



STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION

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January 17, 2014

Sales Tax Reduction Specialists
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To Whom It May Concern:

As a preface to this letter, I would like to express my sincere condolences, on behalf of myself and my staff, on the passing of Mr. Abe Golomb of your office. Several of us in the Taxpayers' Rights Advocate Office have known Abe for a great many years, and appreciated his abiding passion for assisting his clients and protecting their rights, as well as his efforts to work with the Board of Equalization in improving the experience of all California taxpayers.

This is a follow-up to Mr. Golomb's presentation at the May 22, 2013, Taxpayers' Bill of Rights Hearings held in Sacramento. In his presentation he expressed his concerns about the Board of Equalization's (BOE's) Statewide Compliance and Outreach Program (SCOP) undertaking audit functions and improperly discussing tax matters with taxpayers' employees when they visit the business, rather than with the taxpayer. My office has been researching these concerns and I wanted to let you know my thoughts on the matter.

The points Mr. Golomb covered in his presentation to the Board on May 22, 2013 and in his written correspondence of May 17, 2013 (copy attached) can be summarized as follows:

1. SCOP staff members question taxpayers' employees about sales tax matters; however, employees may not be completely knowledgeable about their employers' tax procedures.
2. SCOP staff members intimidate taxpayers by threatening them with a sales and use tax audit, and refer taxpayers for audit if employees do not answer their questions correctly.
3. SCOP staff members have access to taxpayers' state income tax returns. If the gross receipts reported on the income tax returns do not exactly match the reported sales on the sales tax returns, taxpayers or their employees are asked to explain the discrepancy, even though such discrepancies may not mean that a taxpayer has any sales tax exposure.
4. SCOP is going beyond the original intent of the program, which was to make sure that taxpayers have the appropriate permits and licenses, by attempting to perform "audits" during their short visits to the taxpayers' business locations. This is a problem because, in general, SCOP staff members do not have adequate audit background.

In researching Mr. Golomb's concerns, we have focused our attention on new Compliance Policy and Procedures Manual Chapter 10 (CPPM-10), *Statewide Compliance and Outreach Program - SCOP* (see www.boe.ca.gov/sutax/manuals/cppm_10_final.pdf), which is designed to provide comprehensive guidance to SCOP staff on their duties and the expectations of the program.

Mr. Golomb's specific concerns are addressed or referenced in a number of CPPM-10 sections, as described below – all page number references are to CPPM-10. I have included TRA Office comments in each area of discussion.

Questioning Employees about Sales Tax Matters

The TRA Office has shared Mr. Golomb's concern about this matter, and based on our suggestion, the following text was added to *Conducting the Visit* on page 4-3:

Upon entering the business, the SCOP representative should make reasonable attempts to speak to the business owner or manager instead of an employee, due to the following issues:

- *The employee may feel intimidated.*
- *The employee may not be able to provide accurate information about the business operations, customers, vendors, method of recording sales or reporting tax, etc.*
- *Employees are not routinely authorized to discuss confidential information about business' tax reporting.*
- *The business owner or manager may receive inaccurate or incomplete information from the employee about matters discussed during the SCOP visit.*

Comments: The prohibition against improperly discussing sales and use tax matters with employees is clearly stated in CPPM-10. Further emphasis in training may be needed if SCOP representatives are not adhering to this prohibition.

Referring the Business for Audit

In *Requesting Business Records* on page 4-5, SCOP staff are cautioned, "SCOP staff should not threaten or intimidate business owners with an audit."

However, SCOP staff are directed to refer the account for audit if deemed appropriate. As detailed in *Existing Permits (Amended Returns/Audits/Field Billing Orders)* on pages 1-3 through 1-4, SCOP staff are expected to analyze businesses with valid seller's permits for proper reporting by comparing the business operations to information reported on the business' sales and use tax returns. If a business appears to have a reporting discrepancy, SCOP staff members are to further research data in the BOE's records along with third party data. At this point, if a potential discrepancy is noted, SCOP staff must discuss it with the business owner, provide supporting evidence, and allow the business owner to provide documents or information supporting the reported amounts.

If supporting documentation is not provided, the business owner will be given the opportunity to file amended returns. If amended returns are not provided or are still questionable, SCOP staff may proceed with further action, such as recommending the issuance of a Field Billing Order (FBO) or referring the account for audit.

Detailed guidance for referring the account for audit is provided in *Audit Memorandum of Possible Tax Liability (BOE-1164) Procedures* on pages 8-1 through 8-5.

Comments: Threats and intimidation violate a taxpayer's rights and have no place in BOE staff communication with taxpayers; however, referring a business for audit is often an appropriate action for SCOP staff to take, but only after all steps are taken as outlined above.

Use of Data from State Income Tax Returns

As noted above, review of third party data (such as income tax returns, Employment Development Department information, Accurint or LexisNexis information, and other available third party information) is undertaken in addition to review of BOE information (such as registration records, reported sales, and claimed exemptions) when the business appears to have a reporting discrepancy.

Comments: We understand that SCOP policy is that analysis of income tax returns is performed by experienced auditors on SCOP teams.

Performing “Audits”

I understand that Mr. Golomb’s concern about SCOP staff performing “audits” refers to SCOP undertaking audit-like functions, such as analyzing records and business operations to draw conclusions on whether taxable sales have been under-reported, as opposed to performing full audits as detailed in the BOE’s Audit Manual. Mr. Golomb stated in his letter:

The Sales and Use Tax Department has an existing sales and use tax audit program with trained sales and use tax auditors . . . The Sales and Use Tax Department does not need another separate “audit staff” that are attempting to perform sales and use tax audits in five to ten minutes.

Several sections in CPPM-10 delineate SCOP’s purpose. The *Introduction* section on page 1-1 states in part:

The purpose of the Statewide Compliance and Outreach Program (SCOP) is to educate business owners regarding their sales and use tax reporting responsibilities, make sure businesses have the required state tax and fee permits, provide a field presence for the Board of Equalization (BOE) and address the tax gap that exists between sales and use tax revenue due under existing laws and the actual amount that is reported and paid. Many businesses that comply with the law and pay their taxes are being competitively undercut by the underground economy. . . .

The main function of a SCOP representative is to provide outreach, educate and advice [sic] business owners regarding the sales and use tax law. As areas of non-compliance are identified by SCOP staff, potential underreporting referrals could be generated. However, a SCOP representative’s performance will not be rated upon the basis of recovery, which is prohibited by law.

Existing Permits (Amended Returns/Audits/Field Billing Orders) on pages 1-3 through 1-4, referenced above, further explains SCOP’s purpose:

Although a business may be operating with a valid seller’s permit, this should not curtail or diminish the importance of a SCOP business visit. Another important component of the program is to review businesses operating with valid seller’s permits to make sure business owners understand their tax responsibilities and are reporting properly. This also provides an opportunity for the business owners to ask sales and use tax related questions to [sic] a BOE representative. . . . Businesses with valid seller’s permits are to be analyzed for proper reporting by reviewing the business operations and making a comparison to the information reported on their sales and use tax returns. . . .

Requesting Business Records on page 4-4 touches on some of Mr. Golomb’s concerns about the role of the SCOP investigator, such as the extent of any review of records that should be done and the requirement to document what led SCOP staff to conclude there is potential underreporting:

*It is not intended for SCOP staff to request business records at the time of the business visit. In general, SCOP staff **should not** request invoices, financial statements, receipt books, tax returns, or similar documents during a business visit. However, if a business owner questions whether they are collecting and reporting correctly, SCOP staff may offer to review records to make sure the business is in compliance with the sales and use tax laws and regulations. This should only be done in situations where the business owner is willing and open to presenting records during a business visit.*

If during a business visit, the SCOP representative recognizes a potential underreporting issue and believes records may need to be reviewed to determine what course of action to take, attempts should be made to document as much information as possible about what led the SCOP representative to this conclusion (i.e. size of location, # of employees, type of product sold, # of locations, # of bays, # of tables, prices, questionable exemptions based on the nature of the business, conversations held with the business owner, supplier information, hours of operation, etc.). The SCOP representative may attempt to schedule a future appointment with the business owner and BTA I [Business Taxes Administrator I], BTS I [Business Taxes Specialist I], or designee.

When requested by the taxpayer to work directly with their representative, such as a bookkeeper, CPA, or attorney on subsequent account inquiries, SCOP staff should honor that request. In addition, when requested by the taxpayer, copies of all correspondence with the taxpayer should also be sent to the representative. . . .

Existing Accounts with Proper Seller's Permits on page 4-5 provides guidance on specific factors staff should focus on while observing the business operations for the purpose of comparing the observed operations to the sales reported by the business to the BOE.

On occasion, the preparation by SCOP of a Field Billing Order may be deemed appropriate, as described in *Field Billing Order (FBO) Procedures* on page 9-1:

In general, FBOs should only be assessed when SCOP staff has exhausted all other means to gain voluntary compliance and/or it is impossible or impractical to obtain amended returns from the business owner. In addition, FBOs should only be used in circumstances where a liability is disclosed and it has been determined that a more in-depth audit investigation is not warranted. . . . Only a SCOP BTS I has the ability to issue FBOs. . . . If the business owner disagrees with the FBO, the normal appeals process is followed. The business owner will have all the rights afforded to him as if the FBO had been issued during the normal audit process. The BTA I should be responsible for conducting the 10-day meeting. . . .

Comments: The BOE has designed SCOP as a tool for reducing the tax gap, not only by ensuring business owners are properly permitted/licensed and educated on the correct application of tax to their business operations, but also by checking to see that business owners are reporting correctly.

SCOP has great potential for enhancing taxpayer education for business owners who are properly permitted and helping to ensure voluntary compliance. In situations where it is obvious the business owner did not correctly report because he or she did not understand the correct application of the sales and use tax law to the business operations, and the amount of the understatement is readily ascertainable, the most efficient course for both the taxpayer and the state is for SCOP staff to obtain amended returns, or if that is not possible, to issue a FBO.

If an audit is deemed appropriate, it will be assigned to an experienced auditor on the SCOP team, unless the books and records are outside the SCOP team's territory, in which case it will be referred to a district office. The SCOP auditor conducts the audit using standard policies and procedures found in the Audit Manual.

My staff and I have been working closely with the Sales and Use Tax Department to explore the extent to which Mr. Golomb's concerns about SCOP audit functions may be valid. Although SCOP policies and procedures have evolved over the years, the current practice is for SCOP investigators to be overseen and guided by leads who are experienced auditors (Business Taxes Specialist I's). We have been assured that no records are requested or discussions regarding possible under-reporting are held without the guidance, approval, and participation of the lead and/or supervisor (Business Taxes Administrator I).

The TRA Office will continue to monitor SCOP policies and procedures and to make suggestions for improvement as those needs come to our attention. In addition, arrangements have been made for my staff and I to participate in statewide SCOP training sessions – we will provide training on SCOP staff's role in ensuring the rights of taxpayers are protected and on how the TRA Office interacts with BOE staff and management as a resource on rights issues.

I appreciated Mr. Abe Golomb taking the time to bring his concerns about SCOP functions to the Board's attention this year, as well as the other numerous occasions on which he shared his insights and suggestions with the Board.

Sincerely,

Todd C. Gilman
Chief, Taxpayers' Rights and
Equal Employment Opportunity Division

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Enclosure

cc (with enclosure):

Honorable Jerome E. Horton, Chairman
Honorable Michelle Steel, Vice Chair
Honorable Betty T. Yee, Board Member, First District
Senator George Runner, Board Member, Second District
Honorable John Chiang, State Controller
Ms. Marcy Jo Mandel, Deputy State Controller
Ms. Cynthia Bridges, Executive Director, MIC 73
Mr. Randy Ferris, Chief Counsel, MIC 83
Mr. Jeffrey McGuire, Deputy Director, Sales and Use Tax Department, MIC 43
Mr. David Gau, Deputy Director, Property and Special Taxes Department, MIC 63
Mr. Robert Tucker, Assistant Chief Counsel, Tax and Fee Programs Division, MIC 82
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Ms. Susanne Buehler, Chief, Tax Policy Division, MIC 92
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