

# SALES TAX SOLUTIONS & CONSULTING

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## ARE YOU READY FOR AN AUDIT?

Most businesses think they are ready but really they are not. An audit is really nothing more than a review to verify that a business is complying with state sales tax laws, or that's what it should be. States employ sales tax auditors to increase revenue not just to verify enforcement of laws. That may seem unfair, and many auditors would probably object to that statement, but actions speak louder than words.

Here is a simple tool to help you prepare for an audit.

### AUDIT CHECK LIST:

1. \_\_\_\_ First and foremost contact a sales tax professional. Typically businesses that try going through an audit alone end up paying higher assessments, sometimes significantly higher, than those that hire a sales tax professional. Don't go it alone.
2. \_\_\_\_ Review audit document check list provided by auditor. Obtain all relevant documents for the assigned audit periods. If you are not under audit use the following:
  - a. \_\_\_\_ Bank statements/bank register
  - b. \_\_\_\_ Sales reports/records
  - c. \_\_\_\_ Sales invoices
  - d. \_\_\_\_ Exemption certificates
  - e. \_\_\_\_ General Ledger reports/ detail purchase transactions
  - f. \_\_\_\_ Purchase invoices
  - g. \_\_\_\_ Asset invoice documents
  - h. \_\_\_\_ Sales Tax returns and associated documents used to prepare.
  - i. \_\_\_\_ Federal Tax Return.
3. \_\_\_\_ Verify Gross sales on Federal Income tax return and Gross sales on sales tax returns equal or are relatively close. Any variances must be explained.
4. \_\_\_\_ Verify tax was due and paid on all asset purchases.
  - a. Any asset in which tax was not due must be explained.
5. \_\_\_\_ Verify all sales documents are present. Any missing invoices, missing invoice numbers, or unused invoices numbers are identified and clearly explained.
6. \_\_\_\_ Verify all exempt sales have a properly completed exemption certificate with it.
7. \_\_\_\_ Verify all purchase documents are present.
8. \_\_\_\_ Verify tax due and paid on all purchase documents.
  - a. Explain all invoices which tax was not paid.
9. \_\_\_\_ Verify total cash deposits and compare them to gross sales, explain any variances.
10. \_\_\_\_ Review your taxpayer rights. Generally these can be found on the state's website.
11. \_\_\_\_ Contact a sales tax professional, see #1.

## **WHAT TO EXPECT DURING AN AUDIT:**

Although every audit is a bit different there are some general things that you can expect during each audit. Auditors have considerable control and wide latitude of their audits but they must follow some basic procedures.

- The auditor will first contact you by phone to set up a potential audit date.
- You should receive a letter indicating you are being audited, the periods under audit, when and where the audit will take place, and some general documents about your rights.
- The auditor will review all assets purchased during the audit period.
- The auditor will review sales and purchase records. They may choose a sample period to review depending on the volume of documents available. The samples for sales and purchases may be different.
- The auditor will review and analyze all other documents provided.
- The auditor may contact your vendors and request “third party verifications” to verify purchase records.
- The auditor will ask a lot of questions.
- The auditor will want to conduct a sit visit if the audit is taking place at your representative’s offices.
- When the auditor is finished reviewing your records they will issue or provide an “Exception Report” or a list of items they either want more documentation, explanation, or are missing.
  - You then need to provide or they will be taxed.
- When all exceptions have been dealt with or the auditor decides there is no further reason to discuss the open issues they will issue a preliminary assessment. NYS AU-346.
  - You then have a limited time to respond, protest, the assessment. In New York it is generally 30 days.
- At some point the auditor will issue a final assessment letter will be issued. NYS Notice of Determination.
  - You then have 90 days to respond, protest, or agree and pay.
    - The first form of protest is called a Conciliation conference. The Divisions Bureau of Mediation and Conciliation Services (BCMS) will “mediate” between you and the auditor on any open issues. Generally the Conferee will agree with the auditor unless you provide clear and substantial evidence to support your argument.
      - The Conferee will issue a “Determination” based on any agreement negotiated with the auditor, or if unresolved the auditor’s original assessment.
    - You then have 30 days to request a tax hearing (the second form or protest) with an Administrative Judge. At this point you should be contacting an attorney or your representative should suggest one.

## **INADEQUATE RECORDS:**

Inadequate records are defined by the New York State as:

### **“When your records are considered inadequate**

Your records may be considered inadequate if:

- they don’t verify sales receipts,
- they don’t verify whether those receipts are subject to sales tax,

- they don't provide details of each individual transaction (summary reports and daily summary or “Z” tapes are not sufficient),
- they don't verify the taxable status of your purchases,
- they don't show that your business's purchases correlate to your business's sales, it's not possible to conduct a complete audit using those records, you fail to make your records available to the auditor,
- they are not in a form that can be audited by the Tax Department, or an evaluation of your accounting system discloses that the system does not provide adequate internal control procedures which assure the accuracy and completeness of the transactions recorded in the books and records (e.g., the lack of sequentially numbered invoices or guest checks, or the lack of dates on receipts).

### **Consequences of inadequate records**

If your records are considered inadequate, you may:

- be subject to an estimated audit methodology to determine any additional taxes due,
- be subject to penalties and interest if additional tax is found to be due,
- be subject to criminal penalties if you willfully failed to maintain proper records, and
- Have your *Certificate of Authority* suspended or revoked.

***What does this mean?*** NYS can ***ESTIMATE*** sales. They do not have to be accurate. You do! They have to be reasonable, and they define what is reasonable. You must provide “clear and convincing” evidence to prove them wrong.

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