver of Limitations, Information/Document Request, Audit Plan, Memorandum of Tax Liability, California Nexus. Work Items available to be created, are displayed on the **Forms** sub-tab.
- A list of Cases associated with the audit is displayed on the **Associated Items** sub-tab.
- A list of all Work Items related to the audit is displayed on the **Work Items** sub-tab.

REGISTRATION TAB DEFINED

0204.37

The Registration tab provides a listing of all Accounts associated with the Customer.

TIME TAB DEFINED

0204.39

The Time tab is used to add/view the hours spent on the audit. This can be viewed by hours, user, or activity.

STAGES TAB DEFINED

0204.41

The Stages tab provides a history of stages of the audit, when the stage was moved, and by whom it was moved. Stages include, but are not limited to, “Created”, “Pre-Planning”, “Perform Audit”, “Prepare Audit Package”, “Supervisor Review” and “Audit Review”.

STATUSES TAB DEFINED

0204.43

The Statuses tab provides a history of the statuses of the audit, when the status was changed, and by whom the status was changed. Statuses include Audit Review, Canceled, Closed, In Progress, New, PA Review, Posted & Billed, Reaudit in Progress and SUP Review.

OTHER TAB DEFINED

0204.45

The Other tab contains two sub-tabs: Warehouse and Transcripts. The Warehouse sub-tab, also referred to as the Data Warehouse, lists external data available, such as information from the Department of Motor Vehicles, the Franchise Tax Board, and the Employment Development Department. The Transcripts sub-tab provides a listing of the taxpayer's return data, which is where auditors can download transcripts when beginning their audits.

SYSTEM LEAD SCHEDULES

0205.00

TYPES OF LEAD SCHEDULES IN THE SYSTEM

0205.01

Although auditors will use the Excel AWP file to create audit schedules, auditors must either enter manually or import all information from the AWP into the system, using the appropriate lead schedules.

Lead schedules will be categorized into the following five types:

1. **Manual Adjustments** – adjustments based on established difference(s) (for example, recorded versus reported tax, taxable sales reconciliation, or estimated quarterly adjustments basis).
2. **Net Tax** – adjustments for which the tax amounts, rather than the tax measures, are entered or imported into the system (for example, sales tax accrual reconciliation or voluntary disclosure payment).
3. **Percent Error** – used for projection (for example, an error rate based on a statistical sample or block test, markup on cost method, or business observation test).
4. **Transactions** – actual basis examination (for example, fixed assets).
5. **Tax Recovery & Expired Rates** –allows for the selection of a period in which tax applies. This is useful in situations for bad debts or tax paid purchases resold when the tax rate for the original transaction is different than the period in which it is claimed.

An audit can have more than one of the five types of schedules listed above due to multiple errors along with multiple schedules of the same type. If unsure which schedule to choose for an audit, auditors should check with their supervisor.

VERIFICATION COMMENTS

0206.00

GENERAL

0206.01

The Verification tab, located in the Audit springboard, Working Paper tab, Summary working paper in the system, should include comments that are clear, specific, and concise. These verification comments replace the verification comments previously found in the Excel Audit Working Papers (AWP) as an embedded Word document. The embedded Word document should no longer be used. The “Required Comments” sub-tab under the Verification tab are mandatory and are required to be addressed. For instance, even though “self-consumed merchandise” may not always be applicable, an entry is required (example: “Self-consumed merchandise is not applicable in this audit.”). The comments must be placed under the appropriate headings that are provided in the dropdown menus.

The “Other Comments” sub-tab displays other comments that support the verification done by the auditor. Any other comments not found under the Required Comments tab can be found here. These comments are not mandatory however, based on the type of audit being conducted, some may be applicable.

In general, a comment should be made on any point that will be of value in connection with making a determination, making decisions regarding future audits, requiring new permits, correcting taxpayer records, enforcing collection actions, providing guidance on tax application to assist the taxpayer in reporting in the future, etc. For example, in describing a construction contractor’s business activities, it is not only helpful to know if the taxpayer also makes over-the-counter retail sales, but it is equally important to give the degree of such activity (“substantial” or “rarely”). This information assists CDTFA in determining if sales tax, district tax, and local tax returns, among others, are accurate.

Auditors should avoid comments regarding the taxpayer’s personal affairs, political connections or other matters which have no bearing on the foregoing points. Such comments serve no useful purpose and are not relevant to the audit.

Auditors should not use abbreviations or should include the full name and show the abbreviated version when first used. For instance, auditors could write “Federal Income Tax Returns (FITR)” for the first reference and then can use FITR on later verification comments. Verification Comments in the system should be general and only give an overview of what actions were taken by the auditor or a description of what was observed by the auditor. Additional detailed comments must be provided on the Excel AWP schedule comments unless the heading provides enough of a detailed description on its own. Verification comments should **not** be the same as the comments on the AWP schedules. Duplicating comments may cause errors when updates are not made in all areas.

The same thing is true regarding lead schedules versus subsidiary schedules. They should not cover the same material or merely be copied from one to the other. Comments on subsidiary schedules should be much more detailed than those made on the lead schedules in the Excel AWP. Overall, comments should be written in an orderly manner, simply stating the nature of the transactions, the records examined, the taxpayer’s method of reporting, the audit approach, and the results or audit findings.

CONFIDENTIALITY OF COMMENTS

0206.03

An auditor must always take precautions against the disclosure, intentional or otherwise, of audit comments of a confidential nature. If the audit is based on records of a predecessor or some other confidential source, auditors must consult with an audit supervisor regarding what information can be disclosed. See Audit Manual (AM) section 0405.34 for additional information on using predecessor information in a successor’s audit.

EXTENT OF COMMENTS

0206.05

The extent of the comments will depend on the importance of the subject matter and whether the comments are regarding certain changes in the status of the account. Comments should be brief, yet still give complete information. The following comments on the Verification tab, “Required Comments” are always required for all sales and use tax audits, even if the only comment is “Not applicable” and the reason not applicable. (Special Taxes and Fees audits may have different “Required Comments”):

Type of Business Organization (AM 206.09)	Total Sales (AM 206.17)	Fixed Assets (AM 206.25)
Type of Transactions (AM 206.11)	Tax Accrual Account (AM 206.19)	Self-Consumed Merchandise (AM 206.27)
Books and Records (AM 206.13)	Bad Debts (AM 206.21)	Retailer Engaged in Business (Nexus) (AM 206.29)
Reporting Method (AM 206.15)	Paid Bills (AM 206.23)	

In addition to the above list, the following are comments that may be applicable to certain audits and are included in the Verification tab, “Other Comments”:

Auditor’s Position	Manufacturer’s Exemptions
Bankruptcy	Manufacturing and Research & Development
Cash Discounts	Markup Analysis
Claim for Refund	Material Accountability Test
Close-Out Verification	Miscellaneous (see Note below)
Credit Interest	Other (see Note below)
Diesel Fuel Used in Farming and Food Processing	Overpayment
Discussion with Taxpayer	Penalty
District Tax	Racehorse Breeding Stock
Excess Tax Reimbursement	Reason for Reaudit
Exempt Sales	Recorded to Reported
Explanation of Tax Change	Resales
Farm Equipment	Returned Merchandise
Food Products	Sale of Fixtures and Equipment
Interstate Commerce	Sales Tax
Labor	Seller Reimbursement Fee
Lumber Product Assessment	Supervisor’s Comments
Tax Paid Purchases Resold	Timber Harvesting Equipment and Machinery
Taxable Sales	US Government
Taxpayer’s Position	Verification and Findings
Teleproduction Equipment	

NOTES:

- 1) The “Other” category should coincide with the taxpayer’s reporting of “Other” category on their transcript of returns. The “Miscellaneous” category should be used when there is no pre-programmed category.
- 2) Auditors can press enter twice after each comment (or description on lead schedules). This creates space between each heading on the letter to make it easier to read on the Audit Report Letter.

REQUIRED VERIFICATION COMMENTS**0206.07**

Auditors must complete the “Required Comments” for all audits. In the system, the “Required Comments” are located in the Summary schedule, Verification tab.

Additional comments specific to the audit may be required, even though they are not listed under “Required Comments.” For instance, when an audit includes a claim for refund, a comment must be made under “Other Comments” using the “Claim for Refund” selection from the dropdown. Another example is when a penalty comment is required for all audits except those resulting in a tax liability of less than \$2,500 when a penalty is not recommended (see AM section 0506.35). The penalty comment must be entered under “Other Comments” by selecting “Penalty” under the dropdown. See section 0206.31 for more information on “Other Comments.”

TYPE OF BUSINESS ORGANIZATION**0206.09**

Enter the ownership type operating the business (and how ownership was verified), such as, sole proprietor, partnership, limited liability company, corporation, or other entity. Enter the names of all owners, partners, (including their designations in the case of a limited partnership), principal corporate officers and their titles, and members and managers of a limited liability company.

Enter the start date and close-out/cease date (if applicable). Indicate whether there are any prior audits; if none, then state “no prior audit.” If there are any prior audits, then indicate through which period and the result, whether it was a deficiency, credit or No Opinion Warranted (NOW).

AM section 0202.00 describes the procedures and importance of obtaining accurate entity and ownership information, including addresses. When conducting an audit, auditors are responsible for verifying the address(es) and documenting the type of ownership in the audit report, and for ensuring that CDTFA’s records on the account are updated. Auditors should verify the correct entity information matches CDTFA registration, Federal Income Tax Returns, Secretary of State, or other applicable sources to support billing the proper entity. Copies of Secretary of State files or other verification documents can be attached in the Audit case under “Miscellaneous & Documents” type.

Example:

Sole proprietorship. Thomas Smith, owner. Start date: 11/01/2010. Active, No prior audit.

TYPE OF TRANSACTIONS**0206.11**

Under this heading, auditors give a description of the taxpayer's business and the types of transactions encountered in the audit. Auditors should also include information about where the business is located and the types of surrounding businesses for retail operations, along with information on payment method (i.e., credit card, debit cards, or cash) and if cash back is provided to the customer. Auditors may include information on size (e.g., capacity, number of bays for repair shop, square footage, etc.), number of employees, and other items to provide a good overview of the operations to support the audit findings. Screen shots of Yelp, the business's own website, or similar information should be attached for audits of restaurants or other applicable industries.

Example 1:

The taxpayer operates a fast food restaurant with three locations throughout California. Items sold include Chinese hot foods and carbonated beverages. Each location offers dine-in, take-out, and a drive-thru. No alcohol is sold.

San Francisco Location:

- Business hours - 8:00 a.m. to 10:00 p.m. every day
- Facility capacity - 65

Oakland Location:

- Business hours - 8:00 a.m. to 10:00 p.m. Monday through Friday, closed Saturdays and Sundays
- Facility capacity - 23

Sacramento Location:

- Business hours - 8:00 a.m. to 10:00 p.m. every day
- Facility capacity - 85

Example 2:

Taxpayer operates a Mexican food restaurant in the county of San Bernardino. Business hours are Monday - Sunday 8am-11pm and a drive thru is open 24 hours. All sales are rung up through the register. Taxpayer has one register. Taxpayer closes daily sales at 8am every morning. Restaurant serves lunch and dinner meals by dine-in or take out. Taxpayer sells burritos, tacos, quesadillas and other combination plates, and soda drinks. No alcoholic beverages are served. Taxpayer rings up all sales as taxable sales. Taxpayer is located on the corner of the street next to a fast-food restaurant and across the street from another Mexican restaurant. Restaurant has 6 tables and 22 chairs for customers to sit and eat inside. Taxpayer accepts credit cards, debit cards, and cash. No cash back is offered. Taxpayer charges a \$0.50 fee to use credit/debit cards.

Auditors should also be sure to include any special comments relevant to the industry being audited. To ensure comments cover any applicable items, auditors should review related Audit Manual chapters, Industry Guides, and Publications for any specialized industries, or qualify if not addressed due to materiality. Auditors also may refer the taxpayer to the relevant material for more information to assist them in reporting properly in the future.

The sample below describes why certain areas were not addressed.

Example 3:

Auditor did not address tire fees, trade-ins, core charges, oil recycling fees, hazardous waste fees, sublet parts, disposal fees, or other minor charges. Taxpayer can refer to Publication 25 – *Auto Repair Garages and Service Stations*, for additional information on how tax applies. For this audit, these were not addressed due to immateriality or no applicable items noted.

BOOKS AND RECORDS**0206.13**

Comments regarding books and records should be limited to the records or lack of records which have a bearing on the audit procedure or the reliability of the taxpayer's figures.

Comments should describe:

1. Whether the taxpayer uses a single or double entry bookkeeping system. The comment should include the type of computerized system (if applicable) used by the taxpayer and whether the records are maintained in house or are maintained by a bookkeeper or CPA. Auditors should include the type of Point of Sales (POS) system used and document any requests made for POS data and explain if unable to obtain.
2. The supporting records provided to auditors and the period covered by the records. If documentation is not available, the comment must indicate so. Also included should be all attempts to obtain records, and if those attempts were successful or unsuccessful. This should also be recorded in the CRM Notes. If the taxpayer is uncooperative in providing records, all actions taken should be documented, including any actions taken or not taken, towards a subpoena.
3. The adequacy of the records for sales and use tax purposes must be addressed. This information is important for application of a negligence penalty. Adequate records are the type of records maintained by a reasonable and prudent businessperson, engaged in a similar type and size of business, used for accurate sales and use tax preparation. The records only need to be adequate for sales and use tax purposes (that is, not for other purposes, such as for income tax purposes, etc.).
4. Whether sales tax reimbursement is either included in, or added to, the selling price of items sold. If tax is included in the selling prices, a comment should be made as to the notices posted on signage or on sales invoices/receipts for the customer to be aware of that status.
5. If anyone other than the taxpayer prepares the records, then note that person's name or firm name and contact information (for example, CPA firm, bookkeeper, etc.).
6. If the reporting method changed during the audit period, then indicate the period or date when the reporting method changed.

Example:

The taxpayer maintains a double-entry set of books and records supported by source documents. The taxpayer maintains books and records in house using computerized software known as QuickBooks.

Source data provided includes:

- Customer purchase orders – audit period
- Sales invoices – audit period
- Sales journals – audit period
- Monthly profit and loss statements – audit period
- General ledger – audit period
- Federal Income Tax Returns - 2018, 2019, and 2020 (provided by the taxpayer)

Books and records are adequate for sales and use tax purposes. A review of sales invoices indicated that sales tax reimbursement was added to the selling price of taxable sales. Federal income tax returns were prepared by Max Accounting Services: 1205 Merlot Lane, Napa, CA 94558, phone number 916-999-9999.

NOTE: This comment under this heading would need to be modified if the taxpayer did not provide any records during the audit period or if the taxpayer is uncooperative in providing records.

REPORTING METHOD

0206.15

Under this heading, auditors provide a description of how the taxpayer reports sales and purchases subject to use tax on the sales tax return. The comment should indicate who prepared the returns (for example, accountant, taxpayer, etc.). The comment should indicate how the taxpayer or tax preparer compiles data (including the accounting system used) to report amounts on their sales and use tax returns (for example, total sales reported or netted), the types of deductions claimed or netted, and if sales tax is included in the reported total sales (Line 1 of the return). If the taxpayer nets any sales or deductions, auditors should add additional comments on how and when they informed the taxpayer that all sales and deductions should be reported on their return. If the taxpayer reports on a cash basis, auditors should add additional comments on how and when they instructed the taxpayer to report on an accrual basis (with the exception of some leases). If the reporting method changed or there were large fluctuations in reporting during the audit period, this should be addressed in the comments and include the period where the reporting method changed.

Example:

The sales are rung up on the two electronic cash registers. The manager prints out the daily z-tapes at the end of the day, writes the total sales, taxable sales, nontaxable sales, and tax collected on a monthly log. The taxpayer provides the monthly logs to the accountant on a quarterly basis for preparation of the sales and use tax return. Nontaxable sales were netted from the sales and use tax returns. On 9/5/18, the auditor advised the accountant to report total gross sales and claim a deduction for nontaxable amounts going forward.

TOTAL SALES**0206.17**

Under this heading, auditors provide a description of how they verified total sales amounts. If reported total sales are not accepted, additional explanation must be made as to why the reported total sales were not accepted. In addition, auditors must comment on whether the total sales included sales tax or were net of sales tax. Examples of this comment might read:

Example 1:

Reported total sales were reconciled with the federal income tax returns (provided by the taxpayer) filed during the audit period. No material differences noted. See Schedule <12A-2b> for details.

Example 2:

Sales invoices were traced into the sales journals for July 2018 and January 2019 on an actual basis. Sales journals were then traced to sales and use tax worksheets for the audit period. No errors were noted; therefore, further examination was not performed.

Example 3:

Differences between reported total sales and amounts reconciled on the federal income tax returns (FITR) were disclosed for the years 2017 and 2018 (provided by the taxpayer). Additionally, a markup of costs was performed on total sales for the same years on schedule <12A-2c> which resulted in a low markup for this type of industry. Achieved markup was 100%, but for this type of industry, the expected markup is at least 200%. Unreported total sales were included in the audit findings on schedule <12A>.

NOTE: Verification comments should always include an explanation of any fluctuations in sales, markups, or in any of the deductions claimed by a taxpayer.

TAX ACCRUAL ACCOUNT**0206.19**

Under this heading, auditors give a description of how they verified the taxpayer's tax accrual account, and whether the tax amounts reported were accepted or not accepted. If not accepted, additional explanation must be made. This comment might read:

Example 1:

The taxpayer did not maintain a tax accrual account. Tax collected on sales invoices were traced to the sales journal on a sample basis and it was noted the taxpayer collected the proper tax rate. Therefore, recorded sales tax collected was reconciled to reported sales tax paid. No material differences were disclosed. See schedule <12A-3a> for details.

Example 2:

Reconciled reported sales tax to sales tax accrual account; no differences were noted. Reviewed debit entries over \$100 on an actual basis. There were several debit entries for which the taxpayer could not show the original accrual entries. Assessment was made on schedule <12B-2a>. Reviewed debit entries under \$100 on a sample basis; no errors noted.

Example 3:

Taxable sales summary reports, sales invoices, and the general ledger sales tax accrual account were examined and reconciled to reported/paid sales tax amounts for the audit period on an actual basis for 2QYY. The postings to this account were from sales and cash receipts journals. All charges to this account were for payments to CDTFA. Taxpayer does not reconcile account balances to the return. See schedule <12A-1> for adjustments for tax remitted by customers but not reported and for additional comments.

As noted in the examples above, auditors should include comments on how any material debits are addressed that are not payments or state that no material debits (other than payments) were noted in the tax accrual account.

Auditors should also verify that the proper tax rate is charged and comment in the AWP about how they conducted the test or verified the information. Auditors should include comments under the “Excess Taxes Reimbursement” header on how any excess taxes were handled. See section 0206.65 for more information on excess tax reimbursement.

BAD DEBTS**0206.21**

Under this heading, auditors should provide a brief description of how they verified the taxpayer’s taxable bad debts, if any. If no review was done for bad debts, auditors should explain why and explain that the taxpayer was informed of the bad debt deductions when related to sales previously reported as taxable.

Example 1:

No taxable bad debts noted. Taxpayer did not claim any bad debts on the Sales Tax Returns nor on the Federal Income Tax Return (FITR).

Example 2:

The taxpayer did not claim any taxable bad debts during the audit period. However, the auditor noted a bad debt deduction taken on the FITR (obtained from the Internal Revenue Service). The auditor traced the amounts claimed to the accounts receivable journal and noted they were for resale transactions. No adjustment is warranted.

Example 3:

The taxpayer claimed \$180,000 taxable bad-debt deduction in the audit period. The taxpayer agreed to provide a block sample to verify the claimed amounts. Auditor tested September 2019 and March 2021 supporting documents, which included original invoices, remittance notices, and the sales and use tax worksheet. The review showed the original sales included taxable sales transactions. It also revealed the taxpayer recovered some of their claimed bad-debt expenses via their collection efforts.

While the test showed the recorded bad debts were valid, discrepancies were found between the claimed and recorded taxable bad debts as well as the bad debts reported on the FITR (provided by the taxpayer). The adjustment for the allowable bad debts were included in the calculation of the audited collected sales tax and adjusted on schedule <12A-1a>.

PAID BILLS**0206.23**

Under this heading, auditors give a description of how they tested for purchases made by the taxpayer that may not have had sales or use tax paid on the purchase. Generally, the out-of-state purchases of fixed assets, specialized equipment, or repair parts are the items that require the most scrutiny. This is because they are usually the highest cost, out-of-state purchases made. In some cases, however, purchases made without tax paid may be miscategorized in the taxpayer's records as supplies. It is, therefore, important to check the supply purchases from out-of-state vendors, as well. Under this heading, auditors should give a description of how they verified the taxpayer's paid bills, meaning the consumable supplies purchased by the taxpayer that were expensed (not capitalized like fixed assets). If there are unreported ex-tax purchases found to have been acquired under a resale certificate, that should be noted in this section.

Example 1:

Consumable supply items were examined on an (actual, block or statistical sample) basis for the audit period (or any other period). Ex-tax purchases were addressed on Schedule 12B (or purchases were either tax-paid at source or self-accrued by the taxpayer).

Example 2:

Cursory examination for audit period (or period examined) of the consumable supply vendors disclosed that purchases are tax-paid at the source or self-accrued by the taxpayer. No further examination was deemed necessary.

Example 3:

The taxpayer did not report any purchases of consumable supplies. The auditor examined invoices for consumable supplies for 2Q-21 on an actual basis. No material amounts of ex-tax purchases of consumable supplies from out-of-state vendors were noted. However, the taxpayer was advised to report use tax on any future purchases of consumable supplies for which no tax was paid at the time of purchase.

Example 4:

Based on the nature of the taxpayer's type of business, ex-tax purchases of consumable supplies appear immaterial. A spot test of supply purchase invoices was performed for January 2020 and tax was paid to the vendor. Further analysis is unwarranted.

Example 5:

Paid bills were examined using the statistical sampling method. Transactions recorded in GL accounts of interest, including fixed assets, furniture and computer hardware were downloaded and processed by our Computer Audit Specialist. Random samples were selected and traced to the purchase invoices. Unreported ex-tax purchases of consumable items are noted, and a percentage of error is projected to the population. See schedule <12B> and the subsidiary schedules for details.

Example 6:

Auditor reviewed the expense accounts of interest to determine applicable vendors. The taxpayer's accountant filed purchase invoices by vendor and by year. Auditor then reviewed all purchase invoices on an actual basis for the audit period to identify purchases from out-of-state vendors. Questionable transactions are detailed on schedule <12C>; however, no errors noted.

Example 7:

Taxpayer provided a download of expense accounts of interest for 2021 including full vendor addresses. Auditor filtered out California vendors, given no material ex-tax purchases noted from California vendors in the prior audit. Auditor then reviewed sample invoices for any out-of-state vendors to verify taxes were properly handled. When ex-tax purchases were noted from unregistered out-of-state vendors, auditor requested all related invoices for the applicable vendor and these are listed on schedule <12C>. A percentage of error was computed based on the errors noted in the expense account tested for 2021. The percentage of error was then projected to the same expense accounts for the other periods.

FIXED ASSETS**0206.25**

Under this heading, auditors give a description of how they verified the taxpayer's purchases and sales of fixed assets. Comments discussing a sale of fixed assets must be included unless the sale of the business and the sale of assets are otherwise covered in the "Close-Out Verification" comment regarding a closed out/ceased account.

Example 1:

Capital fixed-asset purchases were examined on an (actual, block or statistical sample basis) for the audit period (or any other period) based on the (general ledger accounts, depreciation schedules, etc.). Ex-tax purchases were addressed on Schedule 12C (or purchases were either tax-paid at source or self-accrued by the taxpayer).

Example 2:

The auditor reviewed the FITR depreciation schedule (obtained from the Internal Revenue Service) for the audit period and fixed asset listing for any fixed assets or construction-in-progress subsequent to the FITR schedule period. No ex-tax purchases of fixed assets occurred during the audit period. However, the taxpayer was advised to report use tax on purchases of fixed assets from out-of-state vendors for which no sales tax was paid at the time of purchase.

SELF-CONSUMED MERCHANDISE**0206.27**

Under this heading, auditors briefly give a description of how they verified the taxpayer's self-consumed merchandise, whether it was self-reported at cost or not. Self-consumed merchandise should address any items normally subject to sales tax (for which a resale certificate was issued at the time of purchase) and was then removed from inventory with no use tax paid. This may include items such as soda, cigarettes, and alcohol in the case of a convenience store, but could include bicycles for a seller of bicycles. Auditors should also comment if any discounts were given on the items normally subject to sales or use tax.

Example:

The taxpayer consumed minimal ex-tax inventory, including soda, alcohol, and cigarettes, during the audit period. The amount of self-consumed merchandise was immaterial; therefore, no assessment was made. However, the taxpayer was advised to report, at cost, any taxable merchandise withdrawn from resale inventory for consumption; for example, owner use, but also employee and customer comps.

For larger audits, auditors should be aware that free samples may have been provided to their customers. In those cases the comments should explain how these items were tested and how the reporting of any applicable taxes was verified.

RETAILER ENGAGED IN BUSINESS (NEXUS)**0206.29**

This heading is especially relevant for out-of-state audits for auditors to comment on whether the taxpayer has nexus in California. This heading also pertains to nexus for district tax purposes. The below information explains when auditors must comment.

Retailers with a physical presence in California are generally required to be registered with CDTFA. Examples of a physical presence in this state include, but are not limited to:

- Maintaining inventory or office locations in California.
- Having representatives in California for purposes of taking orders, making sales or deliveries, or installing or assembling tangible personal property.
- Leasing equipment, including a computer server in California.

If an out-of-state retailer has a physical presence in California, auditors must include a comment describing that presence.

Example:

Although the taxpayer's headquarters is located out of state, the taxpayer has six sales agents that visit customer locations in California. In addition, the taxpayer installs equipment in California.

On and after April 25, 2019, RTC section 6203 requires retailers located outside of California (remote sellers, including foreign sellers located outside of the United States) to register with CDTFA and collect California use tax if, during the preceding or current calendar year, the total combined sales of tangible personal property for delivery in California by the retailer and all persons related to the retailer exceed \$500,000, whether those sales of tangible personal property are taxable or exempt (such as being sold for resale or to the US Government). A person is related to a retailer if they have a relationship with the retailer described in section 267(b) of title 26 of the United States Code and the related regulations. Retailers that exceed the \$500,000 sales threshold in the preceding or current calendar year are required to register with the CDTFA to collect the California use tax even if they were not previously required to register. These retailers include retailers that sell tangible goods for delivery into California through the Internet, mail-order catalogs, telephone, or any other means.

Example:

The taxpayer has more than \$500,000 in total combined sales into California in the current calendar year. Therefore, the taxpayer is required to collect, report, and pay use tax at the basic statewide sales and use tax rate, plus any applicable district taxes for all sales made into taxing districts.

District Tax

Retailers with a physical presence in a district are generally required to collect that district's use tax and report and pay it to CDTFA.

In addition, on and after April 25, 2019, RTC section 7262 requires **all** retailers, whether located inside or outside of California, to collect district use tax on all sales made for delivery in any district that imposes a district tax if, during the preceding or current calendar year, the total combined sales of tangible personal property in California or, for delivery in California by the retailer, and all persons related to the retailer exceed \$500,000, whether those sales of tangible personal property are **taxable or exempt**. If an in-state taxpayer does not meet the \$500,000 threshold, auditors must indicate whether they have a physical presence in any districts, requiring them to collect district tax. If the taxpayer is not required to collect district use tax, but charges/collects it from customers as a courtesy, that should be stated.

Example 1:

The taxpayer's sales in California in the current calendar year are under \$500,000. The taxpayer had \$200,000 in taxable sales and \$100,000 in non-taxable sales of tangible personal property in the prior calendar year. The taxpayer has netted all non-taxable sales on last year's sales and use tax returns, totaling \$100,000. Because the total combined sales were \$300,000 and were under the \$500,000 threshold in the prior or current calendar year, the taxpayer is not required to collect, report, or pay use tax or any district taxes. The taxpayer does not have a physical presence in California.

Example 2:

The taxpayer has more than \$500,000 per calendar year in total combined sales in California. The taxpayer is required to collect, report, and pay use tax, including any applicable district taxes for all sales made into taxing districts, regardless of whether the taxpayer has a physical presence in those districts.

NOTE: If the audit period starts before April 25, 2019 auditors should state how the taxpayer was reporting district taxes before and after the changes to RTC 7262.

OTHER COMMENTS**0206.31**

The "Other Comments" tab should be used when there are other areas that require verification pertaining to the audit, but are not listed in the dropdown menu of the "Required Comments" tab. "Other Comments" can be located by accessing the Summary audit working paper, Verification tab, Other Comments sub-tab.

Comments should be meaningful and necessary. When an area reviewed results in no differences, comments should be brief. The following recommended comment structure should be followed when completing the "Other Comments":

1. What was reviewed?
2. How was this area examined/verified?
3. What was the result of the examination?
4. What was the time period of the examination?
5. What books and records were examined?
6. If errors are noted, explain how and when the taxpayer was advised of the correct method (including applicable law and/or regulation sections).

There may be additional comments that are required, specific to each audit. When a comment is not found under "Required Comments," the comment will be included under "Other Comments." "Other Comments" should be just as complete, clear, and concise as "Required Comments." Examples of the captions required in specific circumstances are illustrated in Sections 0206.33 to 0206.85 below.

NOTE: For drop downs under the "Other Comments," auditors should select the appropriate category. The "Other" category should coincide with the taxpayer's reporting of "Other" category on their transcript of returns. The "Miscellaneous" category should be used when there is no pre-programmed category.

CLOSE-OUT VERIFICATION**0206.33**

In the case of a close-out/ceased audit, auditors must show the additional measure of sales tax established as a result of the final sale of assets, if applicable, as a separate lead schedule in the AWP and the lead schedule in the system. When this is done, a close-out/ceased verification comment will not be required in the Verification comments.

In all other cases, auditors must include a brief comment explaining the disposition of fixed assets and inventory at close-out/cease, the date of the close-out, and how and when CDTFA learned of the close-out. If the business was sold, the successor's information should also be included, if known. If the taxpayer reported the sale as taxable, the comments should detail the taxpayer's method of determining the taxable measure and the reasonableness of the amount reported. This verification and comment of the correct reporting should be made even though sales tax on the fixed assets was paid through escrow.

If the asset disposition is exempt, the comments should include the reason for the exemption (for example, occasional sale, resale, interstate sale, etc.) If exempt under Sales and Use Tax Regulation 1595, *Occasional Sales – Sales of Business – Business Organization*, auditors should state under which section the sale is exempt and address any applicable items as further discussed in Audit Manual Chapter 10, *Occasional Sales – Sales of a Business*.

It is important for auditors to work with the compliance team to ensure all aspects of close-out/ceased audits are performed accurately and efficiently (that is, fixed assets and equipment, final return, disposition of inventory, and payment of liability).

When inventory is not transferred to the successor for resale, inventory items that would be subject to tax, if sold at retail, should be examined to determine the materiality of those items' costs. If the inventory is deemed to be of a material amount and it is retained or given away by the taxpayer, those items should be treated as taxable self-consumption and assessed (at cost) in the audit findings.

Example 1:

Business closed out/ceased 12/31/18. Business abandoned, no sale of F&E. Taxpayer would owe tax on any outstanding ex-tax inventory retained for their own use, but amounts noted were minor and not addressed further.

Example 2:

Business closed 12/31/18. Taxpayer incorporated and new permit is xxx-xxxxxx. No taxable sale of assets included since asset sale appear as an exempt occasional sale under Sales and Use Tax Regulation 1595(b)(2) since substantially all the assets were transferred without any substantial change in ownership. Asset sale also exempt under Sales and Use Tax Regulation 1595(b)(4) since assets sold in exchange for stock to a commencing corporation and no material assumption of liabilities were noted. All inventory was transferred to the commencing corporation for resale.

Example 3:

Business closed 12/31/18. Taxpayer sold the business and successor has a permit under xxx-xxxxxx. Given this is a small restaurant with limited fixed assets, auditor did not address further. Any taxable sales of fixed assets were reported through escrow. All inventory was transferred to the successor for resale.

PENALTY COMMENT**0206.35**

Auditors must enter a penalty comment when a penalty is recommended or when the tax liability is \$2,500 or more and no penalty is recommended. Comments should be clear and concise, explaining the rationale for the auditor's recommendation (penalty recommended and no penalty recommended). Canned comments, such as "Negligence not noted" or "No penalty recommended," should not be used without additional explanation. Auditors should explain when a lower percentage of error can still be cause for the recommendation of a penalty due to additional factors that occurred. Alternately, there might be some instances where a higher percentage of error occurred when a more narrow population was tested and the overall understatement is small when compared to total exempt sales or a high volume of sales. See AM Chapter 5, Penalties, for general guidelines and procedures on penalties.

Example 1:

No negligence penalty is recommended. Taxpayer's Point-of-Sale (POS) system was programmed improperly for taxable and non-taxable items. In addition, this is the taxpayer's first audit. Taxpayer corrected the programming of the POS system as of (date) which should correct the problem in the future.

Example 2:

No negligence penalty is recommended as the percentage of error is just over 25% and decreased steadily over the audit period and this is the taxpayer's first audit.

There does not appear to be any intent on the taxpayer's part to materially underreport and the resulting deficiency could be attributed to mere mistakes.

Example 3:

This is taxpayer's second audit and errors noted for ex-tax purchases are similar to errors noted in the prior audit. Taxpayer reported approximately 10% of their ex-tax fixed assets. Given no significant employee turnover and minimal steps taken to ensure use tax reported, a 10% negligence penalty is recommended.

Example 4:

Negligence penalty is not recommended. This is taxpayer's second audit and errors noted are similar to errors noted in the prior audit. However, taxpayer is reporting use tax on line 2 and errors noted in both prior and current audit are minor in comparison to the size of the business.

Example 5:

A 25% fraud penalty is recommended in accordance with RTC 6485. We have concluded there is strong evidence that the understatement was intentional for purposes of the 25% penalty. We contend the large amount of underreporting, coupled with the lack of adequate diligence required of a prudent businessperson, necessitates the imposition of this penalty.

The audit was based upon multiple exterior observations conducted over several months. In addition, one two-hour site test was conducted. Only one site test was allowed by the taxpayer. The results of these observations and this test produced substantially higher amounts of average daily taxable sales than the amounts reported or documented through exterior observations. Additional information is detailed in the memorandum dated 9/1/20 and which was forwarded to Headquarters.

Even though this is the taxpayer's first audit, we contend the taxpayer intentionally misrepresented actual sales. His actions went beyond negligence in his duties to report the correct amount of tax and instead rose to the level of an intentional understatement of tax.

Taxpayer declined to provide actual books or records related to sales other than hand-written documents. During a two-hour, on-site observation conducted by the auditor with the attendance of the taxpayer's representative, auditor heard a customer ask where their computer was. The employee responded that it was being fixed. Taxpayer denied to the auditor that there was a cash register or POS system prior to this observation. Photographs obtained from the taxpayer's website clearly show cash registers being used at the business location.

For tax liabilities over \$25,000, the auditor's supervisor must review and approve the penalty comment. For tax liabilities over \$50,000, the Office Making Audit (OMA), Principal Auditor must review and approve the penalty comment subsequent to approval by the auditor's supervisor. Supervisors and Audit Principals will be deemed to have approved penalty comments when they indicate their approval of the audit as a whole on the staging of the audit.

See AM Chapter 5, *Penalties*, for general guidelines and procedures on penalties.

CLAIM FOR REFUND COMMENT

0206.37

If the taxpayer filed a claim for refund, auditors must verify the claim for refund and include a comment under "Claim for Refund." The comment must clearly explain the description of the refund claimed and why the refund should be granted or denied, in full or in part, and must include the following information:

- The basis of the recommended refund amount which should explain any supporting documentation provided and any related verification. It should also include comments on why related items are exempt or other reasons for the refund.
- Explanation for any portion disallowed.
- The amount of tax to be refunded as established by the taxpayer.
- The amount of tax to be refunded as recommended by the auditor.
- Whether an appeals conference has been requested (for disagreed refund claims only).

Example 1:

The taxpayer filed a claim for refund (case number XXXXXX) for tax-paid to another state which was not claimed on returns. The claim, as filed, was for "\$1 or more." The documentation submitted for verification disclosed an actual claim amount of \$2,135. The taxpayer purchased inventory from another state and paid sales tax on those purchases. The auditor verified the amounts on an actual basis. All claimed amounts are valid and within statute. The claim for refund is accepted and details are included on schedule <12A>.

Taxpayer's Claim: \$1 or more (\$2,135 in tax documentation submitted)

Audited Claim: \$2,135 in tax.

Example 2:

Taxpayer filed a claim for refund (case number XXXXXX) for “\$1 or more.” The documentation submitted for verification disclosed an actual claim of \$99,899. Taxpayer requested credits for the Manufacturing, Research & Development exemption on depreciated fixed assets. Auditor reviewed the supporting documentation on an actual basis and allowed the credit in the audit. For detail of the transactions, please refer to schedule <12B>.

Claim for Refund Case: X-XXX-XXX-XXX

Taxpayer’ Claim: \$1 or more (\$99,899 in tax documentation submitted)

Audited Claim: \$99,899 in tax

If there are multiple claims for refund, auditors should have the above comments for each claim for refund and include the claim-for-refund case number.

Auditors must obtain the CDTFA-101, *Claim for Refund or Credit* (refund claim), or the taxpayer can provide it through Online Services, when a credit item and/or credit period exists. If a taxpayer refuses to file a refund claim, auditors must explain to the taxpayer that without a refund claim, the credit will only offset against the audit deficiency and no refund can be issued beyond the offset deficiency.

In addition, auditors must document in CRM Notes all efforts taken to obtain the claim for refund. Comments should also specifically state what credit items were allowed without a claim for refund to document which credits were timely claimed.

See additional guidance under “Overpayments” under AM 0217.00.

CREDIT INTEREST COMMENTS**0206.39**

If auditors recommend that credit interest be allowed or denied, a comment should be entered regarding the recommendation under the “Credit Interest” comment heading from the dropdown under “Other Comments.”

This statement applies to both refund audits and deficiency audits with credits in one or more quarters. If the credits within the same audit were caused by different circumstances, auditors may recommend that interest be allowed for some quarters and denied for others. Credit interest is **not** allowed for periods where a negligence or fraud penalty is asserted as explained in AM section 0218.05.

If credit interest is allowed, the auditor’s comments should explain why no carelessness was noted. Auditors can refer to “When Interest on Overpayments is Allowed” under AM 0218.07 for guidance for types of reasons for allowing credit interest. Auditors can refer to “When Interest on Overpayment Not Allowed” under AM Section 0218.05 for information when credit interest is not allowed.

A Credit Interest comment is required when any period is a net credit. As noted in the instructions on handling claims for refunds, auditors should always include a credit interest comment because the audit results of net credit periods that offset debits could later be reversed.

AMNESTY**0206.41**

In 2005, a short-term sales and use tax amnesty program was conducted as provided in Revenue and Taxation Code (RTC) sections 7070-7078. The program allowed taxpayers to pay the tax and interest they owed for tax reporting periods that began before January 1, 2003, without paying penalties that usually apply. Taxpayers had to apply for tax amnesty between February 1, 2005 and March 31, 2005.

If an audit includes reporting periods eligible for amnesty, the audit team must make a comment under the “Miscellaneous” comment heading indicating whether or not the taxpayer participated in the amnesty program. If the taxpayer participated in the program, additional details regarding such participation should be provided, including:

- a) Whether or not the taxpayer filed amnesty tax returns, and if so for which reporting periods.
- b) Whether or not amounts reported on the amnesty returns were the same, less than, or greater than the amounts included in the audit.
- c) Whether or not periods included in the audit go beyond the normal three-year audit cycle.
- d) Whether or not periods were covered by a waiver that has expired.

For Notices of Determination issued on or after April 1, 2005, the amnesty penalties will apply to underreporting of tax amounts. If a taxpayer participated in amnesty, but reported less than the liability later determined, the amnesty penalties will apply to the amount of tax not reported. The audit team must apply the double amnesty penalties. In addition, the amount of the 50 percent interest penalty should be identified in a comment made under the “Miscellaneous” comment heading. The audit team must disclose information regarding the amnesty penalties applied to the audit liability to the taxpayer.

DISCUSSION WITH TAXPAYER**0206.43**

When a taxpayer disagrees with any portion of the audit findings, a “Discussion with Taxpayer” comment must be entered. The “Discussion with Taxpayer” comment will list and explain in clear, complete, and concise detail each item and measure amount in the audit with which the taxpayer disagrees and agrees. This comment is required for disagreed or non-committal audits. Each item should be listed in the same order as the description and amounts on the lead schedules.

Example 1 Disagreed:

Results of discussion of audit findings with Lisa Smith, CPA and John Doe, President on November 16, 2020 are summarized as follows:

Item 1-<12A-1>: Difference Between Recorded and Reported Taxable Sales Based on Monthly Worksheets – Audit Period - \$276,533 - Disagrees

Item 2-<12A-2>: Additional Taxable Sales Based on Credit Card Ratio Using Z-tapes for 9-1-20 to 9-30-20 – Audit Period - \$578,956 – Disagrees

Example 2 Non-Committal:

Audit findings were mailed and e-mailed to Kathy Johnson, President on September 19, 2019 and taxpayer did not respond to the CDTFA-79-G, *Letter to Taxpayer Prior to Billing* dated October 15, 2019. Audit results are summarized as follows:

Item 1-<12A-1>: Additional Taxable Sales Based on Prior Audit Credit Card Ratio – Audit Period - \$635,280 - Disagrees

Negligence Penalty: \$49,234

Taxpayer signed CDTFA-82, *Authorization for Electronic Transmission of Data* when first contacted on May 15, 2019. However, as documented in the notes, letters, and e-mails, taxpayer did not respond to any further contacts.

TAXPAYER'S POSITION**0206.45**

Under this header, auditors should clearly detail the reasons or facts the taxpayer believes supports their position. Comments should not deal in generalities or suppositions, but should be a clear presentation of opposing viewpoints, leaving no doubt as to the basis for disagreement. Each item should be listed separately and the taxpayer's position separately explained for each item.

Example 1 Disagreed:

Item 1-<12A-1>: Difference Between Recorded and Reported Taxable Sales Based on Monthly Worksheets – Audit Period

Taxpayer states z-tapes are recorded on the monthly worksheets and not retained. Taxpayer claims z-tape amounts are overstated, due to voids that were not adjusted.

Item 2-<12A-2>: Additional Taxable Sales Based on Credit Card Ratio Using Z-tapes for the period 9-1-20 to 9-30-20:

Taxpayer disagrees and claims their actual credit card ratio is approximately 90% but does not currently have any records to support this contention because z-tapes or other records supporting sales were not retained during the audit period.

Example 2 Non-Committal:

Taxpayer is non-responsive and has not provided any additional information. Taxpayer also disagreed with the prior-audit credit-card ratio, but taxpayer has not provided any additional information in the appeals process and for that reason, no adjustment is recommended in the Decision dated July 10, 2019.

AUDITOR'S POSITION

Under this header, auditors should clearly detail the reasons or facts they believe support their position. Comments should not deal in generalities or suppositions, but should be a clear presentation of opposing viewpoints, leaving no doubt as to the basis for disagreement or the reason the auditor determined no further adjustments were warranted. Comments should explain the audit method used to support the audit findings, along with any secondary support, and should respond to any items noted under the "Taxpayer's Position" heading. Comments should also refer to the related laws or regulations to support the audit findings, if applicable. Each item should be listed separately and the auditor's position must be separately explained for each item.

Example 1 Disagreed:

Item 1-<12A-1>: Difference Between Recorded and Reported Taxable Sales Based on Monthly Worksheets – Audit Period

The auditor scheduled the amounts from the taxpayer's Monthly Worksheets and compared them to reported taxable sales. The differences were scheduled on an actual basis for the audit period. Information from the Monthly Worksheets show the credit card ratio was over 150%. The auditor determined recorded sales were incomplete and additional sales were determined using a projection, based on the credit card ratio.

The taxpayer did not retain purchase invoices and the auditor was unable to determine any markup. However, the reported average daily sales were under \$500 per day which did not appear reasonable for a fast food restaurant selling Mexican food with 2 registers inside and a drive thru.

Item 2-<12A-2>: Additional Taxable Sales Based on Credit Card Ratio Using Z-tapes for the period 9-1-20 to 9-30-20:

Taxpayer retained current z-tapes for 9-1-20 to 9-30-20 which noted much higher daily sales than amounts on the Monthly Worksheets and noted an approximate credit card ratio of 54.56%. The auditor then performed a preliminary observation test on 10-5-20 in line with Audit Manual Section 0810.30. This one-day observation test resulted in a credit card ratio of 56.57% and was in line with the z-tapes provided and the expected ratio for fast food operations with a drive thru.

Given this, the auditor used the taxpayer's records for 9-1-20 to 9-30-20 to compute and project the credit card ratio to the entire audit period. The auditor noted the average daily sales projected was approximately \$2,176, which was in line with the average daily sales on the z-tapes, projection of average daily sales based on an 8-hour observation test, and type of business operations.

Example 2 Non-Committal:

Item 1-<12A-1>: Additional Taxable Sales Based on Prior-Audit Credit Card Ratio:

The prior audit impeached the recorded sales due to negative markup and missing transactions in the testing of the z-tapes to the related sales receipts. A full-day observation over 3 days was completed during the prior audit. Days were selected based on discussion with the taxpayer and information provided on the CDTFA-805, Observation Fact Test Sheet. The test resulted in a credit card ratio of 75.64% which appeared reasonable for a sit-down, Mexican restaurant with average meal prices ranging from \$10 to \$20. See also the Decision dated July 10, 2019 which supported the prior-audit credit-card ratio.

Given this and the fact that no records were provided, the auditor used the credit-card ratio from the prior audit. The ratio was applied to the 1099K credit card deposits to estimate taxable sales.

Negligence Penalty:

Given the taxpayer continued to report similar amounts as were reported in the prior audit and the auditor noted no steps were taken to correct prior errors, a negligence penalty is recommended, as further explained under the penalty comment.

SUPERVISOR'S COMMENTS

0206.49

Supervisor's comments are required for all disagreed or non-committal audits and must be included for any audits with tax and fee (excluding penalties and interest) liabilities over \$25,000. The audit supervisor will review and approve, if appropriate, the auditor's explanation of the non-concurrence. When appropriate, the audit supervisor will contact the taxpayer for further discussion.

SALES FOR RESALE

0206.50

In this area, auditors should address how the resales were examined. Auditors should include if any deductions were combined for testing, what the test period was, the records provided, or if XYZ letters were used and any errors found. If no examination was warranted, explain why. Auditors should also reference any lead schedules in the system and the AWP.

If resales were verified by alternative methods due to resale certificates not issued or not delivered timely, the comments should explain how they were verified when the taxpayer did not provide XYZ letters (e.g., verification to the system's seller's permit verification, customer's business, volume purchased, etc.). The taxpayer should be informed that timely resale certificates should be obtained to support future sales when alternative methods are used to verify resales.

Example 1:

Recorded sales for resale per the sales journal were reconciled to claimed resales for the audit period. No differences were noted. Recorded sales for resale for December 2021 were tested. December 2021 was selected based on a conversation with the taxpayer who indicated this period accurately represented sales for resale for the audit period. Based on cursory review of the taxpayer's customer list, the auditor accepted the test period as representative. All sales for resale invoices for December 2021 were examined on an actual basis and traced to available resale certificates. The resale certificates were verified as taken in good faith, bearing valid sellers' permit numbers, and signed by purchasers in the business of selling furniture. 20% of December 2021 recorded sales for resale were not supported by resale certificates or valid XYZ responses. The 20% rate of error was applied to claimed resales for the audit period. See schedule <12B> for additional information.

Example 2:

Sales for resale were claimed for the audit period and recorded resales reconciled to reported claimed resales. Sales for resale were tested based on stratified random sampling. Tested transactions were traced to the source document and supported by a Resale Certificate on file or through the system's seller's permit verification. Questioned transactions were noted. These transactions were verified through the XYZ process and for the non-responsive, questioned transactions, taxpayer agreed to include as an error. Percentage of error was calculated based on the total error in the sample base. The percentage of error was projected to the reported deductions.

Example 3:

Sales for resale deductions were combined and tested in a stratified statistical sample. Tested transactions were traced to the source document and supported by exemption documentation. Questioned transactions were noted. These transactions were verified through the XYZ process and for the non-responsive, questioned transactions, the taxpayer agreed to include these as errors. Statistical sample was abandoned due to software flaw that was corrected in January 2017. The taxpayer indicated that in the prior audit they found out that anyone had authorization to change the taxability of an item. As a result, the taxpayer contacted the POS agent to change the programming in their system so that the availability to do that is now senior administrator only. The control was taken away from the lower-level employees as of January 2017. The errors only occurred in 2016 because managers were overriding the taxability of the transaction and not because an item was coded incorrectly. Supporting documentation was provided that validated the taxpayer's statement. The error dollar amount was divided by all 2016 transactions in the sample to establish the % of error for 2016. The auditor applied the % of error to the 2016 population to establish the disallowed amount for the audit. See schedules <12A> through <12A-1e> for details.

MANUFACTURING AND RESEARCH & DEVELOPMENT**0206.55**

Auditors should state if the taxpayer is claiming a deduction for sales of manufacturing, research and development, or electric power generation or production, storage, or distribution equipment, or if the taxpayer is claiming a deduction for purchases of such equipment that they reported as purchases subject to use tax on Line 2.

In this section, auditors should address if the taxpayer meets the three conditions listed below. Auditors should also include comments as to whether exemption certificates were provided, the period tested, if the test was on an actual or sample basis, how the test was completed and if there was an error found. If no error was found or no examination was warranted, there must be a comment made to that effect.

Beginning on July 1, 2014, manufacturers and certain research and developers, and beginning on January 1, 2018, certain electric power generators and distributors, may qualify for a partial exemption of sales and use tax on certain purchases or leases of property used in manufacturing, research and development, or the generation or production, or storage and distribution of electric power. To be eligible for this partial exemption, they must meet all three of these conditions:

1. Be engaged in certain types of business, i.e. be a “qualified person.”
2. Purchase “qualified tangible personal property.”
3. Use that qualified tangible personal property in a qualifying manner.

See RTC section 6377.1 and CDTFA’s Industry Guide for Manufacturing and Research & Development Equipment Exemption for more information.

For items to qualify, they must be depreciated for state income or franchise tax purposes as further explained in Sales and Use Tax Regulation 1525.4(b)(13). For asset purchases where the taxpayer paid the full rate on qualifying assets, auditors can address any unclaimed credits if they are related to use tax on the buyer but should inform the taxpayer to file a claim for refund with the vendor for sales tax. For expensed items (as opposed to capital expenditures), auditors can assess the additional tax if a manufacturing exemption certificate was issued or it is subject to use tax.

Example 1 (Sales of qualified equipment):

The Manufacturing and Research & Development exemption was not properly claimed on the Sales Tax Returns for the audit period but they were properly taxed on the sales invoices. Claimed exempt sales were verified on an actual basis. Transactions were traced to the source document and supported by a partial exemption certificate on file. The credit difference will be allowed in the audit. Please refer to schedule <12C-1>.

Example 2 (Purchases of qualified equipment):

The Manufacturing and Research & Development exemption was not properly claimed in the audit period for the depreciated, fixed assets that were reported on purchases subject to use tax of ex-tax purchases from unregistered out-of-state vendors on the Sales and Use Tax Returns. Credit was allowed for the use tax paid to the vendors, whereby the taxpayer paid the full rate in error, to registered vendors, for depreciated assets that were subject to use tax and were shipped from out of state. Auditor verified the related use tax was not otherwise refunded. Taxpayer manufacturers dog food and is thus a qualified person under NAICS 311111. Auditor verified claimed use tax on depreciated assets on an actual basis. The credit difference will be allowed in the audit. Please refer to schedule <12C-1>.

SALES TO THE U.S. GOVERNMENT**0206.60**

In this section, auditors should address how the sales were verified as valid sales to the U.S. Government, whether by copies of credit card slips or U.S. Government purchase orders. Auditors should also include comments regarding the period tested, if the test was on an actual or sample basis, how the test was done, and if there was an error found. If no error was found or no examination was warranted, there must be a comment made to that effect.

Example:

U.S. Government sales were claimed for the audit period. U.S. Government sales were tested on an actual basis. Tested transactions were traced to the purchase orders. Questioned transactions were listed but it was later verified they were Sales to the United States Government. No errors were noted. Please refer to schedule <12B-1>.

EXCESS TAX REIMBURSEMENT**0206.65**

Auditors should examine excess tax adjustments on the audit transcripts for all errors greater than the threshold amount(s) noted below. If the taxpayer collected excess tax and has paid it to the CDTFA, auditors do not need to take further action in the audit. If the excess tax adjustment is in error, auditors should make the adjustment in the audit and obtain a claim for refund from the taxpayer, if necessary. If auditors note sales tax collected was claimed as a deduction on the return and exceeds the taxes paid (after adjusting for bad debts, returns, or similar items), auditors should include comments explaining how they were handled or why it was determined no error was involved.

See below for the thresholds for when auditors must include comments on excess tax adjustments:

- Small audits - Excess tax greater than \$250 per quarter.
- Large audits – Excess tax greater than one-tenth of a percent (0.001) of the tax reported for each quarter up to a maximum of \$5,000. For tax errors greater than \$5,000 per quarter in a large audit, auditors must include a comment.

In cases where there is a credit difference below the threshold amounts detailed above, auditors should notify the taxpayer that credit differences will not be investigated unless specifically requested by the taxpayer.

In addition to any excess tax not handled on the return, auditors should verify the tax rate that was collected on sales invoices, a point of sale system, or other items. Auditors should address the source of the excess tax; for example, whether customers were overcharged due to inaccurate programming of a point of sale system or if customers were charged tax on exempt transactions. Auditors should also address if the specific customers can be identified so that the excess tax can be refunded or not. If excess taxes are not refunded, auditors should include them in the audit (or if not included because it is immaterial) and then refer the taxpayer to Sales and Use Tax Regulation – Reimbursement for Sales Tax on how to report in the future. See AM 0417.00 under “Treatment of Excess Tax Reimbursement” for more information.

Example 1:

Tax accrued for 1Q-17 was higher than the tax charged to customers for that quarter. The State tax rate dropped by ¼% but taxpayer continued to collect tax at the higher rate and did not correct the tax rate in the Point of Sale system until 4-1-17. See schedule <12C> for details.

Example 2:

The excess tax dollar amount of \$628 in the 1Q17 is not true excess tax collected. The auditor verified the taxpayer collected the proper rate and excess tax noted on the transcript was due to an error when preparing the sales tax return. The taxpayer overpaid sales tax and the dollar amount should be applied to the audit liability.

LOCAL TAX

0206.70

Local tax header is currently not available on the Summary working paper. Auditors will use “Miscellaneous” and start the comment with notation “Local Tax.” Local tax comments should be included when the taxpayer has multiple locations, moved locations, or is a special seller (e.g., contractor or mobile operator) to explain how local tax was reported or if other local tax adjustments are needed.

In this section, auditors should address if local tax was properly collected and allocated and if there was a need for any reallocation and for what period(s). Date of knowledge (DOK) should also be noted. Reference any pertinent schedule in AWP for reallocation.

Example 1:

Local tax was reallocated for the periods 4Q-18, 1Q-19, and 2Q-19 based on the date of knowledge of 8/15/19. See working paper worksheet <12D> and attached CDTFA-414-L.

For most businesses, local tax is allocated to the place of business. However, special sellers, such as construction contracts, are allocated countywide for materials and fixtures installed. For additional guidance, auditors can refer to “Local Tax Guidelines” in Exhibit 1 of Chapter 5 of the Compliance Policy and Procedures Manual. See below for an example comment for a construction contractor:

Example 2:

Taxpayer is a construction contractor also making over-the-counter sales (i.e. not installed). Taxpayer reported taxable measure to their place of business. Local tax was reallocated for the periods 4Q-18, 1Q-19, and 2Q-19 based on the date of knowledge of 8/15/19. See schedule <12D> and attached CDTFA-414-L.

Local tax was allocated or reallocated countywide for materials and fixtures installed and to the place of business for over the counter sales, fixed assets, and ex-tax supplies.

DISTRICT TAX**0206.75**

In this section, auditors should address if district tax was properly reported and paid and if there was a need for any redistribution and for what period(s). Date of knowledge (DOK) should also be noted. Reference any pertinent schedule in AWP for redistribution. The examples below may be included under “District Tax” or included as a part of “Nexus” comments.

Example 1:

Taxpayer did not report any taxable transactions on Schedule A. Auditor, however, noted certain sales were transacted in taxing jurisdictions where district tax is imposed. See schedule <12A> for details.

Example 2:

District taxes are reported to the taxpayer’s locations when items are delivered at the taxpayer’s location or distributed to any applicable districts based on where items are shipped. Given no errors noted, based on where district taxes were reported, audited taxable measure was allocated using the system’s pre-pop function.

Example 3:

District taxes are reported to the taxpayer’s job sites when items are delivered to the taxpayer’s job sites or to any applicable districts based on where items are shipped. Audited taxable measure was calculated and distributed on an actual basis to the taxpayer’s job sites because all additional amounts were for items delivered to the taxpayer’s job sites.

LABOR**0206.80**

In this section, auditors should address how labor sales were examined, the period that was examined, records provided, if they were examined on an actual or sample basis, and what the results were. Any errors noted should be explained and if an examination was not warranted, a comment should be made to that effect.

Comments should explain how the auditor determined labor was exempt repair or installation labor versus fabrication labor or taxable services related to a sale.

Example 1:

Labor sales were relatively few in number, so the auditor examined them on an actual basis. Disallowed labor sales consisted of fabrication labor claimed as repair labor and total repair invoices, including materials and tax reimbursement, claimed as repair labor. See <12B> for detail of differences and additional comments. No other errors in claimed labor sales were noted.

Example 2:

Repair labor charges were examined on an actual basis. The auditor noted some invoices were billed lump sum and parts sales were not properly segregated as required per Sales and Use Tax Regulation 1546 when the retail selling price of the parts is over 10%. Since the repair work billed as lump sum was similar to the repair work where parts were segregated, the auditor used the segregated ones to determine that 25% of the charge was related to taxable sales of parts. This was then applied to the invoices billed as lump sum in order to account for the unreported taxable parts sales.

BANKRUPTCY

0206.85

In bankruptcy cases, auditors are required to include the following comments:

- Type of Bankruptcy filed, such as Chapters 7, 11 and 13.
- Petition date (the date the bankruptcy was filed).
- Bar date (or the last day to file a claim), Case Number, and Court of Jurisdiction.

Note: If a taxpayer operates a business after filing a bankruptcy petition, two audit cases may be required, one for the period prior to bankruptcy petition date and one for the period when the business is operated by the trustee under the jurisdiction of the court. Auditors should check with their supervisor to determine the effect of the materiality, and thus the need, to determine if a second audit case is necessary. When both the pre-petition and post-petition filing periods have material audited taxable measure to be billed, separate audit cases should be created for each of those periods.

EXPLANATION OF TAX CHANGE

0206.90

This header is required on all Field Billing Orders (FBO) to explain what was assessed or refunded. This should explain the items included, how they were tested, and how they were handled. This helps to clarify that a full audit was not done and that only the items noted were addressed.

For FBOs, the system has only one tab, titled “Verification Comments”, and does not have “Required” and “Other” tabs as noted on audits. For FBOs, auditors must provide the following verification comments, when applicable as further explained in AM 0213.01:

- (a) Type of Business Organization
- (b) Explanation of Tax Change
- (c) Discussion with Taxpayer
- (d) Overpayment
- (e) Credit Interest
- (f) Penalty

REASON FOR REAUDIT

0206.95

In the Summary-Working Papers, on the Verification tab in the Other comments, the original audit and FBO comments will remain **unchanged** in the system. However, reaudits and revised FBOs may include up to six different comments under the dropdown heading “**Reason for Reaudit**” in the system. These comments include:

- Reason for Reaudit
- Reference to Authority Authorizing Reaudit
- Reaudit Findings and Related Comments
- Taxpayer’s Position (non-concurred or non-committal only)
- Auditor’s Position (non-concurred or non-committal only)
- Waiver of Appeals Conference

Do not delete or modify the original Verification comments. Rather, add **all comments**, under the dropdown “**Reason for Reaudit**” so all details and history are maintained. Auditors will include sub-headers for each type.

The following **sub-headings**, manually entered by auditors, are required under the drop-down option “**Reason for Reaudit**” in the following order:

- R# (R1, R2, R3, etc.) Reason for Reaudit
- Reference to Authority Authorizing Reaudit
- Reaudit Findings and Related Comments Taxpayer’s Position
- Taxpayer’s Position (non-concurred or non-committal only, as appropriate)
- Auditor’s Position (non-concurred or non-committal only, as appropriate)
- Waiver of Appeals Conference (as appropriate)

Reason for Reaudit

This comment identifies the reason for the reaudit. Generally, the taxpayer must request a redetermination of a previously issued Notice of Determination before a reaudit can be ordered. Examples of this comment include:

Example 1:

Taxpayer filed a timely petition for redetermination of liability determined (date of Notice of Determination) as recommended by audit report letter dated (date).

Example 2:

Taxpayer filed a claim for refund of liability determined (date of Notice of Determination) as recommended by audit dated (date).

Example 3:

Taxpayer filed a late protest objecting to the liability determined (date of Notice of Determination) as recommended by audit report letter dated (date).

The audit date will be the date on the Final Audit Results Letter.

Reference to Authority Authorizing Reaudit

This comment identifies the authority authorizing the adjustment(s) to be made in the reaudit.

An adjustment may be ordered as a result of the discussion. Examples of this comment include:

Example 1:

Taxpayer discussed the determination with (name and title of Appeals Bureau representative) who ordered changes per Decision dated (date).

Example 2:

Taxpayer discussed the determination with (name and title of office representative) who ordered changes per CDTFA-836A, *Report of Discussion of Audit Findings* dated (date).

Example 3:

Taxpayer discussed the determination with (name and title of office representative) who ordered changes per Audit Disagreement Case dated (date).

Reaudit Findings and Related Comments

The auditor's findings, upon investigation of the taxpayer's contentions, should be briefly stated under this heading.

When more than one audit adjustment is found to be in order, the detailed comments explaining the reaudit adjustments should be shown on a Reconciliation and Explanation of Reaudit Adjustments Schedule. In such instances, a statement similar to the following will be made under this heading:

“Reaudit adjustments with respect to items 1-<12A>, 2-<12B>, and 3-<12C> above are explained on schedule R(#)-414-A2.”

If changes are recommended that are not contained in the original CDTFA-836-A-*Decision or Report of Discussion of Audit Findings*, they must be fully explained in this section. Care should be taken to obtain either a Supplemental Decision or a Supplemental Report of Discussion of Audit Findings Report from the appropriate authority documenting the adjustments allowed.

In addition, appropriate comments should be made by auditors under this heading regarding those items questioned by the taxpayer but not adjusted in the reaudit.

Below are examples with all four mandatory comments that would be under the drop-down in the system under “Reason for Reaudit”:

Example 1:

Reason for Reaudit: Claim for refund dated 10/4/19 was not received timely to cover 1Q15 through 2Q16.

Reference to Authority Authorizing Reaudit: ADRS requested the change due to the claim for refund dated, October 4, 2019, not having been taken timely to cover 1Q15 through 2Q16.

Reaudit Findings and Related Comments: Disallowed 1Q15 through 2Q16 due to claim for refund dated, October 4, 2019, that was not received timely.

Taxpayer's Position: Taxpayer did not have any contentions. However, taxpayer was later informed claim for refund was not timely for 1Q15 and 2Q16 and agreed with the changes later recommended by ADRS.

Reaudit adjustments are shown on a Reconciliation and Explanation of Reaudit Adjustments Schedule.

Example 2:

Reason for Reaudit: The taxpayer filed a timely petition for redetermination of the liability determined February 19, 2019 as recommended by the February 15, 2019 Audit Report Letter.

Reference to Authority Authorizing Reaudit: Taxpayer discussed the determination with John Smith, Business Taxes Specialist II, who ordered changes per Decision dated June 30, 2020.

Reaudit Findings and Related Comments:

1. Auditor adjusted the taxable dollar amount for non-taxable related charges.
2. Auditor provided breakdown of the sales tax rate for Santa Barbara and Montecito contracts to taxpayer.
3. A sale is deemed to occur at the time and place which the retailer completes his performance with reference to the physical delivery of the property, unless the parties to the sale explicitly agree that title is to pass at a prior time pursuant to Regulation 1628(b)(3)(D).

Taxpayer's Position: The taxpayer disagreed with the following areas:

1. The taxable dollar amounts for the Santa Barbara, Montecito, and Oxnard contracts.
2. The sales tax rate for Santa Barbara and Montecito contracts.
3. The title clause on Santa Paula, Oxnard, and Los Angeles contracts.

No penalty applied same as original audit findings.

Example 3 with Notation Agreed to Reaudit:

Reason for Reaudit: The taxpayer filed a timely petition for redetermination of the liability determined February 19, 2019 as recommended by the February 15, 2019 Audit Report Letter.

Reference to Authority Authorizing Reaudit: Taxpayer discussed the determination with John Smith, Business Taxes Specialist II, who ordered changes per Decision dated June 30, 2020.

Reaudit Findings and Related Comments: Reaudit adjustments are explained on schedule R1-414-A2. The only item is the credit card projection.

Taxpayer's Position: See Decision for taxpayer's position.

As further explained on schedule R1-414-A2 and the Decision, credit card ratio was adjusted to 61.48% based on point of sale reports later provided.

Taxpayer is now in agreement with the Reaudit findings and no penalty applied.

Example 4 with Notation Disagreed and Related Items (add new "Discussion with Taxpayer", "Taxpayer's Position", and "Auditor's Position" comments if the taxpayer disagrees with Reaudit results):

Reason for Reaudit: The taxpayer filed a timely petition for redetermination of the liability determined February 19, 2019 as recommended by the February 15, 2019 Audit Report Letter.

Reference to Authority Authorizing Reaudit: Taxpayer discussed the determination with John Smith, Business Taxes Specialist II, who ordered changes per Decision dated June 30, 2020.

Reaudit Findings and Related Comments: Reaudit adjustments are explained on schedule R1-414-A2. Only item is the credit card projection.

As further explained on schedule R1-414-A2 and the Decision, credit card ratio was adjusted to 61.48% based on point of sale reports later provided.

Discussion with Taxpayer: Results of discussion of audit findings with Jennifer Green, President on November 16, 2020 are summarized as follows:

Item 1-<12A-1>: Additional Taxable Sales Based on Credit Card Projection – Audit Period - \$185,982 – Disagrees

No penalty applied as explained in the original Audit Report Letter.

Taxpayer’s Position: Taxpayer stated there are additional voids and returns that were not properly adjusted on the point of sale reports.

Auditor’s Position: Download provided for the point of sale reports noted around 10% voids and returns which appears more than reasonable and no further adjustments warranted as further explained in the Decision dated June 30, 2020.

Taxpayer’s Position

This comment identifies the item(s) and reason(s) why the taxpayer does not agree with the Notice of Determination for the reaudit. The taxpayer’s contentions are generally the issues discussed before the Appeals Bureau or field office representative. Examples of this comment include:

Example 1:

Item 1-<12A-1> — Taxpayer obtained additional XYZ responses from customers and is of the opinion that the amount of disallowed claimed sales for resale should be reduced.

Example 2:

Penalty — The taxpayer is of the opinion that the negligence penalty for incomplete books and records does not apply. The taxpayer claims the records are complete and can be relied upon for sales and use tax purposes.

A reaudit may be ordered as a result of a Decision of the Appeals Bureau. If the Decision identifies the taxpayer’s contentions, it is not necessary to restate them. However, the Taxpayer’s Position comment is still required. If this situation exists, the comment should read:

“See copy of Decision for Taxpayer’s Position.”

Auditor’s Position

The auditor must make a comment under “Auditor’s Position” when the taxpayer does not agree with the reaudit or revised FBO recommendation. If the taxpayer disagrees to item #3-<12C> even after the reaudit or revised FBO adjustment, the auditor will add their position in the Auditor’s Position section of the verification comments as follows:

“Auditor’s Position: Item #3-<12C>

For reaudit, Mr. Smith sent XYZ questionnaires. Adjustments were made per XYZ responses. No adjustments were given to non-replies. The non-replies were for customers who do not appear to be in the line of business that sells items purchased from the taxpayer.”

Waiver of Appeals Conference

Upon completion, the reaudit or revised FBO should be reviewed with the taxpayer in the same manner as would be followed upon completion of an original audit or FBO. If the taxpayer is still in disagreement with any portion of the reaudit or revised FBO results, but does not want to pursue an appeals conference, auditors must include a statement indicating that fact in the "Waiver of Appeals Conference."

When the taxpayer agrees with the reaudit or revised FBO findings and had previously requested an appeals conference as part of a timely petition for redetermination, administrative protest, or claim for refund, auditors **must comment** on whether an appeals conference is still desired. Auditors will comment as follows under the Waiver of Appeals Conference comment:

"Mr. Smith agrees with the reaudit adjustments and no longer wishes to pursue the appeals conference that was previously requested."

See section 0706.27 for more details.

AUDIT CASE NOTES (CRM NOTES)

0207.00

OVERVIEW

0207.01

Audit case notes, located in the CRM tab, Notes sub-tab, creates a record of contacts, audit team members' actions, taxpayer or taxpayer representative (collectively referred to as "taxpayer") responses, and significant events that occur during the course of an assignment. Completion of audit case notes in CRM Notes are **mandatory** for all audit assignments, including reaudits, FBOs and claims for refund. They should be kept current and professionally written as they will become a permanent part of all working papers and are subject to disclosure under the Information Practices Act. Because the date of the CRM Notes defaults to the current date and cannot be changed, audit case notes **must** be entered on a regular basis, (at least weekly) and not all at one time, at the completion of the audit.

A record of contacts, requests, and audit activities is essential to develop a history of the audit team actions and taxpayer responses (that is, a chronology). Audit case notes should include all requests made to a taxpayer, the reason for such requests, and the taxpayer's response to the request. All testing procedures, audit milestones, and significant events should be recorded. Audit case notes should document any taxpayer delays to the audit process and any issues that may arise between CDTFA and the taxpayer. The CDTFA should be prepared to justify the auditor's and audit supervisor's actions in the appeals process. In addition, complete audit case notes should provide the necessary documentary evidence to support the reasonableness of the actions taken. For example, when a taxpayer is not complying with requests for records, and the auditor does not document the activity as it happens, an accurate picture of the situation is not recorded. That is, if five verbal requests for records are made, but they are all entered in CRM Notes on the same day, not only does that not reflect the true history of the auditor's actions, but it gives the taxpayer the right to argue they were not given enough time or notice.

PREPARATION OF AUDIT CASE NOTES

0207.03

Generally, all auditors, Computer Audit Specialists, audit supervisors, and Audit Principals assigned to the case must make entries on the audit case notes. The following items must be recorded:

Contacts

Any entry that cites a contact must include the person's name and contact information such as address, phone number, or email address, if available. In addition to the items below, any other relevant contacts or events should also be documented:

- Phone contacts – Include the contact person's name, that person's title or position in relation to the taxpayer, and what was discussed and/or agreed upon. When indicating the person contacted, the term "taxpayer," "TP," or his/her title alone should not be used.
- Appointments made – Record the date, location, time, and purpose of the appointment.
- Appointments cancelled or rescheduled – Document which person requested the change and the reason for the request and for what date and time the appointment has been rescheduled.
- Correspondence - Record all letters, memorandums, publications, etc. given to and received from the taxpayer and the subject matter of the correspondence. Letters and memos should not be copied directly into the audit case notes. Letters and memos generated in the system automatically create entries when they are created; however, a Note should still be made to document the action in CRM Notes to document the history and to show it in chronological order.

- Emails – A summary of each email contact should be recorded. Emails containing audit documentation or discussions/agreements relevant to the audit should be saved and included with the audit as an attachment under CRM Attachments. Emails should not be copied directly into the audit case notes.
- Request for Computer Audit Specialist (CAS) – The date and name of the CAS first contacted by the auditor and the type of assistance requested should be documented. A comment is added to CRM Notes when creating “CAS Consultation” Work Item in the audit case.

Record and Document Requests

- Record requests – Record all requests made of the taxpayer including, but not limited to, those for partnership agreements, corporate minutes, waivers, XYZ letters, or other supporting documents, and the deadlines given.
- Information Document Request (IDR) – Record all IDRs issued to the taxpayer, including the IDR number, due date, audit supervisor approval, and any follow-up by the auditor.
- CDTFA-699, *Audit Findings Presentation Sheets (AFPS)* and CDTFA-699A, *AFPS Master Log* - The date the AFPS was presented to the taxpayer, a brief description of what was discussed, the due date for the taxpayer to respond, and any follow-up by the auditor. The CDTFA-699(AFPS) and the CDTFA-699A (AFPS Master Log), can both be found on myCDTFA. These should be used for larger audits with multiple errors and should be presented to the taxpayer during status conferences. Specifically, these should be used to address discrete sections of the audit or errors that are addressed in the audit.

In the system, the AFPS tab is located in the Lead Schedule, Summary tab, AFPS sub-tab. The system requires one of the three radio buttons to be selected per lead schedule added. These buttons are “Non-Committal,” “Agree with Audit Findings,” and “Disagree with Audit Findings.” Auditors must select one of these options in order to “Submit” the Lead Schedule. There are also areas on the AFPS in the system, including “Description of Findings,” “Schedule Reference”, and “Estimated Taxable Measure,” all of which are auto-filled by the system. In addition, there are blocks, such as “Summary of Findings,” “Law/Regulation Section,” and “Auditor’s Position,” which can be filled in by auditors, when applicable.

Audit Plan, Activity, and Testing Procedures

- General Audit Plan - Document the date it was discussed with and approved by the audit supervisor (if applicable), the date it was discussed with, signed by, and provided to the taxpayer, and any changes to the plan over the course of the audit.
- Audit Milestones - Record milestones as they occur. For example, the completion of the verification of a claimed deduction. In audits involving multiple auditors, each auditor should document their respective areas of responsibility.
- Audit Status Meetings – Date held, summary of discussion, and any future action required.
- Testing Procedures – Record the date the CDTFA-472, Audit Sampling Plan, was discussed with the taxpayer, agreed upon testing procedures, and the contact person agreeing to the procedures. Include any changes to the Sampling Plan during the course of the audit.

PREPARING AND COMPLETING AUDITS

PREPARATION OF AUDIT CASE NOTES

(CONT.2) 0207.03

- Audit Working Papers (AWP) - Record which working papers were provided and the dates furnished to the taxpayer and whether they were printed and given to the taxpayer, mailed, sent via email electronically, or delivered through the Online Services portal.
- Prior Audit Percentage of Error (PAPE) – Record the date PAPE was discussed with the taxpayer (if eligible), the date approval was requested, and the date of approval by the Audit Principal. If not eligible for PAPE, auditors should enter a note to that effect.
- Managed Audit Program (MAP) – Record the date the participation agreement was provided to and signed by the taxpayer, the agreed upon procedures and deadlines, dates of review, etc. If not eligible for MAP, auditors should enter a note to that effect.

Not all audits are eligible for PAPE and MAP. When a case is not eligible for PAPE or MAP, auditors **must** make a comment to that effect.

Waiver of Limitations – (AM section 0216.00)

The following should be documented:

- The reason for the waiver request.
- The date the waiver was provided to and signed by the taxpayer.
- The date the auditor received the completed and signed waiver form. The related e-mail, fax, or similar item must be attached in the system to document the timely receipt of the waiver.
- The date the executed waiver was provided to the office designee (usually the audit supervisor).

Computer Audit Specialist (CAS) Responsibility

- Pre-Audit Conference – Record the date and the procedures agreed to by the taxpayer (provide the name with whom discussed) and the auditor's name.
- Data Requests – Record the date requested, to whom the request was made, the format requested, the due date of the data, and who made the request.
- Data Processing and Sampling Characteristics – Record the date(s) the data was validated and reconciled and the date sampling characteristics were discussed with the taxpayer.
- Documents and Schedules – Record the date(s) the sampling data was provided to the auditor.

Supervisor Responsibility

The audit supervisor must regularly review the audit case notes to ensure they meet the guidelines noted in this section. The audit supervisor should document the following on the audit case notes:

- Taxpayer Contacts - Correspondence, phone contacts, and emails with the taxpayer in accordance with the guidelines in this section.
- Auditor Support – Guidance provided to the auditor during the audit process.
- Visits to the Taxpayer's Location – Record the date, the purpose of the visit, and what was accomplished.

- Audit Review – Date the audit was reviewed and staged to “Audit Review” via comment added when staging or, if warranted, the reason the audit was returned to the auditor for correction/clarification.
- Non-concurred Audits – Date of the discussion with the taxpayer and the date the “Results of Discussion with Taxpayer” were documented in the audit Notes.

Audit Principal Responsibility

- Taxpayer Contacts - Correspondence, phone contacts, and emails with the taxpayer in accordance with the guidelines above.
- Aged Audits – Date of review and any guidance provided.
- 10-Day Discussions – Date of discussion with the taxpayer and the results. Also, any correspondence and reports generated from the discussion should be attached in the system, including, but not limited to the CDTFA-836A.

NO OPINION WARRANTED (NOW)

0208.00

The purpose of the No Opinion Warranted (NOW) procedure is to allow auditors to **immediately** end their review without completing any additional work papers or additional forms when their review of records discloses no liability or credit. Auditors can quickly and easily finish the assignment and submit their findings to their supervisor for approval. Only supervisory review is necessary; there is no required review by the office reviewer for NOWs. All reviews that disclose no liability or credit will result in a NOW, **regardless** of the hours spent.

BENEFITS TO THE NOW PROCEDURE

0208.03

Below are the key benefits of the NOW procedure:

- Eliminates unnecessary write-up when no liability (or credit) is disclosed.
- Reduces the number of steps to process an unproductive audit; (i.e., no field office review and no review by Audit Determination and Refund Section (ADRS)).
- Encourages discussion between auditors and their supervisors in both planning the audit and reviewing the recommendation.
- Promotes consistency between offices.

NOW PROCEDURES OUTSIDE OF THE SYSTEM

0208.05

As soon as the auditor's review discloses there is no liability or credit due and no further review is warranted, auditors must:

- Stop their review.
- Save any work papers and supporting documents already prepared/obtained during the review that justifies the NOW recommendation; however, do not start additional work papers. Submitted work papers do not need to be hyperlinked. (Audit supervisors may require additional work papers or information for training purposes only).
- Hold an exit conference with the taxpayer and provide any completed work papers, if applicable, or if requested by the taxpayer. However, work papers are generally not required to be provided to the taxpayer for NOW recommendations. Auditors should always be aware that all documents need to be provided in response to an Information Practices Act request.

Auditors will verify the following and advise their supervisor of any issues discovered for:

- Claims for refund.
- Tax errors.
- Additional tax or excess tax adjustments.
- Unapplied payments.
- Local tax misallocations.

Note: Audits with “**net zero**” liability (audits with material offsetting overpayments and underpayments) should be submitted and processed as tax change audits. This is especially important when there are credits and debits in different periods because periods may expire due to statute and the eligible audit period would no longer be a net zero liability. By processing as an audit, all periods are billed and offset.

NOW PROCEDURES INSIDE OF THE SYSTEM**0208.10**

NOWs in the system will start in the same manner as a normal audit. The following steps are required by auditors and audit supervisors:

Auditor:

1. Stage the audit to Perform Audit.
2. Conduct preliminary testing and complete a review of records to the level expected for a NOW as outlined in section 0208.05 above.
3. Discuss with your supervisor the NOW recommendation. If approved, continue with the NOW report.
4. Hold an exit conference with the taxpayer to discuss the NOW recommendation.
5. Make a note in CRM Notes explaining the reason(s) why the audit case resulted in a NOW (verification comments are **not** required for NOWs).
6. Attach all subsidiary schedules, supporting documents, and forms in the system, if applicable.
7. Enter all necessary information on the Attributes tab.
8. Email and add an "Audit Case Assistance" Work Item (located in the Audit case under the Task tab) or send a bookmark (office preference) to your supervisor, notifying them their review is requested.

Audit Supervisor:

1. Go to the Audit case in the system.
2. Review the Audit case, CRM Notes, and any other relevant information.
3. Move the audit case to the stage "Completed-NOW" if you agree with the NOW recommendation or send the audit case back to the auditor for additional testing or clarification.

NOTE: International Fuel Tax Agreement audits with zero liability are processed as "no change" audits.

4. Send the CDTFA-79-NOW letter to the taxpayer.

DUAL DETERMINATIONS**0209.00**

This section provides guidance on the process for team members to facilitate a dual determination and billing as the result of an audit. Dual determinations may be issued in situations where it has been determined that someone, other than the primary taxpayer, may be liable for tax, interest and penalties owed to the State of California. Some examples include successor liability (RTC section 6814), predecessor liability (RTC section 6071.1), suspended corporation (RTC section 23301 and Regulation 1702.6), responsible person liability (RTC section 6829) or where precise ownership of the business is unknown (Questionable Ownership).

A person against whom a dual determination is issued is referred to as a “dualee.” A billing may be issued against a dualee for some or all of the unpaid liabilities of the primary taxpayer for any periods for which the applicable statute of limitations has not expired. To ensure the proper and timely issuance of a dual billing, auditors must work with the compliance team and adhere to the following procedures.

Dual determinations may be based on the full amount of the liability or a portion thereof, depending on the specific circumstances. In addition, dual determinations can be made on self-assessed or CDTFA-assessed liabilities.

Once auditors determine that a dual determination may be necessary, the audit supervisor will notify the compliance team via an Audit Case Assistance Work Item. This Work Item is available from the Audit springboard, Task tab, Work Items sub-tab. The audit supervisor **must** include the following information in the Work Item:

Source: Audit

Owner: Compliance Principal, or designee

Subscriber: Auditor

Work Add Note:

Type of dual determination to be issued (successor, predecessor, suspended corporation, responsible person liability, or questionable ownership). If the dualee is registered in the system, provide the dualee’s name and the system-generated TIN (Customer springboard, Registration tab, Summary sub-tab).

If the dualee is not registered, inform the compliance team to register and link the dualee to the account being audited and provide the dualee’s name, address and other identification information obtained during the course of the audit.

The Compliance Principal, or designee, will assign the Work Item to a compliance team member to potentially register the dualee and create the Dual/Secondary Billing case, once the audit is complete. The team member must establish whether the Dual/Secondary Billing case will be billed **before** the Customer is linked with any social security information. This will prevent the system from retrieving any FTI information that is not authorized for business purposes. If there is any doubt as to whether or not the Dual/Secondary Billing case will be billed, the Customer should **not** be linked with any social security information.

The compliance team member will draft the dual memorandum, with both team members (compliance and audit) ensuring the memorandum is complete and accurate. It is imperative, **during the audit**, that the auditor start collecting the information necessary to support a dual billing. These items can be attached in the Audit case under CRM Attachments.

Below is a list of some examples of important documents that support a dual billing. For a more detailed list of relevant information to support a dual billing, please refer to the Compliance Policy and Procedure Manual (CPPM) sections 732.000-732.140, 734.000-734.015, and 764.000-764.200 or discuss your specific case with the compliance team member assigned to the case.

Examples of important documents to support a dual billing:

- Copies of sales receipts showing that sales tax is/was collected.
- Copies of bank statements.
- Copies of books, records, and ledgers.
- Copies of voluntarily submitted IRS and FTB income tax returns.
- Copies of signed business checks.
- Copies of menus showing that sales tax is/was collected.
- Copies of merchant statements.
- If the business was sold or purchased, a copy of the bill of sale and escrow documents, if applicable.
- Supplier information including registration documents.
- Landlord information.
- For questionable ownership, conflicting documents showing various items under the other possible owner's name such as records listed above, 1099K information, or other items.

For responsible person liability dual determinations (RTC section 6829), the compliance team may have to perform further investigation to complete and prepare the dual memorandum. If the business is already closed-out, auditors must inform the compliance team once the audit is assigned. If necessary, to avoid expiration of the statute, the audit billing may need to be expedited (to Posted and Billed stage). For all other audits with duals, auditors must inform the compliance team member once the audit is complete (Posted and Billed stage) so the compliance team may create and complete the Dual/Secondary Billing case and a dual determination billing can be issued.

For detailed information on the most common types of dual determinations, refer to CPPM, Chapter 7, Collections.

Successor Liability, CPPM sections 732.000-732.140

Predecessor Liability, CPPM sections 734.000-734.015

Suspended Corporation, CPPM sections 764.060-764.074

Responsible Person, CPPM sections 764.080-764.180

Questionable Ownership, CPPM sections 764.030

Auditors need to maintain contact with the owner of the Dual/Secondary Billing case in compliance to ensure a dual determination billing is not issued **prior** to the completion (Posted & Billed) of the audit.

EXIT CONFERENCE**0210.00****DISCUSSION OF AUDIT RESULTS****0210.01**

After completion of the audit, auditors will arrange an exit conference with the taxpayer and/or the taxpayer's representative. It is strongly recommended the auditor's field supervisor be present at every exit conference where the audit recommendation includes a fraud penalty, a tax liability in excess of \$25,000 or when it is likely that the taxpayer or representative will not agree with the audit findings. With respect to the field supervisors located in the out-of-state offices, in lieu of making a special trip, they should discuss the audit recommendations with the taxpayer by telephone or video conference and document the results of that discussion.

When a taxpayer's representative is involved during the audit process and is representing the taxpayer at the exit conference, auditors should encourage the taxpayer to also attend the exit conference, whether or not an adjustment is necessary. This allows the taxpayer the opportunity to review the audit working papers and raise any questions about the audit at that time. It is essential that auditors provide the taxpayer with a full explanation for all recommended differences, even though the taxpayer may have agreed to certain differences at an earlier time. Auditors should also fully discuss any penalty recommendations with the taxpayer at the exit conference. By making the taxpayer aware of all differences at the time of the exit conference, it is hoped that the number of concurred audits that are subsequently petitioned will diminish.

The name, title, and telephone number of the person with whom the discussion was held and the location of the discussion (if by phone or video conference, specifically state that) must be entered in the audit case notes in CRM Notes. All AWP, publications, Audit Results Letters, other letters, etc. given to the taxpayer or representative must also be entered in CRM Notes.

In special circumstances, such as receiverships, bankruptcies, assignment or probate cases, auditors should discuss the results with the receiver, trustee, assignee, administrator, executor, etc. The name, title, and telephone number of the person with whom the discussion was held and the location of the discussion (if by phone or video conference, specifically state that) must be entered in the audit case notes in CRM Notes.

PREPAYMENT OF AUDIT LIABILITY**0210.03**

As part of the routine audit discussion, auditors should inform the taxpayer of the option to pay the audit liability, in part or in full, prior to the issuance of the Notice of Determination, regardless of whether the taxpayer agrees or disagrees with the audit findings. It is important that the taxpayer understands that the Notice of Determination is the official billing notice and that a prepayment of the audit liability is an advance payment on an audit not yet billed. Additionally, auditors should inform the taxpayer regarding the statute of limitations on the filing of a claim for refund.

Since the purpose of an advance payment is to avoid additional interest charges, the taxpayer should be given accurate information regarding the normal time lapse between completion of the audit and the issuance of the Notice of Determination and the amount of additional interest that will accrue during that period. The taxpayer should also be advised that, when payment is mailed, interest is computed through the last day of the month in which the payment is postmarked.

Auditors should caution the taxpayer that the tax liability, as of the exit conference, is the auditor's proposed recommendation for determination and should not be relied upon as representing the actual billing. In addition, auditors should inform the taxpayer of the review process and the possibility that the results may increase or decrease. If the results change after the exit conference, auditors should explain any differences, regardless of materiality, between the auditor's initial recommendation and the amount to be billed.

Auditors should **never** accept a payment directly from the taxpayer. Advance payments may be made online or sent to the local office or Headquarters using Audit Payment Information Forms CDTFA-1 (available on the CDTFA website) or by use of an audit payment voucher which is found at the bottom of the first page of the Preliminary Audit Results Letter and the Final Audit Results Letter. Payments sent to Headquarters should be sent to the following address:

California Department of Tax and Fee Administration
P.O. Box 942879
Sacramento, CA 94279-0001

It is important that taxpayers do not include advance payments with their regular returns or prepayments.

Auditors should advise the taxpayer that all payments should be accompanied by an appropriate explanation of the reason for the payment. The explanation should include the taxpayer's account number, the period covered by the audit, and a statement that the payment is for an audit deficiency not yet billed.

Auditors should ensure that any credits, that are to be applied to the liability, are completed prior to submitting the audit to prevent interest issues arising later. See also AM 0211.23 for additional guidance on handling unapplied sales tax prepayments or credits on the account.

FURNISHING COPIES OF AUDIT WORKING PAPERS (AWP)

0210.05

During the discussion, auditors must provide to the taxpayer or the taxpayer's representative a copy of all AWP. Taxpayers should be provided a digital copy of the final AWP unless the taxpayer specifically requests a paper copy. If the taxpayer has access to the Online Services portal, auditors should send a copy of the AWP via the portal so there is a record of the taxpayers' receipt of the AWP. When providing a copy of the digital AWP, auditors must redact or remove files containing confidential information such as Federal Tax Information or CDTFA-1164s that have not been redacted.

Instructions on how to send a message to a taxpayer using the portal can be found by searching our intranet website using "How to send a message to a customer through CROS" as your search.

The AWP must include all schedules and documentation containing the facts, information, and computations upon which any additional liability, refund, or "no change" to reported liability is based. The taxpayer's copy of the AWP includes CDTFA-495, *Index To Audit Working Papers*, and all schedules that follow, including the Preliminary Audit Results Letter.

With respect to audit assignments where an evasion penalty is recommended, after the evasion penalty is approved by Assistant Deputy Director, Audit, Field Operations Division, for sales and use tax cases or the Deputy Director, Business Tax and Fee Division for special taxes and fees cases, and returned to the office, the taxpayer or the taxpayer's representative will be provided with a copy of the memorandum requesting that an evasion penalty will be imposed (see AM section 0509.75).

If a copy of the field audit report and determination is to be mailed to the representative, the representative must be a Customer in the system. Auditors should search the system to locate the representative and their Customer number. If the representative is not yet a Customer in the system, auditors should encourage them to create a Customer for themselves in the system using Online Services on the public website.

If they need assistance with Online Services, auditors can assist them using View Support ID or have a compliance team member assist them. Auditors must then request a compliance team member link the representative's Customer to the taxpayer's account. This will allow the reviewer to send the NOD to both the taxpayer and the linked representative.

In the case of a No Opinion Warranted result (NOW), (see section 0201.11) the taxpayer should be provided a copy of CDTFA-79-NOW, *Letter to Taxpayer When No Opinion Warranted*, together with copies of all schedules and comments (if any) that will become part of the audit file. If the decision to complete the case as a NOW is done prior to any schedules having been created, additional schedules should not be created for the sole reason of providing something to the taxpayer.

Documents that are not for release under the Information Practices Act or the Public Records Act should be excluded from the taxpayer's copy of the AWP. These documents include memos from the Legal Division marked "Attorney-Client Privilege," Confidential Operations Memos, unredacted CDTFA-1164s, any documents containing FTI, and any annotated letters (unless confidential data is redacted).

If, at the time of the discussion, the AWP are not complete, auditors may provide the taxpayer all schedules used in the discussion, regarding an audit, FBO, reaudit or revised FBO. Once the AWP are completed, auditors must provide the taxpayer and the taxpayer's representative a copy of the complete set of the AWP (including any previously provided to the taxpayer regarding that specific audit, FBO, reaudit or revised FBO) along with any other releasable documents listed on CDTFA-495 unless the taxpayer has specifically asked the auditor not to provide certain portions of the AWP. Auditors must record accurately in CRM Notes the date on which the AWP were provided to the taxpayer, the name of the taxpayer or representative to whom the documents were delivered, and the method of delivery of the AWP. There is no longer a requirement to mark an X on the CDTFA-495 showing which schedules were given to the taxpayer. If any schedules are withheld from the taxpayer, it must be documented in CRM Notes and an explanation must be given as to why specific schedules or items were not given to the taxpayer.

Original records obtained during an audit should not be retained but must be returned to the taxpayer. Copies of records obtained or records generated during an audit that do not become a part of the AWP should not be retained but should be returned to the taxpayer or confidentially destroyed.

COMPLETE DISCUSSION NECESSARY**0210.07**

It is essential that the taxpayer and/or the representative be fully and accurately informed of the audit findings by personal discussion, whether in person, by phone or by video conference. This is required for three reasons:

- 1) The taxpayer must be afforded every reasonable opportunity to present all evidence which might result in a change or modification of audit recommendations;
- 2) More accurate returns for future periods may be expected if taxpayers are properly advised of the provisions of the laws and regulations; and
- 3) A clear understanding by the taxpayer of audit adjustments will minimize petition cases.

RESULTS OF DISCUSSION OF AUDIT FINDINGS**0210.09**

When a taxpayer disagrees with any portion of the audit findings, a “Discussion with Taxpayer” comment must be entered in the Verification comments, under “Other Comments”. The “Discussion with Taxpayer” comment will list and explain in clear, complete, and concise detail each item and dollar amount in the audit with which the taxpayer disagrees and agrees. The report will clearly detail the reasons or facts that the taxpayer contends supports their position under “Taxpayer’s Position”. It will also include the reasons or facts that the auditor believes supports their position under “Auditor’s Position”, and any additional comments added by the supervisor under “Supervisor’s Comments”. Comments should not be written in generalities or suppositions, but should use a clear presentation of opposing viewpoints, leaving no doubt as to the basis for disagreement. The audit supervisor will review the report of discussion and approve the auditor’s explanation of the non-concurrence. Whenever appropriate, the audit supervisor will contact the taxpayer for further discussion. Taxpayers must be provided a copy of the “Discussion with Taxpayer” comments. This comment will be prepared in the same manner for field billing orders.

COPY OF AUDIT LETTERS TO BE FURNISHED TO THE TAXPAYER**0210.11**

In all instances where an audit results in a tax change, system-generated audit letters (Preliminary Audit Results Letter and Final Audit Results Letter) will be furnished to the taxpayer. In addition, a copy of the audit letters will be provided to the taxpayer’s representative.

The audit letters provided to the taxpayer will include an analysis and description of items comprising the change in the measure of tax.

When a field audit discloses that a tax liability has been reported in excess of the correct amount, the taxpayer should be informed in the same manner as in the case of a deficiency. A claim for refund (Form CDTFA-101) **must** be secured from the taxpayer for consideration by the CDTFA whenever an overpayment (net credit audit) has occurred. See AM 0217.13 for more information.

10-DAY LOCAL OFFICE DISCUSSION**0210.13**

The “10-day” local office discussion is the taxpayer’s next step following the exit conference if there are any remaining disputed items. The office discussion is generally initiated by the taxpayer’s response to the Final Audit Results Letter, an audit letter that allows a taxpayer who does not concur with the audit, FBO, reaudit or revised FBO recommendation 10 days to respond and arrange for a discussion of the non-concurred items. The Audit Principal, section supervisor, or Administrator is responsible for holding the 10-day office discussion and may designate someone other than the exit conference supervisor to hold the discussion.

A completed form CDTFA-836-A, *Report of Office Discussion*, is required for all audits, reaudits, FBOs, and revised FBOs with non-concurred or non-committal findings. Form CDTFA-836-A must document adjustments made as a result of the 10-day discussion, if any, as well as any items for which the taxpayer is still in disagreement. The Audit Principal, section supervisor, Administrator, or their designee, must approve form CDTFA-836-A in the system appropriately.

To protect the statute of limitations of a completed audit or FBO, the Audit Principal, section supervisor, Administrator, or their designee, must attempt to contact the taxpayer by telephone to schedule an office discussion if the taxpayer fails to respond to the Final Audit Results letter. Efforts to contact the taxpayer must be clearly documented in the CRM Notes under the Audit springboard. The Audit Principal, section supervisor, Administrator, or their designee, must ensure a waiver of limitations is secured, if necessary.

TRANSCRIPT OF RETURNS FILED**0211.00****GENERAL****0211.01**

Transcripts of returns serve as a starting point of all audits. Auditors will generate transcripts by accessing the Audit springboard, Other, Transcripts and selecting the type of transcript. Auditors must generate, export, and copy each relevant transcript for the audit period to the Excel AWP file, as necessary. At a minimum, auditors must include the “Sales and Use Tax Return” and “Schedule A” transcripts, or similar transcripts for special taxes and fees audits, in their AWP.

VALIDATION OF TRANSCRIPTS**0211.03**

Auditors will validate returns in the system with information available for the account. Once the returns are validated, auditors will place a comment in the system under the Audit springboard, CRM Notes, indicating that the returns were validated. An example of when a return requires validation is when a return contained a Compliance Assessment. Auditors may also add any special comments, such as “could not validate return for 4th quarter.”

Not all returns require validation. Examples of returns that may not require validation are as follows: (1) where the taxpayer’s returns do not appear to have any problems or errors; (2) where the taxpayer has not made any refund claims; (3) where no additional determination has been issued for the period under audit; or (4) where no amended returns have been filed.

DOWNLOAD RETURN TRANSCRIPTS**0211.05**

Auditors must generate an electronic version of the return transcripts covering periods in the audit. The transcripts must be exported into a spreadsheet from the system. Several steps are required to export the main transcript and all additional schedules. These are then copied into the Excel AWP. Detailed instructions are available on myCDTFA, (CDTFA’s internal website) by searching “Instructions for Importing CROS Transcripts to Excel Audit Working Papers.”

As noted above, if there are separate schedules filed, for instance Schedule A, B, or C, the transcripts of those schedules must be exported individually. The schedules that will need to be exported will differ from one account to another, based on what type of account is being audited.

The sales and use tax “Forms” available under the Transcript tab are:

- Sales & Use Tax Return
- Deductions/Exemptions
- Lumber Tax
- Health Plans Tax Return

The sales and use tax “Schedules” available under the Transcript tab are:

Schedule 530-B

Schedule A: District Tax Allocation

Schedule B: Detailed Allocation by County of Sales and Use Tax Transactions

Schedule C: Detailed Allocation by Site/Location of Sales and Use Tax Transactions

Schedule F: Detailed Allocation by City of Taxable Transactions for Lessors of Motor Vehicles

Schedule G: Fuel Seller’s Supplement to Sales and Use Tax Return

Schedule H: Detailed Allocation by City on Qualifying Transactions of \$500,000 or more

Schedule P: Tax Paid to Other State(s)

Schedule CDTFA-531-Q, section A: Tax Recovery

Schedule CDTFA-531-Q, section A1: Partial State Tax Exemptions Adjustments for Prior Periods

Schedule CDTFA-531-Q, section B: Diesel Fuel Adjustments

Schedule CDTFA-531-Q, section C: Bad Debt Lender Losses

Schedule X: Partial Exemption from Bradley-Burns Local Taxes Aircraft Common Carrier

Other forms and schedules are available under the Transcript tab for special taxes and fees accounts.

Deductions and/or exemptions may not appear in the system on the first transcript option if the taxpayer filed CDTFA-401-A, *State, Local, and District Sales and Use Tax Return* (long form) for any period during the audit. Auditors must also generate the Deductions/Exemption transcript in the system for all audits and export it to the Excel AWP. This makes the review process easier for audit reviewers to determine whether any Deductions/Exemptions were claimed during the audit period.

The principal advantage of exporting the transcript(s) is that figures can be directly copied to the AWP without having to manually transcribe them. Additionally, access to the transcripts within the Excel AWP file make it easier for review. By exporting the applicable cube view, auditors are able to import using the Auditing Program Menus under “Temp TB” so the transcripts are formatted properly. Auditors must not use the option to exclude zeroes that is available in the system. This could result in periods filed as zero, not being shown in the transcript(s).

The figures shown on the generated transcripts are reported amounts, adjusted to reflect any subsequent tax increase or decrease as a result of billings or refunds, errors on returns, and amended returns. However, Compliance Assessments will not show on the transcript. Therefore, if there is a period with no information generated, auditors must check to see whether there was a Compliance Assessment by viewing the Period springboard, Financial tab, Transactions tab, and look for an Estimated Assessment under transaction type, or Financials, Returns, and under status, it would state “Estimated”.

Gasoline Sellers

Auditors can print a “Fuel Reconciliation-MVP & SUT” Report from the system. These reports can be obtained by selecting Report from a New Manager and then selecting Report List tab. Using the green filter box, auditors enter “Fuel Reconciliation” and the report will show as a hyperlink. Auditors can select the hyperlink for that cube and enter the dates to have the report show in the system. Each section of the report can be exported to a spreadsheet, as needed. The first section of the report shows the Seller Account, Gas Tax Sch A, Diesel Tax Sch A and Jet Tax Sch A. Some of these may show as zero, depending on the type of fuel sold by the taxpayer.

This report is a reconciliation schedule between the tax prepaid to vendors and the prepaid tax claimed by the taxpayer. The second section shows the buyer’s (taxpayer’s) account, Gas Tax Sch B, Diesel Tax Sch B, Jet Tax Sch B, Gas Tax Sch G, Diesel Tax Sch G and Jet Tax Sch B.

The third section shows, by month (even though it says by quarter), Gas Tax Sch A, B and G, Diesel Tax Sch A, B and G and Jet Fuel Tax A, B and G and the Tax Difference.

Gasoline and diesel fuel sales tax prepay rates are found on the CDTFA’s webpage at www.cdtfa.ca.gov/taxes-and-fees/prepayment-rates-fuels.htm.

TAXABLE TRANSACTIONS**0211.07**

The amounts shown as “Taxable Transactions” will always be the computed amount based on the reported or adjusted figures.

ESTIMATED RETURNS**0211.09**

Transcripts including periods with an estimated return will not have data for the period where an estimated return was completed. When auditors generate a transcript and notes missing data (indicating no return was filed), they must investigate further to determine whether there is an estimated return for the period or if the taxpayer didn’t have sales to report for the period.

If an estimated return was done for a period in the audit, auditors will perform the audit on the identified period as if no estimated return was prepared. Auditors must make a note under the Audit springboard, CRM Notes, using capital letters with the following information:

NOTE TYPE: Audit Note**NOTE: ESTIMATED RETURN – 2QXX, 3QXX and 1QYY**

Auditors should also include information regarding any payments made for the period.

Estimated Return Adjustments

The following information provides guidance on how Estimated Return Adjustments (estimated returns) will be handled in an audit. “Outstanding collection action” as it pertains to the guidance below includes all the following actions: earnings withholding orders, levies, liens, keeper warrants/till taps and offsets.

1. Estimated return is unbilled.

- The auditor works with the assigned collector who verifies the estimated return is not billed.
- The collector determines if the estimated return should be reversed and if it should be, will follow the procedures to complete and approve the reversal.
- The collector follows normal procedure to complete and approve the reversal and will notify the auditor once completed.
- The auditor will make an adjustment within their audit using zero as their basis and make clear notes under the “Miscellaneous” heading in their Verification Comments detailing that an unbilled estimated return was reversed and tax adjustments are included in the audit for the applicable period(s).

2. Estimated return is billed with no outstanding collection activity and the auditor determines the taxable liability disclosed in the audit is higher/lower than the estimated return.

- The auditor works with assigned collector and verifies there is not any active collection activity on the estimated return billing.
- The collector determines if the estimated return should be reversed and if it should be, will follow the procedures to complete and approve the reversal.
- The collector will let the auditor know the reversal is completed and that payments were redirected (if applicable) to include them as prepayments in the audit.
- The auditor will make clear notes under the “Miscellaneous” heading in the Verification Comments detailing that a billed estimated return, with no outstanding collection activity, was reversed and tax adjustments are included in the audit for the applicable period(s).

3. Estimated return is billed with outstanding collection activity and auditor determines the taxable liability disclosed in the audit is lower than the estimated return.

- The auditor will determine whether there is a material decrease in tax which warrants an adjustment to the estimated return.
- If a decrease in tax is material, auditors will determine the correct amount of tax (including district tax) for the period containing an estimated return. For efficiency, auditors will only take into consideration the most materially affected district tax amounts when computing district tax adjustments to include in the final tax amount. The difference will be displayed in the Excel AWP. Auditors will not upload adjustments in the system lead schedules. Instead, auditors will make clear notes under the “Miscellaneous” heading in their Verification Comments, detailing that the audit contains estimated returns, the period(s) affected, and that the estimated returns need to be adjusted because it is determined the tax liability is lower than the estimated return. Auditors must also make clear comments on the lead and/or subsidiary AWP schedules so the audit supervisor, audit reviewer, or any other third party can easily identify which period(s) contain an estimated return.

Note: The reason the auditor must compute the correct amount of tax for periods containing an estimated return, and not include the decreased tax adjustment within their audit, is because an estimated return with active collection activity cannot be reversed. Doing so would result in the reversal of all active collection activity on the billed estimated return.

- The audit reviewer will review the audit and verify the tax adjustment amount computed by the auditor is correct. The audit reviewer will contact the assigned collector to request an adjustment to the estimated return (in tax dollars) be made.
- The collector’s supervisor must approve any adjustment and enter a note in the system Period springboard.
- The collector will redirect any overpayments made towards the adjusted estimated return as Audit Payments in order to include them as prepayments in the audit.
- The collector will let the auditor know the adjustment is completed and that payments were redirected (if applicable).

4. Estimated return is billed with outstanding collection activity and the auditor determines the taxable liability disclosed in the audit is higher than the estimated return.

- The auditor works with assigned collector and verifies there is active collection activity.
- The auditor will determine whether a material adjustment to the estimated return should be made and discuss with their supervisor. If both the auditor and audit supervisor determine that a material increase in tax is due and it is likely the taxpayer will pay the additional liability, the audit supervisor will contact the Compliance Principal, or their designee, to request they review the details of the account to determine whether the estimated return should be reversed.

Note: Each account must be reviewed on a case-by-case basis. There may not be potential to collect upon an audit liability with a higher tax amount. Therefore, reversing the estimated return may not be the best option since we risk losing existing collections on the original estimated return billing.

- The Compliance Principal or their designee will notify the audit supervisor if the estimated return should or should not be reversed.
- If the estimated return should **not** be reversed, auditors will make clear notes under the “Miscellaneous” heading in the Verification comments detailing that the audit contains an estimated return(s), the period(s) affected, and the estimated return(s) will not be reversed due to the risk of losing existing collection activity on the original estimated return billing or because the additional tax liability disclosed by the audit is immaterial. Auditors must also make clear comments on the lead and/or subsidiary schedules of the AWP so the audit supervisor, audit reviewer, or any other third-party person can easily identify which period(s) contained an estimated return. If the additional audited amount is material, the auditor will assess it in the audit. The auditor will calculate the tax difference between the audited amount and the amount assessed in the estimated return. Auditors will determine the percentage of district tax allocation based on the records reviewed and use that as the basis to capitalize the tax difference into measure. Auditors will then assess the additional measure in the AWP and upload the measure in the system lead schedule. For efficiency, auditors should only allocate to those district funds when material.
- If the estimated return should be reversed based on Compliance Principal approval, auditors will notify the assigned collector of the approval.
- The collector verifies approval for the estimated return reversal has been obtained and tells the auditor when the reversal is completed and that payments were redirected (if applicable).
- Auditors will make clear notes under the “Miscellaneous” heading in the Verification Comments detailing that a billed estimated return, with outstanding collection activity, was reversed and tax adjustments are included in the audit for the applicable period(s).

5. An estimated return exists and no adjustment to the tax liability will be made.

- The auditor uses a basis of zero and enters \$0 in the system for the adjustment amount so other periods may be adjusted, when the audit results in a tax change. Auditors will make no adjustment (\$0) for the period with an estimated return.

**CREDIT FOR TAX PAID TO OTHER JURISDICTIONS
(RTC SECTION 6406 CREDIT)**

0211.11

A credit for sales and use tax paid to other states or political subdivisions is available under RTC section 6406. Offset credit interest and offset credit penalty for negligence, failure to file, and/or fraud will be allowed on RTC section 6406 Credits.

DELINQUENT RETURNS FOR PERIODS INCLUDED IN AN AUDIT**0211.13**

CDTFA's general policy is to encourage taxpayers to voluntarily file any delinquent tax returns before an audit is completed. In some situations, a taxpayer may file a return prior to the issuance of the Notice of Determination. When this occurs, auditors will receive a Work Item and must "accept" or "info only" (the two options available in the system) the return using their best judgment. Currently, reviewers and supervisors do not have this capability in the system. Returns filed by the due date during a period under audit should generally be accepted. This does not validate the accuracy of the returns. Auditors must still review the reported amounts.

When the taxpayer files a delinquent return for reporting periods included in an audit, the following procedures apply:

- If the return is received and accepted (as opposed to "info only" in the system) **after** the determination is issued, any remittance made is considered a payment on account. No adjustment to the audit should be made.
- If the return is received and accepted **before** the determination is issued, the electronic transcript of returns and the AWP's shall be updated to reflect the amounts the taxpayer has reported on the return.
- If the return is received and accepted as "info only" **before** the determination is issued, the electronic transcript of returns and the AWP's will **not** be updated to reflect the amounts the taxpayer has reported on the return and auditors will audit to the original amounts. Any applicable payments should be applied to the audit. An example where "info only" may be appropriate is when audit work is already done and the taxpayer files an amended return to report the items as they have been already scheduled by the auditor.

Auditors must not make changes to the return. If the auditor accepts a return with an error, a Work Item will be sent to the appropriate section for review/correction.

If the Work Item involves a statute audit, (an audit that will result in lost periods due to expiration of the statute) the auditor should contact the team member assigned to the Work Item or if it has not been assigned, contact the section responsible for the Work Item by emailing one of the following email groups:

Return Analysis Unit: BTFD.RAUElectronicMaintenanceRequests@cdtfa.ca.gov

Local Revenue Branch: LRBLocalTaxQ@cdtfa.ca.gov

Include the account number in the email subject line to aid in the distribution of the email. If a specific request needs to be expedited, add "RUSH" in the subject line and provide a brief reason for the rush in the email.

Penalties

A ten percent penalty for failure to file a timely return will be assessed and applied to any delinquent periods included in the audit.

After a delinquent return is received, penalty for failure to file a return will be removed from the audit assessment. In some situations, a taxpayer may file a return prior to the issuance of the notice of determination. When this occurs, the penalty for failure to file a return and any tax reported on the return will be removed from the audit assessment. The audit team may still consider whether a ten percent penalty for negligence in preparing returns is warranted.

DELINQUENT RETURNS FOR PERIODS INCLUDED IN AN AUDIT

(CONT.) 0211.13

The system will automatically assess a ten-percent penalty for any return(s) filed late and/or paid after the due date of the return. Auditors should not try to obtain zero returns to clear delinquencies or to allow the taxpayer to avoid a failure to file penalty.

Delinquent returns for periods included in sales and use tax audits are returned by the Audit Determination and Refund Coordination Unit in ADRS to the respective field office for correction; delinquent returns for periods included in special taxes and fees audits are handled by the Appeals and Data Analysis Branch in the Audit and Carrier Bureau.

WHERE RETURNS ARE NOT AVAILABLE

0211.15

If the taxpayer did not file a return by the time the transcript is generated in the system and the reason is not due to an estimated return, auditors will create an assessment for the delinquent return and include it in the system's lead schedule(s) based on the affected return line items.

If the taxpayer did not file a return but made a return payment for the period, auditors must calculate "Taxable Transactions" based on the amount of tax paid and use this as the taxable transactions base in their audit to project any errors and/or perform a taxable transactions reconciliation.

PRINCIPAL ACCOUNTING OFFICE LOCATED OUT-OF-STATE

0211.17

If an investigation discloses that the taxpayer's primary accounting office is not located in California, the field office will not attempt to conduct the sales and use tax audit, secure the records from out-of-state, or correspond with out-of-state representatives of the taxpayer regarding the audit unless requested to do so by Headquarters. They will instead secure a CDTFA-122 and a CDTFA-82, if necessary, and the sales and use tax audit will then be transferred to the out-of-state office.

EXPIRED PERIODS

0211.19

If there are expired periods in the audit, auditors must contact the audit supervisor to update the audit period. Once the audit period is updated, the auditor must make sure to update all transcripts and lead schedules, including Summary and Penalty schedules.

WRONG CLASSIFICATIONS OF DEDUCTIONS

0211.21

If a taxpayer has erroneously classified a deduction on a return, the auditor must make detailed comments disclosing the deduction that is incorrectly classified and describe its proper classification. Auditors must discuss with the taxpayer the correct way to claim the deduction on future returns.

UNAPPLIED SALES TAX PREPAYMENT OR CREDITS

0211.23

Unapplied sales tax prepayments on filed returns or credits otherwise displayed on the Customer springboard must be investigated by auditors.

Auditors must:

- Check the Customer springboard for any credits.
- Review any associated accounts where the credit originated to determine which account has a credit.
- Determine if the credit amount is an overpayment that needs to be applied to the audit liability.
- Work with the compliance team to apply the overpayment as an audit prepayment prior to the audit being staged to Posted and Billed.
- Make a note in the Audit springboard, CRM Notes stating in capital letters the following:

REDIRECTED CREDIT OVERPAYMENT TO AUDIT PREPAYMENT FOR 2QYY.

VERIFICATION OF CREDITS OR ERRORS

0211.25

- To verify if a credit has already been refunded:
 - o Account springboard → Financial → Refunds
 - o Period springboard → Financial → Refunds
- To view refund information:
 - o Account springboard → Financial → Refunds
 - o Customer springboard → Task → Cases [look for Appeal/Claim for Refund case]
- To verify if an underpayment has been billed:
 - o Period springboard → Financial → Bill Items
- To show the amount paid:
 - o Period springboard [Look at the Financial Box in the top right, look at the credits line]

LOCAL TAX ALLOCATION/REALLOCATION AND DISTRICT TAX REDISTRIBUTION 0212.00

GENERAL 0212.01

CDTFA has contracts with counties and incorporated cities to administer the Bradley-Burns Uniform Local Sales and Use Tax Law. Taxpayers in conforming taxing jurisdictions will file combined state and local tax returns with CDTFA.

CDTFA-414-L AUDITOR'S WORK SHEET LOCAL TAX ALLOCATION 0212.03

Auditors will prepare Form CDTFA-414-L, when required. Auditor's may generate and download an electronic version of the applicable local tax transcript by going to the Audit springboard, Other tab, Transcripts sub-tab. The field auditor will prepare Form CDTFA-414-L, when needed, in connection with audits initiated in the field.

ALLOCATION OF TAX CHANGE RECOMMENDED BY AUDIT 0212.05

Auditors will perform the local tax allocation when completing the lead schedule.

After determining reported amounts were reasonably allocated by the taxpayer, the general rule for allocating a tax change recommended by an audit is to prorate it to local jurisdictions in the same ratios as reported by the taxpayer for the twelve-quarter summary provided on the lead schedule. Allocation on an actual basis is required in those instances, such as transactions of a non-recurrent nature, where the jurisdiction in which the taxable event occurred can be readily and definitely ascertained. Depending on the lead schedule used, auditors will allocate using a percentage basis or actual basis, either by transaction or by amount, per jurisdiction, per quarter.

Refer to Compliance Policy and Procedures Manual (CPPM), chapter 5, Exhibit 1 for a comprehensive discussion of the local tax allocation guidelines.

LOCAL TAX REALLOCATION 0212.07

A traditional Form CDTFA 414-L **must** be used if an audit requires a local tax reallocation (as generally indicated in Section II, *Correct Allocation*, of Form CDTFA 414-L). An Excel version of the traditional CDTFA 414-L is the preferred format and is available on the myCDTFA intranet website under "Tax and Fee Resources", "Resources for Auditors", "CDTFA-414-L Auditors Worksheet – Local Tax Allocation." However, auditors may choose to use the PDF version of Form CDTFA-414-L (found on the myCDTFA forms search). On Form CDTFA-414-L, auditors will provide a complete explanation of the basis for any reallocation adjustments in the explanation box on the form and/or part of the e-mail to Local Tax. Form CDTFA-414-L should be saved in the system as an Attachment in CRM of the Audit springboard, regardless of the format used. The guidance in Audit Manual (AM) sections 0212.09 - 0212.21 regarding how to complete Form CDTFA-414-L, Tax Area Codes, Date of Knowledge (DOK), and reasons for reallocation applies.

Where the DOK occurs more than one quarter past the last day of the audit period, auditors should include on Form CDTFA-414-L all periods covered by the DOK, not just the periods in the audit period. For example, the audit period ends June 30, 2018 but the DOK by the auditor is January 15, 2019. If a reallocation is necessary for 3Q18 and 4Q18, the auditor should include these periods on Form CDTFA-414-L.

LOCAL TAX REALLOCATION

(CONT.) 0212.07

Work Item Procedure

After the audit reviewer completes their review of the CDTFA-414-L, they will create a Work Item named “Local Reallocation Request” in the system. The audit reviewer will input the following information below into the Work Item:

- Auditor name
- Auditor phone number
- Date prepared
- Taxpayer name
- Taxpayer account number
- DOK
- DOK established by (result of an audit, etc.)
- Periods questioned
- Explanation of the basis for reallocation

Once the Work Item is created, the system will route it to the ADRS – Allocation and Summary Unit. The Local Revenue Branch (LRB) will access the CDTFA-414-L in the CRM tab of the Audit springboard and will reallocate local tax, as applicable.

Since LRB must monitor and make corrections to subsequent returns, it is important to have a complete explanation of the original errors disclosed in the audit. This explanation provides LRB with the information necessary to advise the taxpayer how to revise any subsequent incorrect returns and how to properly report local tax in the future.

Where a NOW audit discloses a local tax reallocation of over \$250, a comment of the reallocation must be made in the CRM Notes of the Audit springboard. Auditors should then prepare Form CDTFA-414-L and create a Work Item. Audits that result in a NOW but have a local tax reallocation may remain as a NOW in the system and do not need to be processed as a change audit, as previously instructed.

LOCAL TAXING JURISDICTIONS

0212.09

List the local taxing jurisdictions horizontally across the top of the CDTFA-414-L form using one column for each jurisdiction. The name of the jurisdiction may be abbreviated if necessary. Also list the first five digits of the area code for each jurisdiction as well as the symbols UA (Unincorporated Area — code 998) and CW (County Wide — code 999), where applicable.

If a redevelopment agency is involved, list the four-digit “In-Lieu” code along with the appropriate abbreviation.

The form in the system provides space for five taxing jurisdictions. Auditors can add columns for additional ones or use additional pages.

LOCAL TAX REPORTED

0212.11

List by period the amounts reported by the taxpayer, in whole dollars, under the appropriate taxing jurisdictions. Normally, the entire audit period will be listed on the transcript. However, reallocations are usually restricted to three quarters to conform to the limitation provisions of the law (see AM section 0212.15 and RTC section 7209). If Headquarters has prior knowledge of an improper distribution, the ADRS — Allocation and Summary Unit will contact the field office with information regarding the periods to be reallocated. Transcripts of earlier returns will be furnished upon request when field offices have prior knowledge of erroneous distribution.

TAX AREA CODE

0212.13

In either a reallocation or an assessment, the tax area code(s) must reflect the period(s) of the audit, taking into account city incorporations, annexations and/or taxpayer location moves during the audit period. For example, the tax area code for the City of Elk Grove (34013) is effective for periods after and including October 1, 2000. Prior to October 1, 2000, the area now incorporated as Elk Grove was in the unincorporated area of Sacramento County (tax area code 34998). Therefore, any reallocations or assessments for periods prior to October 1, 2000, in what is now within the city limits of Elk Grove, should be allocated to the unincorporated area of Sacramento County. The effective date of a local tax area code can be found in the system under User Tools→ TAC Effective Dates.

DATES DETERMINING REALLOCATION

0212.15

Enter the commencing date of the reallocation, the date that first knowledge of improper distribution was obtained, and the source of that knowledge into the appropriate spaces. The dates will be determined in accordance with RTC section 7209. Therefore, if the knowledge of improper distribution is obtained when an audit is started, auditors will reallocate the tax for the two preceding funding periods, which usually includes the preceding three quarterly periods, but can extend to periods before that time, based on when the local tax funded to the jurisdiction(s). For example, if the first knowledge of improper distribution is obtained 10/06/2017 (4Q–2017), the auditor would commence reallocation from 01/01/2017 (1Q–2017) through the end of the audit period. Date of knowledge is based on when CDTFA obtains knowledge of the improper distribution.

REASONS FOR REALLOCATION

0212.17

Provide a complete explanation of the basis for any reallocation adjustments in the space provided. Since the ADRS — Allocation and Summary Unit must monitor and make corrections to subsequent returns, it is important to have a complete explanation of the original errors disclosed in the audit. This explanation provides the ADRS — Allocation and Summary Unit with the information necessary to advise the taxpayer how to revise subsequent incorrect returns and how to properly report in the future.

DISTRICT TAX REDISTRIBUTION

0212.19

The redistribution period for district tax is limited to three quarters prior to the DOK, which is the date CDTFA **obtains** knowledge of the distribution to a district other than the district entitled to the tax (see Revenue and Taxation Code section 7269). Therefore, if the knowledge of improper distribution is obtained when an audit is started, auditors will reallocate the tax for the two preceding funding periods, which usually includes the preceding three quarterly periods, but can extend to periods before that time, based on when the district tax funded to the jurisdiction(s). The DOK is to be clearly documented. If the knowledge of improper distribution is obtained during an audit, auditors will redistribute the tax for the preceding three quarters from the DOK. For example, if the DOK is January 4, 2018, auditors can redistribute the district tax for the second, third, and fourth quarters of 2017.

When an auditor obtains knowledge that a redistribution of district tax is necessary, a district tax redistribution schedule is to be prepared. Auditors will name the schedule “Taxpayer District Redistribution Schedule” and attach it in CRM Attachments. In addition to an explanation of the redistribution, the following must be provided:

- Auditor name
- Auditor phone number
- Date prepared
- Taxpayer name
- Taxpayer account number
- DOK
- DOK established by (result of an audit, etc.)
- Periods questioned
- Explanation of the basis for reallocation

Work Item Procedure

After the audit reviewer reviews the redistribution schedule, they will create a Work Item named “District Reallocation Request” in the system. The audit reviewer will input the above information into the Work Item. Once the Work Item is created, the system will route it to the Local Revenue Branch (LRB). LRB will access the district redistribution schedule in the CRM tab of the audit and will redistribute district tax as applicable.

In instances where a retailer reports district tax that is greater than the amount due and no other jurisdiction is due the tax, and the retailer is unable to return the amounts to the purchaser, the balance will remain with the jurisdiction to which it was improperly reported.

For example: A retailer engaged in business in Humboldt County properly reports Humboldt County’s Transactions and Use Tax (HBGT) but improperly reports the City of Rio Dell’s Transactions and Use Tax (RDGT) and fails to report the City of Eureka’s Transactions and Use Tax (ERKA) and the City of Eureka Supplemental Transactions and Use Tax (ERST), on transactions during several quarters. Because the auditor discovered the error on February 8, 2020, a district redistribution schedule should be prepared beginning with the 2Q 2019 through the end of the audit period (4Q 2019). The retailer improperly reported \$10,000 of RDGT and failed to report a combined total of \$7,500 of ERKA and ERST during the three quarters, leaving an excess of \$2,500 that is greater than the amount due to any district. The retailer is unable to return the excess amount to the purchasers; therefore, the excess \$2,500 should remain with the RDGT.

In instances where a retailer reports district tax that is greater than the amount due, and the retailer did not collect the tax from the purchaser, a refund is due to the retailer. When a retailer reports district tax that is less than the amount due, and the additional district tax due is comprised of multiple district taxes, the auditor must compute the amount of additional tax due and prorate the taxable measure to all jurisdictions within the parent code.

Example: In 4Q 2017 a retailer engaged in business in Los Angeles county makes \$50,000 in sales subject to the Los Angeles district rate of 2.5% (LACT, LATC, LAMT, LAMA, LACH) but improperly reports district tax to the county of San Bernardino at 0.5% (SBER). The auditor will prepare a district redistribution schedule for the 0.5% that was incorrectly reported and provide it to LRB. The auditor will then assess the additional 2% difference in the audit. However, since the parent code for Los Angeles on the Sales and Use Tax Return and on the system lead schedule includes all district tax rates for Los Angeles and cannot be separated, the auditor must perform the following calculation to adjust the district taxable measure to ensure the correct amount of additional tax is being assessed:

Sales subject to Los Angeles District Tax:	\$50,000
Rate that should have been reported:	2.50%
Rate reported on Return (San Bernardino)	0.50%
Difference in Rates (2.50% - 0.50%)	2.00%
Additional District Tax to Assess	\$1,000
Los Angeles Measure to Adjust (\$1,000/2.50%)	\$40,000

The auditor will then enter \$40,000 for the Los Angeles parent code on the lead schedule. This represents the adjusted taxable district measure computed to properly assess the \$1,000 district tax difference.

For periods beyond three eligible quarters to reallocate from the DOK, auditors should only include the net difference and not credit some districts and debit other districts because the auditor is then, in essence, reallocating periods that are beyond the three eligible quarter statute of limitations from the DOK. For ones with the same district rates and beyond statute to reallocate, auditors can offset and just include the net amount. For ones with different district rates, auditors will need to adjust using the tax amounts and/or measure similar to the example above.

For credit periods beyond three eligible quarters from the DOK or in any period eligible for reallocation, there are a few exceptions where credit for districts can be left as computed based on recorded/reported difference. See below for the exceptions:

- Valid Credits - Taxpayer reported a district in error for which taxes were not collected. For instance, the sale was only subject to the countywide rate but the taxpayer reported in error to a city in the same county at a higher rate.
- Within the Same Parent Code – These are not true credits but just moving amounts within the same parent code. For this case, auditors are not reallocating but just assessing the additional tax for the related district (i.e. city).

REALLOCATION/REDISTRIBUTION THRESHOLD

0212.21

When reallocating taxes between jurisdictions, the threshold for reallocation of tax is \$250 for all errors, per quarter. The threshold applies to reallocations between all of the various tax funding programs including state, local, county, districts, and state add-ons. It also applies to redistribution between different districts within the same tax funding program (for example, BART, LACT). A reallocation should be made when either one error of \$250 or more or multiple errors totaling \$250 or more occur in any quarter.

FIELD BILLING ORDER

0213.00

In the system, Field Billing Orders (FBO) are generally prepared in the same manner as a regular audit. The main difference is that an Audit Plan case and extensive comments are usually not required for an FBO. (see AM section 0201.09)

WHEN ARE FIELD BILLING ORDERS USED

0213.01

FBOs are used:

- In lieu of tax returns, where a liability is disclosed for a period(s) prior to the taxpayer's application for a permit or license and it is impossible or impractical to secure returns.
- To recommend additional liability or refund disclosed as the result of investigation.
- To recommend use tax liability owed by a person not registered with the CDTFA.
- When a survey of the account indicates an audit is not warranted, but liability is disclosed. For instance, an audit error noted in one area (i.e. fixed assets), but a full audit is not warranted.
- A period is approaching the statute date and the taxpayer is unwilling to sign a waiver for that period and the auditor does not have sufficient information to estimate the entire audit period. An FBO is used to bill an estimate for the expiring period only.
- To address an error that is limited to a specific period where the auditor determined a full audit is not warranted.
- A claim for refund when a full audit is not warranted.
- To separate out liability in a portion of a regular audit where a penalty is imposed and a portion where no penalty is imposed. For example, when a negligence penalty is appropriate for the regular audit period based on recorded versus reported sales, but a negligence penalty is not appropriate for the mandatory tips for which tax was not collected, but rather, the recording of mandatory tips as exempt was due to a computer programming error in the taxpayer's system.
- To assess a one-time purchase of use tax on purchases subject to use tax where no tax was collected or remitted.
- When information is received that a liability, such as district tax or local tax, was not reported for less than 12 quarters. This could be for as little as only one quarter.
- When a resale certificate(s) is(are) found to be invalid.
- When an audit needs to be split, for instance, in the case of a taxpayer filing bankruptcy.
- To quickly address a single area of liability where a full audit is not warranted.

REQUIRED VERIFICATION COMMENTS FOR FBOS

0213.03

Auditors must provide the following verification comments, when applicable:

- (a) Type of Business Organization
- (b) Explanation of Tax Change
- (c) Discussion with Taxpayer
- (d) Overpayment
- (e) Credit Interest
- (f) Penalty

AUDIT PROCESSING AND CLOSING

0214.00

FORMS AND WORKING PAPERS

0214.01

Upon completion of the audit assignment, auditors must ensure all file naming conventions are correct and all files are placed in the appropriate springboard in the system. In addition, all hyperlinks within the Excel Audit Working Papers (AWP) should be tested and verified to be properly working prior to submitting the audit for review. When the audit is complete, auditors will stage the audit to the “Supervisor Review” stage.

Below is a brief summary for some of the tasks to complete before submitting the audit:

- Verify proper entity (corporation, LLC, partnership, sole proprietor) and mailing address for correct billing.
- Verify any claims, cases or tasks are completed, as applicable.
- Verify any audit payment applied or any other credit or account balance issues.
- Verify any indicators are addressed that will prevent billing.
- Verify Power of Attorney or representative is linked, as necessary.
- Verify comments with a spelling and grammar check.
- Verify Hyperlinking and References.
- Verify all attachments are included in the system. (XYZ letters, Vendor Surveys, etc.)
- Verify file names are correct and descriptive for sorting, in order, by schedule name, form, or date, if applicable.
- Verify all required forms and an audit plan are attached.
- Verify a notation is made if security is available, especially in bankruptcy audits.
- Verify for closed-out/ceased partnership accounts, a comment is made indicating that there are general partners listed in the “Verification Comments” in the system, if applicable.

REQUIRED PAPER COPIES TO RETAIN

0214.03

During an audit, and whenever warranted, if an auditor receives the following forms in paper copy, instead of submitted through Online Services, the auditor must maintain (in the office files) the paper copies with wet signatures, or valid digital signatures per Audit Manual section 0103.15:

- CDTFA-82 – Authorization for Electronic Transmission of Data
- CDTFA-101 – Claim for Refund or Credit
- CDTFA-122 – Waiver of Limitations
- CDTFA-245-COR-1 – Corporate Officer/LLC Member Registration Update
- CDTFA-392 – Power of Attorney

Auditors must attach a digital copy of the completed CDTFA-82, CDTFA-245-COR-1, and CDTFA392 on the Audit springboard, CRM tab (Attachment sub-tab), and cross-reference it to an appropriate case in the system, if necessary. A digital copy of the completed CDTFA-122 must be attached on the Audit springboard, CRM tab (Attachment sub-tab). A digital copy of the completed CDTFA-101 must be attached on the Audit springboard, CRM tab (Attachment sub-tab), and cross-referenced to the related Claim for Refund case.

The office making the audit (OMA) must maintain paper copies of these original forms, **not** received through Online Services, until the audit case is closed. Once the audit case is closed, the paper copies of these records shall be confidentially destroyed.

REQUIRED PAPER COPIES TO RETAIN

(CONT.) 0214.03

The Audit Principals, Section/Branch Supervisors or Office Administrators, or their designee, are responsible for reviewing and purging these documents on an annual basis. A closed-audit report shall be used to identify those audit cases that are closed and no longer require the retention of the above documents.

Below are the criteria for the system **closing an audit** once it has moved to the “Posted & Billed” stage. This process is done automatically in the system and all of these conditions must have been met for the audit to be closed.

- 90 days have passed since the audit was posted
- The statute date for each period in the audit has expired
- The Audit Bill Item has been finalized
- None of the following cases are active on the account:
 - o Administrative Protest
 - o Petition for Redetermination
 - o Petition for Redetermination (Dual/Secondary)
 - o Petition for Redistribution
 - o Claim for Refund

Normally, when an audit is staged to “Posted & Billed,” the system will not show the case in the owner’s active “My Work” list, even though it is not technically closed. However, any action that updates the Audit springboard (for example, statute, period change, etc.) will remove the case from the hidden state and it will then display until the system’s closure rules are met.

SUPERVISOR REVIEW

0214.05

When the audit is complete, auditors will stage the audit forward to “Supervisor Review” which will notify the supervisor via a Work Item the audit is ready for review. After reviewing the audit, supervisors will complete the “Supervisor Review” Work Item. Supervisors should perform: (a) an overall check for completeness and proper arrangement of audit working papers, (b) a sufficient review of pertinent working papers to ensure that the auditor has followed instructions regarding special or unusual problems in the audit, and (c) a review of the audit comments to ensure that the comments adequately describe the situations involved in the audit.

If comments are needed on audit schedules in the AWP, supervisors should create a text box on the schedule to add the comments. The comments are preceded by the supervisor’s initials and title (for example, “KLZ - Supervisor”). The “Supervisor Comments” for **disagreed** audits and “Penalty” comments, if needed, are also added to the Verification Comments on the Summary Schedule.

If the audit is approved, the supervisor will stage the audit to “Audit Review.”

If the audit is not approved and needs to go back to the auditor for correction, the supervisor will stage the audit back to “Prepare Audit Package.” If the changes required do not affect the outcome of the audit, the supervisor may send an email to the auditor detailing all necessary changes or create and assign an “Audit Case Assistance” Work Item (which is located on the Audit springboard under the Task tab).

Minor changes/comments may be provided in an informal manner by the audit supervisor and/or audit reviewer in the preferred manner by each local office. However, the audit supervisor or the auditor must send any updated working papers or an updated Audit Results Letter to the taxpayer, when requested changes are related to guidance on how tax applies, or other items for which the taxpayer needs to be updated.

CHANGES REQUESTED BY THE SUPERVISOR

0214.07

When the audit supervisor does not approve the audit and requests substantial changes affecting the outcome of the audit, the supervisor will create and assign an “Audit Case Assistance” Work Item (which is located on the Audit springboard under the Task tab) to the auditor.

The audit supervisor will also stage the Audit case back to the “Prepare Audit Package” stage. The auditor will complete the Work Item by making the corrections to the audit, as requested. Once the corrections are made, the auditor will stage the audit to the “Supervisor Review” stage, complete the Work Item and enter a CRM Note.

Once the audit has been reviewed and approved by the audit supervisor, they will stage the audit forward to “Audit Review.”

CHANGES REQUESTED BY AUDIT REVIEWER

0214.09

When there are changes that need to be made to the audit, the audit reviewer will create a “Change Request” Work Item and make the owner of the Work Item the audit supervisor. The audit reviewer will stage the audit back to the “Supervisor Review” stage. Once the audit supervisor reviews the “Change Request” Work Item, the audit supervisor will change the owner of the “Change Request” Work Item to the auditor and stage the audit back to the “Prepare Audit Package” stage.

The auditor will make the requested changes, complete the Work Item, and stage the audit forward to “Supervisor Review.” The audit supervisor will review the AWP and verify all changes were addressed. When the audit supervisor approves the audit, the audit is staged to “Audit Review” and a note is made in CRM Notes that changes to the audit have been made, as requested.

AUDIT PRINCIPAL REVIEW

0214.13

Once the audit reviewer completes the review and approves an audit requiring approval of the Audit Principal, the audit reviewer will stage the audit to “Audit Principal Review” and a subsequent Work Item will automatically be generated and assigned to the Audit Principal.

If the Audit Principal approves the audit, they should indicate this on the Work Item and stage the audit back to “Audit Review” so the reviewer can stage the audit to “Posted & Billed.”

If the audit is not approved and needs to go back to the auditor or supervisor for correction, the Audit Principal will create and assign an “Audit Case Assistance” Work Item (which is located on the Audit springboard under the Task tab). The Audit Principal will then stage the audit back to “Supervisor Review.” The “Audit Case Assistance” Work Item must indicate why the audit is not approved and provide specific instructions and comments why it is not approved.

AUDIT MANUAL

DEPUTY DIRECTOR, FIELD OPERATIONS DIVISION (FOD) AND BUSINESS TAX AND FEE DIVISION (BTFD)

0214.15

The Deputy Director, Field Operations Division (FOD) and the Deputy Director, Business Tax and Fee Division (BTFD), or their designee, must review and approve audits including a fraud penalty. The Deputy Director, FOD will approve fraud-penalty audits under the Sales and Use Tax program, while the Deputy Director, BTFD will approve fraud-penalty audits under the Special Taxes and Fees programs. Audits requiring Deputy Director, FOD or BTFD approval, will be sent electronically by the Office Administrator from the Office Making Audit (OMA). The fraud memo and any attachments or exhibits must be saved in the Audit springboard, CRM Attachments.

An email requesting approval of the audit will be sent to the Deputy Director, FOD or BTFD, with a copy to the Technical Advisor and Secretary for the Deputy Director, FOD or BTFD, on the email requesting approval. The subject line and body of the email should state "Request for Approval_Audit Case_ Account #_Taxpayer Name_Statute Date" (for example: Request For Approval_ A654321_ 108-123456_Joe's Plumbing_July 31, 2020).

Team members of the office of the Deputy Director, FOD or BTFD will notify the OMA of approval by email. Any documents related to the approval should be attached to the email so they may be added as an attachment in the Audit springboard by the local office.

RELATED ACCOUNT AUDITS

0215.00

AUDITS OF MORE THAN ONE LOCATION

0215.01

In order to keep all related accounts on a consistent basis for audit selection purposes, all related sales and use tax accounts are generally audited simultaneously for the same period. For Special Taxes and Fees accounts, the taxpayer is generally given the option of auditing all related accounts concurrently. However, processing of a completed audit should not be delayed while audits of related accounts are in process.

The term “related account” includes any person holding a permit under more than one tax or fee program administered by CDTFA.

In the case of a Sales and Use Tax (SUT) auditor being assigned an audit for a Customer who also has Special Taxes and Fees (STF) account(s), the SUT auditor should notify STF of the SUT audit being conducted. Auditors can notify the Audit Examination Branch (AEB), by email, at BTFDAEBSupervisors@cdtfa.ca.gov.

In the system “related accounts” are **only** those accounts found under the **same Customer**. Related accounts are **not** when there are **similar** owners, but they are not under the same Customer, those should be treated as an audit lead, rather than a related account.

Auditors can create audit leads, as needed, for any accounts where ownership is merely similar, but not the same. These audit leads will then show if an audit is being done or will include comments as to why no further follow up was warranted. The audit lead will be closed after the other account is reviewed. These types of audit leads are helpful to show auditors have addressed any relevant accounts to ensure similar issues on similar accounts are addressed.

In the case of successor and predecessor accounts, although they are related to some extent, they are not related in a legal sense, because they are different “persons.” When a situation includes predecessor/successor accounts, a comment on the predecessor account should be in CRM Notes that includes the successor account number and it should be noted as the successor account. For the successor account, the initial comment in CRM Notes should be the predecessor account number and it should be noted as the predecessor account.

RELATED ACCOUNTS AUDIT REPORTS AND SUMMARIES

0215.03

The system lists all accounts belonging to the taxpayer under the Customer springboard, Registration, Accounts. In conducting audits of related accounts, auditors should verify whether the taxpayer’s other accounts are correct and whether they are still active. Auditors should notify their Compliance section of any changes (additions or close-outs) to the taxpayer’s accounts, using either a “Request Account Maintenance” or “Request Site Maintenance” Work Item.

FORM CDTFA-122, WAIVER OF LIMITATIONS**0216.00****WAIVER OF LIMITATIONS-INTRODUCTION****0216.01**

Form CDTFA-122, *Waiver of Limitation* (waiver), is a legal agreement that a taxpayer may voluntarily enter into with CDTFA. A waiver that is signed by the taxpayer prior to the statute expiration date extends the three-year statute of limitations (or eight years in cases where no return was filed) for the period indicated on the CDTFA-122. The waiver requests the signature of a CDTFA employee, but the employee signature is not required for the waiver to be considered valid. A waiver duly signed by only the taxpayer is still a valid waiver.

If the taxpayer signs a waiver prior to the statute expiration date, such waiver allows CDTFA to examine the taxpayer's records, and possibly assess additional tax, for the periods that would otherwise expire under the statute of limitations. In addition, a signed waiver allows any credits in the period indicated on the waiver to be offset against any tax liability and it extends the period within which a taxpayer may file a timely Claim for Refund.

WAIVER OF LIMITATIONS — PERIOD AND TIME LIMITS**0216.03**

Waivers normally will be obtained for a **minimum** of six months or two calendar quarters and will be dated through one of the following expiration dates: January 31, April 30, July 31, October 31, or other date consistent with the return filing due date of the tax/fee program. The same procedure is followed if the taxpayer is on an irregular reporting basis. For taxpayers on an irregular reporting basis, the waiver must be signed by the taxpayer prior to the expiration date of the irregular reporting period. If an extension of more than six months is needed, the request and extension will be by full calendar quarters instead of by month, regardless of the taxpayer's reporting basis. It should be noted that any extension must be executed within the time limits covered by the expiring waiver form. These guidelines also apply to waiver extensions, where at least one waiver has previously been obtained and a new one is needed.

BENEFITS GAINED BY SIGNING A WAIVER**0216.05**

A taxpayer may benefit from signing a waiver as follows:

- The waiver keeps the original audit period intact, so the taxpayer may not have to provide records from a different time period than were originally requested by the auditor.
- The waiver avoids CDTFA's immediate issuance of a Notice of Determination (FBO) in cases where the statute of limitations will expire.
- The waiver holds the period(s) in question open for filing a Claim for Refund or for offsetting any overpayment of tax against an existing tax liability.
- A waiver provides the taxpayer and CDTFA with the ability to adapt to both foreseen and unforeseen time constraints. The waiver gives the taxpayer and CDTFA the time necessary to thoroughly address difficult audit issues before those issues result in a billing.
- The waiver can, at times, expedite the audit process by allowing time to resolve audit issues "up front," rather than during the appeals process.
- The waiver may eliminate needless "red tape" which may result from a billing issued with good intentions, but possibly incorrect, due to time constraints that did not allow the detailed review necessary to reach a fair and equitable conclusion.

TAXPAYER SIGNATURE

0216.07

To preclude any question about the validity of a waiver, the original waiver must be signed by:

- The owner in the case of a sole proprietorship,
- A partner in the case of a partnership,
- A managing member in the case of a limited liability company or
- A corporate officer in the case of a corporation, or
- A person holding a written power of attorney from the owner, a partner, or a corporate officer.

Note: Any CDTFA-122 signed by a power of attorney **must** be accompanied by a copy of the signed power of attorney. The power of attorney form **must** be signed prior to the CDTFA-122 being signed.

The essential elements of a valid written power of attorney are:

- The document must be dated and identified as a “power of attorney.”
- The document must clearly authorize the agent (controller, assistant controller, or some other person) to act in a manner consistent with the signing of a waiver. Ideally, the power of attorney will authorize the agent to act in “sales and use tax (or other applicable tax or fee program) matters.” However, a less specific description may be acceptable if it can reasonably be interpreted to impose upon the agent the right to execute the CDTFA-122, *Waiver of Limitations*.
- The person granting the power of attorney must be the owner, partner, or a corporate officer of the company being audited.

Form CDTFA-392, *Power of Attorney*, may be used to document power of attorney status.

Note: A verbal authorization by the taxpayer to discuss confidential information with a representative, does not give the representative the authority to sign a waiver. See section 0101.65 of the Audit Manual for more information about verbal authorizations.

With respect to corporations, if the title of the person signing the waiver is other than the chairman of the board, president, secretary, or chief financial officer, auditors must verify, by examining the corporate documents (for example, articles, bylaws, minutes, etc.) whether the titled position is a corporate officer and has the authority to sign the waiver.

With respect to partnerships, if the person signing the waiver is not listed as a partner in the system on the Customer springboard, Registration tab, Summary sub-tab, auditors must verify the validity of the person’s status as a partner by reviewing the partnership agreement. Any changes in partners must be reported to the compliance team as provided in Audit Manual (AM) section 0202.01.

A copy of the written power of attorney (CDTFA-392 or other document with the required information) must be attached in the system under both the Audit and Account springboards, CRM Attachments.

In addition, a paper copy of the power of attorney is submitted when turning in the audit and saved in the office file (see AM section 0214.03). Powers of Attorney granted previously, can be found in Documentum. Documentum can be viewed in the system, from the Account springboard, “View Images” button, located in the top, right-hand corner of the screen.

In the system, auditors should ensure the compliance team links the Power of Attorney to the Customer or Account. The link request may be done by use of a “Request Account Maintenance” Work Item.

TAXPAYER SIGNATURE

(CONT.) 0216.07

If a taxpayer returns a signed waiver to the auditor by mail, the auditor must attach the postmarked envelope to the original waiver and save it in the office file. The postmarked envelope must also be attached in the system, along with the signed waiver. If the auditor obtained the signed waiver in the field, the auditor must have the waiver date stamped immediately upon returning to the office.

WHEN TO REQUEST A WAIVER OF LIMITATIONS

0216.09

Auditors should request a waiver in cases where there is a sufficiently documented understatement or overstatement that can be billed/refunded without additional examination for the period(s) in question, and there is insufficient time to perform an audit to be used as a basis for a determination before the expiration of the three-year period. Auditors should also request a waiver when a taxpayer requests a postponement while an audit is in progress, when the taxpayer requests a postponement before an audit is about to commence, or while an audit is in progress. If the taxpayer refuses to execute a waiver in these cases, auditors will make determinations on an estimated basis if information is available to support an understatement of reported tax.

DOCUMENTING THE NECESSITY FOR A WAIVER OF LIMITATIONS

0216.11

When auditors determine that it is necessary to request a waiver from a taxpayer, auditors must document the reason(s) for requesting the waiver on the Audit springboard, CRM Notes.

Auditors must also document the following:

1. If the extension of the statute of limitations totals two years or more, auditors must document approval by the Audit Principal before presenting the waiver to the taxpayer for signature.
2. The date the auditor mailed, emailed or hand delivered the waiver to the taxpayer.
3. The date the taxpayer signed the waiver.
4. The date the auditor mailed, emailed or hand delivered a copy of the signed waiver to the taxpayer.

PREPARATION OF WAIVERS

0216.13

Auditor's Responsibility:

Auditors must ensure the waiver/waiver extension is accurately prepared to secure expiring periods. Auditors must pay specific attention to waiver extensions with regard to the original waiver and the periods for which the extension is being secured.

When creating a waiver in the system, it is **critical** that auditors ensure the dates that are pre-filled are accurate. A problem can occur when a taxpayer files a tax return late because the system will show the date the return was filed as the "limitation statute date" (the date used to automatically populate the waiver letter expiration date). Auditors should ensure when they encounter this issue, that they always change the incorrect "limitation statute date" to be the **subsequent, accurate** statute date (see section 0216.03 for waiver expiration dates). Do not change the date to a date **prior to** the filing date. Failing to correct this issue will result in an incorrect waiver expiration date being input into the waiver letter and will prevent the waiver from being tracked in reports, possibly resulting in the period being lost because the waiver expired.

For example, if a quarterly filer filed their first quarter 2021 return late on May 15th, rather than April 30th, the “limitation statute date” will be May 15th. Prior to creating the waiver letter, auditors should manually change the May 15 “limitation statute date” to July 31, the subsequent statute date.

When creating a waiver extension, it is also **critical** to review the original waiver (or the previous waiver extension) prior to creating the waiver extension, to ensure the dates that are pre-filled are correct. The due dates for returns will vary for various tax and fee programs administered by CDTFA and any other irregular period filers, but this practice should be followed, when necessary.

Auditors will create waivers in the system through the use of a “Waiver of Limitations” case. A waiver case will be opened by accessing the Audit springboard, Task, Forms, and then clicking the Waiver of Limitations hyperlink. Once auditors verify the correct statute dates to include on the waiver, they will stage the waiver case to either “Approved” or “Supervisor Approval”, depending on whether office policy requires supervisor approval. When a supervisor approves the dates to be included on the waiver and stages the waiver case to “Approved,” auditors will then stage the waiver case to “Generate Waiver” to print the waiver. The generated waiver is located under the Waiver of Limitations case, Items tab, Letters sub-tab or Account springboard, CRM, Letters. However, all generated letters can be found under the Account springboard, CRM, Letters.

Auditors will prepare a minimum of two copies of the completed waiver and distribute them as follows: the original signed copy will be maintained in the office file and a copy will be sent to the taxpayer. The original signed copy may be confidentially destroyed after the audit (claim) has been closed (or refunded). The Audit Principal, or their designee, will be responsible for verifying the audit or refund case is closed and for destroying the forms.

Auditors must attach completed waivers to the Audit springboard, CRM, Attachments and should also attach the proof of date received (i.e., date on envelope or office date stamp).

Audit Supervisor’s Responsibility

Audit supervisors are responsible for ensuring auditors timely request and obtain a valid waiver/waiver extension(s) from each taxpayer for assigned audits with period(s) expiring due to statute. Generally, unless there are circumstances such as a close out, an audit period should include at least twelve quarters.

Audit supervisors may approve the decision to allow a period(s) to expire if the amount of tax is immaterial or no tax liability exists and there is a good business reason to do so.

Auditors should make comments in the Audit springboard, CRM Notes, regarding the reason(s) periods were allowed to expire and, where applicable, if an audit is completed with less than 12 quarters.

Audit Principal’s Responsibility

Audit Principals are responsible for ensuring that:

- Audit supervisors monitor and review audit inventory assigned to auditors to ensure that all waiver/waiver extensions have been obtained to properly secure expiring periods.
- All inventory in field office review (for example, audits, FBOs, etc.) contains a valid waiver/waiver extension to properly secure expiring periods.

Receiving a CDTFA-122, Waiver of Limitations

When auditors receive a signed waiver/waiver extension, auditors must complete the Representative Information section under the Attributes tab, within the Waiver of Limitations case, and timely stage the case to “Waiver Received.” This will create a task for the supervisor who will review and then stage the waiver to “Taxpayer Accepted.”

Note: Within the discussion above, “timely” means the date on which the signed waiver is received from the taxpayer or the date the auditor returns to the office with the signed waiver.

Administrator Quarterly Review

On a quarterly basis, Administrators must ensure auditors have obtained all waiver/waiver extensions that secure expiring periods with respect to audit inventory assigned to an auditor or audit inventory in the review stage. Administrators may delegate this responsibility; however, Administrators are accountable for any period(s) that expire under the statute due to waiver/waiver extension errors. Administrators may be asked to provide additional information regarding the circumstances leading to any lost period(s) and to provide information on any action taken to avoid future occurrences.

WHERE MORE THAN ONE PLACE OF BUSINESS IS OPERATED 0216.15

Where a taxpayer operates more than one place of business, and has multiple accounts, the waiver should specifically cover all locations under audit. The waiver must include all account numbers. However, if the waiver form does not provide adequate space for description of all account numbers and periods involved, then auditors must prepare a separate waiver for each account. In some cases, the waiver must be created outside of the system. The signed waiver will be scanned and attached in the system under CRM Attachments.

WAIVER MAY BE TAKEN IN LEGAL CASES 0216.17

Auditors should not allow taxpayers to cause undue delay in the completion of a bankruptcy, assignment for the benefit of creditors, or probate audit. This is important because of the following final dates for filing claims:

- Bankruptcy:** Six months from the date first set for the first meeting of creditors unless otherwise ordered by the court.
- Assignment:** Final date established by the assignee – must be at least 150 days (and not more than 180 days) from the date of written notice to creditors of the assignment.
- Probate:** Four months from the date of a written request to issue a deficiency determination by a personal representative or administrator.

Auditors may take a waiver in legal cases where there appears to be a good reason and after consultation with the Collection Support Bureau that the extension will not interfere with the administration of the case. In any event, the agreed-upon extension date in the waiver must not be beyond the final date for filing claims as stated above.

WAIVERS ON AUDITS RECOMMENDING PENALTY FOR FRAUD 0216.19

Whenever a penalty for fraud on the audit is recommended, the three-year statute of limitations period does not apply. However, auditors should still obtain a waiver to secure expiring periods, if necessary, as the fraud penalty recommendation may later be deemed unwarranted.

YEARLY REPORTING PERIOD

0216.21

Waivers for accounts reporting on a yearly basis must be obtained within three years after the last day of the calendar month following the one-year period for which the amount is proposed to be determined, or within three years after the return is filed, whichever period expires later.

Expiring Liability With No Waiver 0216.23

Audit reviewers must stage audits to Posted & Billed and ensure the Notice of Determination is issued prior to the date on which the liability would expire. If it is not possible to do so, the office will prepare an early estimated Field Billing Order (FBO) for the expiring period(s) or prepare an early estimated billing for the audit. Verification Comments must be made and include the following:

1. Reason for an early estimated billing (for example, waiver, bankruptcy, etc.)
2. When there is no penalty assessed on an early estimated billing, the reason for no recommended penalty.
3. For a dual determination, the reason for the dual.

For an early estimated billing, with fraud, a memorandum from the Administrator, to the Deputy Director, Field Operations Division, is required before processing.

When the exact amount of additional measure of tax is not known, auditors should make a reasonable estimate. Auditors should follow the procedure of making a separate determination for expiring periods **only** when a delay in submission of a completed audit report is directly attributable to actions of a taxpayer who refused to sign a Waiver of Limitations.

Prior to requesting an estimated billing, the Audit Principal, or their designee, **must** send Letter qL0021, *Letter to Taxpayer Prior to Billing*, to a taxpayer who refuses to sign a Waiver of Limitations. The letter advises the taxpayer of the upcoming bill and confirms the auditor’s discussion of why the early billing is necessary.

WHEN SEPARATE DETERMINATION ISSUED FOR EXPIRING PERIOD

0216.25

Auditors must make a notation in the Verification Comments under the Summary working paper in the system whenever a separate determination is issued for an expiring period prior to the completion of the audit. When a separate determination for expired period(s) was levied for a tax liability, auditors must enter an appropriate comment, explaining the reason for the downward, upward, or no adjustment in the Verification Comments.

Although this is not a true reaudit, the comment should be made under “Reason for Reaudit” to explain the updated amounts. In addition to the appropriate notation discussed above, auditors must note the following:

- The measure of the determination dated (show date) for (show period) was overstated by (show measure of overstatement).
- The measure of the determination dated (show date) for (show period) was understated by (show measure of understatement).
- The liability for (show period) was determined on (show date) and totaled \$ (show amount). (Applies when the separate determination for the expired period was made for the same liability as disclosed by audit.)

OVERPAYMENTS**0217.00****AUDITOR'S COMMENTS****0217.01**

An audit report recommending approval or denial of a claim for refund must contain specific information as to the nature of the claimed overpayment, the amount to be refunded (as established by the taxpayer) and the amount of tax or fees to be refunded, as recommended by the auditor. These comments are entered under the caption "Claim for Refund" in the Verification Comments under the Summary Schedule in the system. The hours spent on verification of the claim are now recorded on the Time tab, in the system.

CLAIMS FOR REFUND**0217.03**

CDTFA may grant refunds or offsetting credits within the periods specified in the applicable business tax law (see RTC section 6902). The audit team should secure claims for refund when there are overpayments. This policy will protect the taxpayer's interest for any item in an audit or filing period that resulted in a net credit. Exceptions are noted in AM sections 0217.11 and 0217.13. Also see Publication 117 for specific refunds involving Special Taxes and Fees programs.

Auditors should encourage the taxpayer to file their claim for refund through CDTFA's Online Services portal. Otherwise, auditors must obtain the CDTFA-101, Claim for Refund or Credit (refund claim) or a letter in lieu of the form, when a credit item and/or credit period exists. If a taxpayer submits a letter in lieu of the form, the letter must include: 1) the specific reason, 2) the amount and, 3) the period for which the taxpayer is claiming a refund. If a taxpayer fails to file a refund claim, auditors must explain to the taxpayer that without a refund claim, the credit will only offset against the audit deficiency, and no refund can be issued beyond the offset deficiency. In addition, auditors must document, in CRM notes, all efforts taken to obtain the refund claim. Comments should also specifically state what credit items were allowed without a claim for refund to document which credits were timely claimed.

Additional guidance and further instructions on handling claims for refund are located on myCDTFA under "Reference Guide for Field Team Members on Handling Refunds and Credits."

FORM AND CONTENT OF CLAIM**0217.05**

With respect to claims for refund or credit, RTC section 6904, and similar provisions for special taxes and fees, state:

"Every claim shall be in writing and shall state the specific grounds upon which the claim is founded."

Taxpayers may file a claim for refund, and should be encouraged to do so, via the Online Services portal. No special form of claim is necessary to comply with this requirement of the law; however, Form CDTFA-101, Claim for Refund or Credit, may be used for this purpose. The exception is for diesel fuel claims for refund filed by Ultimate Vendor, Users and Exempt Sellers. These programs have specific claim for refund forms that must be used to file claims for refund.

These general guidelines can be used when filing a claim for refund for most of the tax and fee programs administered by CDTFA.

However, there are specific guidelines when filing a claim for refund for the following programs:

- Childhood Lead Poisoning Prevention Fee
- Cigarette Tax Stamp Program
- Covered Electronic Waste Recycling Fee (eWaste)
- Diesel Fuel Tax
- Hazardous Waste Generator Fee
- Lead-Acid Battery Fees
- Motor Vehicle Fuel Tax and Aircraft Jet Fuel Tax
- Tax on Insurers
- Water Rights Fee

Taxpayers can be referred to Publication 117 for more information on filing a claim for refund for the above programs.

When advising the taxpayer on the content of the claim, auditors should **stress** that the statute (Regulation 35036(a)) requires a claim for refund must be in writing, must be signed by the claimant or the claimant's authorized representative, and must include:

- 1) The specific grounds or reasons upon which the claim is founded;
- 2) The reporting period for which the claimed overpayment was made;
- 3) The amount of the refund being claimed, if known; and
- 4) Information necessary to contact the claimant or claimant's authorized representative.

Auditors should advise taxpayers to avoid generic language where possible, such as "unclaimed sales for resale for the fourth quarter." Rather, taxpayers should identify the specific transactions for which the claim for refund is being filed.

The original, signed copy of the claim for refund will be maintained in the field office file. The original, signed copy may be confidentially destroyed after the audit (claim) has been billed (or refunded). The Audit Principal, or their designee, will be responsible for reviewing and destroying the forms on an annual basis. (See section 0214.03)

Auditors must attach the completed claim for refund document in the system under the Claim for Refund Case, as an attachment. The attachment must then be cross referenced in the Audit case, as necessary. Auditors must create a "Claim for Refund" Case, as further explained in the refund guide located on myCDTFA under "Reference Guide for Field Team Members on Handling Refunds and Credits."

Claim for refund forms should be forwarded to the Appeals and Data Analysis Branch for special taxes and fees accounts or Motor Carrier Office for interstate user or use fuel accounts.

SUBSEQUENT REFUND CLAIMS**0217.07**

A subsequent refund claim, based on the same transaction(s) and theory as an original refund claim, is treated as an amendment to the original claim. For example, a taxpayer files a claim for refund on the theory that a sale of tangible personal property to Customer A was a sale for resale of \$50. Thereafter, the taxpayer files a second claim for refund for the same period asserting that the sale of property to Customer A was a sale for resale but in the amount of \$75 rather than \$50. The second claim is considered an amendment to the original claim because it is based on the same transaction and theory but for a different dollar amount. When the subsequent refund claim is based upon the same transaction(s) but a different theory as the original refund claim, this claim is also treated as an amendment to the original claim. For example, a taxpayer files a claim for refund on the theory that a sale of property to Customer B was a sale for resale in the amount of \$50. Thereafter, the taxpayer files a second claim for refund in the same period asserting that the sale of property to Customer B was an exempt sale in interstate commerce in the amount of \$50. Again, the second claim is considered an amendment to the original claim because it is based on the same transaction, but a different theory.

A second claim that is based upon a different transaction is considered a new claim for refund. To do otherwise would allow a particular period to potentially remain open indefinitely as long as one claim for refund had been filed for that period. For example, a taxpayer files a claim for refund on the theory that a sale of property to Customer C was a sale for resale. Thereafter, the taxpayer files a second claim for refund for the same period asserting that a sale to Customer D was also a sale for resale. The second claim is not an amendment to the first claim even though it is based on the same theory. It is a new claim because it is based on a different transaction. The new claim must be filed within the period specified by statute to be considered valid.

WHEN OUT OF STATUTE DEFICIENCIES MAY BE OFFSET**0217.09**

CDTFA may offset amounts granted for timely claims for refund against deficiencies that occur during the periods covered by the claim for refund, even though the deficiencies are offset after the expiration of both the statute of limitations and any agreements extending the time for addressing such deficiencies.

Under the doctrine of “equitable setoff,” a claim for refund opens the taxpayer’s entire tax liability for the period in question. Thus, even though CDTFA is barred by the statute of limitations from issuing a deficiency assessment attributable to one reporting period, it is proper for CDTFA to apply an overpayment against that underpayment in a different reporting period, provided **both** periods are covered by the claim for refund.

While CDTFA can offset debit liabilities against overpayments within the claim period, such offsets can only be applied **up to the refund amount**. A Notice of Determination cannot be issued for any liability remaining in periods that have expired because of the statute of limitations. This interpretation of RTC sections 6487 and 6901 was upheld in *Sprint Communications Company v. State Board of Equalization* (1995) 40 Cal.App.4th 1254 (see *Business Tax Law Guide, Sales and Use Tax Court Decisions*).

WHEN OUT OF STATUTE OVERPAYMENTS MAY BE OFFSET**0217.11**

Credit for overpayment of tax for one or more reporting periods covered by the waiver of limitations may be allowed as an offset up to the total amount of net underpayments established for any period(s) covered by the audit, regardless of whether the audit discloses a net overpayment or underpayment for the entire audit period. This does not apply to all Special Taxes and Fees accounts. Please see Publication 117-*Filing a Claim for Refund*, for which accounts qualify.

A WAIVER OF LIMITATIONS DOES NOT PERMIT A REFUND IN THE ABSENCE OF A CLAIM FOR REFUND

0217.13

If the overpayment of tax or fees for the period(s) covered by the waiver of limitations exceeds the total amount of net underpayments established for any filing period(s) covered by audit, no refund of the excess can be made unless a timely claim for refund has been filed.

A claim for refund filed within the period for which a waiver has been given will be considered a timely claim. If, however, the overpayment is not more than the net underpayments, the entire amount thereof may be applied as a credit.

When the last day for filing a timely claim for refund falls on a Saturday, Sunday, or holiday, the claim for refund may be filed on the next business day with the same effect as if it had been filed upon the day appointed.

PETITION FOR REDETERMINATION CASES

0217.15

A timely claim for refund should be obtained if there are credit items included in an audit that recommends additional liability and the taxpayer is not in agreement with the audit report. Without a timely claim for refund, any excess of credits remaining for any period(s) would be barred by the statute of limitations.

SAMPLING FOR REFUND CLAIMS

0217.17

Sampling and projection techniques may be used by taxpayers to determine the amount of overpayment of tax liability using criteria similar to the techniques used by auditors (see AM sections 0405.20 and Chapter 13). If sampling and projection techniques are not appropriate for some or all of the transactions, the amount of the refund will be determined on an actual basis. Once the taxpayer has filed a claim for refund and has requested or suggested determining the amount of refund by means of sampling, auditors should contact the taxpayer to determine if sampling is feasible, and if so, develop a mutually agreeable sampling plan. The CDTFA-472 may be used for this purpose. Auditors may choose to consult a Computer Audit Specialist (CAS) on the sampling plan. The preferred method of sampling is statistical sampling as described in AM Chapter 13. Claims for refund using statistical sampling need to meet the same evaluation requirements of any statistical sample. If statistical sampling is not feasible, non-statistical sampling procedures, as discussed in AM Chapter 4, should be considered.

CREDIT AND DELINQUENCY INTEREST COMPUTATIONS 0218.00**INTEREST RATES 0218.01**

The interest rate applicable to overstatements and understatements of tax liabilities can be found on CDTFA's website (<http://www.cdtfa.ca.gov/taxes-and-fees/interest-rates.htm>).

CREDIT INTEREST 0218.03

Where an audit includes both debits and credits, and interest is recommended on the credits, auditors must make sure the "Calculate Credit Interest" box on the Summary working papers (Audit springboard, Working Papers tab, Summary sub-tab) is selected.

"Calculate Credit Interest" is selected by default. Auditors should only need to update if credit interest is not being allowed.

WHEN CREDIT INTEREST ON OVERPAYMENTS IS NOT ALLOWED 0218.05

Credit interest on overpayments is not allowed when statutorily prohibited or in cases of intentional overpayment, fraud, negligence, or carelessness. The following examples illustrate when credit interest would not normally be recommended:

- The taxpayer knowingly overpaid the tax liability.
- The taxpayer makes an overpayment caused by clerical or computational errors, such as inclusion of receipts for periods other than which the return is intended, omission of allowable deductions, use of incorrect tax rate, or errors of addition or subtraction on the tax return or made on supporting schedules submitted/compiled with the tax return, and the taxpayer has been notified in writing of such errors on one or more previous returns.
- Audit situations where it is determined the taxpayer has overpaid the tax liability, but a negligence penalty would have been assessed had the audit resulted in a net deficiency.
- There are tax overpayments caused by repeated errors in similar transactions, when the taxpayer has been notified, in writing, including comments in the audit working papers that such transactions are either non-taxable or are tax exempt.

WHEN CREDIT INTEREST ON OVERPAYMENTS IS ALLOWED 0218.07

The following situations illustrate when credit interest on overpayments is generally allowed:

- Clerical or math errors made in filing returns resulting in overpayments
- Inclusion of prior period receipts in current period
- Omission of allowable deductions
- Over-reported purchases subject to use tax
- Refunds of unapplied payments
- Overpayments of tax resulting from excess tax reimbursement
- Refunds as a result of the Appeals process
- Refunds of erroneous billings
- Misinterpretation of the law resulting in overpayment
- Net credit returns
- Timing differences
- Excess or duplicate prepayments involving a claim for refund

PREPARING AND COMPLETING AUDITS

CREDIT INTEREST ON UNJUST ENRICHMENT

0218.09

CDTFA will not refund excess tax or fee reimbursement unless the retailer submits proof that the tax or fee has been or will be returned to the customer.

DELINQUENCY INTEREST

0218.11

Interest will be computed even if the return was filed late or remains unpaid as of the date of the audit.

RECOMMENDATIONS REQUIRING ADMINISTRATOR'S APPROVAL

0219.00

Whenever a fraud or intent to evade penalty or jeopardy determination is recommended, a memorandum is required from the field office Administrator or someone acting on their behalf. For fraud or intent to evade penalties or jeopardy determinations involving sales and use tax, the memorandum is sent to the Deputy Director, Field Operations Division (FOD) or their designee. For fraud or intent to evade penalties or jeopardy determinations involving special taxes and fees programs, the memorandum is sent to the Chief, Audit and Carrier Bureau (ACB) or their designee.

JEOPARDY DETERMINATIONS

0219.01

The purpose of a jeopardy determination is to provide a means of protecting the State's interest when there is **substantial** evidence that **any** further delay in collection activity would **seriously impair or jeopardize** CDTFA's ability to collect taxes due. The amount determined in a jeopardy determination is immediately due and payable, and is final after 10 days (RTC section 6536 and similar special tax and fee sections). Taxpayers may be required to post a security deposit (at the discretion of the Division) in order for CDTFA to accept a petition for redetermination of a jeopardy determination (RTC section 6538 and similar special tax and fee sections). The taxpayer may file the petition online within the appropriate time frame (10-days), and the system will route it for review and, if security is not posted, team members may reject the petition.

For sales and use tax, if a jeopardy lien is needed, the original request for a jeopardy determination is routed to the Deputy Director, FOD, or their designee with a copy sent to the Collection Support Bureau (CSB), FOD. If the request for a jeopardy determination is approved, the Deputy Director, FOD, or designee will notify CSB to proceed with a jeopardy lien or warrant, if requested. A jeopardy lien is distinguished from other Notices of State Tax Lien only in that the jeopardy lien has no requirement for a preliminary (30-day) notice.

All jeopardy determination billings are **posted and billed** by the Office Making Audit (OMA) after approval is received.

Use the following examples as a guide for deciding when a jeopardy determination is warranted:

- Taxpayer is dissipating assets.
- Evidence exists that the taxpayer is placing assets in the names of other persons for purposes of concealment.
- Taxpayer's assets are being attached by creditors or are in imminent danger of attachment.
- There is a pending sale of property that represents the **last remaining asset** and without the funds from such sale, collection is doubtful.
- There is evidence that the taxpayer intends to file a petition in bankruptcy or make an assignment for the benefit of creditors.
- There is evidence that creditors intend to file an involuntary petition in bankruptcy against the taxpayer.

A recommendation for a jeopardy determination should be well documented and fully supported. It should include all of the facts and circumstances that support the recommendation and set forth the specific evidence that indicates a jeopardy determination is warranted. To request a jeopardy determination, auditors must prepare a memorandum that includes the following:

- The taxpayer's name and address.
- The source and status of the underlying liability.
- The taxpayer's overall financial condition, including a list of **all** known assets and liabilities.
- The amount of equity available for a lien or levy.
- The taxpayer's present and future income potential, including the taxpayer's ability to earn wages or pay the liability if there is no jeopardy determination.
- Documentary evidence to support a jeopardy determination.
- Information as to the county or counties where a Notice of State Tax Lien is to be filed.
- Whether or not a lien is to be recorded with the Secretary of State.
- Whether or not a warrant is requested. This must include the name of the person to whom the warrant is to be sent, the asset(s) to be levied upon, and the amount of advanced fees that may be required.

Specific Special Taxes Programs

Determinations issued to "Unlicensed Persons" under the Cigarette and Tobacco Products Tax Law, the Diesel Fuel Tax Law, or the Motor Vehicle Fuel Tax Law are required to be issued as a jeopardy determination; therefore, the memo requesting approval does not need to include information on the taxpayer's overall financial condition and their present and future income potential.

For special taxes and fees accounts, the original request for a jeopardy determination is routed to the Chief, Audit and Carrier Bureau (ACB), with a copy sent to CSB. If the request for a jeopardy determination is approved, the Chief, ACB, will notify CSB to proceed.

All jeopardy determination billings are posted and billed by the OMA after approval is received.

Include a copy of the memorandum in the Miscellaneous & Documents type of the Audit springboard, CRM Attachments. Add a notation, "Jeopardy Determination — see memo."

For more information, see CPPM sections 753.000, Warrants and Levies, and 757.000, Notices of State Tax Liens, Abstracts of Judgment and Liens.

FORM LETTERS**0220.00**

The below letters are those available in the system. These letters are not all available for all tax/fee programs. Letters in the system are program specific.

Audit Engagement Letter-**qL0001**-(CDTFA-5024 (previously CDTFA-80C))

Audit Report Letter-**qL0002**-(CDTFA-5020) sent in auditor's Name (Will be replaced by Audit Results Letter-qL0028, CDTFA-5184, when available)

Audit Findings Letter-**qL0003**-(CDTFA-5019) sent in Audit Principal's Name (Will be replaced by Audit Results Letter-qL0028, CDTFA-5184, when available)

Audit Engagement Letter 10-Day Follow Up-**qL0005**-(CDTFA-80-DTG)

Request to Transfer Audit-**qL0006**-(CDTFA-80-AT)

Audit Plan Introduction-**qL0011**-(CDTFA-5045)

Transfer Returned Letter-**qL0013**-(CDTFA-80-ATR)

Taxpayer Educational Consultation Program Appointment Confirmation Letter (Findings)-**qL0014**-(CDTFA-1297)

Taxpayer Educational Consultation Program Letter (No Findings)-**qL0015**-(CDTFA-5027)

Letter to Taxpayer When No Opinion Warranted-**qL0016**-(CDTFA-79-NOW)

Letter to Taxpayer Prior to Billing-**qL0021**-(CDTFA-79-G) (Required when doing estimated billing due to wavier not signed, unable to contact, or to prevent losing items to statute.)

IFTA No Change Letter **qL0024-1** (CDTFA-2008 FIS)

IFTA Clearinghouse **qL0026**

Audit Findings Presentation Sheet-**qL0027**-(CDTFA-699)

Preliminary Audit Results Letter (Special Taxes only)-**qL0028-4**-(CDTFA-5210)

Discussion of Audit Findings-**mL0309**-(CDTFA-836-A)

Information/Document Request-**mL0266** (CDTFA-698-A)

Formal Demand Letter-**mL0263** (CDTFA-698-B)

Waiver of Limitations-**mL0319** (CDTFA-122)

**CROSS REFERENCING TAXPAYER REGISTRATION INFORMATION
IN CDTFA PROGRAMS**

0220.05

Cross referencing taxpayer registration information in CDTFA programs assists in identifying current sales and use tax permit holders that may need to be registered for other programs, including, but not limited to, Underground Storage Tank Maintenance Fees, Cigarette and Tobacco Product Taxes, Tire Recycling Fees, Environmental Fees, and Electronic Waste (eWaste) Recycling Fees.

To assist in identifying taxpayers with obligations in multiple tax or fee programs, the following questions are listed in Attributes in the system. When performing sales and use tax audits, auditors are required to provide a “Y” or “N” response to each of the below questions in Attributes using the buttons located there.

Business with 50 or more employees?

The Environmental Fee applies to certain business organizations with 50 or more employees who are employed more than 500 hours (per employee) in California in the prior calendar year.

For more information, see Publication 90, *Environmental Fee*.

Does this business sell TVs, Computers or Portable DVD players?

Sellers of certain video display devices must register to collect and remit eWaste Fees on their sales of these products. For more information, see Publication 95, *Electronic Waste Recycling Fee*.

Seller of Lead Acid Battery?

Purchases and sales of lead-acid batteries are subject to the below separate fees:

- **California Battery Fee**
Fee imposed on the purchaser of a replacement lead-acid battery, which the retailer collects from the purchaser.
- **Manufacturer Battery Fee**
Fee imposed on the manufacturer or importer (when there is no manufacturer subject to the jurisdiction of California) on its sales of lead-acid batteries.

For more information, see the Lead-Acid Battery Fees Guide located at:

<https://cdtfa.ca.gov/industry/lead-acid-battery-fees.htm>

Seller of Tires?

Sellers must pay a fee for each new tire sold. For more information, see Publication 91, *California Tire Fee*.

Seller of Cigarette/Tobacco Products?

All cigarette and tobacco product importers, distributors and, wholesalers in California are required to register with CDTFA. Tobacco products include any product containing, made, or derived from tobacco or nicotine that is intended for human consumption. Examples include, but are not limited to, cigars, little cigars, chewing tobacco, pipe tobacco, snuff, and electronic cigarettes. Cigarette and tobacco cessation products are not tobacco products.

Auditors must inspect the taxpayer's stock of cigarettes in open cartons and loose packages by random sampling to determine whether proper tax stamps have been affixed to the cigarette packages. A comment stating whether the cigarette packages inspected bear the proper tax indicia should be entered. If the taxpayer does not sell cigarettes, a statement to that effect should be made. Both of these items are handled via the Attributes tab and by checking "Yes." A second option opens to mark "Yes" if indicia was inspected.

When checking purchase records, auditors should be alert to any purchases of cigarettes from persons who are not licensed distributors or wholesalers. Any unusual distribution/sales by a retailer of cigarettes should be thoroughly examined.

For more information, see Publication 93, *Cigarette and Tobacco Products Taxes*.

Distribution of Cannabis?

A cannabis distributor is a person who procures, sells, and/or transports cannabis products, between licensed cannabis businesses, such as cultivators, manufacturers, or retailers. A microbusiness licensed to act as a distributor must comply with all the same requirements as a distributor.

For more information, see Publication 557, *Tax Help for the Cannabis Industry*.

Seller of Alternative Fuels?

Use fuel vendors are required to file the Vendor Use Fuel Tax Return-CDTFA-501-AV and report the gallons/units of use fuels sold by fuel type and location. The total(s) from the schedule will be reported on Line 1 of the return.

For more information, see Use Fuel Tax Guide or Publication 12, *California Use Fuel Tax: A Guide for Vendors and Users*.

**CROSS REFERENCING TAXPAYER REGISTRATION INFORMATION
IN CDTFA PROGRAMS**

(CONT.2) 0220.05

Underground Storage Tanks (UST)?

The fee is collected from the owner of an underground storage tank based on the number of gallons of petroleum placed in the tank during the reporting period.

If yes, include the following information in the Verification Comments:

- UST Maintenance Storage Fee account number(s) of the tank owner or operator, if applicable. Provide no more than five account numbers and addresses (principal locations only).
- Address where the tank(s) is(are) located.
- The name, address, and phone number of the tank owner(s) or operator(s), if applicable.
- Other information that may identify or locate tank owners.

If the taxpayer was requested to provide the above information but did not do so, auditors should comment to that effect.

For more information, see Publication 88, *Underground Storage Tank Fee*.

Related Accounts?

A related account is an account that is under the same Customer but has a separate account number. A taxpayer can have multiple accounts at the same location. For example, an SUT and a TIR account, both at the same location. A taxpayer may also have multiple sales and use tax accounts with different locations. For more information on related accounts, see section 0215.00.

If marked “Y,” auditors must enter a comment, in CRM Notes, noting the related accounts and audit case number or a brief comment noting why an audit on a related account was not warranted.

Does Taxpayer use or accept cryptocurrency?

When performing audits, auditors in the Field Operations Division and the Business Tax and Fee Division should ask the taxpayer if they accept or use cryptocurrency for their business. Based on the taxpayer’s response, the auditor must respond to the audit attribute questions, “Does Taxpayer use or accept cryptocurrency?” by selecting the “Yes” or “No” button.

If the taxpayer accepts or uses cryptocurrency, it is important to determine which transactions involved cryptocurrency and the value of the cryptocurrency at the time of those transactions. This can be done by reviewing similar transactions around the same period of time or looking up the historical valuation of the cryptocurrency in question on various major cryptocurrency exchange websites. The auditor should ensure the sales (or purchases) were reported on the return and tax was paid as appropriate.

PUBLICATIONS PROVIDED

0220.10

In addition to the publications listed above, auditors may email, provide the location on the CDTFA website, or hand deliver other publications, regulations, law sections, or other information pertinent to the taxpayer's business and transactions. These publications help taxpayers understand their tax and fee reporting requirements and application of tax and fee laws.

List all publications and other materials furnished to taxpayers, either by providing the publication or referring them to the publication(s) on the CDTFA website, (e.g., Publications 17, 70, 76, Regulation 1668, etc.) in Verification Comments and in CRM Notes.

PREPAYMENT OF SALES TAX ON MOTOR VEHICLE FUEL PROGRAM

0221.00

GENERAL

0221.01

All audits of sellers of motor vehicle fuel (MVF), diesel fuel (including dyed diesel fuel), and jet fuel, must include verification of any prepayments made and claimed under the Sales and Use Tax MVF and Special Taxes and Fees programs. Since separate accounting funds are maintained among these programs, it is critical that audit differences affecting the MVF and Special Taxes and Fees accounts be separately identified.

See CDTFA's website at: <https://www.cdtfa.ca.gov/taxes-and-fees/prepayment-rates-fuels.htm>.

SPECIAL PROCEDURES FOR GASOLINE RETAILERS

0221.03

All retailers of MVF are subject to the provisions of the Prepayment of Sales Tax on Motor Vehicle Fuel Distributions Program. Their online sales and use tax return includes supplemental Schedule G, which allows the retailer to:

- Claim credit for prepayments of sales tax made on purchases of MVF, diesel fuel and jet fuel and
- Claim credit for tax paid to other states.

When preparing the audit report, auditors must separately identify any differences in the sales tax prepayment amounts reported on Schedule G in the AWP and in the "Fuel Reconciliation – MVP & SUT Report." Auditors must follow the special guidelines below when preparing audit reports on gasoline, diesel fuel, and jet fuel retailers.

A. Errors in Claiming Sales Tax Paid to Suppliers and Wholesalers

Credit and debit adjustments to amounts claimed on returns for prepayment of sales taxes on MVF, diesel fuel and jet fuel will be reflected on the fuel reconciliation report.

When adjustments are made to prepaid sales tax claimed, a separate lead schedule is needed because these errors require an adjustment to the "Prepayment of Sales Tax on Motor Vehicle Fuel Distributions," (SG) fund. Auditors will select "Total Gallons Distributed/Transferred" for the "Category" under "Input" on the lead schedule and then select the applicable fuel type under "Reason for Non-Compliance."

B. Errors in Claiming Credit for Tax-Paid to Other States

Adjustments for errors in claiming credit for tax-paid to other states will be reflected on the fuel reconciliation report. Because these errors do not require adjustment to the "SG" fund, a notation is not required in the "Verification Comments."

If adjustments are needed, auditors will select "Credit for sales tax prepaid to fuel suppliers" for the Category under "Input" on the lead schedule and then select the "Tax Paid to Other States" under "Reason for Non-Compliance."

Audit reports, except as noted above, should be prepared following the general guidelines of this chapter for sales and use tax audits.

FUEL RECONCILIATION MVP AND SUT REPORT**0221.05**

For accounts where the taxpayer makes retail sales of gasoline, a “Fuel Reconciliation MVP & SUT” report or Schedule G transcript must be generated, exported, and copied to the Excel AWP.

The report provides information about sellers, buyers, and prepaid sales tax for the account entered. The steps to produce the report are shown below.

Steps for Generating the “Fuel Reconciliation – MVP & SUT Report”:

- 1) In the system, from New Manager, select the Report manager
- 2) Select the “Report List” tab
- 3) Filter for “Fuel Reconciliation” to find the “Fuel Reconciliation – MVP & SUT” and select the “Generate” hyperlink
- 4) Enter the account number and date range
- 5) Select the “Generate” button; the report will display
- 6) Export the report using the Menu button at the top right of the table

The Schedule G transcript is available in the Audit springboard under the “Other” tab under “Transcripts.”

When preparing reaudits and adjusted FBOs, auditors should provide a complete explanation of fuel fund additions or reductions in the “Verification Comments,” when necessary.

SPECIAL PROCEDURES FOR GASOLINE SUPPLIERS AND WHOLESALERS**0221.07**

Suppliers and wholesalers of MVF are assigned a Motor Vehicle Fuel Pre-Collection account in addition to their regular sales and use tax account. Such suppliers and wholesalers are required to report pre-collection sales tax on the Motor Vehicle Fuel Pre-Collection return.

All taxpayers holding a Motor Vehicle Fuel Pre-Collection account will have that account examined in conjunction with their related sales and use tax account, even though only one or two quarters may be involved. This procedure will facilitate alignment of the Motor Vehicle Fuel Pre-Collection accounts with their related sales and use tax account and ensure that amounts are being reported properly. The related sales and use tax account number should be noted in the CRM Notes on the Audit springboard.

An FBO may be prepared when an audit is not warranted. When this is done, an FBO should be completed following the same guidelines as outlined above for the audit report.

A penalty of 10 percent of the amount of any prepayment due but not paid shall be added for any supplier or wholesaler who fails to make a timely remittance to CDTFA of the prepayment amounts, plus interest, at the modified adjusted rate per month, or a fraction thereof, from the date the prepayment became due and payable until the date of payment.

A 25 percent penalty rather than the 10 percent penalty mentioned above, shall be added if such failure to timely remit the prepayments was done knowingly or intentionally by the supplier or wholesaler (RTC section 6480.4). This penalty is applied in addition to any other applicable penalties recommended.

MISCELLANEOUS

0222.00

REVENUE AND TAXATION CODE SECTION 7091 — IF THE AUDIT TEAM'S ACTIONS WERE UNREASONABLE

0222.01

RTC section 7091 and similar statutes for special taxes and fees, provide that a taxpayer may be entitled to reimbursement for fees and expenses related to a hearing before the Office of Tax Appeals (OTA) if the OTA finds that the action taken by CDTFA was unreasonable, that is, not substantially justified. Some taxpayers may seek reimbursement for the fees and expenses which they incur during the course of an audit on the basis that CDTFA made unreasonable demands, had no justifiable basis for asserting tax, or conducted the audit in an arbitrary or unprofessional manner. Therefore, it is very important that team members document their actions. Such documentation should be included in the Audit springboard in CRM Notes (see AM section 0207.01). The documentation should include all requests made to the taxpayer and the reason for such requests. It should also include any demands by the taxpayer or issues that arose during the audit process presented by a taxpayer that may cause issues to arise between CDTFA team members and the taxpayer. It is important to keep in mind that CDTFA team members may be required to justify their actions before the OTA at a later date, and, therefore, CDTFA team members must have documentary evidence to support the reasonableness of their actions.

ERROR OR DELAY BY CDTFA OR DMV EMPLOYEE

0222.03

Pursuant to Regulation 1703, subdivision (b)(1)(E), for tax liabilities that arise during taxable periods starting on or after July 1, 1999, CDTFA, in its discretion and as discussed below, may relieve all or any part of the interest imposed on a person by RTC sections 6480.4, 6513, 6591, and 6592.5. Effective January 1, 2002, the CDTFA may, in its discretion and as discussed below, relieve all or any part of the interest imposed by any provision of the Sales and Use Tax Law. Such relief may be granted under either of the following circumstances:

- Where the failure to pay tax is due in whole or in part to an unreasonable error or delay by an employee of CDTFA acting in his or her official capacity.
- Where failure to pay use tax on a vehicle or vessel registered with the Department of Motor Vehicles (DMV) was the direct result of an error by the DMV in calculating the use tax.

An error or delay shall be deemed to have occurred only if no significant aspect of the error or delay is attributable to an act of, or a failure to act by, the taxpayer.

Similar interest relief is available under the Motor Vehicle Fuel Tax Law, Use Fuel Tax Law, Cigarette and Tobacco Products Tax Law, Timber Yield Tax Law, Energy Resources Surcharge Law, Emergency Telephone Users Surcharge Law, Hazardous Substances Tax Law, Integrated Waste Management Fee Law, Oil Spill Response, Prevention, and Administration Fees Law, Underground Storage Tank Maintenance Fee Law, Fee Collection Procedures Law, and Diesel Fuel Tax Law.

Any person seeking relief because of an error or delay by a CDTFA or DMV employee, shall file with CDTFA a statement, under penalty of perjury, setting forth the facts on which the claim for relief is based and any other information CDTFA may require. For this reason, it is very important to document the cause for any delay occurring during the course of an audit. Such documentation should be included in the Audit springboard, CRM Notes (see AM section 0207.01).

AGED AUDITS AND OTHER PERFORMANCE MEASURES**0222.05**

CDTFA management may, from time to time, set or adjust audit program-level performance measurements. These performance measurements are **only** for internal evaluation purposes. For example, aged audits (how many months and/or hours an audit is in process) is one of the performance measurements CDTFA uses to evaluate field offices. These performance and evaluation measurements are not designed, intended, or suitable to be used as decision factors to close an audit in process. These performance measurements may not be used as the sole criteria to close an audit in process.

RTC section 7087 provides that the total amount of revenue collected or assessed shall not be used to evaluate team members or to impose revenue quotas or goals, other than quotas or goals with respect to accounts receivable.

CORRESPONDENCE WITH TAXPAYER'S REPRESENTATIVE**0222.07**

When requested by the taxpayer, copies of all correspondence with the taxpayer must be sent to the representative. When a representative is involved with an audit, petition, or claim for refund, there is an expectation that the representative will receive copies of correspondence sent to the taxpayer even though a specific request has not been made. When in doubt, CDTFA team members should confirm with the taxpayer and/or the taxpayer's representative if copies should be sent to the respective representative.

When correspondence is sent to taxpayers regarding audits, reaudits, petitions, appeals, refunds, compliance issues, collection cases, or other correspondence, CDTFA team members should review the taxpayer files for representative authorizations and ensure that the representative is copied accordingly on all correspondence. All system-generated correspondence, notices, statements, or reports, must also be copied to the taxpayer's representative.

Auditors can check for a specific representative by going to the Audit springboard, Audit tab, Attributes sub-tab.

Auditors should ensure Attributes are updated to provide the current representative. If the taxpayer changed representatives, as noted on a prior CDTFA-82 – *Authorization for Electronic Transmission of Data*, CDTFA-392 – *Power of Attorney*, or other items, auditors should include comments in CRM Notes. This is to document that no copies need to be sent to the prior representative because they are no longer representing the taxpayer.

INTEREST ON CLOSE-OUTS**0222.09**

Interest on a closing period will always be computed from the last day of the month following the end of the quarter in which the close-out/cease occurred, except accounts with a regular due date other than the last day of the month.

URGENT CLOSE-OUTS

0222.11

CDTFAs are authorized to make determinations on close-out/ceases after the date the business is discontinued but prior to the due date of the returns. Determinations should not be made in lieu of obtaining closing returns. Final returns should be secured from the taxpayer, whenever possible. Failure-to-file penalties do not apply on tax determined **before** the due date of the return, even if no return was filed.

The finality penalty applies in the usual manner if the determination is not paid before it becomes final. (RTC section 6565.)

- When the audit report is prepared and the taxpayer files a return and makes payment, processing is as follows: After the determination is made, the remittance is considered a payment on account.
- Before the determination is made, if it is subsequently discovered that a return was filed by the taxpayer and paid in full or in part prior to the date of the determination, such return will be deemed a return to the extent of the amount paid. The determination will be adjusted accordingly.

Penalties for negligence or intentional disregard of the sales and use tax law or authorized rules and regulations (RTC section 6484 penalties) may be asserted for the closing period even though the determination is made before the return is due. Penalties for fraud or intent to evade (RTC section 6485 penalties) will apply in the same manner.

Important Note: Audits on closed out/ceased accounts should **not** be Posted & Billed until or after the actual date the return is due. Doing so would result in interest accruing prior to the due date for the filing period. There may be exceptions to this, but they must be evaluated on a case-by-case basis. One example would be for an account that is in bankruptcy and the Collection Support Bureau must file a claim prior to the due date. If an auditor encounters a case involving a return on a closed-out/ceased account with an urgent need for billing, they should consult their CROS Point of Contact (CPOC), as this would require **monthly, manual interest adjustments.**

**WHERE RETURNS ARE NOT AVAILABLE,
INCOMPLETE OR UNDECIPHERABLE (PAPER RETURNS)**

0222.15

If any return is not available, incomplete, or undecipherable at the time the transcript is exported from the system, enter the amount of tax paid as disclosed by the return or the return payment record in the “Total Tax” column of the transcript. Calculate “Gross Sales” and “Taxable Transactions” based on the amount of tax paid. Place an appropriate symbol (“Note 1”) in front of the calculated measure and key it to an explanation. The amount of tax paid as disclosed by the return payment record may include delinquency charges. The payment of delinquency charges results in Headquarters overstating the “Taxable Transactions” and “Total Tax.” In such cases, auditors should ascertain the amounts reported and the tax paid from the taxpayer’s records.

ACCOUNTS ON MONTHLY REPORTING BASIS

0222.20

When return transcripts are prepared for a sales tax account on a monthly reporting basis, the detail will be shown by month with subtotals for each quarter.

VERIFICATION OF DEBIT AND CREDIT BALANCES

0222.25

When starting an audit assignment, auditors should view the Account springboard to determine if there is a balance. If there is either a debit balance or a credit balance, perform the following to verify debits and credits.

- To verify if a credit has already been **refunded**: Account springboard, Financial tab, Refunds sub-tab or Period springboard, Financial tab, Refunds sub-tab
- To verify **refund** information: Account springboard, Financial tab, Refunds sub-tab or Customer springboard, Task tab, Cases sub-tab (look for Appeal/Claim for Refund case)
- To see whether a tax error has been **billed**: Period springboard, Financial tab, Bill Items sub-tab
- To see the **amount paid**: Period springboard (Look at the Financial Box in the top right, look at the credits line) Financial tab, Payments sub-tab.

If the examination concludes that a tax credit difference has not been refunded, then comments should be made in the “Verification Comments” and the process under “Credit Balance on Account” or “Credit Returns” in the “Reference Guide for Team Members on Handling Refunds and Credits” on the handling of credit balances on accounts should be followed.

Note: Refunds may not be due if the amounts are found to be excess tax reimbursement. Auditors should verify this when examining the taxpayer’s records and appropriate comments should be included.

If, after investigation, it cannot be clearly determined how a tax error was handled, team members should contact the Return Processing Branch for sales and use taxes and the Appeals and Data Analysis Branch (ADAB) for special taxes and fees.