

Memorandum

To : Ms. Kristine Cazadd
Executive Director (MIC 73)

Date: May 8, 2012

From : Jeffrey L. McGuire, Deputy Director
Sales and Use Tax Department (MIC 43)



Subject : Board Meeting May 30-31, 2012

Item N: Administrative Agenda

Proposed Audit Manual Revisions:

Sections 0442.00, *Cooperative Audits*, and 0806.40, *Undercover Pour Test*

In accordance with the established procedures for audit and compliance manual revisions, I am submitting the proposed new Audit Manual (AM) Chapter 4 section 0442.00, *Cooperative Audits*, and revisions to AM Chapter 8 section 0806.40, *Undercover Pour Test*.

The proposed revisions, which incorporate current policies and procedures, have been reviewed and approved by SUTD management, provided to Board Members, and posted at <http://www.boe.ca.gov/sutax/pmr.htm> to solicit comments from interested parties. There were no comments received from interested parties.

The new AM section 0442.00 and revised AM section 0806.40 are attached for your reference. We request your approval to forward it to the Board Proceedings Division for placement on the next Administrative Agenda as a consent item. If you have any questions, please let me know or contact Ms. Susanne Buehler at 324-1825.

JLM:nvm
Attachment

Approved:


Ms. Kristine Cazadd
Executive Director

Item N
5/30-31/2012

COOPERATIVE AUDITS

0442.00

OVERVIEW

0442.01

An audit transfer without transfer of control occurs in interdistrict cooperative audits where the controlling district office assigns a portion of an audit or a related audit to one or more cooperating district offices. In this case, the controlling district office consolidates the audit findings and transmits the completed audit to ADRS.

An interdistrict cooperative audit is an audit with participation by auditors from more than one district office. It occurs under the following conditions:

- A district office starts an audit and transfers that audit to another district office for completion.
- A portion of an audit or a related audit is assigned to another district office.

Where the taxpayer's or related account's records are located in more than one district office, the audit is coordinated by the controlling district office. Generally the controlling district office is in the best position to obtain information with regard to the overall functioning of the operations of the accounts involved. In most cases, the DOA is the controlling district.

RESPONSIBILITIES OF THE CONTROLLING DISTRICT OFFICE

0442.02

The controlling district office assigns a portion of an audit or a related audit to cooperating district offices, consolidates the findings and transmits the completed interdistrict cooperative audit to ADRS. In addition, the controlling district office is responsible for the following:

1. General review to verify that the cooperating district offices followed the procedures outlined and made their respective portion of the audit in a consistent and uniform manner.
2. Completion of the final Form BOE-204, *Interdistrict Cooperative Audit – Audit Verification*.
3. Conducting an exit conference to discuss consolidated audit findings.
4. Transmittal of the completed audit to ADRS.

Instructions to cooperating district offices should contain sufficient detail to ensure all phases of an audit are handled uniformly and for the same audit period. The anticipated degree of difficulty or complexity of an audit must be taken into account when providing cooperating district offices such instructions.

Assignments to cooperating district offices are transmitted by Form BOE-204. Form BOE-204 should include specific instructions including the following information:

1. A brief description of the taxpayer's operations.
2. The name and phone number of the person to be contacted at the taxpayer's office.
3. Audit procedures that have been or will be performed by the controlling or cooperating district offices.
4. Specific verification instructions, such as test periods. The cooperating district office should follow these instructions unless there is a compelling

reason why this cannot be done. When the cooperating district office finds that any of the instructions are not appropriate, it should discuss alternatives with the controlling district office.

5. Informative matter that may pertain to unusual transactions, such as areas of potential error. This may include information on the taxability of fixtures and equipment when the audit is a close-out, selling prices, type of clientele, etc.
6. Information pertaining to Form BOE-122, Waiver of limitation.

RESPONSIBILITIES OF THE COOPERATING DISTRICT OFFICE **0442.04**

A cooperating district office will give priority to requests from a controlling district. It must follow the specific instructions as expeditiously as possible. Any significant deviations must be discussed with the cooperating district. In addition, the cooperating district office is responsible for the following:

1. Discussion of the audit findings with the local representative of the taxpayer, with copies of AWP's provided to the representative.
2. Review of the work assigned to and completed by the cooperating district office. It is the responsibility of the cooperating district office reviewer to ensure that the partial audit is accurate and complete in the same manner as a completed audit report. The reviewer should also ascertain that the partial audit was completed as instructed by the controlling district office.
3. Preparation of Form BOE-204 (include Auditor ID, Class, Name and hours).
4. E-mail notification to controlling district's Audit Control of the completed cooperative audit.

Interdistrict AWP's must conform to procedures set forth in AM Chapter 3, *Audit Working Papers*. In addition, the AWP's must include a summary of differences established by each cooperating district office and the letters identifying the district office must precede the index on the AWP's.

UNDERCOVER POUR TEST

0806.40

The prior approval of the District Principal Auditor or Branch Office Supervisor is required for an undercover pour test. The auditor is encouraged to perform an undercover pour test when the taxpayer has indicated on the Bar Fact Sheet (AM section 0802.15) a pour size that exceeds the 1.5 ounces for mixed drinks, over-the-rocks, and straight shots, and the pour size cannot be verified by other means.

When an undercover test is conducted, a complete report must be prepared and included in the audit working papers. This report should include the date and time the test was conducted, the name of the bartender, the approximate number of customers present, the type of drink, how it was measured, and other pertinent information. When possible, such tests should be done when a full-time bartender is on duty that has been employed for a significant length of time. In addition, if possible, the tests should be conducted during a period (i.e., hour) that is most representative of the business activity. This may entail conducting the test after normal work hours.

To assist the auditor, the procedure to conduct an undercover pour test is described in Appendix C. Unless an employee of the Department of Justice or the Department of Alcoholic Beverage Control (ABC) accompanies the auditor(s), the taxpayer or bartender may legitimately refuse to let the alcohol be taken off the premises for testing. The auditor may contact the Department of Justice or ABC to obtain their assistance or information (e.g., reports on any prior undercover tests).

After an undercover test is conducted, the results of the test should be discussed with the taxpayer and/or bartender at the time it is completed. Since the undercover pour test is designed to capture the taxpayer's standard pour for use in the mark-up calculation and to project sales, it is important when analyzing the results of the test for the auditor to consider that the pour size may vary according to the type of drink, the proof of the alcohol, and the temperature of the drink. ~~The auditor should also keep an open mind and use good judgment when the taxpayer asserts that their regular pour size is larger than the test results.~~ The pour size This may also vary occur when the taxpayer serves mainly ~~regular, repeat customers or there are other influencing variables, such as tips received or~~ those discussed in AM section 0802.20. Auditors should also keep in mind that tipping may influence the size of the pour and auditors are instructed to provide a reasonable tip when paying for the first round of drinks. The audit working papers should document that a tip was given during the undercover pour test.