

Welcome...

IMA Northeast Regional Council

8TH ANNUAL FALL CONFERENCE

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The Association of
Accountants and
Financial Professionals
in Business



STOWE & DEGON LLC
CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

The Sales Tax Man (or Woman) Cometh!

- **Surviving A Sales Tax Audit**
- **Why Me????**
- **Why Was My Company Selected For An Audit?**



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Common Sales Tax Audit Rationale:

Audit Cycle:	It's simply your time again.
Industry:	Your Company is in an industry that the state is targeting.
Automation:	A data warehouse program convinces the state that you have nexus in that state. Beware Fulfillment by Amazon (FBA)!
Audit by Association:	A supplier or customer was audited and your company was red flagged!
Informant Calls:	Informant calls come from disgruntled or former employees, competitors or estranged spouses. Informant calls provide the DRS with regular information regarding tax or bookkeeping practices used in an attempt to evade the payment of taxes.
Random Chance	An auditor randomly noticed your business location and jotted down your name. New Jersey has "nexus agents" sitting in unmarked cars along the New Jersey border.
Exchange Agreements:	Exchange Agreements with the IRS and other states. The DRS shares information with the IRS concerning a taxpayer's gross sales or receipts. AND the IRS has "stepped up" their agreements with the States. The IRS is now sharing "RAR" Reports with the states. Connecticut, particularly shares information with the neighboring states of Massachusetts and Rhode Island.



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What should I expect from an audit?

- The Audit Process: To start preparing, make sure you understand the audit process, the information that will need to go back and forth between your organization and the auditor, and the time required for each step in the process:
 - ♦ Request for information
 - ♦ Preliminary Schedules
 - ♦ Revised Schedules
 - ♦ Final schedules and assessment
 - ♦ Appeals

Anticipate taking at least a month to prepare for the audit; the number of hours will vary, but plan to spend at least 40 to 60 hours. For small companies, an audit can generally be wrapped up in a few weeks. For mid-size companies, an audit can be open for a good 6 months. For the largest taxpayers, audits can drag on for years. There are times when as one audit period closes, it's time to start the next period.

What Kind of Documentation Will the Auditor Need? General Audit Procedures:

- **Exemption Certificates:** In a business that has a permit to make retail sales, the agent will normally begin reviewing sales. After verifying sales, the agent will attempt to verify deductions, for the entire audit period or a test period if one has been agreed to. The two most common deductions are sales for resale and interstate sales. In reviewing these two areas, the agent will want to review the sales invoices as well as other documentation. In examining the sales for resale, resale certificates will be examined to determine whether they are properly completed and that the sale in question is covered by the certificate.

What Kind of Documentation Will the Auditor Need?

General Audit Procedures:

- **Fixed Asset Purchases:** After exempt sales are verified or if the audit involves a company that is not a retailer, the agent will usually examine capital assets in detail (for all years under audit) and trace them back to the original invoice. Often the largest (\$) assessments in a sales/use tax audit come from the “use” tax portion of the audit. Those purchases where sales tax was not “charged” on the invoice (billed to you) and you (the buyer) did not self-assess use tax.

What Kind of Documentation Will the Auditor Need? General Audit Procedures:

- **Non-Asset Expense Purchases**: Your day-to-day expenditures. One method for shortening the audit time is the use of a test period. This is especially useful in the sales tax area for a business that has a large volume of invoices. When the test period is used, the results of the audited test period are applied to the total for the entire audit period. Often a test period will result in a lower tax liability than a detailed review of all periods. **BUT BE CAREFUL!!** Make sure the test period is a “fair” representation of your purchases!

What Kind of Documentation Will the Auditor Need? General Audit Procedures:

- **Detail of Sales and Use Tax Returns you have filed**. Copies of your Federal Returns for the audit period. Copies of your State Tax Returns. Copies of 1099's you have issued. Why?

What Kind of Documentation Will the Auditor Need? General Audit Procedures:

- Statute and Waiver Issues: Auditors frequently request that you sign a waiver that “interrupts” the running of the statute of limitations for the audit period.

The statute is the period of time that either the DRS or the taxpayer can make amendments to the audit. As a result, the waiver holds the statute open to allow time for the audit to be completed without losing periods to the statutes.

REMEMBER:

This waiver also gives companies additional time to gather any “missing” exemption certificates!

The Auditor has completed the “fieldwork” and has issued *preliminary* workpapers with an assessment amount! Is that it?

Do I have to “live” with that assessment?

RELAX - ---BREATH!

Review the preliminary work papers carefully! Go “line item by line item”!



This is your opportunity to still “prove” to the auditor that you should not be assessed tax on a particular invoice. Why? How?

- Check for documents related to the invoices being assessed. Ensure the tax wasn't paid in a separate billing or the item wasn't returned. Also double check to see if use tax was paid, if the vendor didn't charge tax.
- Exemptions: It is important to know whether any items getting assessed are actually tax-exempt. For an example: for manufacturers, in particular, the taxability of a purchase can get very complicated!
- Correct figures: Make sure the auditor's figures are correct!
- Vendors: Did any of your suppliers get audited for the same period and get tax assessed on the same purchases? Remember: sales or use tax is only paid once. Prior to the beginning of the audit, send out XYZ letters to your vendors. ***Please see additional hand-out.***

Final Schedules and assessment: Once you agree (or not agree) with the auditor's findings, you will receive a final assessment called a Proposed Assessment. You will still have the opportunity to "Appeal the Assessment".



MOST OF ALL – Learn from Your Mistakes!

Audits are a necessary part of business and an opportunity to examine your current processes for liabilities. Once an audit is complete – learn from your mistakes and implement procedures to correct those mistakes.



PERFECTION
always
starts with
MISTAKES