



STATE BOARD OF EQUALIZATION

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March 16, 2005

VIA INTERNET

Dear Interested Party:

The Sales and Use Tax Department is proposing to revise Audit Manual Chapter 4, *General Audit Procedures*, by incorporating the changes described below. The full text of the changes, displayed on the following pages, is provided for the convenience of interested parties who may wish to submit comments.

The proposed changes are:

- **AM Section 0401.25.** Provides that without a subpoena or the taxpayer's permission auditors may not access files to which the taxpayer has "forbidden" access.
- **AM Section 0401.35.** Instructs auditors how to handle suspected money laundering activities.
- **AM Section 0402.25.** Explains when auditors should ask the taxpayer to sign form BOE-146, Waiver of Credit Interest.
- **AM Section 0403.05.** Updates the term "subdistrict" with "branch office."
- **AM Section 0403.10.** Adds IRIS screens and the Internet as sources for obtaining taxpayer information before starting the audit.
- **AM Section 0403.12.** Advises auditors to discuss how summary records are maintained during the initial meeting with the taxpayer.
- **AM Section 0403.16.** Explains Board policy on contact with taxpayers represented by counsel.
- **AM Section 0404.10.** Refers auditors to new Exhibit 11 for sample audit programs for general retailers, manufacturers and wholesalers, and liquor stores. Deletes last paragraph explaining whether testing should be expanded or completed. The information is out of context in this section and is already included in AM sections 0405.15, Short Tests, and 0405.20, Use of a Test Basis.
- **AM Section 0405.23.** Explains that separate forms BOE-472, Audit Sampling Plans, should be completed for each audit area tested.
- **AM Section 0405.27.** Explains when auditors may request records directly from a taxpayer's financial institution.

- **AM Section 0405.33.** Updates titles for the reorganization of the Sales and Use Tax Department.
- **AM Section 0406.60.** Updates concessionaire section for May 30, 2001 revisions to Regulation 1699, *Permits*.
- **AM Section 0408.25.** Refers auditors to Compliance Policy and Procedure Manual section 830.005 for specific examples of how penalty and interest may apply to use tax due on vehicle purchases.
- **AM Section 0408.27.** Advises auditors that certain property tax records can be useful as another source of asset information.
- **AM Section 0409.51.** Explains that new form BOE-504-BPA, Cover Letter for Special Printing Aids XYZ Letter, is to be sent with special printing aid XYZ letters. Provides that XYZ responses should be included in the audit working papers as subsidiary schedules.
- **AM Section 0409.63.** Provides that when the Board plans to assess tax on a purchaser for an improperly given resale certificate, the auditor must make a copy of the resale certificate given by the purchaser to the seller.
- **AM Section 0410.10.** Replaces the term “remittance advices” with “other documents demonstrating direct payment by the United States” to conform to the March 23, 2004 revisions to Regulation 1614, *Sales to the United States and Its Instrumentalities*.
- **AM Section 0410.15.** Provides that the General Services Administration “GSA SmartPay” program is effective through November 28, 2008.
- **AM Section 0411.25.** Updates titles for the reorganization of the Sales and Use Tax Department.
- **AM Section 0414.12.** Advises auditors to send a copy of returned BOE-52, Certificate of Verification of Out-of-State Delivery, to the Audit Support Unit when forms are received from Arizona, Mexico, New Mexico, Oklahoma, Texas or Utah.
- **AM Section 0417.07.** Explains that form BOE-52-L2, Notice of Pending Refund of Excess Tax Reimbursement can be used as an acknowledgement by customers of the retailer’s intention to refund excess tax reimbursement.
- **AM Section 0419.15.** Deletes bullet section stating that a purchaser of receivables can not claim a bad debt deduction. Refers auditors to new AM section 0419.17 for information on lender bad debts.
- **AM Section 0419.17.** Explains audit procedures for bad debt deductions claimed by lenders.
- **AM Section 0419.20.** Updates the section to reflect the Board’s policy of generally not questioning the validity of tax imposed by another state.
- **AM Section 0419.30.** Updates Property Tax Section name.

- **AM Sections 0419.35 and 0419.40.** Deletes sections. The information is included in AM chapter 6, *Vehicle, Vessel, and Aircraft Dealers* and should not be duplicated in AM chapter 4.
- **AM Section 0419.45.** Explains audit procedures for section 6388 and 6388.5 exemptions for new and remanufactured trucks, truck tractors, trailers and semitrailers.
- **AM Section 0419.50.** Updates procedures for verifying tax exemption cards with the U.S. State Department, Office of Foreign Missions.
- **AM Section 0419.55.** Deletes section. The information is included in AM chapter 8, *Bars and Restaurants* and should not be duplicated in AM chapter 4.
- **AM Sections 0431.00, 0432.00 and 0433.00.** Updates various sections in accordance with the change in the point of prepaid sales tax on fuel. Effective January 1, 2002, prepaid sales tax is imposed on the first removal of fuel at the terminal rack or upon entry into California.
- **AM Section 0432.45.** Explains the time periods the fuel exemption for watercraft common carriers was in effect, discontinued and then reinstated.
- **AM Section 0435.00.** Explains audit procedures under the reinstated Managed Audit Program.
- **Exhibit 1.** Revises boxes 14 and 15 to show that the audit review function has been transferred from Headquarters to the field offices.
- **Exhibits 2, 3, 5, 9, 12 and 13.** Replaces the following forms with new versions:
 - BOE-1164, Audit Memorandum of Possible Tax Liability
 - BOE-1032, Information on Out-of-State Retailers
 - BOE-472, Audit Sampling Plan
 - BOE-504-CPA, Statement Concerning Property Purchased without Payment of California Sales Tax – Special Printing Aids
 - BOE-504-CFS, Statement Concerning Property Purchased without Payment of California Sales Tax (feed, fertilizer)
 - BOE-837, Affidavit for Section 6388 or 6388.5 Exemption
 - BOE-526, Managed Audit Program Participation Agreement

Adds new form BOE-504-BPA (cover letter for form BOE-504-CPA).

- **Exhibits 4 and 6.** Updates titles and section names for the reorganization of the Sales and Use Tax Department.
- **Exhibit 11.** Deletes form BOE-379-A exhibit. Form was related to section 0419.40 that was deleted. Information regarding exempt sales of aircraft is in AM chapter 6, *Vehicle, Vessel, and Aircraft Dealers*.

Adds sample audit programs for general retailers, manufacturers and wholesalers, and liquor stores.

- **Exhibit 14C.** Adds form BOE-52-L2, Notice of Pending Refund of Excess Sales Tax Reimbursement as an exhibit.
- **Exhibit 15.** Adds sample memo to be sent regarding suspected money laundering activity. Related to AM section 0401.35 revisions.

If you have any comments or suggestions *related solely to the proposed changes described above*, you may contact the Department at AM.RevisionSuggestions@boe.ca.gov, or you may submit your suggestions to:

Lynn Whitaker
Sales and Use Tax Department
State Board of Equalization
P.O. Box 942879
Sacramento, CA 94279-0044
Fax: (916) 322-0187

All comments regarding the proposed changes must be received by **May 16, 2005** in order to be considered by staff. Thank you for your consideration. I look forward to your comments and suggestions.

Sincerely,

/s/ Jeffrey L. McGuire

Jeffrey L. McGuire
Tax Policy Division
Sales and Use Tax Department

AUTHORITY — EXAMINATION OF RECORDS & ISSUANCE OF SUBPOENAS 0401.25

Government Code sections 15618 authorizes an auditor to examine records of the taxpayer and of persons doing business with the taxpayer. Revenue and Taxation Code section 7054 provides additional authority for the examination of records pertaining to the sales and use tax. Similar provisions are found in other tax and fee programs administered by the Board.

Government Code section 15613 authorizes the Board to issue a subpoena for the attendance of witnesses or to produce books, records, accounts and papers.

By developing a good working relationship with the taxpayer, an auditor should rarely have to rely on a subpoena as a means of obtaining records. ~~However, if~~ a taxpayer refuses to make requested records available, or places undue restrictions or conditions on their use, the auditor's supervisor should be consulted immediately. Once notified, the supervisor should request the necessary records from the taxpayer and explain to the taxpayer, either verbally or in writing, the relevance of the records being requested. If the taxpayer continues to deny access to necessary records, the District Principal Auditor should ~~prepare a written request~~ send a letter to the taxpayer detailing the specific records being requested and the relevance of the records, including a reasonable compliance date. If the taxpayer fails to comply with ~~the~~ this request, the District Administrator may request the issuance of a subpoena duces tecum based on the specific records ~~refereneed-detailed~~ in the District's previous letter.

Without a subpoena or the taxpayer's/representative's permission, under no circumstances should the auditor take it upon herself/himself to review, schedule, photocopy, or otherwise access information from files to which the taxpayer has "forbidden" access.

Requests for the issuance of subpoenas must be made by District Administrators and submitted to the Chief of Field Operations or the Collections and Third District Operations Manager for approval and forwarding to the Legal ~~Division~~ Department. When the Legal Department has prepared the subpoena, it will be forwarded to the requester with complete instructions for service. Further information concerning the subpoena process, authority and use is contained in Exhibit 4 — Policy and Procedure For Subpoena Requests.

In cooperation with the Department of Justice, the Board has agreed to provide assistance in the enforcement of money laundering violations by reporting suspected violations. If potential violations of money laundering or monetary instrument transaction reporting laws are suspected, a report documenting the suspected violation should be prepared and forwarded to the Chief of Field Operations or the Collections and Third District Operations Manager. That office will then forward the report to the Department of Justice. This report should be submitted in a form similar to that shown in Exhibit 15.

The law contains two money laundering offenses that staff should look for when conducting their regular functions. These are referred to as the “facilitation” offense and the “capturing” offense.

The facilitation offense includes conducting or attempting to conduct a transaction involving a monetary instrument or instruments exceeding \$5,000 through a financial institution with the intent to promote, manage, establish, carry on or facilitate the promotion, management, establishment or carrying on of any criminal activity.

The capturing offense involves the laundering of illegally derived proceeds. It includes conducting or attempting to conduct a transaction involving a monetary instrument or instruments exceeding \$5,000 through a financial institution with knowledge that the monetary instrument represents the proceeds of criminal activity.

Auditors should not spend a significant amount of time investigating potential money laundering violations. However, any suspected violations which are discovered in the course of regular auditing procedures should be reported.

WAIVER OF CREDIT INTEREST POLICY

0402.25

Claims For Refund. The taxpayer should always be allowed a reasonable time in which to support a claim for refund. Under most circumstances, ninety days is considered reasonable.

If the taxpayer has been granted a ninety-day delay and requests additional time, consideration should be given to obtaining a waiver of credit interest. The Board may require a claimant to sign a Form BOE-146, Waiver of Credit Interest, as a condition to deferring action on a claim for refund (Revenue and Taxation Code section 6908(b)). In some cases, it may be appropriate to allow up to an additional ninety days because of the size of the claim and large amount of supporting detail required. However, delays beyond six months should not be allowed without a waiver of credit interest or the approval of the Deputy Director, Sales and Use Tax Department, or designee.

An extension of time beyond twelve months from the date the taxpayer was first notified in writing to compile the necessary data in support of the claim should not be allowed even if the taxpayer is willing to sign a waiver of credit interest or an extension to an existing waiver of credit interest. If the taxpayer does not provide the supporting data within the twelve-month period, the claim for refund will be denied for failure to support the grounds upon which the claim was based. Exceptions to this policy must be approved by the Deputy Director, Sales and Use Tax Department, or designee.

Deficiency Audits With Credits. If the taxpayer contends that there are other credits which offset or exceed a deficiency disclosed by an audit in process and requests a delay to obtain information supporting such credits, completion of the audit may be delayed for up to ninety days. A notation should be made on the BOE-414-Z of the date and reason for the delay. Should the taxpayer request a further delay, the deficiency audit should be completed as a non-concurred audit and processed in the usual manner.

With regard to the credits in question, it is critical that the auditor obtain a timely claim for refund which includes the taxpayer's specific contentions. The claim for refund, and when appropriate a waiver of credit interest, should be forwarded to the Audit Determination and Refund Section with all pertinent information concerning the credits and the waiver of credit interest. Subsequent action by the district office, if any, will be requested by Headquarters.

It should be noted that refunds are to be considered priority assignments. In those cases where a taxpayer has given the Board a waiver, it becomes even more imperative that prompt action be taken.

Authorized Signatory. To preclude any question about the validity of a waiver, the Form BOE-146, Waiver of Credit Interest, must be signed by (1) the taxpayer in the case of a sole proprietorship, (2) a partner in the case of a partnership, (3) a corporate officer in the case of a corporation, or (4) someone holding a written power of attorney from one of those persons.

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

1. The document must be dated and identified as a "power of attorney."
2. 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 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 Form BOE-146, Waiver of Credit Interest.

3. The person granting the power of attorney must be the owner, partner, or a corporate officer of the company being audited.

With respect to corporations, if the title of the person signing the waiver is other than chairman of the board, president, secretary, or chief financial officer, the auditor must verify, by examining the corporate articles or bylaws regarding corporate officers, that the titled position constitutes a corporate officer.

With respect to partnerships, if the person signing the waiver is not listed as a partner on the IRIS TAR AI screen, the auditor will verify the validity of the person's status as a partner by reviewing the partnership agreement. Any changes in partners must be reported to district compliance as provided in section 0219.03.

A copy of the written power of attorney must be obtained and attached to the copy of the waiver(s), Form BOE-146, and transmitted to Headquarters with the audit report if the waiver signatory is other than a corporate officer, partner or owner.

STARTING AN ASSIGNMENT — GENERAL

0403.05

~~Usually~~ Generally, an assignment should be started only after proper arrangements have been made in advance. In rare instances, it may be desirable to start an assignment without notifying the taxpayer, as in the case of a surprise investigation of a person suspected of fraudulent reporting practices.

If the necessary records are located in an area handled by another district or ~~subdistrict~~branch office, the audit assignment normally should be transferred to that district or ~~subdistrict~~branch office along with Form BOE-579. This form should be accompanied by a fact sheet setting forth as much pertinent information as is available, including any audit memoranda, that will assist the receiving office in completing the case. The auditor's supervisor may, in unusual circumstances, ~~make~~ arrangements for the auditor to ~~make~~conduct the audit at the other location.

PRELIMINARY ARRANGEMENTS

0403.10

Certain preliminary steps to be taken before starting an assignment are:

(a) If available, examine the district master file to determine type of business, starting date, ownership, close outs, reorganizations, and general record of reporting; and to review refund notices, delinquencies, audit memos, etc. Taxpayer information may also be obtained electronically by reviewing:

- The IRIS TPS TP screen for prior audit information and petition and claim for refund status. If an appeal is noted, check the APL PR screen for more information.
- The IRIS COM BA screen for comments input from all IRIS subsystems. If payment problems are noted, the auditor may request that compliance staff review the account on ACMS for additional information.
- The Internet to find information on company history, product lines, store locations, recent mergers and acquisitions, etc.

(b) Contact the taxpayer to arrange for:

- Exact time for starting assignment.
- Records to be supplied for start of assignment.
- Name and position of person to be contacted. *(The auditor must leave their his or her name and telephone number with the taxpayer at this time.)*
- Desk space /work area.

(c) Verify registration information, including:

- insuring ~~The~~ current ownership is the same as the permit. Sole proprietors may not know that becoming a partnership or incorporating is a change in ownership.
- The accuracy of the assigned area code(s).
- The accuracy and currency of all subpermits.
- The correctness of the taxpayer's local and transit tax allocation procedures.
- Any other area(s) which could impact the accuracy of the reported local tax.

If any errors are discovered, the auditor is to take *immediate* corrective action including:

- Obtaining the date when the change or error first occurred.
- Notifying district compliance as described in section 0219.03 (or preparing other forms as required by District Compliance) if an area code change is required.
- Notifying Compliance of new or closed-out subpermits.

The appropriate BOE-80 series "Audit Engagement Letter" should be used to confirm arrangements to begin audits or to establish contact with the taxpayer.

Normally the initial contact with the taxpayer will be by telephone. When the audit appointment results from a telephone contact, the appointment must be immediately confirmed by mailing the BOE-80-A, "Confirm Start Date" letter together with Pamphlet No. 70, "The California Taxpayers' Bill Of Rights," Pamphlet No. 76, "Audits," and Pamphlet No. 17, "Appeals" unless the audit will commence within a week of

making the appointment.

DISCUSSION WITH TAXPAYER

0403.1512

When the auditor arrives at the taxpayer's place of business at the appointed time, ~~they~~ the auditor should have a preliminary discussion with the taxpayer or with the person who has charge of the records before starting the audit work. A representative tax return should be examined, and the taxpayer should be requested to point out the source of the figures used to compile the return. A discussion about how the ledgers and summary records are maintained is imperative at this time.

The auditor should determine, by direct questioning of the taxpayer, the exact nature of the business activity for the audit period. Inquiry should be made about changes in key clerks, accountants and/or accounting systems, as variations in the type of business, or in the methods of conducting business will have an effect on the approach to making an audit.

CONTACTS WITH THIRD PARTY REPRESENTATIVES

0403.1714

In order to protect the taxpayer, it is imperative that before any discussion or correspondence is initiated with a person claiming to be a representative of the taxpayer, the auditor secures written authorization from the taxpayer. It is not generally necessary to obtain this authorization when the taxpayer introduces or refers the auditor to their representative. It is also not necessary to obtain an authorization when the representative is a professional governed by a code of ethics, e.g., a certified public accountant or attorney. However, it is a good practice when contacted unilaterally by a professional to acknowledge the contact in writing with a copy to the taxpayer. ~~The taxpayer~~ Taxpayers should receive copies of all correspondence between the Board and their representative concerning their case(s).

LIMITATIONS ON CONTACTS WITH TAXPAYERS REPRESENTED BY COUNSEL

0403.16

Board employees who are not attorneys are not required to refrain from contacting or speaking with taxpayers who are represented by legal counsel, a CPA, or other representatives, even in those instances where the representative has requested that the employees do refrain. Disregarding a representative's request should be done only after consulting with the employee's supervisor and be based, in part, on the representative's degree of cooperation with Board staff and the fact that the taxpayer does not timely comply with the Board action requested through the representative.

If the taxpayer or his or her representative has requested that no contact with the taxpayer be made without the taxpayer's representative present, the auditor should notify his or her direct supervisor and fully document the request on Form BOE-414-Z. In addition, all subsequent contacts with the taxpayer should be documented on the BOE-414-Z to protect against potential claims or allegations of harassment. A supervisor or lead person may also accompany the employee for difficult negotiations.

If the taxpayer or his or her attorney has obtained a restraining order forbidding contact by the Board without the attorney present, the Board employee must comply with the order. In such cases, the Chief of Field Operations or the Collections and Third District Operations Manager, Internal Security and Audit Division, and the Chief Counsel should be notified of the order for appropriate action.

AUDIT PROGRAM

0404.10

All audits must be guided by an organized plan. A carefully thought-out, but flexible, overall plan (audit program) is the first step towards good working papers and a good start. Such a plan forces advance thinking and a proper overview of the assignment as a whole. As such, audit programs are **mandatory** and must be completed for all audit assignments. Audit programs must be written on a separate schedule and included as a memo in the audit. Much of the information needed to prepare the audit program can be obtained from the BOE-472, Audit Sampling Plan. [See Exhibit 11 for sample audit programs for general retailers, manufacturers and wholesalers, and liquor stores. These sample programs may be used as a guideline in developing a program for your audit.](#)

Audit programs are influenced by the results of the preliminary investigation, surface examination of the records, and limited testing procedures. As such, audit programs need to be flexible and are subject to change as circumstances warrant.

~~If many errors are found in any test, it should be expanded so that a good base for calculating a percentage of error will be available. On the other hand, if no errors are developed in the first period tested, if the records are in good condition, and if the personnel are well informed on the correct application of the tax, often times the testing may be terminated with one period. The auditor must use their judgment based on observations of the records, plant and personnel to decide just how much verification is required.~~

USE OF FORM BOE-472, AUDIT SAMPLING PLAN

0405.23

In an effort to document the sampling method used in an audit, the Board has developed Form BOE-472 — Audit Sampling Plan. (See Exhibit 5) Its purpose is to establish the most efficient means of developing a sampling plan and document: (1) the sampling method that will be used to determine a percentage of error in the population being tested and (2) the projection of the sample results.

The purpose of the BOE-472 is to establish the most effective and efficient means of developing a sampling plan. *This form must be used in all large audits (defined here as any audit with a cell designation of 1D through 4D) or any time sampling is performed.* This plan will provide much of the information that will later be needed to complete the working paper documentation and audit comments.

Prior to determining the type of testing to be used in a given audit situation, the auditor must make a thorough examination of the business operation for the period under audit. This examination should include a review of source documents, changes in business activity, and changes in accounting procedures and key personnel. Once this information has been evaluated, a determination of the best method of testing can be made. Form BOE-472 will assist the auditor and taxpayer in identifying crucial elements of the audit sampling plan. This form is to be used as a tool to gather information in conducting samples, as well as to educate taxpayers about the sampling process and make the taxpayer aware of important considerations that might impact the audit. This form also identifies special situations that might arise during a test and allows both the taxpayer and auditor to agree on how to handle them. It should be completed with assistance and input from the taxpayer, prior to the actual selection of the sample, and used in conjunction with information and guidelines provided in the appropriate sections of the Audit Manual.

The information and methods documented in this form are not binding on either the taxpayer or Board staff. The sampling plan can and should be continually evaluated (and changed, if necessary) based upon information obtained during the audit process. However, if any deviation from this sampling plan is required, the deviations will be fully explained and discussed with the taxpayer.

While BOE-472 includes many situations that might arise in sampling, it cannot include them all. As such, the form should be modified (in Section 11, "Other") to address any situations not included in previous sections of the form. Once the information has been evaluated, the auditor is in a position to determine the best method of testing.

This form is to be included in the audit working papers as a ~~memo~~-subsidiary schedule. A separate plan should be completed for each area tested. For example, if the audit includes a sample test of both paid bills and resales, two BOE-472s should be completed. (Exhibit 5)

OBTAINING FINANCIAL INFORMATION

0405.27

Board staff must first try to obtain from the taxpayer any data or documents which should have been retained in accordance with Revenue and Taxation Code section 7053. However, if all other available avenues of information have been exhausted and approval of the district administrator has been obtained, Board staff may request the information directly from the taxpayer's financial institution either by obtaining the taxpayer's authorization or by issuing a subpoena duces tecum.

Procedures for requesting records directly from a financial institution, including procedures to comply with the California Right to Financial Privacy Act, are explained in detail in CPPM sections 135.070 through 135.073.

USE OF PRIOR AUDIT PERCENTAGES OF ERROR IN CURRENT AUDITS

(CONT.) 0405.33

If stratified dollar limitations were used in the last two audits, generally the same dollar stratification should be used in the current audit. However, if there is an indication during the limited testing that a different stratification level may be appropriate in the current audit, the new stratification level should be used. If so, the prior percentages of error will have to be adjusted to reflect the new stratification level.

For example, a decrease or increase in the stratification level will affect the sample base (by deleting or including sample items), the population base (by deleting or including population items) and the percentage of error (by deleting or including error items) in prior audits. These recalculations must be made so that the proposed percentage of error to be used in the current audit is an accurate representation of the prior audit percentages of error at the new stratification level.

This information should then be used by the District Principal Auditor and audit supervisor to evaluate such taxpayers for inclusion in this program.

Those taxpayers meeting the criteria described above should then be contacted and the program explained to them by an auditor and audit supervisor. The taxpayer ~~should~~must also be informed that this procedure will not be used in consecutive audits.

After the discussion with eligible taxpayers, a detailed outline (Exhibit 6) should be prepared for each interested taxpayer indicating why they would make a good candidate for inclusion in this program. Each outline should include:

- (a) Name and account number of the eligible taxpayer
- (b) Nature of taxpayer's business
- (c) Current audit period
- (d) Portion(s) of audit where a prior percentage of error is to be used
- (e) Prior audit periods and corresponding percentages of error for those portion(s)
- (f) Population(s) to which the prior percentage(s) of error was applied
- (g) Proposed percentage of error to be used for the portion(s) in the current audit
- (h) Population(s) to which the proposed percentage(s) of error will be applied in the current audit
- (i) Any other pertinent information

This outline should then be sent by the District Principal Auditor to the ~~Program Planning Tax Policy~~ Manager (with a "cc" to the Chief of Field Operations or the Collections and Third District Operations Manager) for review and evaluation (Exhibit 6, page 1). The district will be notified of the decision regarding the review and evaluation. Upon completion of the audit, the district will prepare an evaluation memo (Exhibit 6, page 2) to the ~~Program Planning Tax Policy~~ Manager (with a "cc" to the Chief of Field Operations or the Collections and Third District Operations Manager), detailing the **tax change** of that portion(s) of the audit utilizing the prior percentage of error along with an estimate of the number of audit hours saved. A copy of the evaluation and authorization memos should be included as memo schedules in the audit working papers.

CONCESSIONAIRES

0406.60

For sales and use tax purposes, concessionaires are independent retailers who are authorized, through contract with, or permission of, another retail business enterprise (the prime retailer), to operate within the perimeter of the prime retailer's own retail business premises. Concessionaires appear to be wholly under the control of the prime retailer, and to make retail sales that to the general public might reasonably be believed to be the transactions of the prime retailer. Certain departments are leased to others under contracts which take various forms but the The usual bases for payment of store occupancy to the lessor prime retailer are:

- (a) Percentage of net or gross sales with possible provision for minimum rental payment
- (b) A fixed rental
- (c) A profit-sharing arrangement

The prime retailer's general ledger should contain a clearing account for concessionaire operations. ~~The store has sales tax liability for the operations of lessees who are not registered with the Board for the period of operation~~ The prime retailer may be held jointly and severally liable for sales and use taxes imposed on unreported retail sales by the concessionaire while operating as a concessionaire. The prime retailer will be relieved of this liability for the period in which the concessionaire holds a permit for the location of the prime retailer, or the prime retailer has a written statement (as provided in Regulation 1699) taken in good faith in which the concessionaire affirms that he or she holds a seller's permit for the prime retailer's location(Regulation 1699).

If ~~there are~~ the prime retailer has concessionaires, the auditor should secure a complete list of all leased departments operated during the audit period, showing the ~~department's concessionaire's name, and number, address of operator, phone number,~~ and ~~the sales tax~~ seller's permit number, if any, ~~held by lessee~~. Even ~~though when the department store~~ prime retailer does report the concessionaires' sales transactions, special attention should be given to the possible liability for use tax of the concessionaire for operating supplies, giveaways, etc., since these are often shipped into ~~the State~~ California from the concessionaires' out-~~of-~~state home office or purchased from out-~~of-~~state retailers.

EXAMINATION OF SELECTED GENERAL LEDGER ACCOUNTS

0408.25

The verification procedure should include an examination of debits in certain general ledger accounts. This is necessary as invoices covering capital expenditures frequently are not filed with the other purchase invoices. From the documentary reference, it is possible to trace the originating documents. Taxable purchases not previously scheduled on which tax was not added by the vendor, should be scheduled and verification made that the taxpayer is responsible for tax. These items are generally located in the following accounts:

Asset Accounts	Expense Accounts
Delivery Equipment	Advertising
Furniture and Fixtures	Donations
Inter-Company Accounts	Expendable Tools
Leasehold Improvements	Experimental and Exploration
Machinery and Equipment	Manufacturing Expense
Nonexpendable Tools	Repairs
Work in Progress	Research and Development
	Supplies
	Samples
	Promotional

This phase of the examination can be done at the same time these accounts are being examined for additional taxable sales.

The auditor should examine invoices representing purchases of significant taxable additions to fixed asset accounts.

Unsupported debits to the fixed asset accounts should be questioned by the auditor and listed on a subsidiary schedule. The taxpayer should be provided with a copy of this schedule and given a reasonable period of time to obtain support for the items in question before closing the audit. If no support is provided, use tax should be asserted against the taxpayer. When necessary, a Waiver of Limitation, Form BOE-122, should be obtained.

The examination of asset accounts may reveal that the proper amount of use tax has not been paid to the Department of Motor Vehicles on the purchase price of a vehicle. Generally, this occurs in those instances in which (1) the change in ownership was not recorded with the Department of Motor Vehicles; (2) the selling price was substantially different than the measure on which tax was collected by the Department of Motor Vehicles; or (3) the vehicle has special equipment attached which was not included in the measure on which tax was collected by the Department of Motor Vehicles.

In such instances, the use tax is to be asserted against the purchaser. [\(See the tables in CPPM 830.005 for specific examples of how penalty and interest may apply to use tax due on purchases of vehicles.\)](#)

The measure of additional tax is not to be included in Form BOE-414-A, Report of Field Audit, on the seller, even ~~though~~ when disclosed by audit of the seller.

In recommending the additional measure against the purchaser, either Form BOE-414-A, Report of Field Audit, or Form BOE-414-B, Field Billing Order, will be used, depending on the extent of the examination of the purchaser's records.

Form BOE-111, Certificate of Vehicle, Mobilehome or Commercial Coach Use Tax Clearance, will be issued by the district office for those vehicles on which tax is recommended by audit or F.B.O. and the change in ownership was not recorded with the Department of Motor Vehicles.

OTHER RECORDS

0408.27

Other records may be useful in establishing purchases subject to use tax including property tax records such as the Business Property Statement that taxpayers are required to file with their county assessor's office on an annual basis. The statement lists all equipment the taxpayer uses in his or her business along with the purchase price and acquisition date.

USE OF BOE-504 — XYZ LETTER PROCEDURE

0409.51

The auditor must ~~insure~~ ensure that the taxpayer understands that any of the above other evidence by itself is not the equivalent of a resale certificate timely taken in good faith, and may not relieve the seller of the liability for the tax.

In absence of any valid resale documentation, the auditor may determine that it is appropriate for a seller to use the Form BOE-504 series of forms (hereafter called "XYZ" Letters) procedure to help satisfy their burden of proving that a sale was not at retail even though a valid resale certificate was not obtained or to substantiate a claim that their customer paid the tax directly to the state. [Copies of the forms are available on eBOE.](#)

The "XYZ" Letter procedure utilizes the following forms:

- BOE-504-A, explains the "XYZ" Letter procedure
- BOE-504-B, Sample "XYZ" Cover Letter
- BOE-504-C, Statement Concerning Property Purchased Without Payment of California Sales Tax, for use when auditing in-state sellers
- BOE-504-COS, for use when auditing out-of-state sellers *
- BOE-504-CLS, for use when questioning sales made to leasing companies *
- [BOE-504-BPA](#) and BOE-504-CPA, for use when questioning ex-tax sales of special printing aids ([also see AM section 1103.30](#)) *
- BOE-504-CFS, for use when questioning ex-tax sales of feed, fertilizer, seed or annual plants—*
- BOE-504-CUS, [for](#) use when questioning ex-tax sales made to U.S. Government supply contractors *

**—These forms are "PC" forms and are available on disk only. The disk is available in each district office and should be printed out as needed.*

When it is appropriate to use the "XYZ" Letter process, the auditor will provide the taxpayer with a copy of forms BOE-504-A, B, and C ([or -COS, -CLS, -CPA, -CFS or -CUS as appropriate](#)). The auditor should discuss the "XYZ" Letter process with the taxpayer and explain that a [satisfactory](#) response to an "XYZ" Letter inquiry alone is not necessarily enough to support a sale for resale. The auditor should also explain that since the "XYZ" Letter is not a substitute for a timely resale certificate, additional documentation or information may be required. Where the use of "XYZ" Letters is not advisable or appropriate, and the taxpayer insists on using the procedure, the taxpayer must be advised in writing that their customer's response may not be accepted as verification of an exempt transaction.

A period of four weeks will be allowed for the taxpayer to prepare and send the "XYZ" statements and for the customer to reply. It is recommended that the "XYZ" statements be returned directly to the Board. If this is the case, the auditor should provide the taxpayer with return envelopes with the address of his or her district branch office. If the taxpayer elects to have the "XYZ" statements returned to them, the auditor should explain to the taxpayer that the likelihood of having staff contact the customer or sending an additional mailing is greater.

The taxpayer may customize the "XYZ" cover letter (BOE-504-B [or BOE-504-BPA for special printing aids](#)) by using the text contained therein on their own letterhead,; however, the text in the sample letter should be used without additions, deletions, or

changes. The taxpayer may ask their customers to forward payment of tax reimbursement if the transaction is identified as taxable. The statement should clearly state that the payment of tax be forwarded to the taxpayer and not the Board. All modifications to the cover letter must be approved by the auditor's supervisor.

The "XYZ" statement (BOE-504-C, COS, CLS, CPA, CFS, or CUS) must be used as provided by

the auditor. The use of a standardized "XYZ" statement will reduce any possible controversy over whether the proof provided is satisfactory. When verifying unique types of sales (e.g. printing aids, animal feed, fertilizer, etc.), auditor should provide the specialized forms to the taxpayer. The auditor should put his or her office designation in the space marked "DMA" and their initials in the space marked "Auditor's Initials," both located at the top right of the "XYZ" statements.

The taxpayer's customer is requested to return the completed "XYZ" statement within 10 days. The 10-day requirement is intended to encourage a prompt response from the customer. If the taxpayer chooses the recommended procedure of having the completed "XYZ" statements sent directly to the Board, the taxpayer may add a statement in the letter (BOE-504-B) asking their customer to send a copy of the completed "XYZ" statement to them by fax or mail. The original "XYZ" statement, however, must either be sent or faxed to the Board by the taxpayer's customer. If the completed "XYZ" statements are to be sent directly to the taxpayer, only a signed original will be accepted.

If a second "XYZ" Letter is necessary, the auditor should establish a reasonable period of time based on the circumstances involved.

[As explained in section 0302.80, XYZ responses are part of the audit working papers and should be included as a subsidiary schedule to the resale examination schedule.](#)

TAX ASSESSED ON PURCHASER

0409.63

Whenever a purchase from a California seller is assessed tax because the purchaser issued a resale certificate to the seller, which the seller accepted in good faith, a copy of this certificate should be obtained from the seller at the time of audit and included in the audit working papers of the purchaser's audit.

Because the issuance of a resale certificate shifts the tax from the seller to the customer, it is imperative that a copy of the resale certificate be obtained while the auditor is reviewing the seller's records. A verbal comment by the purchaser that a resale certificate was given to the seller is insufficient. Often customers will indicate concurrence when the audit is completed but change their mind when the Notice of Determination is received and contend that no such certificate was issued and the incidence of tax should be on the California seller. Without written evidence to refute this claim, the Board's position cannot be sustained.

AUDITING PROCEDURE

0410.10

An audit of this deduction should be made in the same manner as an audit of a deduction for sales for resale. Ordinarily the number of such sales is limited and the audit should be made on a complete basis. If, however, the number of items claimed is exceptionally large and the average unit of sale is comparatively small, a test basis may be used. Documentary evidence required to support the deduction, where the sale is made directly to the United States Government, a subdivision or agent, should consist of one or more of the following documents:

- Purchase orders
- ~~Remittance advices~~
- Copy of U.S. Government credit card or credit card number
- Other documents demonstrating direct payment by the United States
- Shipping and other documents if there is a question whether the merchandise was sold directly to an individual who is in the armed services

In the absence of documentation to support claimed sales to the U.S. Government, the auditor may determine that it is appropriate for a seller to use the BOE-504 series of forms (BOE-504-CUS) procedure to help satisfy their burden of proving that a sale was not at retail even though exempt documentation was not obtained (~~S~~see section 0409.51 for procedures).

Sales to contractors who are engaged in work on projects owned by the United States Government are not sales to the Government. If the contractor is actually selling tangible personal property to the U.S. Government, such sales are sales for resale and should be verified as such. Mention is made of this in this section only because many retailers classify such sales as sales to the United States Government and erroneously claim the deduction under that heading rather than sales for resale. If the auditor has reason to believe the material purchased was not actually sold by the contractor-customer to the U.S. Government, a Form BOE-1164, Audit Memorandum of Possible Tax Liability (see section 0401.20), should be prepared setting forth all pertinent phases of the transaction.

SALES TO FEDERAL EMPLOYEES USING U.S. GOVERNMENT BANKCARDS 0410.15

The federal government issues credit cards to its employees for purchases of goods and services. Beginning November 30, 1998, the purchases are under a new program called "GSA SmartPay" and is effective [for 5 years through November 28, 2008](#). Cards will now be issued by Citibank, First National Bank of Chicago, NationsBank, Mellon Bank, and U.S. Bank. The new cards bear 16-digit account numbers with unique prefixes, government designed artwork, and are imprinted with "United States of America" at the top. In the right-hand corner, cards contain a logo which says "SmartPay." The cards also bear wording that denotes the card is for "Official Government Use Only." The General Services Administration administers the program for all departments and agencies of the U.S. Government.

Purchases made with most of the new cards are directly billed to the government and will represent nontaxable sales to the U.S. Government. Those purchases directly billed to the employee are subject to sales tax. To determine which government credit cards are government-billed and which are employee-billed, retailers will have to consider the type of card, the type of transaction, and the card account numbers. Generally, through use of the Bankcard System and coding authorization, purchases are automatically denied if a particular type of card is used to make a type of purchase for which that card was not issued.

For **FLEET CARDS**, there are two types of U.S. Government "fleet" cards which may be issued to federal employees to make fleet type purchases (e.g., gasoline, oil, etc.). One is a Voyager card and the other is a MasterCard. The Voyager cards contain 16-digit account numbers that start with the prefix 8699. The MasterCard cards contain 16-digit account numbers that start with the prefix 5568. All fleet type purchases made with these cards are billed directly to the U.S. Government and are not taxable.

For **PURCHASE CARDS**, there are two types of U.S. Government "purchase" cards which may be issued to federal employees to make purchases of goods (e.g., office supplies, parts, etc.). One is a VISA card and the other is a MasterCard. The Visa cards contain 16-digit account numbers that start with the prefix 4486 or 4716. The MasterCard cards contain 16-digit account numbers that start with the prefix 5568. All purchases of goods made with these cards are billed directly to the U.S. Government and are not taxable.

For **TRAVEL CARDS**, there are two types of U.S. Government "travel" credit cards which may be used by federal employees to make travel type purchases (e.g., hotels, car rentals, restaurants, etc.). One is a VISA card and the other is a MasterCard. The Visa cards contain 16-digit account numbers that start with the prefix 4486 or 4716. The MasterCard cards contain 16-digit account numbers that start with the prefix 5568. Federal government travel cards may either be billed to the U.S. Government or to the federal employee depending upon the account number. If purchases made with travel cards are billed to the employee, the sales are subject to tax. To determine whether purchases made with federal government travel cards are government-billed or employee-billed, retailers must look at the 6th digit of the account number of the card. If the 6th digit is 1, 2, 3, or 4, purchases are billed to the employee and are taxable. If the 6th digit is 0, 6, 7, 8, or 9, purchases are billed to the U.S. Government and are not taxable. This procedure applies to both VISA and MasterCard travel cards.

In some instances, some federal agencies will issue **INTEGRATED CARDS** for the

purpose of “fleet,” “property,” and “travel” purchases. These cards are provided by MasterCard and contain a 16-digit account number that starts with 5568-16. All fleet and property purchases made with these cards are billed directly to the U.S. Government and are not taxable. However, travel purchases may be either government-billed or employee-billed depending upon the account number. To determine whether travel purchases are government-billed or employee-billed, retailers must again look at the 6th digit of the account number of the card. If the 6th digit is 1, 2, 3, or 4, purchases are billed to the employee and are taxable. If the 6th digit is 0, 6, 7, 8, or 9, purchases are billed to the U.S. Government and are not taxable.

Exception: All purchases made with integrated MasterCard credit cards provided by the Bureau of Reclamation employees, including travel purchases, are billed directly to the U.S. Government and are thus exempt from tax. Bureau of Reclamation employees will have to identify themselves to the retailer and show proof of Bureau employment to obtain the exemption.

Retailers who make U.S. Government credit card sales should retain the credit card receipt containing the imprint of the credit card and the sales invoice to support exempt transactions to the U.S. Government. If the purchase is by telephone, the retailer should note the credit card account number and purchaser’s name on the credit card receipt.

LEASES

0411.25

In general, a lease of tangible personal property to a United States contractor is subject to tax whether or not such contractor is properly authorized to act as a purchasing agent of the United States. However, leases are exempt when they are (1) to contractors that occupy the legal status of agents of the United States and (2) to non-agent cost-plus federal contractors, other than Department of Defense contractors, that act as agents when procuring from General Services Administration ("GSA") Supply Sources ("FSS" or "ADPS") pursuant to a letter of authorization issued by a federal contracting officer which has language creating an agency relationship.

It has been the policy of the Department of Defense not to designate government contractors as legal agents of the United States. Therefore, a lease between a Department of Defense contractor and a vendor would not include the United States as a party to such lease, notwithstanding any FAR provision which attempts to characterize the buyer-lessee as an agent for the Department of Defense. Consequently, lease payments made by a Department of Defense contractor, which are charged as direct consumable supplies to a fixed price contract or cost reimbursement contract are subject to the sales or use tax.

Should a Department of Defense contractor nevertheless claim agency relationship with respect to a lease, the contractor should be requested to provide documentation to support such claim. The documentation should be submitted to the [Program Planning Tax Policy](#) Manager (with a "cc" to the Chief of Field Operations [or the Collections and Third District Operations Manager](#)) for communication with the Secretary of Defense to ascertain the Department's position with respect to the specific contract.

A period of four weeks will normally be sufficient for the taxpayer to prepare and send the certificate and for a reply to be received. The taxpayer should prepare the certificate to be completed in triplicate. It is recommended that the certificate be returned directly to the Board. If this is the case, the auditor should provide the taxpayer with return envelopes with the address of his or her district or branch office. Please note, business reply envelopes (no postage necessary) should not be used.

The taxpayer may customize the cover letter, Form BOE-52-L, by using the text contained therein on their own letterhead; however, the text in the sample letter should be used without additions, deletions or changes. Any modifications to the cover letter must be approved by the auditor's supervisor.

The taxpayer's customer is asked to return the completed certificate within 10 days. The 10-day requirement is intended to encourage a prompt response from the customer. If the taxpayer chooses the recommended procedure of having the completed certificate returned directly to the Board, the taxpayer may add a request to the cover letter asking its customer to also send a copy of the completed certificate to the taxpayer. The taxpayer's customer should send the originally signed and completed certificate to the Board (may be sent by facsimile). However, if the taxpayer's customer sends the certificate directly to the taxpayer and then the taxpayer sends the certificate to the Board, the Board will accept only the originally signed and completed certificate and will not accept a facsimile copy. If a second certificate is necessary for verification, the auditor should establish a reasonable period of time for completion based on the circumstances involved.

Use of Form BOE-52 by Audit Staff

When the auditor has good reason to believe that merchandise was not shipped as specified by the shipping documents, or that empty boxes may have been shipped to purchasers as a means to support the interstate commerce exemption, it may be appropriate to use Form BOE-52 as a verification method for receipt of out-of-state shipments. In addition to the certificate, Form BOE-52-L1 (Exhibit 14B) provides a suggested cover letter for use by the districts in explaining the purpose of the certificate and requesting the purchaser's statement regarding receipt of the item and place of delivery. The decision to use this verification method should be based on the materiality of the questioned transaction(s) and on the surrounding circumstances. The auditor should prepare the certificate to be completed in triplicate. Postage-paid return envelopes may be included in the mailing to increase the likelihood of response for this case in which the Board is seeking verification of shipment without seller involvement.

Returned Form BOE-52s

As explained above, the seller, or the auditor when the seller is not involved, should prepare the certificate to be completed in triplicate. The original certificate should be included in the audit working papers. If out-of-state delivery is indicated, [to Arizona, Mexico, New Mexico, Oklahoma, Texas, or Utah, a copy should be sent to the attention of the Revenue Opportunity Specialist in the Audit Support Unit \(MIC: 44\). For all other areas,](#) a copy should be sent to the taxing authority in the state of the purchaser, for example the Department of Revenue [of that state](#). The final copy should be given to the seller for their records.

REFUNDS OF EXCESS TAX REIMBURSEMENT

0417.07

Regulation 1700 provides that refunds of amounts of excess tax reimbursement paid to the Board as sales tax may be refunded to the retailer upon submission of "evidence sufficient to establish that excess amounts have been or will be returned to the customer."

This has been construed to mean that the retailer must actually refund amounts collected as excess tax reimbursement to their customers rather than give a credit unless they can show one of the following:

- The customer agrees to a credit.
- The customer's debt to the retailer is acknowledged by the customer or made certain by a court proceeding.
- The amounts to be credited are small and apply to numerous customers.

The retailer should maintain records as provided in Regulation 1700(b)(3) as evidence that the excess amounts have been or will be returned to the customer.

No refund of excess tax reimbursement is allowable without acknowledgement from customers. The BOE-52-L2, Notice of Pending Refund of Excess Sales Tax Reimbursement, (Exhibit 14C) is available to assist the retailer in obtaining sufficient evidence from customers to establish the excess tax amount reimbursements have been or will be returned. The retailer can simply complete the BOE-52-L2 letter for each customer affected and retain the customers' signed responses. The notice informs the customer of the amount of indebtedness in writing and provides a check box for the customer to indicate their preference of a refund or credit to their account for the amount of excess sales tax paid. The retailer must obtain and maintain the signed acknowledgement in their records as proof of the refund or credit being given.

Taxpayers are not required to use this form, however any other type of acknowledgement must satisfy all of the requirements under Regulation 1700 (b)(3)(B). It is not necessary to include copies of the signed acknowledgements in the audit working papers, however verification comments should include complete comments or statements regarding the examination of the acknowledgements and their retention by the taxpayer. Form BOE-52-L2 is available on eBOE.

~~In order to assure that such excessive reimbursement will, in fact, be returned or credited under the above circumstances to the customer, it is suggested that prior to recommending to refund in an audit, a letter similar to the following be obtained from the taxpayer:~~

~~In order to qualify for consideration of refund of excess sales and use tax reimbursement collected by me during the period _____, the undersigned seller, hereinafter referred to as seller, agrees to do the following:~~

- ~~• Notify in writing each person from whom excessive tax reimbursement was collected the amount of tax that will be returned if and when the Board of Equalization refunds the tax to the seller.~~
- ~~• Provide an affidavit listing the persons to whom such notices were mailed or delivered and the amounts involved.~~
- ~~• Return the excessive tax reimbursement to the customers, or credit~~

~~the customers' accounts under conditions prescribed by the Board of Equalization.~~

~~I understand that failure to return the tax to the customer, or validly credit their account, within 30 days from the date received by the seller will subject the seller to appropriate action for recovery of the tax plus appropriate penalties.~~

~~Seller~~ _____

~~By~~ _____

~~Title~~ _____

~~Permit No.~~ _____

~~Address~~ _____

Bad Debts Incurred by Lessors

- A bad debt deduction is allowable on reported taxable rental receipts which are found to be worthless and charged off for income tax purposes.
- On leases or renewals of leases, the lessor is required to collect use tax from the lessee at the time rentals are paid by the lessee and to pay the tax during the corresponding reporting period. If the lessor has computed and paid tax to the state on lease payments that were due but not paid by the lessee, then the lessor has made a tax overpayment subject to refund or credit. Therefore, the taxpayer may claim a refund without having to write off the account as a bad debt for income tax purposes. If however, the account was properly written off and claimed as a bad debt deduction, it should be allowed.
- When leases of tangible personal property situated in this State are not subject to use tax because of the exempt status of the lessee (e.g. insurance companies), the lessor nevertheless is subject to sales tax measured by the rental receipts. Therefore, taxes are due from the lessor on the basis of rentals payable and not rentals paid, and a valid bad debt deduction may result for sales tax purposes.

Bad Debt Deductions to Persons Other Than the Retailer

- A successor who pays full consideration for receivables acquired from their predecessor is entitled to a bad debt deduction to the same extent that the predecessor would have been had they continued the business.
- ~~A purchaser of receivables, other than a successor, cannot obtain a bad debt deduction on accounts that cannot be collected.~~
- A retailer who sells receivables at a discount cannot obtain a bad debt deduction for the amount of the discount.
- [See section 0419.17 for audit procedures on bad debt deductions claimed by lenders on purchased receivables.](#)

Bad Debts of Construction Contractors

- When under a time and material contract a contractor bills their customer for tax reimbursement computed upon a marked-up price for materials, pays the tax accordingly and the receivable is thereafter found to be worthless and charged off for income tax purposes, or if the contractor is not required to file income tax returns, charged off in accordance with generally accepted accounting principles, a bad debt deduction may be taken by the contractor for the total amount. The contractor is a retailer in this situation.
- Since a contractor is the retailer of fixtures (other than those used in performance of contracts with the United States) bad debt losses incurred in connection with the furnishing and installing of fixtures are to be treated in the same manner as those resulting from other types of retail sales.

BAD DEBTS INCURRED BY LENDERS ON PURCHASED ACCOUNTS RECEIVABLE

0419.17

General

An account receivable (“account”) may be sold with or without recourse. “With recourse” means the retailer must reimburse the purchaser of the account (“lender”) for any losses the lender suffers. “Without recourse” means the retailer has no obligation to reimburse the lender even if the lender cannot recover the full amount of the debt.

Accounts sold with recourse: A lender who purchases an account with recourse may not take a bad debt deduction under the Sales and Use Tax Law with respect to any loss it suffers on that account (i.e., uncollectible debt for which it fails to obtain reimbursement from the retailer). However, a retailer who sells an account with recourse may take a bad debt deduction for the amount of uncollectible debt for which the retailer actually reimburses the lender pursuant to their contract, to the extent that such loss represents amounts on which the retailer reported and paid tax. These rules remain the law, and have not been affected by the provisions of Regulation 1642(h)(3) and (i).

Accounts sold without recourse: Regulation 1642(h)(3) and (i) apply to bad debt losses incurred on accounts created as a result of retail sales of tangible personal property for which the retailer remitted California sales or use tax on or after January 1, 2000. Transactions prior to January 1, 2000, may qualify for treatment under the Board’s memorandum opinion in WFS Financial, Inc. as discussed below.

Regulation 1642 subdivisions (h)(3) and (i)

Auditors reviewing lenders’ claims for deduction or refund for which the retailer remitted California sales or use tax on or after January 1, 2000 should review Regulation 1642(h)(3) and (i). The subdivisions describe the conditions that must be met to claim a deduction or refund, the election agreement between the retailer and the lender, and election agreements between lenders and affiliated entities.

WFS Memorandum Opinion

On December 14, 2000, the Board issued a memorandum opinion on a claim by a financial institution, WFS, for a refund for bad debts incurred from accounts purchased without recourse. The WFS Financial, Inc. opinion sets forth the requirements of when such transactions can qualify for bad debt deductions. The opinion can be found in the memorandum opinion section of the Business Taxes Law Guide.

The Legislature’s adoption of AB 599 (Stats. 2000, Ch. 600) superceded and replaced the WFS Financial, Inc. memorandum opinion. Revenue and Taxation Code sections 6055 and 6203.5, as amended by AB 599, are incorporated into and explained in Regulation 1642. The WFS decision applies through December 31, 1999, but not after the provisions of Regulation 1642(h)(3) and (i) became operative on January 1, 2000. Regulation 1642 (h)(3) and (i) generally apply to bad debts incurred in connection with transactions occurring during the 4th quarter 1999 since the taxes on those transactions were generally paid after January 1, 2000. However, the WFS decision itself applied to a claim for refund that included the 4th quarter 1999. Accordingly, to ensure fair and uniform treatment of all lenders and for administrative ease, a lender may rely on the provisions of either WFS **or** Regulation 1642(h)(3) and (i) for bad debts incurred in connection with transactions that occurred during the 4th quarter 1999. The provisions of WFS and Regulation 1642(h)(3) and (i) are otherwise mutually exclusive.

It is imperative to note that the determination of whether WFS or Regulation 1642(h)(3) and (i) applies is based on the date the taxes were remitted (usually ascertained based on the date at which the sale occurred), not the date the bad debts were incurred. For bad debts incurred in connection with sales of tangible personal property during the 3rd quarter 1999 and earlier, only the provisions of WFS apply and **not** the provisions of Regulation 1642(h)(3) and (i). Generally for bad debts incurred in connection with

sales of tangible personal property during the 1st quarter 2000 and later, only the provisions of Regulation 1642(h)(3) and (i) apply and **not** the provisions of WFS.¹

Since the determination of whether WFS or Regulation 1642(h)(3) and (i) applies is based on the date tax was paid, but the timing of the bad debt deduction is based on the date the loss is written off, there will be claims submitted which include losses covered by both WFS and Regulation 1642(h)(3) and (i) which were written off in the same reporting period. For example, in the 2nd quarter 2002, a lender writes off two accounts as worthless, one for a sale that occurred in the 1st quarter 1999 and the other for a sale that occurred in the 1st quarter 2000. Tax had been paid for the first transaction prior to January 1, 2000, and the provisions of WFS apply to the loss from that account. Tax had been paid for the second transaction after January 1, 2000; therefore, provisions of Regulation 1642(h)(3) and (i) apply to that loss. Since the lender's right to claim the losses from these two accounts was established during the 2nd quarter of 2002, the deduction for both accounts should be taken on the lender's return for that reporting period. This means the statute of limitations for filing the lender's claim related to the losses on both accounts starts to run on July 31, 2002 (the due date of the return for the 2nd quarter 2002).

Indirect Loans

If a consumer wishes to make a purchase on credit without using an existing credit account, the consumer may apply for a loan for that particular purchase. This is the method used for most purchases of automobiles, aircraft, and vessels, as well as many other large purchases, such as jewelry. The retailer may coordinate the loan application process, with the consumer signing a credit contract with the retailer who thereafter assigns the account to a lender. This type of loan is commonly called an "indirect loan" because the consumer does not contract directly with the lender who will service the loan, but rather contracts with the retailer. Since the retailer will then assign the account to the lender, bad debts from these accounts may qualify for deduction under Regulation 1642(h)(3) and (i).

Direct Loans

Alternately, a consumer may arrange his or her own financing by contracting for a loan directly with a lender. This type of loan is commonly called a "direct loan" because the consumer contracts directly with the lender who will service the loan. In a direct loan situation, the consumer pays for his or her purchase with the proceeds from the loan (plus any down payment or other amounts paid out of the consumer's own funds). Methods of remitting the loan proceeds to the retailer include:

- a check issued by the lender in the retailer's name, which may be sent directly to the retailer or physically delivered by the consumer;
- a check issued in the names of both the retailer and the consumer which must be executed by both parties (and which may also be sent directly to the retailer or be physically delivered by the consumer, although the latter is more common because the consumer must also execute the check);
- and a direct electronic funds transfer from the lender to the account of the retailer.

The Board held in a separate case that bad debts incurred on certain direct loans are also eligible for deduction under WFS guidelines. In that case, although the purchaser contracted for financing directly with the lender, the lender worked closely with the dealer and remitted payment directly to the dealer. If instead the loan proceeds were to come into the full possession of the consumer (e.g., the consumer deposits the funds into the consumer's own account and then draws from that account to pay the purchase price), the loan would not qualify under WFS. Furthermore, for a direct loan to qualify under WFS, the dealer must receive payment in a manner that is essentially the same as for indirect loans that qualify

Due to reporting requirements of 1642(h)(3) and (i), it is *theoretically* possible to have an annual basis retailer sell account receivables to a lender, which would make 1642(h)(3) and (i) apply to sales made for the entire year of 1999.

under WFS. While no specific time frame is required, this usually occurs within ten days of the date of sale. For example, when the loan is for the purchase of a vehicle, a qualifying direct loan would result in the lender's name being placed as lien holder on the ownership certificate as part of the initial registration of the vehicle in the consumer's name. Of course, the other conditions specified in WFS must also be satisfied.

The Board's decision that a lender making a direct loan might qualify for a bad debt deduction under WFS is also applicable to claims for bad debt deductions or refunds under Regulation 1642(h)(3) and (i). However, no deduction or refund is allowable unless and until the lender and the retailer who paid the tax file the election as explained in Regulation 1642(h)(3) and (i). Furthermore, Regulation 1642(h)(3) and (i) applies only when the lender has purchased the account directly from the retailer, or when the lender holds the account pursuant to the lender's contract directly with the retailer. Thus, even if a lender providing a direct loan can convince the retailer to sign an election agreement with the retailer, that does not automatically mean that the losses on the account will qualify for deduction or refund under Regulation 1642(h)(3) and (i). For Regulation 1642(h)(3) and (i) requirements with respect to a direct loan, a lender claiming a bad debt deduction or refund will be regarded as satisfying these conditions if the transaction would have qualified for deduction under WFS (as modified by the Board's ruling on direct loans).

For example, a consumer obtains a line of credit with a lender, perhaps secured by a second deed of trust on the consumer's home. The consumer then uses a check to access the line of credit to purchase a big-ticket item. The retailer receiving the check has no contact whatsoever with the lender except to deposit the check and obtain the funds. The lender and retailer thereafter enter into an election agreement. The loss on this account cannot qualify for deduction or refund under Regulation 1642(h)(3) and (i) since the lender cannot be regarded as having purchased the account from the retailer or holding the account pursuant to a contract with the retailer. On the other hand, a consumer applies for a loan from his or her credit union to purchase a vehicle. The consumer then purchases a vehicle under the normal vehicle sales contract giving him or her a stated number of days to pay the purchase price to the dealer. If the consumer does not make payment timely, the sales contract provides for the dealer to carry the loan (which the dealer could promptly assign to a lender, perhaps even the consumer's own credit union). During the completion of the paperwork and during the sale transaction process, the consumer provides information to the dealer regarding the credit union loan. The dealer contacts the credit union directly and after the necessary paperwork is completed, the credit union deposits the funds directly into the dealer's account. This direct loan will be regarded as satisfying the requirements that the lender purchased the account from the dealer, and if the other requirements of Regulation 1642(h)(3) and (i) are satisfied, the lender is eligible to claim a bad debt deduction or refund under Regulation 1642(h)(3) and (i).

Refinanced Loans

When a loan is refinanced with the original lender, there are two situations where a deduction for bad debts incurred on the refinanced loan will be allowed provided all other requirements for a deduction are satisfied. One is when the refinancing is for the purpose of lowering the amount of the payment (through a reduced rate or extension of the term). The other is when the purpose of the refinancing is to obtain additional funds to pay for necessary repairs to the property purchased with the funds from the original loan, but only when the lender makes payment directly to the repair facility. When calculating the amount of the bad debt loss on qualified refinanced loans whose principal amount is increased to pay for repairs, the percentage of taxable loss must be reduced by the nontaxable portion of the repairs (in addition to the other adjustments for the nontaxable portion of the original loan). Losses incurred from refinanced loans through a different lender do not qualify for bad debt deductions, nor do losses from refinanced loans where the borrower withdrew any funds other than amounts paid by the lender directly to a repair facility for necessary repairs to the property originally financed.

Audit Procedures

When reviewing claims for deduction or refund based on lender bad debts, the auditor should:

- Verify the accuracy of the claim for deduction or refund;
- Confirm the records provided adequately support the claim for deduction or refund;
- Ensure the records provided by the claimant are complete, as required by Regulation 1642(e);
- Confirm that the lender holds a Seller's Permit or a Certificate of Registration – Lender;
- Confirm that there is a valid election agreement on file specifying the claimant is the person entitled to claim the deduction or refund for that account; and
- Verify local and district tax deallocation from the jurisdiction that received the original local or district tax allocation.

For a lender to claim a bad debt deduction or refund, Regulation 1642(i)(2)(B) requires that “the account must have been found worthless and charged off by the lender for income tax purposes.” The standard practice of the lending/financial industry requires bad debts to be written off after a prescribed number of days regardless of any collection activity or payment arrangements made with the debtor, and without regard to whether the account is actually worthless. Thus, although accounts may be written off in accordance with industry standard practice, this does not necessarily mean they are worthless. For example, an account may be written off after the prescribed amount of time has passed, but the lender may have a payment plan in effect with a debtor. Although the account may be written off as a bad debt for other purposes, such an account would not generally be considered “worthless” for purposes of Regulation 1642 while the payment plan remains in effect.

Audit staff must include in the general comment section of the audit working papers a comment as to whether the claim for refund qualifies under WFS or Regulation 1642(h)(3) and (i). Both the lender's and retailer's accounts must be cross referenced, indicating the claim for refund, the basis of the claim (WFS or Regulation 1642(h)(3) and (i)), and the periods covered for each. The audit must include a review of the election agreement(s) to ensure each agreement is valid under Regulation 1642(h)(3)(A), (i)(3), or (i)(4)(A), as applicable, and pertains to the transactions under audit.

Computing the Amount of the Bad Debt Loss: A lender must provide a listing of all transactions (electronic or hard copy) for which it claims a bad debt deduction or refund, and must also be able to provide source documents for all such transactions. Transactions should be selected for review based on the auditor's discretion and not that of the lender. The amount of the bad debt for which the claim for deduction or refund is filed frequently includes some nontaxable elements (e.g., tax, license, earned or unearned interest, late fees, etc.). It would thus be highly unusual for a lender to be entitled to a bad debt deduction for the entire amount of its losses on an account. Rather, the lender must adjust the amount of its losses so its claimed deduction includes only the allowable taxable amounts. There are three basic methods of verifying the lender's claim for a bad debt deduction or refund: Actual Basis, Statistical Sampling and Mean Allowable.

Regardless of the method used, prior to beginning verification of the claim, all claimants should be informed that it might later be necessary to expand the size of the sample to ensure a representative sample is taken so the accuracy of the claim is assured. A claimant must be able and willing to provide documentation to support all transactions included in the claim, regardless of accessibility. Transactions for which the claimant is not capable and willing to provide supporting documentation must be disallowed, even in cases where the claimant purports to have documentation but cannot provide copies because they are not readily accessible.

1. **Actual Basis:** The lender provides a listing of accounts on an actual basis and computes the amount of the allowable bad debt loss on each account on a transaction-by-transaction basis. The information included in the listing must include the items in Appendix 2 of the regulation. Under this method, the lender computes the claimed bad debt loss for sales and use tax purposes on an actual basis and staff is verifying the accuracy of the lender's listing. Staff should utilize statistical sampling techniques to verify the accuracy of the lender's claimed refund. Staff must follow the guidelines for performing a statistical sample set forth in Audit Manual Chapter 13.

When statistical sampling is used staff must select a sample size of no fewer than 300 transactions. If the population is less than 300, the transactions should be examined on an actual basis. The auditor may discover no material discrepancies after testing a sufficient portion of the sample that the auditor is comfortable in concluding the amount of bad debt loss claimed by the taxpayer is correct. If so, the auditor, in his or her discretion, may terminate the test and accept the amount of bad debt loss claimed by the taxpayer. In reaching this conclusion prior to completing the test, the auditor must consider all factors relevant to the sample, the most important of which is the size and uniformity of the population. When the sample discloses material discrepancies among the lender's listing, the sample differences must be evaluated before projecting to the population. The Board's Statistical Sampling Evaluation program will be used to evaluate the differences. If the sample evaluates well, a percentage of error should be computed and applied to the population of transactions included on the lender's listing to determine the allowable refund amount. If the sample discloses discrepancies and does not evaluate well, staff should consider expanding the sample.

2. **Statistical Sampling:** The lender has provided a listing of the bad debt accounts written off per their books but they have not computed the allowable bad debt loss as described in Regulation 1642(d). The amount listed may include non-taxable elements such as tax, license, interest, late fees, repossession fees, etc. Staff must perform a statistical sample of the transactions to compute the allowable portion of the bad debt loss. Staff must follow the guidelines for performing a statistical sample set forth in Audit Manual Chapter 13. Staff must select a sample size to examine no fewer than 300 transactions. If the population is less than 300, the transactions should be examined on an actual basis. The lender must provide a listing for the sample that computes the allowable portion of the bad debt on a transaction-by-transaction basis in accordance with Regulation 1642(d). Staff must verify the accuracy of the sample data.

Under this method, the lender provided the total write off amount for the population. It includes items not allowable under Regulation 1642. The sample is used to compute an audited allowable amount on a transaction-by-transaction basis. Thus every transaction examined in the sample will show a difference between the audited and claimed bad debt. These differences must be evaluated using the Board's Statistical Sampling Evaluation program. When the sample evaluates well, it will be used to compute an audited allowable bad debt percentage. The allowable bad debt percentage is the audited allowable amount per the sample (computed in accordance with Regulation 1642) divided by the total bad debt claimed in the sample. The allowable bad debt percentage will be applied to the total claimed bad debt to arrive at the total audited allowable bad debt amount. If the sample differences do not evaluate well, staff should consider expanding the sample. On the other hand, the auditor may discover no material discrepancies after testing a sufficient portion of the sample that the auditor is comfortable in concluding the amount of bad debt loss claimed by the taxpayer is correct. If so, the auditor, in his or her discretion, may terminate the test and accept the amount of bad debt loss claimed by the taxpayer. In reaching this conclusion prior to completing the test, the auditor must consider all factors relevant to the sample, the most important of which is the size and uniformity of the population.

3. **Mean Allowable:** The third method is similar to the second method described above. Under this method a mean allowable bad debt per account is computed in lieu of an allowable percentage. The verification procedures staff must perform are identical to those described in method two above.

When the sample evaluates well, it will be used to compute an audited allowable mean bad debt per account.

The mean allowable amount per account is computed by taking the allowable write off amount per the sample (computed in accordance with Regulation 1642) divided by the total number of accounts examined in the sample. The mean allowable amount per account will be applied to the total number of accounts contained in the population to arrive at the total allowable bad debt. If the sample differences do not evaluate well, staff must expand the sample or provide adequate comments to support the application of the results of the sample.

Required Documentation — Vehicles: The following is a list of information staff must review when verifying a claimed bad debt deduction or refund incurred in connection with the financing of a vehicle. However, to the extent this information is not relevant to the actual computation of the allowable bad debt deduction or deallocation of tax, it need not be scheduled. For example, if a statistical sample uses the loan origination number as the basis for selection, this number must be available for all transactions within the population and must be scheduled. If there is a valid reason for not scheduling that information, adequate supporting comments must be included explaining how the information was made available and why it was impractical to include such information in the supporting schedules.

Total Population of Claim on Electronic Media (disc or CD-ROM)

- Must exclude or readily identify loans that do not qualify
- Must identify loan origination date (date contract entered into)
- Must include seller's/dealer's name and address (city and state)
- Must include consumer's name and address (city and state)
- Must include the following additional information:
 - Reference number – number assigned to each loan
 - Type of vehicle/property – e.g., vehicle, RV, mobile home, etc.
 - Date of repossession charge off – the date charged off for income tax purposes
 - Loan number – actual loan account number
 - Charge off or loss per records – amount charged off for income tax purposes
 - Summarized number of transactions in each local tax and district tax area

Sample Selection

- Minimum sample size of 300 loan contracts selected using statistical sampling procedures (i.e., random, systematic with random start, etc.). If the total population is equal to or less than 300, verification will be on an actual basis.
- For each loan in the sample - evidence that the uncollectible portion has been charged off for income tax purposes or in accordance with GAAP. Printouts from taxpayer accounting system will suffice.
- For losses claimed under Regulation 1642(h)(3) and (i), an election agreement for each loan as required by Regulation 1642 (i)(3)(A) and, if applicable, the election agreement required by either Regulation 1642 (h)(3)(A) or (i)(4)(A).

Documentation and Information for Selected Sample

- Complete contract file, including the “No Recourse” statement. If “No Recourse” statement is not available, copy of the contract/agreement between dealer and the financial institution establishing that the lender holds the account without recourse.
- Reference number – number assigned to each loan
- Loan origination date – date contract entered into
- Date of repossession charge off – the date charged off for income tax purposes
- Loan number – actual loan account number
- Sales price of vehicle – total amount subject to tax including document preparation charge and taxable smog
- Nontaxable charges such as charges for optional service contracts, Smog Impact Fee, Smog Check Certificate fee, etc.
- Sales tax reimbursement collected from the consumer on sale
- Vehicle License Fee
- Insurance – net amount
- Down payment
- Any adjustments to the principal
- Finance charges – net amount
- Payments on principal
- Value of repossession – sales price for subsequent sale
- Charge off or loss per records – amount charged off for income tax purposes
- Repossession expense – auctioneer’s fees, reconditioning, etc.
- Recovery – payments made after the loan is charged off on records
- Reversals – adjustments for non-sufficient funds (NSF) checks, etc.
- Taxpayer must compute the amount of refund per Regulation 1642

Local Tax Verification: When reviewing a claim for refund under WFS or Regulation 1642(h)(3) and (i), it is imperative the local and district taxes are properly deallocated. For example, when the claimed bad debt loss relates to sales of vehicles, the name and address of the dealer and consumer must be included for each transaction scheduled to properly deallocate the local and district taxes on an actual basis. For loans approved by the lender on a transaction-by-transaction basis, the lender should allocate the local and district taxes on an actual basis. In cases where transaction-by-transaction information is not available and the deallocation cannot be done on an actual basis, the regulation provides that the lender may allocate local and district taxes on an appropriate basis subject to approval by the Board. When verifying the accuracy of such an alternative method, the field auditor must fully explain (1) the basis for concluding whether the alternative method is accurate and (2) specifically how the local tax deallocation

was calculated.

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CREDIT FOR TAX PAID TO OTHER STATES, SECTION 6406 CREDIT

0419.20

Credit for sales or use tax imposed by other states and paid on purchases of tangible personal property may be taken as a credit against the amount of tax due. The property must have been purchased for use, consumption or storage (not resale) in California, ~~and the tax paid must have been legally due in the state to which it was paid.~~ The department's administrative practice is not to question the validity of the imposition of a tax by another state. If the purchaser can show that tax was paid to another state on a transaction subject to use tax in California, the credit is allowable.

The only two exceptions to this general practice are: (1) when the taxpayer obtains a refund of the tax paid to the other state prior to our review of the transaction, or (2) when it can be shown that the purchaser or vendor is intentionally reporting tax to the other state in order to take advantage of the section 6406 credit.

With respect to vehicles, vessels and aircraft, the section 6406 credit shall be denied when tax on the sale or purchase of the vehicle, vessel or aircraft was first due in California.

Auditing procedure normally includes verifying the purchase invoices to ascertain that the purchase price was included on Line 2 of the return and to verify the amount of section 6406 credit claimed on the return. The auditor must also verify that the tax (amount of credit claimed) was paid either to the retailer located in another state or to that state itself. ~~The tax which was paid must have been properly imposed on the purchaser.~~ Section 6406 also provides that credit is not allowed on out of state tax measured by periodic payments made under a lease for a period prior to the storage, use or other consumption of the property in this State.

The amount of tax credit claimed may not exceed the lesser of (1) the tax actually paid and owed to another state, or (2) the tax computed using the combined state and local tax rates in effect at the time the property was first brought to California. Section 0203.16 describes the method of handling the difference developed in this portion of the audit.

The section 6406 credit is apportioned to the county tax and transit tax against which it is allowed in proportion to the amounts of those taxes.

AUDIT OF CHARITABLE ORGANIZATIONS

0419.30

Sales made by charitable organizations are exempt provided the conditions included in Regulation 1570 are met. Compliance Policy and Procedures Manual section 255.050 also contains information relating to charitable organizations.

Included among the conditions that must be met is that each year a “welfare exemption” from property taxation must be secured. The exemption claim is filed through the County Assessor’s Office by March 15 of each year. Sales are taxable during a year for which an organization does not qualify for a “welfare exemption.” The procedure by which an organization qualifies for an exemption appears in CPPM. The auditor should ascertain that the exemption covers all real and/or personal property owned by the organization and situated at the location from which the sales are made. An organization not owning the real property must qualify for an exemption of the personal property at that location.

Organizations that started after the filing date should make application to the County Assessor to find out whether or not they qualify for the exemption. The organization should receive a letter, which informs them that they qualify, from the Assessor or [Division of Assessment Standards the Assessment Policy and Standards Division of the Board’s Property and Special Taxes Department](#). Such a letter exempts them from the payment of sales tax pending their qualifying at the normal filing time.

Sales or use tax applies to sales to charitable organizations of tools, supplies, and equipment when the property is used or consumed by the organization. Effective January 1, 1990 sales or use tax does not apply to purchases by the organization of tangible personal property for the purpose of donation.

All claimed exempt watercraft sales must be supported by properly completed exemption certificates. It is especially important that questionable certificates be followed up to substantiate their validity.

Occasionally a purchaser may issue an exemption certificate for items that may be taxable or nontaxable depending upon attachment and/or usage. In which case, items of a consumable nature should be considered as taxable unless the purchase order indicates these items as exempt.

The sales of watercraft and their component parts are exempt, provided the conditions included in Regulation 1594 are met.

To be considered a "component part" of a watercraft for purposes of the exemption the property must be an integral part of the watercraft, affixed or attached thereto in a substantial manner when in use. All property affixed or attached to the structure of the watercraft used while thus affixed or attached for navigation, operation, or for the comfort or convenience of the passengers and crew is exempt.

Property is not considered a component part of a watercraft for purposes of the exemption if it is a kind commonly treated as expense items and is not affixed or attached to the watercraft in a substantial manner when in use. For further details, see Pamphlet Number 40, Tax Tips For The Watercraft Industry.

~~During an audit of a California aircraft dealer or dealer/broker the auditor shall schedule leads on certain apparently valid and properly supported exempt sales of aircraft as follows:~~

- ~~• All exempt sales to nonresidents other than bonafide dealers~~
- ~~• Any exempt sales to common carriers or foreign governments which seem to be valid but which might have some questionable aspects~~
- ~~• All brokerage transactions~~

~~Form BOE 379 A, Aircraft Exempt Sale Referral, was developed for this purpose (Exhibit 11). The auditor shall perform sufficient verification to ensure that no transactions are listed which are properly the liability of the taxpayer under audit, i.e., list only transactions which audit verification indicates are the responsibility of the purchaser rather than the dealer.~~

~~Whenever the auditor disallows sales of aircraft to nonresidents, convincing verification should be obtained that the purchaser was or is a California resident. Evidence of a factual abode of some permanency in California should be obtained in these situations:~~

~~It should be determined that the dealer has not in effect encouraged false documentation. If it can be established that the dealer knew the facts stated in the documentation were not true, the tax plus applicable interest and penalties should be assessed against the dealer. A dual determination against the purchaser might be justified in some situations.~~

~~All such listings of transactions should provide as much information as possible but should include as a minimum: The name and address of the purchaser and seller; the type of aircraft including make, size, description and identification number; the state in which the aircraft is registered; the selling price; and the basis on which the transaction was claimed as exempt, i.e., nonresident, common carrier, foreign government or brokerage. A separate Form BOE 379 A should be prepared for each transaction.~~

~~Transactions should also be listed during audits of other accounts involving exempt sales or aircraft where the purchaser would be responsible for tax such as:~~

- ~~• Sales of aircraft by other instate sellers (nondealers) to residents and nonresidents.~~
- ~~• Sales of aircraft by out of state sellers (dealers and nondealers) to California residents and sales to nonresidents that may have some indications that the aircraft was purchased for use in California.~~

~~The Forms BOE 379 A on such ostensibly exempt sales transactions should be forwarded directly to the Consumer Use Tax Division. They will correlate this data with their own sources of information and prepare use tax billings where appropriate.~~

NEW OR REMANUFACTURED TRUCKS, TRUCK TRACTORS, TRAILERS, OR SEMITRAILERS

0419.45

Sections 6388 and 6388.5 provide sales and use tax exemptions on the sale, or storage, use or other consumption of certain vehicles and trailers delivered inside California. Regulation 1620.1, *Sales of Certain Vehicles and Trailers for Use in Interstate or Out-of-State Commerce*, clarifies these exemptions and describes the records needed to support the exemptions.

Section 6388 Exemption (Regulation 1620.1(b)(2)):

This exemption typically shows up in audits of vehicle manufacturers or remanufacturers who deliver a vehicle [as defined in subdivision 1620.1(a)(8) "vehicle" includes certain trailers] to a purchaser who is not a resident of California for use exclusively in out-of-state or foreign commerce, when the purchaser:

1. Purchases the vehicle from a dealer located outside California.
2. Removes the vehicle from California within 30 days from the date of delivery.
3. Provides an affidavit to the manufacturer or remanufacturer, stating:
 - a. The name and location of the out-of-state dealer from whom the vehicle was purchased.
 - b. The name and location of the in-state manufacturer or remanufacturer that delivered the vehicle to the purchaser and the date of delivery.
 - c. That the purchaser is not a resident of California.
 - d. That the vehicle was purchased for use exclusively outside California.
 - e. That the vehicle was removed from California within 30 days of the delivery date, and
 - f. The date of removal, and
4. Provides evidence of out-of-state vehicle registration [state of registration, license plate number and Vehicle Identification Number (VIN) or serial number] to the manufacturer or remanufacturer within 60 days of providing the affidavit to the deliverer.

To file the affidavit, the purchaser should use form BOE-837. Alternative documentation is permissible as long as it contains all the information required by form BOE-837.

Audits of vehicle manufacturers and remanufacturers: Manufacturers and remanufacturers should have an affidavit and registration documentation on file to support a claimed exempt transfer of a vehicle. *Note:* It is rebuttably presumed that a vehicle registered outside California and apportioned for use within California is not purchased for use exclusively outside California.

Audits of purchasers: The Board may audit purchasers claiming exemption under Regulation 1620.1(b)(2). Under this exemption, purchasers must maintain internal records documenting that the qualifying vehicle was taken out of California within the time mandated by statute and was used exclusively outside California. Examples of documentary evidence are bills of lading showing the first functional use of the vehicle, vehicle logs/reports, fuel receipts, hotel bills, and copies of license or registration fee receipts showing the date of payment. Purchasers should also be able to show that they are residents of somewhere other than California.

Section 6388.5 Exemption (1620.1(b)(3)):

This exemption typically shows up in audits of trailer manufacturers or remanufacturers, dealers, or purchasers. To qualify for exemption, the purchaser must use the trailer exclusively in interstate, out-of-state, or foreign commerce and meet the following criteria:

1. A trailer that is manufactured or remanufactured outside California must be removed from California within 30 days from the date of delivery; or a trailer that is manufactured or remanufactured within California must be removed from California within 75 days from the date of delivery.
2. If the trailer is registered outside the state, the purchaser or purchaser's agent provides the delivering manufacturer, remanufacturer, or dealer a copy of the current out-of-state license and registration for the trailer showing the VIN or serial number; or, if the trailer is registered in-state under the PTI (Permanent Trailer Identification) program, the purchaser or purchaser's agent provides the delivering manufacturer, remanufacturer, or dealer a copy of the federal document assigning or confirming the purchaser's or lessee's USDOT (United States Department of Transportation) number, FMC (Federal Maritime Commission) number, or a copy of the current SSRS (Single State Registration System) filing with the DMV. A purchaser or purchaser's agent may not use an FMC number if the purchaser has a current USDOT number. Evidence of registration outside California must be submitted to the dealer, manufacturer, or remanufacturer no later than 60 days after the timely providing of an affidavit described in subdivision 1620.1(b)(3)(A)3. Evidence of a USDOT number, FMC number, or SSRS filing must be submitted with the affidavit. [Descriptions of the PTI, USDOT, FMC, and SSRS programs are described in Regulation 1620.1(a).]
3. The purchaser or purchaser's agent must also provide a valid affidavit to the manufacturer, remanufacturer, or dealer, stating:
 - a. The name and location of the dealer from whom the trailer was purchased,
 - b. The name and location of the California dealer, manufacturer or remanufacturer that delivered the trailer to the purchaser and the date of delivery,
 - c. That the vehicle was purchased for use exclusively outside the state, or exclusively in interstate or foreign commerce, or both,
 - d. That the vehicle was removed from the state within the appropriate time periods provided for in subdivision 1620.1(b)(3)(A)(1), and
 - e. The date of removal.

As noted in the previous section, the purchaser must use form BOE-837 or its equivalent as the affidavit.

Audits of purchasers: Purchasers of trailers under this exemption must maintain internal records documenting that the qualifying trailer was taken out of California within the mandated time and was used exclusively in out-of-state, foreign or interstate commerce. Examples of documentary evidence are bills of lading (also indicating the first functional use of the vehicle), vehicle logs/reports, fuel receipts, hotel bills, and copies of license or registration fee receipts showing the date of payment.

Note: the exemption under 1620.1(b)(3) only applies to trailers and semitrailers – it does not apply to trucks or truck tractors.

All claimed exempt sales of new or remanufactured vehicles must be supported by written evidence of out of state license and/or registration and an affidavit as required by section 6388 or 6388.5. The affidavit can be in any form provided it satisfies the requirements of those sections (Exhibit 12). However, for any affidavit to be valid, written evidence of out of state license and/or registration is required. The written evidence of out of state license and/or registration can be in the form of a prorate registration even though the vehicle is base plated in California.

In auditing a purchaser who is engaged in business in this state, the purchaser must provide documentary evidence that any vehicle claimed as exempt pursuant to section

~~6388 or 6388.5 was removed within the time provided by these sections. Examples of documentary evidence are fuel receipts, hotel bills, bills of lading for the first use of the vehicle and copies of license or registration fee receipts showing the date of payment. For the exemption under section 6388 to apply, the purchaser must also show that the vehicle was first used and functionally used thereafter out of state. For the exemption under section 6388.5 to apply, the purchaser must also show that the vehicle was used exclusively outside the state, or exclusively in interstate or foreign commerce, or both.~~

~~An example of use in interstate commerce is if the purchaser removed the trailer or semitrailer from this state within the appropriate time limits with an interstate payload. Failure of the purchaser to substantiate compliance with these two requirements are grounds for disallowance of the exemption and assessment of sales tax against the purchaser measured by the acquisition cost of the vehicle.~~

SALES TAX EXEMPTION FOR FOREIGN DIPLOMATS

0419.50

Effective February 15, 1986, the U.S. Department of State began issuing Tax Exemption Cards to foreign diplomatic personnel who are exempt from sales tax. Each card includes the name of the person to whom it is issued, personal identification information, a photograph, an expiration date, and a tax exemption number. Many diplomatic personnel who enjoyed an exemption from sales taxes under the former program (in which cards were issued by the Board) have been denied immunity entirely. The U.S. Department of State cards will specify either that the holder of the card is exempt from sales tax on all sales or that the holder of the card is exempt from sales tax only on transactions which exceed an amount stated on the card. For example, if the tax exemption card is granted for a minimum level of exemption of \$50, as indicated on the card, the purchaser must purchase merchandise aggregating over \$50 in a single transaction to qualify for the exemption. The total purchase may be composed of all taxable merchandise or a combination of taxable and non-taxable merchandise, i.e., a sale of cigarettes for \$6 is exempt if sold together with \$45 non-taxable food products. Separate purchases in the same store will not qualify if the amount of each transaction does not exceed the amount indicated on the card, even though the combination of all individual purchases in that store may exceed that amount.

To support the exemption, the retailer must prepare and retain an invoice or other written evidence of the sale and should enter the name of the purchaser, the number of the exemption card, the name of the foreign mission, the expiration date of the card, and the minimum level of exemption specified on the card, if any.

[Questions regarding the validity of tax exemption cards may be directed by telephone to the U.S. State Department, Office of Foreign Missions.](#)

~~The U.S. Department of State will provide the Board with quarterly printouts of current card holders and will respond to telephone inquiries regarding the validity of cards issued in the interim on a routine basis. The printouts will be maintained by the Special Projects Team of the Planning, Evaluation and Technology Section. Any questions regarding the validity of a card should be directed to that unit.~~

For special rules regarding sales of vehicles, see Chapter 6, "Vehicle, Vessel and Aircraft Dealers."

Taiwan Diplomats Tax Exemption Cards - The United States' Taiwan Relations Act established a nonprofit corporation called the American Institute in Taiwan, which functions much like a foreign embassy. The Act also exempted the Institute from any taxes imposed by any state or local taxing authority. Pursuant to the Act, the United States Department of State issues a tax exemption card to members of the Institute.

Sales or use tax does not apply to the sale or use of personal property sold to Taiwan diplomats holding a tax exemption card, to the level of exemption stated on the card. Questions regarding the status of a tax exemption card of a Taiwan diplomat may be made by telephone to the American Institute in Taiwan at (703) 525-8474. The fax number is (703) 841-1385. The address is 1700 N. Moore St., 17th Floor, Arlington, VA 22209.

When auditing businesses such as restaurants, fast food establishments, concessionaires, soda fountains, and other similar establishments particular attention should be paid to exempt food sales with respect to the 80-80 Rule of Regulation 1603. The 80-80 Rule applies if:

1. more than 80% of the retailer's gross receipts at a retail location come from the sale of food products (not including such items as carbonated or alcoholic beverages, or cigarettes) **and**
2. more than 80% of the retail food product sales are taxable because they are:
 - food products sold as a meal
 - food products furnished, prepared, or served for consumption at facilities provided by the retailer
 - food products ordinarily sold for immediate consumption at an establishment which is defined as a "drive-in"
 - food products sold as hot prepared food

Sales such as "cold food to go" which may become taxable under the 80-80 criteria **should not** be used in computing the taxable percentage.

Likewise, food which is furnished in a form **not** suitable for consumption on seller's premises **should not** be included in the computation. These foods will not become taxable even if the retailer meets the 80-80 criteria, and include such foods as:

- items not ordinarily consumed because they require further processing, cutting or assembly such as:
 - a whole cold chicken
 - party trays of meats and cheeses
 - hors d'oeuvres prepared and sold to go
- food products typically altered before being consumed
 - a dozen dinner rolls (assembled with a meal, cut and buttered)
 - a whole pie or cake (cut into individual portions)
- container size not suitable (obviously has more than one serving, and must be subdivided before serving)
 - one quart of salad
 - one quart of ice cream
 - bottled ice cream toppings
 - a loaf of bread
 - a bottle of barbecue sauce

When the taxpayer operates more than one type of food operation, e.g., several drive-ins and fast food restaurants or concession stands at swap meets or fairs, each individual location will be considered separately in determining if they meet the criteria.

For businesses that meet the conditions of the 80-80 Rule, food sales on a "take-out" or "to go" basis are subject to tax when the food is *in a form suitable for consumption on the seller's premises*. This includes bulk quantities of food sold in a "drive-in" establishment described in Regulation 1603(b). However, if a "drive-in" establishment does not meet the 80% criteria, the sales of items such as a dozen donuts or six pints

~~of milk will remain exempt under the definition of bulk quantities in the regulation.~~

~~If a retailer has a food operation business or a location of the type that would ordinarily meet the 80-80 criteria, they should report tax on all food product and beverage sales except: 1) the sale of cold food products in a form not suitable for consumption on the seller's premises (see above), and 2) exempt food sales to the U.S. Government or sales for resale. In addition, effective April 1, 1996, sellers that meet the 80-80 criteria can elect not to report tax on "to go" sales of cold food products, e.g., hot beverages, and hot bakery goods. In order to do so, those sales must be separately accounted for and substantiated by supporting documents, such as cash register tapes. Without adequate documentation, sellers are required to report tax on such sales, and a test should be made to determine if all sales should be taxable under the 80-80 Rule.~~

~~If the test of current sales does not meet the 80-80 criteria, but falls in the range of 75%-80%, the taxpayer should be advised to periodically test sales to insure that the 80-80 criteria is not exceeded, and to apply tax prospectively if the criteria is exceeded. The taxpayer must document and retain the results of any tests performed.~~

AUDIT OF MOTOR VEHICLE FUEL RETAILERS — PREPAYMENT OF SALES TAX

0431.00

GENERAL

0431.05

~~Distributors and brokers~~ Effective January 1, 2002, wholesalers and suppliers subject to the motor vehicle fuel ~~license~~ tax are required to collect prepayments of the retail sales tax from their purchasers on the first distribution-removal of fuel at the terminal rack or upon entry into this state and all subsequent transfers of motor vehicle fuel except aviation gasoline in this state. This process continues down to the level of the motor vehicle fuel retailer. Each person making prepayments to suppliers may claim the amount paid as a credit against their sales and use tax liabilities due for the same period. The initial point of imposition was previously on the first distribution of fuel in this state.

All routine audits of motor vehicle fuel sellers must include verification of the accuracy of prepayments made and claimed under the “SG” and sales and use tax programs. Since two separate tax programs and funds are involved, it is critical that audit differences attributable to each program be properly identified and uniformly handled.

REPORTING REQUIREMENTS

0431.10

All retailers of motor vehicle fuel subject to the provisions of the “Prepayment of Sales Tax on Motor Vehicle Fuel Program” should be utilizing a modified sales and use tax return (BOE-401-GS). This return includes a Schedule G (BOE-531-G) which allows the retailer to:

- claim credit for prepayments made on purchases of MVF, ~~and~~
- claim credit for tax paid to other states.

A net figure is carried forward from Schedule G to Line 21-20 on the face of the sales and use tax return.

AUDITING PROCEDURES

0431.15

A subsidiary schedule will accompany all gasoline retailers’ BOE-414- (Transcript of Returns Filed — Sales and Use Tax). This schedule will reflect amounts reported and claimed on Schedule G of their returns. Such amounts should be verified along with other return amounts. Schedule G must be completely and correctly prepared to ~~insure~~ ensure proper funding and allocation of tax. Particular attention should be given to:

- **Credit for Sales Tax Prepaid to ~~Distributors or Brokers~~ Fuel Suppliers**

— All credits claimed must be supported by invoices showing the amount of sales tax prepaid to licensed ~~distributors or brokers~~ suppliers or wholesalers. Invoices must show the precollection as a separate amount and include the ~~distributor’s or broker’s supplier’s or wholesaler’s~~ “SG” account number. If the “SG” number is not listed on the purchase invoice, it should be verified that the supplier does hold the required “SG” permit. If a separate statement of the precollection is not shown on the invoice, no credit will be allowed. While the proper time to claim the credit is the period in which the purchase has been made (generally, the period in which the invoice date is included), the credit should not be disallowed merely because it was claimed in a subsequent period.

It is **critical**, however, that amounts claimed on the return reconcile to the |
invoiced amounts.

**PROCEDURES WHERE RETAILER IS ALSO A
DISTRIBUTOR/BROKERSUPPLIER/WHOLESALER**

0431.20

All taxpayers holding an “SG” account will have that account examined in conjunction with their related sales and use tax account.

On occasion a ~~distributor/brokersupplier/wholesaler~~ will sell gasoline at retail, claim the prepayment credit on their SG return and not pass the credit on to their retail account. Rather than assessing the “SG” account and crediting the related sales tax account, the auditor should comment on the back of the audit report/FBO or on the front of the BOE-596 under general comments, that a prepayment offset has been allowed. These comments will assist the Refund Section in their reconciliation of the sales tax prepayments on MVF by noting that the problem has been addressed.

Where a ~~distributorsupplier~~/retailer makes their first ~~distribution-sale~~ at retail (into the tank of a motor vehicle) and nets the precollection and credit from both the “SG” and sales and use tax return, ~~you-the auditor~~ need not adjust the return amounts.

LOCAL TAX ALLOCATION

0431.25

Routine audit procedures should be utilized with regard to the examination of the retailer’s reported local tax amounts. Since the “Sales Tax Paid to ~~Distributors and BrokersFuel Suppliers~~” credit is taken after the local tax allocation has been computed, no special field procedures are required.

BAD DEBTS

0431.30

Retailers who are not ~~distributors or brokers-wholesalers or suppliers~~ should have no bad debt credits related to prepayments.

ELIGIBILITY FOR REMOVAL FROM PREPAYMENT STATUS

0431.35

Taxpayers who have requested and been removed from prepayment status on their returns (~~as provided insee~~ sections 6471 and 6471.4), must continue to meet the criteria for removal. It should be verified that the taxpayer continues to qualify: i.e., taxable sales of motor vehicle fuel exceed 75% of their gross receipts. The most recent twelve-~~—~~month period should be examined. Compliance staff should be advised of those who no longer qualify.

CLOSE-OUTS

0431.40

The credit for prepayments made to suppliers by the seller of a business **cannot** be transferred to the purchaser of that business. Any prepayment credits remaining at the time of closeout should be claimed on the final return.

WORKING PAPERS

0431.45

Audit workpapers will follow procedures similar to those currently used in adjusting a section 6406 tax credit. A separate audit schedule should be prepared for each Schedule G line item requiring correction, indexing each schedule as G, followed by the line number of the item being adjusted (e.g., Schedule ~~G4-G3~~ — Total Sales Tax Paid ~~to Distributors and Brokers~~). A detailed schedule of differences should also be shown and segregated by month, vendor name and “SG” account number. The audit workpapers showing these differences should accompany the audit report transmitted to ~~the~~ headquarters.

Verification comments should include a discussion of what work was done to verify all items related to Schedule G amounts, i.e., repayment of the one-time credit, credit for sales tax paid to [distributors/brokerswholesalers/suppliers](#), carry-over of the one-time credit and credit for tax paid to other states.

SPECIAL MOTOR VEHICLE FUEL TRANSACTIONS

0432.00

RETAILERS WHO PREMIX OR BLEND MOTOR VEHICLE FUEL AND LUBE OIL

0432.10

A retailer who purchases motor vehicle fuel and adds lubricating oil thereby making premixed fuel which they sell as boat fuel to consumers is technically acting as a [distributorsupplier](#). Because of the small quantities of premix blended by such retailers, and the insignificant amounts of gasoline tax involved, it is not administratively practical to require them to be licensed as [distributorsuppliers](#), post bond, and file monthly returns.

Retailers (usually boat marinas) who purchase motor vehicle fuel and add lubricating oil, thereby making premixed fuel which they sell to consumers are making taxable sales of premix and the entire selling price, including state and federal excise taxes, is subject to sales and use tax.

RETAILERS WHO PURCHASE PREMIX FROM A [DISTRIBUTORSUPPLIER](#)

0432.15

The auditor should see that the manufacturer-supplier of premixed fuel is licensed as a [distributorsupplier](#), or that wholesaler-supplier of premix fuel is licensed as a [brokerwholesaler](#).

CREDIT CARD SALES

0432.20

The service station [dealer-operator](#) is responsible for sales tax on the retail selling price of all motor vehicle fuel and other products sold or delivered by them unless adequate support is maintained for any deduction claimed. Duplicate credit card invoices generally are acceptable in support of exempt transactions.

MASTER CONTRACT SALES

0432.25

Some oil companies enter into master sales contracts with consumers to provide motor vehicle fuel and other products for delivery through company-owned or independent [dealer-operator](#) service stations at specified prices. Examples of this are the contracts the State of California had with some of the major oil companies for motor vehicle fuel and other supplies.

The oil company becomes the retailer of the fuel sold and delivered at the service station level pursuant to the contract and is responsible for the sales tax on such sales. The independent service station [dealer-operator](#) is making sales for resale and should obtain a resale certificate from the oil company involved to cover such sales.

Generally, contract sales are recorded at the service station level on a credit card invoice at the pump price which includes sales tax reimbursement. The purchaser is billed by the oil company at the contract price plus sales tax reimbursement on the contract price. In reporting and paying tax on these sales, the oil company is not allowed to claim a tax-paid purchases resold credit.

If the independent service station operator receives credit from the oil company for the full amount of the credit card charge, the operator will be receiving credit for sales tax reimbursement. Therefore, in addition to maintaining documentation as to the amount of the sale and the fact that it is a sale for resale, the independent service station operator should have records to show that sales tax reimbursement was not received and retained on any portion of the sale. In some cases, this will consist of a

computer listing received from the oil company, at the end of each accounting period reflecting the charge back to the [dealer-operator](#) of the full amount of sales tax reimbursement on the credit card invoices for master contract sales, and the amount of sales to which the tax applies.

SALES TO THE U.S. GOVERNMENT

0432.30

Generally these sales are recorded at the service station level on a credit card invoice at the pump price which includes sales tax reimbursement. Since such sales are entirely exempt from sales tax, the service station operator must have documentation to support the deduction. Some oil companies make a charge back to the [dealer operator](#) for the amount of the tax. The charge back is supported by a computer printout notifying them of the amount of sales to the U.S. Government included in their credit card sales. The charge back and printout are acceptable as proof of sales to the U.S. Government.

In some instances, the burden of support for these exempt sales may fall entirely upon the [dealeroperator](#), in which case reliance would be placed on copies of credit card invoices reflecting that the sale was to the U.S. Government and a reduction of the selling price by the amount of sales tax included. Copies of such credit card invoices are acceptable as support for the deduction. It is anticipated that, if necessary, the oil company credit card department will be able to furnish the local [dealer-operator](#) with further documentation. In any event, the auditor should insist on adequate support for the deduction.

SALES TO LOCAL GOVERNMENTS

0432.35

Sales to local government entities (cities, counties, and school districts) are made by local service stations at regular pump prices. With the exception of a few local governments which have participated in the State's master contract, these sales generally are not made pursuant to any negotiated contract, and the [dealer-service station operator](#) is responsible for reporting and paying the sales tax. Sales to local governments who have participated in the State's master contract should be handled in the same manner as outlined in section 0432.25.

Sales of diesel and special motor vehicle fuels (excludes gasoline) to local governments are exempt from the federal excise tax. However, it is the general practice to bill the total pump price on the credit card sales slip. At the time the credit card invoice is turned into the oil company for credit, the oil company normally credits the [dealer operator](#) for the full amount of the invoice, including sales tax. In turn, the oil company bills the local government the price shown on the credit card invoice less the federal excise tax and charges sales tax reimbursement on the net amount. The oil company then claims the credit as a deduction on its federal excise tax return. This results in a reduction in the sales price of the motor vehicle fuel. If the oil company notifies the local [dealer-service station operator](#) of the amount of federal excise tax not billed to local governments **and** adjusts its credit to the [dealer-operator](#) for the amount of sales tax thereon, the [dealer-operator](#) is entitled to adjust his reported gross receipts by the amount of the federal excise tax. If the [dealer-operator](#) receives credit for the full pump price plus tax thereon, and no adjustment is made, the [dealer-operator](#) will be held responsible for sales tax on the total amount of the sale since the [dealer's operator's](#) gross receipts remain unchanged.

Sales of gasoline to local governments are no longer exempt from the federal excise tax.

SALES OF GASOLINE FOR USE IN AIRCRAFT

0432.40

Sales of gasoline for use in propelling aircraft are exempt from sales tax provided the distribution and sale of the gasoline is subject to the California motor vehicle fuel ~~license~~-tax and not subject to refund. Since January 1, 1990, no refund of any motor vehicle fuel tax has been granted for fuel used in propelling aircraft. In recent years there has been increasing use of automotive gasoline to propel small aircraft. The automotive gasoline is normally delivered into the aircraft when sold at an airport, however automobile service stations may sell gasoline for use in propelling aircraft and deliver it into the purchaser's storage containers.

The exemption for gasoline delivered directly into the fuel supply tank of an aircraft may be supported by a properly completed sales invoice or an aircraft exemption certificate. If a sales invoice is used, it must show the purchaser's name and address, the aircraft identification number, the number of gallons sold, the price per gallon, the amount of the sale, and the name and address of the seller. If the aircraft fuel is delivered into the purchaser's storage facilities, the exemption should be supported by an aircraft fuel exemption certificate as well as a sales invoice. A suggested form of an aircraft exemption certificate is included in Regulation 1598.

Gasoline used for inflight testing of aircraft is used for propulsion of aircraft and is exempt from sales or use tax. This exemption applies only to gasoline used for *propelling aircraft*. Gasoline used while the aircraft is *stationary* during construction or during the repair, modification, or maintenance of aircraft is not exempt from the tax.

In years past, aviation gasoline was sometimes used in boats, motor vehicles, and stationary equipment. Because of the high price and limited availability of aviation gasoline, these other taxable uses will rarely be encountered.

SALES TO AIRCRAFT COMMON CARRIERS AND OPERATORS OF WATERBORNE VESSELS

0432.45

Effective July 15, 1991, sales of fuel and petroleum products delivered to the purchasing carriers in California are subject to sales tax except as provided by Regulation 1621(b)(3)(B) for air common carriers. ~~___ and 1621(b)(3)(C) for water common carriers.~~ The seller must obtain an exemption certificate (See Regulation 1621) from the common carrier to support the claimed exemption. Between July 15, 1991 and December 31, 2002, a similar exemption existed for water common carriers. The water common carrier exemption was discontinued from January 1, 2003 to March 31, 2004. The exemption was reinstated April 1, 2004 and remains in effect until January 1, 2014.

SALES TO AUTO LEASING FIRMS

0432.50

Sales of gasoline to firms leasing automobiles on a "wet rental" basis are sales for resale when the lease of the automobile is a "continuing sale". A "wet rental" is one in which the total rental charge includes gasoline furnished by the lessor.

If the lessor has paid sales or use tax with respect to their purchase of a leased automobile, or if the lease is of mobile transportation equipment, the lessor is the consumer of gasoline furnished under a "wet rental," unless the sales price of the gasoline is separately stated from the vehicle rental charge.

Sales of gasoline to lessors for resale should be substantiated in the same manner as other sales for resale. Independent service station ~~dealers-operators~~ should document

such resales on credit card purchases with a resale certificate and a copy of the sales slip or statement showing the amount of the sale.

When a lessee on a “wet rental basis” purchases gasoline and is reimbursed by the lessor, the purchase is subject to sales tax since the service station ~~dealer-operator~~ is making a retail sale.

AUDIT OF FUEL
DISTRIBUTORS/BROKERS SUPPLIERS/WHOLESALERS –
PREPAYMENT OF SALES TAX

0433.00

GENERAL

0433.05

~~On the first taxable distribution in this state of MVF and most fuels subject to Use Fuel Tax, each distributor or broker is required to collect a prepayment of the retail sales tax from the person to whom the motor vehicle fuel is distributed/transferred. Once the prepayment requirement applies, each subsequent seller, other than the retailer, is required to collect and report the prepayment from their purchaser at the same rate. Fuels subject to the requirement to precollect sales tax include gasoline and gasohol (motor vehicle fuel); diesel, including dyed diesel; and aircraft jet fuel. Wholesalers and suppliers of these fuels are required to collect a prepayment of a portion of the sales tax when they remove fuel at the terminal rack, enter fuel into California, or sell the fuels at any point after removal from the terminal rack. Retailers or other sellers of fuel who have prepaid the sales tax to their suppliers may claim a credit for that prepaid tax when they file their sales and use tax returns.~~

Each ~~distributor and broker~~ supplier and wholesaler must furnish their customer with a receipt or invoice separately stating the amount of precollected tax. ~~Distributors and brokers~~ Suppliers and wholesalers are required to show their “SG” account number on their receipts and invoices.

All taxpayers holding an “SG” account, must have this account investigated 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 “SG” accounts with their related sales and use tax account and ensure that amounts are being properly reported.

Amounts reported under the “SG” program will be posted to a ~~modified BOE 414-MVU~~ BOE-414-SG Transcript of Returns Filed – SG Fuel Accounts. ~~This form will be annotated in the upper left hand corner indicating that scheduled amounts relate to the taxpayer’s “SG” returns. If the audit work sheet is prepared in the field, a blank BOE 414-MVU should be utilized.~~

PREPAYMENT CREDITS

0433.10

The amount of prepayment paid by a ~~distributor or broker~~ supplier or wholesaler to their supplier on the purchase of MVF will constitute a credit against the amount required to be collected and remitted to the Board on their prepayment return. Credits are to be taken for the period in which the purchase was made. All credits claimed must be supported by purchase documents, invoices and receipts which separately state the amount of tax prepaid. All purchase documents should be retained in the same manner as other books and records.

AUDITING PROCEDURE

0433.15

An inventory reconciliation should be made to verify that recorded withdrawals are correctly reported in gallons. Total gallons sold (excluding exempt ~~distributions~~ sales) times the prepayment rate should agree with the reported prepayment of sales tax.

~~In general, the auditor should verify claimed deductions in the same manner as in any other sales tax audit. With respect to exempt distributions to qualified distributors,~~

~~each office will have on file a list of qualified distributors. This list will be periodically updated by the Fuel Taxes Division of the Special Taxes Department.~~

On occasion a ~~distributor/brokersupplier/wholesaler~~ will sell gasoline at retail, claim the prepayment credit on their SG return and not pass the credit on to their retail account. Rather than assessing the “SG” account and crediting the related sales tax account, the auditor should comment on the back of the audit report/FBO or on the front of the BOE-596 under general comments, that a prepayment offset has been allowed. These comments will assist the ~~Centralized Review Audit Determination and Refund~~ Section in their reconciliation of the sales tax prepayments on MVF by noting that the problem has been addressed.

Where a ~~distributor/retailersupplier/wholesaler~~ makes their first ~~distribution sale~~ at retail (into the tank of a motor vehicle) and nets the precollection and credit from both the “SG” and sales and use tax return, ~~you the auditor~~ need not adjust the return amounts.

REPORTING ERRORS

0433.20

When a notified ~~distributor/brokersupplier/wholesaler~~ fails to collect the prepayment on their ~~distributionsale~~/transfer of MVF subject to the prepayment requirements, but can prove that the full sales tax has been subsequently reported, a notation to that effect should be made in the audit and such amounts should not be determined against the ~~distributor/brokersupplier/wholesaler~~. In such an instance, the ~~distributor or broker supplier or wholesaler~~ should be notified in writing of the precollection requirements. If the ~~distributor/brokersupplier/wholesaler~~ has not shown the precollection on the invoice and is unable to prove that the sales and use taxes due have been paid, the amount of unreported precollections should be determined against the ~~distributor/brokersupplier/wholesaler~~.

AUDIT WORKING PAPERS

0433.25

Schedule numbers should correlate with the line numbers on the “SG” return (e.g., Schedule ~~2a — Ex-tax Fuel Sold to Qualified Distributors~~^{2.1 Fuel sold to the United States Government or its agencies and instrumentalities}). Audited differences for each line category will be forwarded to a “Summary of Differences” Schedule, 414-SG-1.

Audited differences for “Tax Prepaid to California Vendors,” should also be forwarded to Schedule 414-SG-1. A detailed breakdown of audited amounts must be provided by month, vendor name and “SG” account number. This schedule should accompany the audit report ~~sent to the Audit Determination and Refund Section transmitted to the Centralized Review Section.~~

BAD DEBTS

0433.30

A refund of the prepayment may be allowed to any person who is unable to collect the prepayment from the purchaser, insofar as the sales of the fuel are represented by accounts which have been found to be worthless and charged off for income tax purposes. If any of those accounts are thereafter collected by the seller, the gallons of fuel represented by the amounts collected must be included in the next return and the prepayment on those gallons of fuel must be paid to the state.

LOCAL TAX ALLOCATION

0433.35

No local sales and use tax allocation is involved since no allocation of funds is made

until the prepayments are claimed by the retailer.

NEW CAR DEALERS

0433.40

Many new car dealers importing new vehicles into this state with partially filled fuel tanks are making the first taxable ~~distribution sale~~ of such fuel when the vehicle is sold at retail. Amounts attributable to such importation are generally considered too minimal to warrant registration of such dealers as ~~distributors-suppliers~~ under the MVF ~~License~~-Tax Law or the "SG" program. However, dealers who purchase gasoline for subsequent retail sale must be coded "G" (MVF retailer) and may require registration as a ~~broker/wholesaler~~, depending upon the type of operation.

MANAGED AUDIT PROGRAM

0435.00

The board's first managed audit program (MAP) was available to taxpayers from January 1, 1998 to January 1, 2003. There was no MAP in 2003. Beginning January 1, 2004, the MAP was reinstated through December 31, 2009. The new MAP differs from the previous program in that:

- Prepayment accounts may participate in the MAP.
- The Board may grant relief of liability under Revenue and Taxation Code section 6596 in cases where taxpayers who have participated in the MAP rely on erroneous advice from the Board and fail to pay amounts due.

The information in the following sections reflects the provisions of the MAP beginning January 1, 2004.

MANAGED AUDIT PROGRAM – GENERAL

0435.05

A managed audit is essentially a self-audit. Under the direction of a Board auditor, an eligible taxpayer is provided written and oral instructions to enable the taxpayer to perform the audit verification and prepare the working paper schedules necessary to complete a particular portion of the audit. The advantages to the taxpayer and to the state include the following:

- It is less likely that the taxpayer will feel it necessary to take audit issues through the administrative appeals process or litigate audit findings.
- The auditor will spend fewer hours on the audit and fewer hours at the taxpayer's business.
- Questions of taxability are more likely to be resolved during the audit process.
- The taxpayer is likely to become more knowledgeable about how the sales and use tax affects his/her business.
- Because of the knowledge gained from the managed audit, it is less likely that the taxpayer will be out of compliance in those areas he/she has audited.
- The taxpayer will be more familiar with the audit process.
- It is likely that a more cooperative, ongoing relationship with the Board will be established.
- Where a liability is disclosed, interest will be computed at one-half the normal rate.
- Section 6596 relief may be provided in cases where taxpayers who have participated in the MAP rely on erroneous advice from the Board and fail to pay amounts due.

ELIGIBLE ACCOUNTS

0435.10

It is extremely important that the auditor conduct a thorough review of the taxpayer's operations prior to proceeding into the managed audit process. Taxpayers should not be considered a candidate for the managed audit process if their business operations consist of transactions which require an in depth knowledge of the law.

While it is the auditor's responsibility to determine whether a taxpayer is eligible to participate in a managed audit, a taxpayer may initiate the review process by requesting ~~to conduct~~ a managed audit be conducted. For example, taxpayers seeking a tax clearance or who have been notified of audit may wish to conduct a managed audit to expedite the clearance or routine audit process. Staff should consider all reasonable requests for participation, keeping in mind our primary goal is the cost

savings in staff hours that can be used to perform other productive audits. Accordingly, interested taxpayers should submit their request for participation to the appropriate District Administrator/District Principal Auditor. In that application, the taxpayer is required to clearly explain how they meet the statutory requirements of Section 7076. Thus, the managed audit review process may either be initiated by the auditor or the taxpayer.

Accounts that may be eligible for the MAP shall include those meeting all of the following criteria:

- ~~• Any person who has not received written notification pursuant to section 6471 that he or she is required to make prepayments of tax (currently, those taxpayers with a measure of tax liability averaging \$17,000 or more per month);~~
- Any person whose business involves few or no exemptions;
- Any person whose business involves a single or small number of clearly defined taxability issues;
- Any person who agrees to participate in the MAP; and,
- Any person who has the resources to comply with the managed audit instructions provided by the Board.

Examples of situations in which a managed audit should not be used include cases where:

- The taxpayer's books and records are inadequate;
- The taxpayer has complex issues relating to the allocation or reallocation of local tax;
- The taxpayer is a business with inadequate achieved markups;
- The issues involved are very complex (for example, research and development contracts); or
- There is a question regarding negligence or intentional underreporting (fraud).

Although eligibility provisions contain some restrictive language, this should be balanced with the taxpayer and/or representative's level of sophistication in understanding and dealing with any issues that may arise. Any inquiries regarding the eligibility of an account for the MAP should be sent by the District Principal Auditor to the Program Planning Tax Policy Manager (with a "cc" to the Chief of Field Operations or the Collections and Third District Operations Division Manager).

APPLICATION OF INTEREST AND PENALTIES

0435.15

(a) Interest:

If a tax liability is disclosed as a result of an approved MAP audit, and the audit is completed pursuant to the participation agreement, interest will be computed at one-half the normal statutory interest rate for the total unreported tax liability. Interest will be calculated using the standard interest rate calculation rules, but at one-half the normal rate until the tax liability is paid in full unless the Board voids the agreement.

The one-half interest rate will apply even if the entire audit was not performed under a MAP audit and even if the portion performed by the auditor results in a tax liability. For example:

- An audit is conducted on a manufacturer whose only deduction is for sales for resale.
- It is agreed that the taxpayer will perform a managed audit of sales for resale and asset purchases, which discloses additional tax liability. This review would normally comprise a substantial portion of the audit if performed by the auditor.
- The review of lease transactions by the auditor also discloses additional tax liability. This portion of the audit is not deemed to be conducive to taxpayer review, and does not entail much expenditure of time by the auditor.

Under these circumstances the entire tax liability would be computed at the one-half interest rate since there was a MAP Participation Agreement. If the Board determines ~~if that~~ the taxpayer fails to comply with the provisions of the agreement or complete its portion of the MAP and the auditor finds it necessary to perform a significant amount of verification, the one-half interest rate will not apply. This will also be true if a negligence or fraud penalty is imposed during the audit period. (See section 0435.20(b).)

If the MAP audit results in a credit or refund, the standard net running balance method will be used to compute interest. If the audit has both debit and credit periods, the one-half interest rate would apply for debit periods and the full statutory credit interest rate would apply for credit periods.

(b) Penalties:

There is no change to procedures for applying penalties as warranted under the MAP. However, if after their preliminary review of records, the auditor feels believes that the taxpayer was negligent, a managed audit should not be conducted ~~as the taxpayer may also be negligent in conducting the managed audit~~. Nor should the managed audit be used if the auditor believes there was fraud during the audit period.

(c) Petitions for Redetermination or Claims for Refund

There is no change to procedures for filing timely petitions or claims for refund for managed audits.

AUDIT PROCEDURE

0435.20

It is primarily the responsibility of the auditor to determine whether a taxpayer should be considered for the MAP. The auditor's immediate supervisor is responsible for approval of the auditor's recommendation. This information must be documented by the auditor in the Assignment Contact History (Form BOE-414-Z).

(a) Preliminary Review

As part of the normal audit procedure, auditors will review the taxpayer's operations and determine whether the minimum eligibility requirements are met (as described in Section III) for the MAP. This includes a facility tour (if appropriate); a review of the chart of accounts, general ledger, Federal Income Tax returns, sales journals, sales invoices, depreciation schedules, purchase invoices, sales and use tax returns, and reporting procedures; and an evaluation of the taxability of the sales and/or purchases, as well as of the taxpayer's knowledge and understanding of the tax laws applicable to the transactions being reviewed. In addition to the minimum eligibility

requirements for the MAP, the taxpayer must also agree to perform a significant portion of the audit.

Audit staff may also consider the use of a Computer Audit Specialist to improve audit efficiency (reduce audit hours), if the account meets the criteria outlined in Audit Manual section 1304.40.

If all or a portion of the audit is allowed under MAP, any resulting tax liability, even for those areas of non-MAP, will be computed at the one-half interest rate. For this reason, the auditor must exercise judgment in considering accounts for eligibility under the MAP.

Following is an example of a taxpayer that would not be eligible under the MAP:

- An audit is conducted on a manufacturer whose only deduction is for sales for resale.
- After initial review of records, the auditor finds significant problems with the taxpayer's internal controls, missing sales invoices, and/or a total lack of documentation to support claimed resales.
- It is ~~determined that it is~~ necessary for the auditor to perform the test of resales, and ~~that~~ this will involve a significant amount of time similar to time that would normally be expended on the audit.
- ~~After Also during the~~ review, the auditor finds there are very few purchases that may be subject to use tax and that this will involve an amount of time similar to that ~~which would normally be expended on the an~~ audit.

In this case, the taxpayer should not be considered for a MAP audit and receive the benefit of the one-half interest rate because participation in a MAP would be of little benefit to the State in reduction of audit hours.

(b) Managed Audit Program Participation Agreement

After the auditor has discussed the taxpayer's eligibility for the MAP with his/her supervisor ~~either in person or via the telephone~~, and they are in agreement with the taxpayer's participation, the taxpayer should be presented with Publication ~~no.~~ 53, *Guide to the Managed Audit Program* which includes the *Managed Audit Program Participation Agreement* (Form BOE-526). The provisions of the MAP should be explained to the taxpayer. If the taxpayer agrees to participate in the MAP, Form BOE-526 will be completed by the auditor with the following information:

- Taxpayer's name and account number;
- Audit period;
- A reasonable time period (generally within 90 days) the taxpayer is allowed to complete the work ~~(generally within 90 days); however, audit staff should use their discretion to accommodate larger business operations;~~
- Information on the types of transactions and records to be reviewed; and
- The method for review and the periods for the records to be reviewed.

This agreement will then be signed and dated by the taxpayer and the District Principal Auditor. A copy of the signed agreement will be provided to the taxpayer. The original signed agreement must be attached to the completed Headquarters' audit report packet, with a copy retained in the audit working papers.

The Board may void the MAP agreement if it determines that:

- The taxpayer has failed to complete the managed audit by the due date in

accordance with the provisions in this agreement:

- The taxpayer has refused to cooperate with the Board during the verification process described in paragraph 4 of the agreement or has refused to cooperate with the Board if it audits any transactions pursuant to paragraph 5 of the agreement;
- Any penalties for negligence or fraud are imposed during the audit period under sections 6484, 6485, 6485.1, or 6514.1;
- There is jeopardy of collection under 6536; or
- The payment of the liabilities and interest was not made within the time period specified by the Board.

Before the Board can void a MAP agreement, a summary of the specific circumstances of the case and reasons for voiding the MAP must be provided to and approved by the Chief of Field Operations or the Collections and Third District Operations Manager. If the MAP agreement is voided, the taxpayer will not be entitled to the one-half interest rate. The taxpayer's actions should be documented on form BOE-414-Z, and the taxpayer should be notified in writing by the District Principal Auditor that the MAP Participation Agreement is terminated with an explanation of the reasons. The front of the audit report should continue to be marked as a managed audit for program evaluation purposes with an explanation for the termination shown on the back of the audit report. Also, the AUD MC screen in IRIS should have the flag set to "N" for managed audit, otherwise, the reduction in the interest rate will be triggered.

Participation in the MAP is voluntary on the part of the taxpayer. None of the above actions by the taxpayer should have a negative impact on how the audit is completed or the scope of the audit verification to be performed by the auditor. The only impact will be that the taxpayer will not receive the benefit of the one-half interest rate should the audit result in a tax liability.

(c) Verification of Taxpayer's Examination

A very important factor for the success of the MAP is the verification of work performed by the taxpayer. While it is not expected, nor necessary, that the auditor check 100 percent of the work performed by the taxpayer, the auditor should conduct a review of the work to the extent that the auditor is satisfied that the work performed is ~~substantially~~ accurate. This verification should confirm that the instructions provided to the taxpayer were followed accurately and that any problem areas of taxability were sufficiently addressed. The auditor should instruct the taxpayer to separately maintain the records (sales invoices, purchase orders, resale certificates, etc.) that the taxpayer used in its examination until the auditor verifies the taxpayer's examination.

(d) Audit Comments

The verification comments should describe test and verification procedures used by the taxpayer and auditor. In addition, comments should be made regarding any discussions with the taxpayer regarding areas of underreporting.

(e) Audit Report

The audit report should be prepared by the auditor and transmitted using

normal procedures; however, a notation should be made on the top right corner on the front page of the audit report indicating that this is a managed audit.

(f) Failure to Complete or Comply with Managed Audit Program Participation Agreement

- ~~— In the unlikely event the taxpayer, after entering into a MAP Participation Agreement, elects not to complete the audit or cooperate with the verification, the auditor will complete the audit as normal. The taxpayer will not be entitled to the one-half interest rate. The taxpayer's actions should be documented on Form BOE-414-Z and the taxpayer should be notified in writing by the District Principal Auditor that the MAP Participation Agreement is terminated with an explanation of the reasons. The front of the audit report should continue to be marked as a managed audit for program evaluation purposes.~~
- ~~— Should the taxpayer, after entering into a MAP Participation Agreement, elect not to perform the audit as agreed and the auditor finds it necessary to perform a significant amount of verification, the one-half interest rate will not apply. Again, the taxpayer's actions should be documented on Form BOE-414-Z and the taxpayer should be notified in writing by the District Principal Auditor that the MAP Participation Agreement is terminated with an explanation of the reasons. The front of the audit report should continue to be marked as a managed audit for program evaluation purposes.~~
- ~~— Participation in the MAP is voluntary on the part of the taxpayer. Neither of the above actions by the taxpayer should have a negative impact on how the audit is completed or the scope of the audit verification to be performed by the auditor. The only impact will be that the taxpayer will not receive the benefit of the one-half interest rate should the audit result in a tax liability.~~

(g) Regulation 1705, "Relief from Liability"

- ~~— The managed audit may not be used as a basis for relief under Revenue and Taxation section 6596 in any subsequent audit. However, a prior audit may give rise to relief under section 6596 with respect to the managed audit. [See Revenue and Taxation Code section 7076.6.]~~

(h) Petitions for Redetermination or Claims for Refund

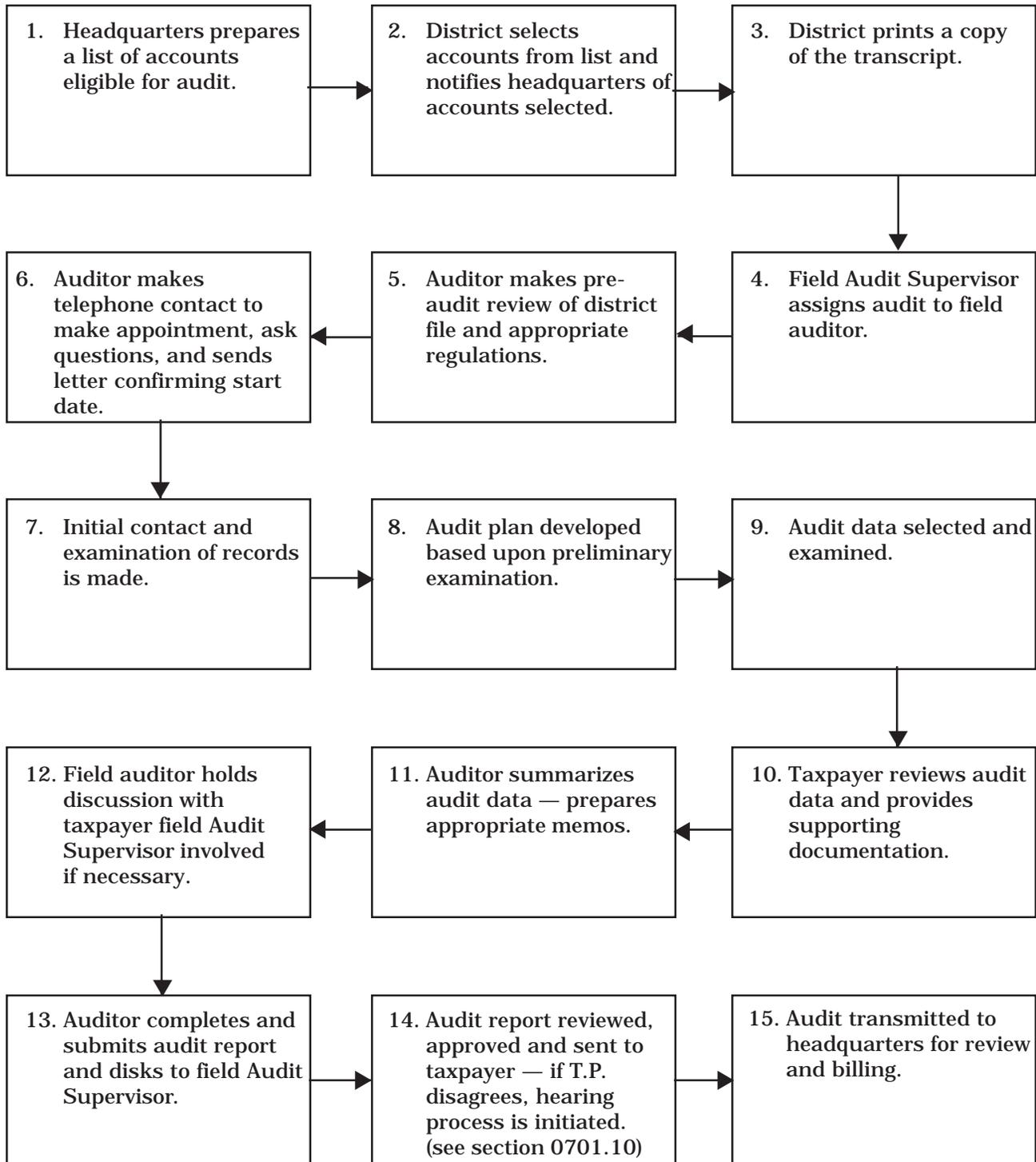
- ~~— There is no change to procedures for filing timely petitions or claims for refund for managed audits.~~

(if) Review Procedures for Managed Program Audits District Audit Review

The ~~Centralized Review Section~~ Audit Determination and Refund Section will ensure that the interest calculation is correct for all managed audits and that the "interest through date" is correct prior to billing. Once the audit report is approved for billing, a copy of the audit report and the MAP Participation Agreement will be made and forwarded to the Program Planning Tax Policy Manager (with a "cc" to the Chief of Field Operations or the Collections and Third District Operations Manager) for evaluation of the MAP.

AUDIT PROCESS FLOW CHART

EXHIBIT 1



GENERAL AUDIT PROCEDURES

FORM BOE-1164 — AUDIT MEMORANDUM OF POSSIBLE TAX LIABILITY

EXHIBIT 2

BOE-1164 REV. 13 (10-03)

AUDIT MEMORANDUM OF POSSIBLE TAX LIABILITY

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

TO _____ — Auditing	FROM _____ — Auditing
<input type="checkbox"/> BUYER'S — FILE	<input type="checkbox"/> SELLER'S — FILE
ACCOUNT NO. _____	ACCOUNT NO. _____
NAME _____	NAME _____
STREET _____	STREET _____
CITY _____ STATE/ZIP CODE _____	CITY _____ STATE/ZIP CODE _____
PHONE () _____	PHONE () _____

NOTE: Check one or more blocks as appropriate and line out inapplicable words in parenthesis.

Records of the (buyer) (seller) show the following questioned transactions:

- Tax assessed in audit of (buyer) (seller) Period _____ to _____
- Seller has valid (resale) (exemption) certificate from buyer on file (*Attach photocopy of certificate to BOE-1164*)
- (Buyer) (Seller) states that a (resale) (exemption) certificate (was) (was not) given
- (Resale) (Exemption) certificate was issued by the buyer for tools and supplies
- (Sales) (Use) tax was remitted to seller when paying the indicated ex-tax invoices
- Tax (not added) (incorrectly computed)
- Other (*describe*) _____

ATTACH COPIES OF INVOICES **OR** SCHEDULE ITEMS BELOW

Date	Invoice No.	Purchase Order No.	Amount	Description of Merchandise	Shipped From

See attached invoices and/or schedule.

Above listing covers Period _____

to _____

Sample Listing

COMMENTS AND RECOMMENDATIONS

AUDITOR _____	AUDITOR PHONE () _____	DATE _____
---------------	-------------------------	------------

Prepare in duplicate and give original to supervisor. Duplicate to be retained with audit. (Refer to A.M. Sections 0401.20 and 0408.20)

date

FORM BOE-1032 — INFORMATION ON OUT-OF-STATE RETAILERS

EXHIBIT 3

BOE-1032 REV. 5 (2-03)

INFORMATION ON OUT-OF-STATE RETAILERS

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

TO: Out-of-State Compliance

Date _____

SUBMITTED BY: District Office _____

Auditor _____ Auditor Phone _____

Short Form Option:

(Check this box and attach a copy of the invoice in lieu of completing the entire 1032 form.
However, please complete items 3 and 8 if known, and check the appropriate box on line 6(b).)

1. Out-of-State Retailer (or vendor)

Name _____

DBA _____

Street _____

City, State and Zip _____

Phone Number _____

2. Purchaser (or buyer)

Name _____

Account Number _____

Street _____

City _____

Phone Number _____

3. Sales Representative (who solicited sale)

Name _____

Account Number _____

Address _____

City and State _____

4. Date of Invoice _____

5. Invoice Number _____

6(a). Amount of Purchase (attach copy of invoice) _____

6(b). Use Tax Paid by Purchaser or Included in Audit Yes No

7. Description of Property Sold _____

8. How Sale Was Solicited _____

9. Other Information _____

All items should be completed.
(Refer to A.M. Section 0408.22)

date

POLICY AND PROCEDURE FOR SUBPOENA REQUESTS SUBPOENAS DUCES TECUM

Authority and Use. The Board of Equalization is authorized by Section 15613 of the Government Code to issue a subpoena for the attendance of witnesses or the production of books, records, accounts and papers. A subpoena requiring a person to bring books, records, accounts and papers with them is called a “subpoena duces tecum.” When in the course of a field audit or investigation of a taxpayer’s business, the Board’s representative is denied access to business records which are necessary in order to carry out the functions of the Board, the subpoena power may be invoked. The subpoena should be considered only when the records are known or believed to exist, the potential liability to be revealed by the records is significant, and all other methods of obtaining the records have been unsuccessful.

Procedure. All subpoenas will be prepared by the Legal Department in Headquarters utilizing information provided by the district. Districts should prepare the request in the form of a memorandum from the District Administrator to the Chief of Field Operations or the Collections and Third District Operations Manager. The Chief of Field Operations or the Collections and Third District Operations Manager will forward approved requests to the Legal Department for drafting and issuance.

Information Needed. The memorandum should include the following information:

- a. The taxpayer(s) name, dba(s), address, and tax number(s) applicable to the records being requested.
- b. The name and address of the person or entity upon whom the subpoena is to be served.
- c. The name and title of the Board employee who will examine the documents.
- d. The Board address where the documents are to be examined.
- e. If necessary, a date and or time when the records are to be produced or examined. A date/time may be appropriate if the employee who will examine the records will be available only before or after a certain date. Normally the Legal Department will calculate and specify the appropriate dates based on time frames which are controlled by statute.
- f. The time period covered by the documents that are being requested.
- g. The specific documents that are being requested. Request only the records needed for the audit. Do not state “any and all records” or similar omnibus requests.
- h. The efforts that have already been made to obtain the documents being sought. Attach copies of letters written, and indicate whether the request was ignored or refused.
- i. The name and telephone number of a contact person in the district office making the request, in case additional information or clarification is needed.

- j. If service is being made on a financial institution for production of a customer's financial records, the California Right to Financial Privacy Act requires that the customer affected also be served with a copy of the subpoena, and have a period of time in which to notify the financial institution of intent to move to quash the subpoena. Therefore, the following additional information is required:
- customer's name, address, and account number at the financial institution
 - character of the customer —
 - corporation
 - corporation that has forfeited its charter or right to do business or that has dissolved
 - joint stock company or association
 - partnership
 - unincorporated association
 - public entity
 - minor
 - fiduciary — guardian, conservator, trustee, executor, etc.
 - candidate for election for public office
 - any other natural person not described above.

The above information is necessary in order that the subpoena and the declaration of materiality under penalty of perjury supporting the issuance of the subpoena may be prepared with the degree of particularity necessary to insure against infringements of the taxpayer's constitutional guarantees relating to unreasonable search and seizure and due process of law.

Preparation and Service of Subpoena and Declaration. The Legal Department will prepare the Subpoena Duces Tecum, Declaration, Notices and Acknowledgment of Receipt, and Proofs of Service. The documents will be sent to the District Administrator together with complete instructions for serving the subpoena. Subpoenas being served on financial institutions for the production of customer records include instructions to the financial institution to estimate and obtain approval of their research and copying charges before complying with the subpoena. The instructions provided by Legal must be followed exactly to protect the rights of both the taxpayer and the Board.



STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION
SALES AND USE TAX DEPARTMENT
450 N STREET, SACRAMENTO, CALIFORNIA
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-00XX
916-XXX-XXXX • FAX 916-XXX-XXXX
www.boe.ca.gov

XXXX XXXXXX
First District, XXX XXXXX
XXXX XXXXXX
Second District, XXXXXXXX
XXXX XXXXXX
Third District, XXXXXXXX
XXXX XXXXXX
Fourth District, XXXXXXXX
XXXX XXXXXX
State Controller, XXXXXXXX
XXXX XXXXXX
Executive Director

Use of Sampling in Auditing

The primary purpose behind the Board of Equalization’s audit program is to determine, with the least possible expenditure of time for both the taxpayer and the Board, the accuracy of reported amounts. Sampling serves to accomplish this purpose.

Sampling is a process of drawing a conclusion about an entire body of information based on measurements of a representative sample of that information. Sales and use taxes are transaction taxes, meaning that tax is determined on a transaction-by-transaction basis. Therefore, verification must be done at the source document level. Since in many cases it is economically impractical to audit all transactions, the Board encourages the use of sampling whenever feasible.

There are generally two methods of sampling: judgment sampling and statistical sampling. A judgment sample includes all samples obtained by nonstatistical sampling methods. The most common type of judgment sample is the examination of a block period of time (for example, day, week, month, or quarter). A statistical or random sample is a sample in which each item in the population has an equal or known chance of being selected for examination. Examples of statistical or random sampling techniques include unrestricted sampling, stratified sampling, systematic sampling with random start, and cluster sampling.

While judgment samples are not necessarily less accurate than statistical samples, there is no way of objectively evaluating the accuracy or reliability of the test. The advantages of statistical sampling over non-statistical sampling are:

- It provides a selection process which is representative of the types of transactions involved and eliminates bias, since every item in the population has an equal or known chance of being selected.
• It provides an advance estimate of the sample size required for a given objective.
• The results can be objectively evaluated.
• Multiple samples may be combined and evaluated.
• Properly conducted statistical sampling can yield more reliable results than judgment sampling.
• It is a method approved and recommended by the American Institute of Certified Public Accountants (AICPA).

Other factors to be considered in determining the best type of sample to conduct are the format, condition, storage, and availability of business records. The auditor and taxpayer should discuss the most beneficial approach to examining source documents after the auditor has had an opportunity to review the business records but prior to the selection of the sample.

The attached BOE-472, Audit Sampling Plan, was developed to facilitate the use of sampling by helping the auditor and taxpayer to document the sampling plan and to set the criteria by which the sample results will be evaluated. The purpose of this form is to obtain information regarding the taxpayer’s operations in order to establish the most effective and efficient means of developing a sampling plan. The form covers many common situations that might arise in sampling and should be discussed with the taxpayer. This form should be completed with the assistance of the taxpayer, prior to the selection of the sample.

The information and methods documented in this form are not binding on either the taxpayer or Board staff. The sampling plan can, and should, be continually evaluated (and changed, if necessary) based upon information obtained during the auditing process. In addition, it is possible that stratification or expansion of this sample may become necessary depending on the results produced by this process. However, should any deviation to this plan be required, it will be fully discussed with the taxpayer.

If you have any questions regarding this form and accompanying information, please contact your auditor.

BOE-472 (S2F) REV. 4 (12-03)
AUDIT SAMPLING PLAN

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

TAXPAYER NAME	SCHEDULE NUMBER
AUDIT PERIOD to	ACCOUNT NUMBER

The purpose of this form is to establish the most efficient means of developing a sampling plan. Please complete all sections below.

1. Define the objectives of this test, including population to be tested:

See AM sections 1302.10 and 1302.15,

2. The sample period and records to be examined in performing this sample include the listed items, but these items may be modified if new or additional information is discovered:

The sample period and a complete list should be made of all possible records that may be necessary to make all decisions regarding the correctness of the test items. See AM section 1302.15. For example, "Sales for resale for the period of XX to YY."

- a) Filing method used for the population:

3. The sampling unit will be:

The sampling unit is the item being selected for review: i.e., a period of time, transactions (sales invoice, check, purchase invoice, etc.), clusters, etc.

4. The method of selecting the sampling unit tested will be:

For example, block sampling, statistical sampling with random selection, systematic statistical sample with random start, cluster sample, etc. See AM section 1304.00

date

GENERAL AUDIT PROCEDURES

(Cont. 2) Exhibit 5

Page 3 of 6

BOE-472 (S2B) REV. 4 (12-03)

TAXPAYER NAME	SCHEDULE NUMBER
AUDIT PERIOD to	ACCOUNT NUMBER

a) If you plan to conduct a statistical sample, identify the procedure(s) to be used:

b) If you plan to conduct a block test, please list the reasons why a statistical test was not possible:

5. The statistical sample size will be:

Indicate the number of sample units. See AM section 1303.00

a) The method and/or reason for determining the above sample size:

See AM sections 0405.20(c) and 1303.00

6. If a block sample is used, list the selected test period(s):

7. The sample base will be:

Units: _____

Dollars: _____

date

BOE-472 (S3F) REV. 4 (12-03)

TAXPAYER NAME	SCHEDULE NUMBER
AUDIT PERIOD to	ACCOUNT NUMBER

8. The population base will be:

Units:

Dollars:

9. The Board has a policy requiring a minimum of three errors in a sample or stratum (excluding actual basis examinations and cluster samples) for that sample or stratum to be projected.

a) If three or more errors are found in the sample or stratum, the results of the sample will be projected using the following procedures:

b) If less than three errors are found in the sample or stratum, the auditor will use one of the alternatives listed below to handle the errors in that sample or stratum. The auditor, if necessary, will discuss the alternatives with the taxpayer after the sample results are known and then make a decision on the alternative to use.

- Examine specific customers, vendors, accounts, known errors, etc., on a detailed basis for that sample or stratum.
- If feasible, expand that sample or stratum.
- Accept the reported/claimed amounts for that sample/stratum, if the circumstances warrant.

10. The following procedures will be used for the treatment of some specific situation(s) should they occur. Any additional items will be addressed in Section 11, "Other."

a) Duplicate sample units (sampling with or without replacement):

Indicate whether duplicate sample units will or will not be replaced with another sample unit.

b) Missing sample unit(s):

See AM sections 1302.25(g)

date

GENERAL AUDIT PROCEDURES

(Cont. 4) Exhibit 5

BOE-472 (S3B) REV. 4 (12-03)

TAXPAYER NAME	SCHEDULE NUMBER
AUDIT PERIOD to	ACCOUNT NUMBER

c) Sample unit is a void or canceled transaction:

See AM sections 1302.25(e) and (f)

d) Sample unit is an error but the transaction is corrected at a later date:

See AM sections 1302.25(f)

e) Sample unit is a "credit" item:

See AM sections 1302.25(f)

f) Sample unit is a partial/down/installment or progress payment:

See AM sections 1302.25(d)

g) Sample unit is for "tax" only:

See AM sections 1302.25(f)

h) Sample unit is an error but the transaction later resulted in a bad debt:

See AM sections 1302.25(f)

date

BOE-472 (S4) REV. 4 (12-03)

TAXPAYER NAME	SCHEDULE NUMBER
AUDIT PERIOD to	ACCOUNT NUMBER

11. Other:

This sampling plan is a collaborative effort by the auditor and taxpayer to determine the most efficient method of establishing an estimated percentage of error, if any, for the population being tested. The information and methods documented in this form are not binding on either the taxpayer or Board staff. This sampling plan may be modified if new or additional data is encountered. Should any deviation to this plan be required, it will be fully discussed with the taxpayer.

A copy of this sampling plan was provided to the taxpayer on _____ .
DATE

AUDITOR'S SIGNATURE

TAXPAYER'S SIGNATURE FOR RECEIPT OF COPY

EXAMPLES OF PRIOR AUDIT PERCENTAGE MEMOS

EXHIBIT 6

Page 1 of 2

State of California

Board of Equalization

Memorandum**To** : Tax Policy Manager [MIC:92]**Date:** December 1, 2003**From** : District Principal Auditor**Subject** : Request to Use a Prior Audit Percentage ABC Company SR KH 12-345678

We would like to use a prior audit percentage in the current audit of ABC Company. Staff has reviewed their accounting procedures and determined that there has been no change since the last audit. In addition, there have been no changes to the personnel handling their accounts payable and there have been no changes to any laws or regulations affecting their business. The following is an outline of our proposal as specified in Audit Manual Section 0405.33:

- (a) ABC Company
SR KN 12-345678
- (b) The taxpayer is a manufacturer and distributor of consumer electronics.
- (c) The audit period is 1/1/00 - 12/31/02
- (d) The prior audit percentage would be used in the paid bills portion of the audit.
- (e) For the audit period, 1/1/94 - 12/31/96, the percentage of error was 1.78 percent.
For the audit period, 1/1/97 - 12/31/99, the percentage of error was 2.01 percent.
- (f) For the audit period, 1/1/94 - 12/31/96, the population was \$2,300,000
For the audit period, 1/1/97 - 12/31/99, the population was \$4,100,000
- (g) We propose the use of 2.01 percent in the current audit.
- (h) The population to which this percentage of error will be applied is \$5,600,000

We have discussed this approach with the tax manager and she is agreeable to the use of the prior percentage of error. The tax manager was informed that this approach would not be used in consecutive audits. We both agree that given the relative consistency in the error rates, populations, accounting procedures and personnel, the use of a prior percentage of error would save significant audit time while achieving substantially the same result as a new test.

Thank you for your consideration. Please let me know if you have any questions.

cc: Chief of Field Operations or Collections and Third District Operations Manager
I. M. Auditor

date

State of California

Board of Equalization

Memorandum

To : Tax Policy Manager [MIC:92]

Date: December 1, 2003

From : District Principal Auditor

Subject : Evaluation of Use of a Prior Audit Percentage ABC Company SR KH 12-345678

We have completed our audit of ABC Company for the period of January 1, 2000 through December 31, 2002. As previously approved, the prior audit error percentage was used in the paid bills portion of this audit. The tax change resulting from the use of the prior audit error percentage is \$8,723. We estimate that a total of 40 audit hours were saved by utilizing this method.

Please let me know if you have any questions.

cc: Chief of Field Operations or Collections and Third District Operations Manager
I. M. Auditor



STATE OF CALIFORNIA
 STATE BOARD OF EQUALIZATION
 450 N STREET, SACRAMENTO, CALIFORNIA
 (P.O. BOX 942879, SACRAMENTO, CALIFORNIA 94279-0001)
 TELEPHONE (916) XXX-XXXX
 FACSIMILE (916) XXX-XXXX

XXXX XXXXXXXX
 First District, XXXXXXXX

 XXXX XXXXXXXX
 Second District, XXXXXXXX

 XXXX XXXXXXXX
 Third District, XXXXXXXX

 XXXX XXXXXXXX
 Fourth District, XXXXXXXX

 XXXX XXXXXXXX
 Controller, XXXXXXXX

 XXXX XXXXXXXX
 Executive Director

Tax Permittee

Use of XYZ Letter Procedure to Verify Claimed Sales for Resale

This letter summarizes the sample letter procedure explained to you by our auditor. The auditor questioned certain sales claimed on your tax returns as sales for resale because they were not supported by a valid resale certificate taken in good faith at the time of sale.

Under the California Sales and Use Tax Law, you as the seller are liable for payment of the tax unless you can present satisfactory evidence that the property was in fact purchased by your customer for resale or that your customer paid the tax directly to this state.

If the auditor has also questioned sales other than resale, such as sales in interstate and foreign commerce, sales to the United States Government, or transportation charges, documentation to support the claimed exemption must also be provided. The auditor will provide you with an information sheet describing how the law applies and the type of supporting documentation required to support the questioned claimed exempt sale.

The "XYZ" letter procedure outlined in this document is recommended by the Board as a method by which you, the seller, can help to satisfy the burden of proving that a sale was not at retail even though a resale certificate was not timely obtained, or your customer paid the tax directly to the state. This procedure should only be used when you cannot locate the appropriate supporting documentation, such as resale certificates, purchase orders, sales contracts, etc., within your company records.

It is recommended that the "XYZ" response forms be returned directly to the Board. However, you may choose to have the letters returned to you for forwarding to the Board. In either case, the auditor will review all documentation submitted. Because the XYZ letter is not a substitute for a timely resale certificate, you or your customer may be required to submit additional documentation or information to your auditor. You should be aware that if the auditor determines the "XYZ" process is appropriate and you choose to have the forms returned directly to you instead of to the Board, the likelihood of having staff contact your customer or sending an additional mailing will be greater.

The attached sample letter and statement form are provided for your convenience. If the statement form does not fit your particular circumstances, the auditor will work with you to customize the form. You may reproduce the statement form and send it to the customers in question to obtain their signed statements regarding the disposition of the purchased property. If you choose the recommended procedure to have the forms returned directly to the Board, the auditor will provide return envelopes.

In order to communicate fully with your customers, you may

- Customize the letter by placing the text on your letterhead.
- If you choose the recommended procedure to have the responses sent directly to the Board, you may add a statement in the letter to your customer asking that your customer send you a copy of the response by fax or mail.
- If your agreement of sale permits it, ask your customer to forward payment of tax if the transaction is identified as taxable. You should clearly indicate that the tax should be forwarded to you and not to the Board of Equalization.

Please note that any changes you make to the sample letter or form must be approved by Board staff before mailing.

The auditor will allow a four week period for you to send the statements and for your customers to reply. If you have chosen the recommended procedure to have the responses sent directly to the Board, the auditor will timely provide you copies of the responses received. While the auditor will carefully consider the statements received within the allowed period, late responses may be reviewed and allowed if appropriate.

Please be aware that a statement will not be accepted as satisfactory proof if incomplete, if found to be untrue, or if the Board has or receives information that refutes such statement. Unlike a valid resale certificate, a purchaser's statement of resale taken after the sale does not relieve the seller of liability for the tax if it is found that the property was purchased for the buyer's use and the applicable tax was not paid to the state prior to the date of your letter to your customer.

BT-504-B REV.11 (1-97)

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

SAMPLE LETTER

Requesting Purchaser's Statement

XYZ Company
1234 5th Street
Los Angeles, California 90013

Auditors of the California State Board of Equalization are currently examining our records in connection with the California Sales and Use Tax Law. They have questioned certain nontaxed sales made to you, as covered by the invoices listed on the attached sheet.

Would you please indicate the disposition of this property by checking the appropriate box and completing the statement. The Board will **not** accept the statement if it is not filled out completely and signed by an authorized representative.

Your prompt response is necessary for us to support any claims for exemption that are in order. Please return the inquiry statement within 10 days using the enclosed envelope or fax to (____) _____.

GENERAL AUDIT PROCEDURES

(Cont. 2) Exhibit 9

Page 3 of 9

BT-504-C REV. 12 (1-97)

**STATEMENT CONCERNING PROPERTY PURCHASED
WITHOUT PAYMENT OF CALIFORNIA SALES TAX**

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

DMA _____

Auditor's Initials _____

Please complete this inquiry statement to indicate the disposition of certain non-taxed purchases you made from the seller listed below. Please fill out the form completely, check the appropriate boxes, and sign as your company's authorized representative. The form should be returned within 10 days.

NAME OF SELLER FROM WHOM YOU PURCHASED ITEMS WITHOUT SALES TAX	SELLER'S PERMIT NO.
--	---------------------

DATE	INVOICE NUMBER	PURCHASE ORDER NUMBER	AMOUNT	DESCRIPTION

Please check one of the boxes below. If one of the first four boxes is checked, please enter your sales tax permit number below.

- The above purchase was purchased for resale and was resold in the form of tangible personal property. It was not used for any purpose other than retention, demonstration, or display while being held for sale in the regular course of business.
- The above property was purchased for resale and is presently in resale inventory. It has not been used for any purpose other than retention, demonstration, or display while being held for sale in the regular course of business.
- The above property was purchased for leasing and tax measured by rental receipts has been paid directly to the Board with our sales tax returns.
- The above property was purchased for our own use and not for resale; and
 - Tax in the amount of _____ was paid directly to the Board with our sales tax return for the reporting period _____.
 - Tax in the amount of _____ was added to the billing and remitted to the Seller.
 - The purchase is a taxable transaction and tax is applicable.

COMMENTS

NATURE OF BUSINESS		
PURCHASER'S SALES TAX PERMIT NUMBER		PURCHASER'S NAME
SIGNATURE		TITLE
DATE	PHONE	CITY

The information provided above is subject to verification by the State Board of Equalization.

BT-504-CLS (1-97)

**STATEMENT CONCERNING PROPERTY PURCHASED
WITHOUT PAYMENT OF CALIFORNIA SALES TAX**

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

DMA _____

Auditor's Initials _____

Please complete this inquiry statement to indicate the disposition of certain non-taxed purchases you made from the seller listed below. Please fill out the form completely, check the appropriate boxes, and sign as your company's authorized representative. The form should be returned within 10 days.

NAME OF SELLER FROM WHOM YOU PURCHASED ITEMS WITHOUT SALES TAX	SELLER'S PERMIT NO.
--	---------------------

DATE	INVOICE NUMBER	PURCHASE ORDER NUMBER	AMOUNT	DESCRIPTION

Please check the boxes below. If none of these apply, please explain below.

- The above purchase was purchased for resale and was resold in the form of tangible personal property. It was not used for any purpose other than retention, demonstration, or display while being held for sale in the regular course of business.
- The above property was purchased for resale and is presently in resale inventory. It has not been used for any purpose other than retention, demonstration, or display while being held for sale in the regular course of business.
- The above property was purchased for leasing and tax measured by rental receipts has been paid directly to the Board with our sales tax returns.
- The above property was purchased for leasing and tax measured by the purchase price has been paid directly to the Board with our sales tax return for the period in which the property was first leased.
- The above property (not "mobile transportation equipment") was purchased for leasing to a sublessor.
- The above property ("mobile transportation equipment") was purchased for leasing and tax measured by the fair rental value has been paid directly to the Board with our sales tax return for the period in which the equipment was first leased.
- The above property was purchased for our own use and not for leasing or resale, and
 - Tax in the amount of _____ was paid directly to the Board with our sales tax return for the reporting period _____.
 - Tax in the amount of _____ was added to the billing and remitted to the Seller.
 - The purchase is a taxable transaction and tax is applicable.

COMMENTS

NATURE OF BUSINESS		
PURCHASER'S SALES TAX PERMIT NUMBER		PURCHASER'S NAME
SIGNATURE		TITLE
DATE	PHONE	CITY

The information provided above is subject to verification by the State Board of Equalization.

SAMPLE LETTER FOR SPECIAL PRINTING AIDS
Requesting Purchaser's Statement

XYZ Company
1234 5th Street
Los Angeles, California 90013

The California State Board of Equalization is currently examining our records for compliance with the California Sales and Use Tax Law. They have questioned certain nontaxed sales of special printing aids made to you as indicated on the invoices listed on the attached sheet. These nontaxed sales are not supported by a valid resale certificate.

Please indicate the disposition of these special printing aids by placing the applicable letter in the corresponding response column for each invoice listed.

Unless printers specifically state that they are retaining title to the special printing aids on their customer's contract or sales invoice, printers are considered the retailers of the special printing aids and may purchase special printing aids for resale. However, special printing aids are considered purchased for the purchaser's own use and not for resale if the purchaser:

- Only resells printed material and not special printing aids. For example, book/newspaper publishers or manufacturers purchasing product labels or packaging for resale with the product. The printed material is resold, but the publisher or manufacturer is the end user of the special printing aids
- Buys the printed matter for their own use
- Is a print broker who resells the printed material but maintains ownership of the special printing aids

Your prompt response is necessary to support any claims for exemption. The board will **not** accept the statement if it is not filled out completely and signed by an authorized representative. Please return the inquiry statement within 10 days using the enclosed envelope or fax to (____)

_____.

Sincerely,

Encl:

date

BOE-504-CPA REV. 3 (4-03)

**STATEMENT CONCERNING PROPERTY PURCHASED
WITHOUT PAYMENT OF CALIFORNIA SALES TAX – SPECIAL PRINTING AIDS**

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

DMA _____
Auditor's Initials _____

Please complete this inquiry statement to indicate the disposition of certain non-taxed purchases you made from the seller listed below. Please fill out the form completely and sign as your company's authorized representative. The form should be returned within 10 days.

NAME OF SELLER FROM WHOM YOU PURCHASED ITEMS WITHOUT SALES TAX				SELLER'S PERMIT NO.	
DATE	INVOICE NUMBER	PURCHASE ORDER NUMBER	AMOUNT	DESCRIPTION	RESPONSE <i>List boxes (a) through (i) that apply</i>

Please place the appropriate letter and information in Response area above. If none of these apply, please explain in Comments below.

Note: Manufacturers purchasing product labels or packaging for resale with a product are considered end users of special printing aids and should select either D or E even though the printed material is resold. (See the cover letter accompanying this form for more information.)

- A. A special printing aid **was purchased for resale** and resold in a sale subject to California tax.
- B. The special printing aid **was purchased for resale** and resold to the US government.
- C. The special printing aid **was purchased for resale** and sold with a nontaxable sale of printed material other than US Government (ie. Interstate commerce, newspaper, printed sales message). **Our sale of the special printing aids was:**
 - C1. a sale for resale. We separately stated the sale price of the special printing aids and obtained a resale certificate for the special printing aids from our customer. The separately stated sales price was at least the amount of the sales price we paid for the special printing aids or their components.
 - C2. subject to tax. Tax was paid to the Board with our sales tax return. *Indicate amount of tax and period reported under Response above.*
 - C3. subject to tax. Tax was paid to the Board as a result of an audit that included the above purchases either on an actual basis or as a result of a percentage of error based upon a test. The purchases sampled in the audit were similar in nature to the above transaction; we believe tax on the above transaction has been paid to the Board as a result of the audit. *Indicate amount of tax and audit period under Response above.*
 - C4. subject to tax. However, we did not pay tax with our sales tax return or through an audit
- D. The special printing aid **was not purchased for resale**. However, tax was paid directly to the Board with our sales tax return. *Indicate amount of tax and period reported under Response above.*
- E. The special printing aid **was not purchased for resale** and tax is applicable.

COMMENTS _____

NATURE OF BUSINESS _____

PURCHASER'S SALES TAX PERMIT NUMBER _____ PURCHASER'S NAME _____

SIGNATURE _____ TITLE _____

DATE _____ PHONE _____ CITY _____

The information provided above is subject to verification by the State Board of Equalization.

date

GENERAL AUDIT PROCEDURES

(Cont. 6) Exhibit 9

Page 7 of 9

BOE-504-CFS REV. 1 (9-02)

**STATEMENT CONCERNING PROPERTY PURCHASED
WITHOUT PAYMENT OF CALIFORNIA SALES TAX**

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

DMA _____
Auditor's Initials _____

Please complete this inquiry statement to indicate the disposition of certain non-taxed purchases you made from the seller listed below. Please fill out the form completely, check the appropriate boxes, and sign as your company's authorized representative. The form should be returned within 10 days.

NAME OF SELLER FROM WHOM YOU PURCHASED ITEMS WITHOUT SALES TAX	SELLER'S PERMIT NO.
--	---------------------

DATE	INVOICE NUMBER	PURCHASE ORDER NUMBER	AMOUNT	DESCRIPTION

Please check the appropriate boxes below. If none apply, please explain on the "Comments" line.

Miscellaneous items purchased for resale

- I have sold the property. I did not use it for any purpose other than resale inventory, demonstration, or display. It was for sale from the time I bought it until I sold it.
- I currently hold the property in my resale inventory. I have not used it for any purpose other than demonstration or display and it has been for sale at all times.

Feed purchased to feed animals

I purchased the feed listed above

- To feed animals I sell in my business or whose offspring I sell.
- To feed animals commonly used to produce food (meat, dairy products, eggs, etc.).

Seed and plants purchased to plant or feed to animals

- I purchased the seeds or plants listed above to grow products I will sell.
- I purchased the seed listed above to feed directly to, or to produce feed for, (1) animals I sell in my business, or (2) animals commonly used to produce food (meat, dairy products, eggs, etc.).

Fertilizer

- I purchased the fertilizer listed above for applying to land or plants to grow (1) feed for animals commonly used to produce food, (2) plant products I will sell in my business, or (3) food crops.

Items purchased for your own use

- I purchased the items listed above for my own use, not for resale, and
 - I paid tax to the Board of Equalization in the amount of _____ with my sales and use tax return for the reporting period _____.
 - Tax in the amount of _____ was added to the billing and paid to the seller listed above.
 - The purchase is a taxable transaction and no tax has been paid on it.

COMMENTS _____

NATURE OF BUSINESS _____

PURCHASER'S SALES TAX PERMIT NUMBER (If you are not required to hold a permit, please note.) _____ PURCHASER'S NAME _____

SIGNATURE _____ TITLE _____

DATE _____ PHONE _____ CITY _____

The information provided above is subject to verification by the State Board of Equalization.

Date

BT-504-CUS (1-97)

STATEMENT CONCERNING PROPERTY PURCHASED WITHOUT PAYMENT OF CALIFORNIA SALES TAX

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

DMA _____

Auditor's Initials _____

Please complete this inquiry statement to indicate the disposition of certain non-taxed purchases you made from the seller listed below. Please fill out the form completely, check the appropriate boxes, and sign as your company's authorized representative. The form should be returned within 10 days.

NAME OF SELLER FROM WHOM YOU PURCHASED ITEMS WITHOUT SALES TAX	SELLER'S PERMIT NO.
--	---------------------

DATE	INVOICE NUMBER	PURCHASE ORDER NUMBER	AMOUNT	DESCRIPTION

Please check the boxes below. If none of these apply, please explain below.

- The above purchase was purchased for resale and was resold in the form of tangible personal property. It was not used for any purpose other than retention, demonstration, or display while being held for sale in the regular course of business.
- The above property was purchased for resale and is presently in resale inventory. It has not been used for any purpose other than retention, demonstration, or display while being held for sale in the regular course of business.
- The above property was purchased for leasing and tax measured by rental receipts has been paid directly to the Board with our sales tax returns.
- The above property was purchased for resale to the United States Government. In accordance with the title provisions of the U.S. Government supply contract, the U.S. Government took title to the property prior to any use of the property by us.
- The above property was purchased for our own use and not for resale; and
 - Tax in the amount of _____ was paid directly to the Board with our sales tax return for the reporting period _____.
 - Tax in the amount of _____ was added to the billing and remitted to the Seller.
 - The purchase is a taxable transaction and tax is applicable.

COMMENTS

NATURE OF BUSINESS		
PURCHASER'S SALES TAX PERMIT NUMBER		PURCHASER'S NAME
SIGNATURE		TITLE
DATE	PHONE	CITY

The information provided above is subject to verification by the State Board of Equalization.

GENERAL AUDIT PROCEDURES

(Cont. 8) Exhibit 9

Page 9 of 9

BT-504-COS (1-97)

**STATEMENT CONCERNING PROPERTY PURCHASED
WITHOUT PAYMENT OF CALIFORNIA SALES TAX**

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

DMA _____

Auditor's Initials _____

Please complete this inquiry statement to indicate the disposition of certain non-taxed purchases you made from the seller listed below. Please fill out the form completely, check the appropriate boxes, and sign as your company's authorized representative. The form should be returned within 10 days.

NAME OF SELLER FROM WHOM YOU PURCHASED ITEMS WITHOUT SALES TAX	SELLER'S PERMIT NO.
--	---------------------

DATE	INVOICE NUMBER	PURCHASE ORDER NUMBER	AMOUNT	DESCRIPTION

Please check the boxes below. If none of these apply, please explain below.

- The above purchase was purchased for resale and was resold in the form of tangible personal property. It was not used for any purpose other than retention, demonstration, or display while being held for sale in the regular course of business.
- The above property was purchased for resale and is presently in resale inventory. It has not been used for any purpose other than retention, demonstration, or display while being held for sale in the regular course of business.
- The above property was purchased for leasing and tax measured by rental receipts has been paid directly to the Board with our sales tax returns.
- The above property was purchased for our own use and not for resale; and
 - Tax in the amount of _____ was paid directly to the Board with our sales tax return for the reporting period _____.
 - Tax in the amount of _____ was added to the billing and remitted to the Seller.
 - Tax was paid directly to the Board as the result of an audit determination dated _____ covering the period _____ to _____. The Board's audit specifically included the above transaction in the audit assessment.
 - Tax was paid directly to the Board as the result of an audit determination dated _____ covering the period _____ to _____. The Board's audit examined our purchases on a test basis with a percent of error computed and applied. Because the purchases sampled in the audit were similar in nature to the above transaction, we believe tax on the above transaction has been paid to the Board as a result of this audit.
- The purchase is a taxable transaction and tax is applicable.

COMMENTS

NATURE OF BUSINESS		
PURCHASER'S SALES TAX PERMIT NUMBER		PURCHASER'S NAME
SIGNATURE		TITLE
DATE	PHONE	CITY

The information provided above is subject to verification by the State Board of Equalization.

General Retailers

Step	Task
1	Locate all books and records available for audit.
2	Get a description of the product sold. Visit the store if the audit is not performed on-site.
3	Find out who prepared the returns during the audit period. Have them show you the source(s) of their figures.
4	Run AUD TR to obtain a transcript of returns (414-M). Close to when you turn in the audit run it again to verify that no adjustments have been made that affect your audit results.
5	Review the sales tax return worksheets for accuracy, consistency, and method of reporting.
6	Reconcile reported sales per 414-M to books, FITRs, and financial statements.
7	Perform a sales tax accrual analysis.
8	Verify sales detail. Spot test sales invoices/Z-tapes to sales journal. Compare sales journal to general ledger on an actual basis.
	Compute book markups by year.
9	<ul style="list-style-type: none"> a Determine if markups are acceptable. b If not acceptable, conduct a markup test.
	Verify the accuracy of claimed deductions:
10	<ul style="list-style-type: none"> a Sales for resale - Resale certificates, qualifying purchase orders, auditor judgment. b Labor - Watch for fabrication/assembly labor, services in connection with the sale of tangible personal property. c Government - Federal government only. Check for purchase orders. d Interstate Commerce - Bills of lading, shipping documents. e Bad Debts - Taxable sales only. f Freight - Separately stated freight out, no handling fee.
	Check for potential use tax liability (usually minimal):
11	<ul style="list-style-type: none"> a Fixed assets b Consumable supplies c Withdrawals from inventory

NOTE: These audit programs are general in nature, and will not cover all potential situations that could be encountered. They should only be used as a starting point for a customized audit program for each taxpayer.

Date

Manufacturers and/or Wholesalers

Step	Task
1	Locate all books and records available for audit.
2	Get a description of the product sold, a tour of the facility, and an explanation of the manufacturing process.
3	Find out who prepared the returns during the audit period. Have them show you the source(s) of their figures.
4	Run AUD TR to obtain a transcript of returns (414-M). Close to when you turn in the audit run it again to verify that no adjustments have been made that affect your audit results.
5	Review the sales tax return worksheets for accuracy, consistency, and method of reporting.
6	Reconcile reported sales per 414-M to books, FITRs, and financial statements.
7	Look for miscellaneous sales - sales of assets, sales to employees, etc.
8	Sales tax accrual analysis.
9	Verify the accuracy of claimed deductions:
	a Sales for resale - Resale certificates, qualifying purchase orders, auditor judgment.
	b Labor - Watch for fabrication/assembly labor, engineering charges, services in connection with the sale of tangible personal property.
	c Government - Federal government only. Check for purchase orders.
	d Interstate Commerce - Bills of lading, shipping documents.
	e Freight - Separately stated freight out, no handling fee.
10	Check for potential use tax liability:
	a Fixed assets
	b Consumable supplies
	c Research and development
	d Manufacturing aids
	e Withdrawals from inventory
	f Samples

Liquor Stores

Step	Task
1	Locate all books and records available for audit.
2	Find out who prepared the returns during the audit period. Have them show you the source(s) of their figures.
3	Run AUD TR to obtain a transcript of returns (414-M). Close to when you turn in the audit run it again to verify that no adjustments have been made that affect your audit results.
4	Review sales tax return worksheets to verify accuracy, consistency and method of reporting.
	Reconcile sales:
	a Reported sales per 414-M to books, FITRs, and Profit & Loss Statements (P & L).
5	b Recorded sales per the P & L to the FITRs.
	c Taxable and nontaxable sales per P & L to reported/claimed amounts.
	<i>Note: Analyze deli sales and purchases separate from liquor store sales and purchases.</i>
6	Analyze the FITRs for overall markup.
7	Verify sales correctly posted to P & L. Trace from register tape to sales journal to general ledger to P & L.
8	Verify purchases correctly segregated and posted (taxable vs. nontaxable). Trace from purchase invoices to cash disbursements journal to P & Ls.
9	Calculate markup for taxable and nontaxable sales.
10	If all of the above is acceptable, with no reconciliation, segregation, or posting errors, and markups are reasonable, write up the audit.
	<i>Note: Markups vary depending on location and type of business.</i>
11	If the markups are reasonable, but a material reconciliation difference exists between taxable sales recorded and reported, schedule the differences and assess in the audit.
12	If purchases need to be segregated, segregate them into the same categories as sales and recalculate markups.
	If the markups are unacceptable, do a shelf-test:
a	If both the overall and taxable markups are low and there are no posting entry errors noted, impeach total sales and do a taxable shelf-test. Markup taxable purchases (adjusted for pilferage and self-consumption) using the markup obtained from the taxable shelf-test. Compare audited taxable sales to reported and assess tax on the difference.
	<i>Note: This type of error indicates unrecorded, unreported sales that were never rung on the register. This type of audit would be done on a taxable measure basis.</i>
13	b If the overall markup is acceptable and there are no posting errors noted, but the taxable markup is low, accept total sales as reported and do a shelf-test on nontaxable items (food). Compute audited food sales using the shelf-test markup and compare to claimed exempt amounts. Disallow over-claimed amounts.
	<i>Note: This type of situation indicates a key-ring error. This type of audit is done on a total sales basis and makes the taxpayer support his/her claimed deduction.</i>
c	If both the overall and nontaxable markups are low and there are no posting errors noted, but the taxable markup is reasonable, accept reported/claimed figures. The overall markup is pulled down due to nontaxable sales.

Prior to beginning the audit, familiarize yourself with the application of tax to liquor stores by reviewing Publication 24, "Tax Tips for Liquor Stores."

Date

Liquor Stores (continued)	
Step	Task
	Miscellaneous items:
	When computing audited sales using a shelf-test markup, be sure to adjust purchases for inventory
a	fluctuations, segregation errors, actual theft of inventory (supported by documentation), self-consumed, and 1% pilferage. Watch for climbing inventories.
	Watch self-consumption of taxable items. Include unreported items at cost in audit findings. Amounts
b	can be estimated, but make sure they are reasonable. Claimed self-consumed items should be itemized by category (soda, liquor, beer, wine, cigarettes, cleaning and paper supplies) and analyzed in the working papers, to determine if amounts appear reasonable.
	Remove non-merchandise sales (lottery sales, money orders, check cashing, etc.) prior to markup
14	c calculation.
	Shelf-tests should compare current costs with current selling prices. Make sure if CRV is included in
d	cost, it is also included in selling price and vice versa. Comment as to whether CRV is or is not included in the markup computation.
e	Note any changes in the type of business during the audit period (for example, added deli).
f	Based on internal controls (or lack of), a bank reconciliation may be necessary.
g	Are there material amounts of unclaimed bad debts/checks? Write-off only allowed on taxable portion.
h	Check sales and purchases of assets and consumable supplies (usually minor).
i	Verify cigarette indicia
j	Verify cigarette rebates are properly reported.

AUDIT MANUAL

FORM BOE-837 — AFFIDAVIT FOR SECTION 6388 OR 6388.5 EXEMPTION

EXHIBIT 12

BOE-837 (FRONT) REV. 3 (4-03)

AFFIDAVIT FOR SECTION 6388 OR 6388.5 EXEMPTION FROM CALIFORNIA SALES AND USE TAX

Page 1 of 2
STATE OF CALIFORNIA
BOARD OF EQUALIZATION

Revenue and Taxation Code (RTC) sections 6388 and 6388.5 provide exemptions from the taxes imposed on the sale, storage, use, or other consumption of certain new and remanufactured vehicles and trailers. The RTC section 6388 exemption applies to the sale or use of certain new or remanufactured vehicles. The RTC section 6388.5 exemption applies to the sale or use of certain new or remanufactured trailers. Additional information about these exemptions and additional requirements to meet these exemptions is available on the back of this form and in Regulation 1620.1, Sales of Certain Vehicles and Trailers for Use in Interstate or Out-Of-State Commerce.

CHECK AND/OR FILL IN ALL APPROPRIATE BOXES AND BLANKS BELOW

I have purchased a vehicle or trailer the sale and use of which is exempt from California sales and use tax per section [] 6388 [] 6388.5.

Vehicle or Trailer Information:

The vehicle is a [] truck, [] truck tractor, [] trailer, [] semitrailer, [] trailer coach, or [] auxiliary dolly, described as:

Table with 5 columns: MAKE & MODEL, VIN/SERIAL NO., YEAR, PURCHASE PRICE, UNLADEN WEIGHT. Row 2: MANUFACTURER/REMANUFACTURER, PLACE OF MANUFACTURE/REMANUFACTURE, DATE OF DELIVERY.

The vehicle or trailer was moved outside California within [] 30 [] 75 days of delivery (check one). Date moved: _____

Seller and Deliverer of Vehicle or Trailer:

I hereby certify that the vehicle or trailer described above was purchased from _____ (name of dealer or mfr./remfr.)

located at _____ (dealer or mfr./remfr.'s address - street, city, state, zip code), and was delivered by

_____ (name of California dealer or mfr./remfr.), located at _____ (California dealer or mfr./remfr.'s address - street, city, state, zip code)

Leasing and Registration Information:

The vehicle or trailer described above [] is [] is not being leased. If being leased, name and address of lessee:

Vehicle or trailer is licensed or registered in _____ (state where registered) (If a trailer is registered in California, provide owner's or lessee's USDOT number or FMC number)

Purchaser Information:

The purchaser is a [] corporation [] limited liability company [] partnership [] sole proprietor, which [] is [] is not a resident of California. The vehicle was purchased for use outside California (section 6388) or the trailer was purchased for use exclusively outside California or exclusively in interstate and foreign commerce, or both (section 6388.5). If the trailer or vehicle is registered outside California, a copy of the purchaser's or lessor's out-of-state registration, or license and registration, will be provided within 60 days from the date of this affidavit. If the trailer is registered in California under the PTI program, a copy of the purchaser's or lessee's USDOT number, FMC number, or current SSRS filing is attached.

I understand that if I do not meet the requisite exemption provisions detailed on the back of this form, I am required by the California Sales and Use Tax Law to report and pay tax, and interest and penalties (if appropriate), directly to the California State Board of Equalization, the tax to be measured by the purchase price of the above listed vehicle or trailer even though I have furnished an affidavit of exemption to the manufacturer, remanufacturer, or dealer.

PURCHASER'S NAME

Table with 3 columns: SIGNATURE OF PURCHASER OR PURCHASER'S AGENT, TITLE, PHONE NUMBER, DATE. Includes a small icon for a signature.

For exemption requirements and instructions on completing this affidavit, please see back of form.

Date

BOE-837 (BACK) REV. 3 (4-03)

SECTION 6388 - NEW OR REMANUFACTURED VEHICLES PURCHASED FROM OUT-OF-STATE DEALER

Applies to the sale, storage, use, or other consumption of a new or remanufactured truck, truck tractor, trailer, or semitrailer, with an unladen weight of 6,000 pounds or more, or a trailer coach or auxiliary dolly, purchased from a dealer located **outside** California for use **outside** California, and delivered in California by the manufacturer or remanufacturer to a purchaser who is not a resident of California. The purchaser must:

1. Remove the vehicle from this state within 30 days from and after the date of delivery.
2. Provide a valid affidavit to the manufacturer or remanufacturer, that is accepted by such person in good faith, stating:
 - The name and location of the out-of-state dealer from whom the vehicle was purchased
 - The name and location of the in-state manufacturer or remanufacturer that delivered the vehicle to the purchaser, and the date of delivery
 - That the purchaser is not a resident of California
 - That the vehicle was purchased for use exclusively outside California
 - That the vehicle was removed from this state within 30 days of the delivery date, and
 - The date of removal
3. Provide evidence of out-of-state vehicle registration (state of registration, license plate number, and VIN or serial number) to the manufacturer or remanufacturer within 60 days of providing the affidavit to the deliverer.

Notwithstanding the forgoing provisions, it is rebuttably presumed that a vehicle registered outside California and apportioned for use within this state is not purchased for use exclusively outside this state.

SECTION 6388.5 - NEW OR REMANUFACTURED TRAILERS PURCHASED FOR OUT-OF-STATE OR INTERSTATE COMMERCE USE

Applies to the sale, storage, use, or other consumption of a new or remanufactured trailer or semitrailer with an unladen weight of 6,000 pounds or more purchased from a California or non-California dealer that was manufactured or remanufactured either within or without this state for use exclusively outside California or exclusively in interstate or foreign commerce, or both; **and** delivered by the manufacturer, remanufacturer, or dealer, to the purchaser in California. The purchaser or purchaser's agent must:

1. Remove the trailer from this state within 30 days from and after the date of delivery, if the trailer is manufactured or remanufactured outside California; or remove the trailer from the state within 75 days from and after the date of delivery, if the trailer is manufactured or remanufactured within California.
2. If the trailer is registered outside the state, provide the delivering manufacturer, remanufacturer or dealer a copy of the current out-of-state license and registration for the trailer showing the Vehicle Identification Number (VIN) or serial number. Evidence of registration outside California must be submitted to the dealer, manufacturer or remanufacturer no later than 60 days after the timely providing of an affidavit.
3. If the trailer is registered in-state under the PTI program, provide the delivering manufacturer, remanufacturer or dealer a copy of the federal document assigning or confirming the purchaser's or lessee's USDOT number, FMC number, or a copy of the current SSRS filing with the DMV. The purchaser or purchaser's agent may not use the FMC number if the purchaser has a current USDOT number. Evidence of a USDOT number, FMC number, or SSRS filing must be submitted with the affidavit.
4. Provide an affidavit to the manufacturer, remanufacturer or dealer, that is accepted by such person in good faith, stating:
 - The name and location of the dealer from whom the trailer was purchased
 - The name and location of the California dealer, manufacturer or remanufacturer that delivered the trailer to the purchaser
 - That the trailer was purchased for use exclusively outside the state, or exclusively in interstate or foreign commerce, or both
 - That the trailer was removed from the state within the appropriate time periods, and
 - The date of removal

INSTRUCTIONS

*This affidavit must be provided to the entity delivering the vehicle or trailer no later than **30 days** from the date the vehicle or trailer is taken outside California.*

Fill in all sections and check all appropriate boxes. If the vehicle or trailer was sold and delivered by the same entity, write "Same" in sections for deliverer.

If a trailer is registered in California under the Permanent Trailer Identification Program (PTI), proof of a United States Department of Transportation (USDOT) number, Federal Maritime Commission (FMC) number, or current Single State Registration System (SSRS) filing must be attached to the affidavit.

If a vehicle or trailer is registered outside California, proof of out-of-state registration that includes the vehicle or trailer VIN or serial number must be furnished to the deliverer of the vehicle or trailer no later than 60 days after the purchaser provides the affidavit to the deliverer.

For transactions that include the purchase of more than one vehicle or trailer, you need not file a separate affidavit for each vehicle or trailer, but may instead append a list of the vehicles or trailers included in the transaction, identifying each one by a vehicle identification number (VIN) or serial number. You must, however, report the date each vehicle or trailer was removed from the state and provide copies of current out-of-state license and registration document or USDOT number, FMC number, or SSRS filing applicable to each vehicle or trailer, as required.

Persons who purchase a vehicle or trailer for the purpose of leasing it, qualify for the exemption if the lessee meets the respective exemption criteria summarized above. A lessor must provide the name and address of the lessee. On leases of trailers that qualify for PTI registration, the lessor must provide proof of the lessee's USDOT number, FMC number, or current SSRS filing. For all other leases, the lessor must provide proof of out-of-state registration.

If you have questions about these exemptions or completion of the affidavit, please call 800-400-7115.

Date

FORM BOE-526 — MANAGED AUDIT PROGRAM PARTICIPATION AGREEMENT

EXHIBIT 13

Page 1 of 4

BOE-526 (S1F) REV. 2 (2-04)

STATE OF CALIFORNIA

MANAGED AUDIT PROGRAM PARTICIPATION AGREEMENT

BOARD OF EQUALIZATION

NAME	ACCOUNT
------	---------

This is a Managed Audit Program (MAP) Participation Agreement between the California State Board of Equalization (Board) and _____ (taxpayer)

TAXPAYER'S NAME

in accordance with sections 7076.1 through 7076.5 of the California Revenue and Taxation Code. (All subsequent references to section numbers refer to the California Revenue and Taxation Code.)

1. For the managed audit to be conducted under the MAP for the period beginning on _____ and ending on _____, the taxpayer represents that
 - The taxpayer's business involves few or no statutory exemptions and a single or a small number of clearly-defined taxability issues, and
 - The taxpayer agrees to participate in the MAP and has the resources to comply with the managed audit instructions provided by the Board.
2. The taxpayer shall complete the managed audit on or before _____ in accordance with the instructions in this agreement. The taxpayer shall make available to the Board by this date all computations, all transaction worksheets (as described in paragraph 3 below), and all books, records, and equipment relating to the managed audit for verification by the Board.
3. The types of transactions covered by this managed audit are listed in Section 1 of the Appendix of this agreement. In performing the managed audit, the taxpayer shall
 - Review and separately maintain for verification by the Board the books, records, and equipment specifically identified by the Board in Section 2 of the Appendix,
 - Follow the specific procedures listed in Section 2 of the Appendix to determine the amount of the unreported tax liability, if any,
 - Schedule the transactions relating to each of the books, records, and equipment identified in Section 2 of the Appendix by completing transaction worksheets provided by the Board, in accordance with the instructions in Board publication 53, *Guide to the Managed Audit Program*, a copy of which has been given to the taxpayer, and
 - Follow the special instructions (criteria), if any, described in Section 3 of the Appendix.
4. When the taxpayer has completed the managed audit, the Board may verify the results of the managed audit by reviewing the documents prepared by the taxpayer, by examining the books, records, and equipment of the taxpayer, and by taking any other necessary actions to verify the results of the managed audit, including requesting further information and documentation from the taxpayer.
5. If the Board determines that certain types of transactions should be audited by the Board and not by the taxpayer under the MAP, the Board shall notify the taxpayer either during or after the managed audit which types of transactions will be reviewed by the Board and what books, records, and equipment the Board must examine. If the Board determines that an unreported tax liability exists for those types of transactions which the Board audits pursuant to this paragraph, the interest rate set forth in paragraph 7 shall apply with respect to that liability unless the Board voids this agreement pursuant to paragraph 10.
6. Upon completion of the managed audit by the taxpayer, the verification of the managed audit by the Board, and the audit by the Board of transactions not audited under the MAP, the liability, if any, may be determined and collected by the Board and petitioned by the taxpayer in the manner provided in chapter 5 (commencing with section 6451) and chapter 6 (commencing with section 6710) of Revenue and Taxation Code part 1, division 2. As provided by section 6565, all determinations made by the Board under these

Date

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provisions of the Revenue and Taxation Code are due and payable at the time they become final. If they are not paid when due and payable, the Board shall add to them a penalty of 10 percent of the amount of the determination, not including interest and penalties.

- 7. Upon completion of the managed audit and verification by the Board, interest shall be computed at one-half the rate that would otherwise be imposed for liabilities covered by the audit period, in accordance with section 7076.4. This reduced interest rate shall remain in effect until the tax liability is paid in full unless the Board voids this agreement as provided in paragraph 10.
- 8. As provided in section 7076.2, subdivision (b), the information provided by the taxpayer shall be the same information required for the completion of any other audit that the Board may conduct.
- 9. Nothing in this agreement shall limit the Board's authority, under section 7054, to examine the taxpayers' books, records, and equipment. Nothing in this agreement shall limit the authority of the Board to determine an unreported tax liability or a refund or credit greater than or less than the unreported tax liability or refund or credit computed by the taxpayer in the managed audit.
- 10. The Board may void this agreement if the Board determines that
 - The taxpayer has failed to complete the managed audit by _____ in accordance with the provisions in this agreement, DATE
 - The taxpayer has refused to cooperate with the Board during the verification process described in paragraph 4 above or has refused to cooperate with the Board if the Board audits any transactions as provided in paragraph 5 above,
 - Any of the penalties under sections 6484, 6485, 6485.1, 6514, or 6514.1 should be imposed during the audit period,
 - There is jeopardy of collection under section 6536, or
 - The taxpayer has not paid the tax, interest, and penalties resulting from the managed audit (1) within 30 days of the issuance date of the related *Notice of Determination* or (2) as agreed upon in a formal installment payment agreement.

If the Board determines that this agreement should be voided, the Board shall notify the taxpayer in writing. If the Board voids this agreement, interest shall be computed at the full rate as provided in section 6591.5. In addition, the Board may proceed to examine the taxpayer's books, papers, records, and equipment in a manner to be determined by the Board, and any liability may be determined and collected by the Board and petitioned by the taxpayer in the manner provided in chapter 5 (commencing with section 6451) and chapter 6 (commencing with section 6701) of the Revenue and Taxation Code.

- 11. The Board has given the *Guide to the Managed Audit Program* to the taxpayer for instructional purposes. If there is a conflict between that publication and the Sales and Use Tax Law or this agreement, the Sales and Use Tax Law and this agreement shall control.

SIGNATURE (name of taxpayer)	DATE
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NAME/TITLE (print full name and title)

SIGNATURE (Board of Equalization District Principal Auditor)	DATE
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NAME/TITLE (print full name and title)

Date

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APPENDIX
Managed Audit Program Participation Agreement

NAME		ACCOUNT NUMBER
AUDIT PERIOD From		To

SECTION 1

The types of transactions to be audited by the taxpayer are checked below:

- Sales for Resale
- Sales of Property Shipped Outside California
- Shipping and Delivery Charges
- Sales to the United States Government
- Purchases from Out-of-State Vendors
- Other: _____
- Installation Labor
- Repair Labor
- Cash Discounts
- Property Purchased For Resale

SECTION 2

The books, records, and equipment that are to be reviewed by the taxpayer are checked below:

- Sales Invoices
- Sales Contracts
- Resale Certificates
- Bills of Lading
- Other: _____
- Freight Bills
- Other Shipping or Delivery Documentation
- Purchase Orders
- Purchase Invoices

The procedures to determine the amount of any unreported tax liability are described on pages 4 through 11 of the *Guide to the Managed Audit Program*. The taxpayer will be reviewing the books, records, and equipment checked above for the following periods:

TEST PERIODS

_____	_____	_____
_____	_____	_____

Description of method for review: _____

SECTION 3

Special Instructions (Criteria):

- None
- Other: _____

continues on reverse

date

GENERAL AUDIT PROCEDURES

EXHIBIT 14C

BOE-52-L2 (8-03)

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

Sample Letter for Seller
Notice of Pending Refund of Excess Sales Tax Reimbursement

[Customer Name]
[Address]
[City, State, Zip Code]

[Date]

Dear [Customer],

A review of our sales records disclosed that we erroneously collected excess tax reimbursement from you in the amount of [] for the period [xx-xx-xx] to [yy-yy-yy]. Excess tax reimbursement occurs when the sales tax reimbursement is overstated due to a mathematical or clerical error or when reimbursement is computed on a transaction, which is not subject to tax or on an amount in excess of the amount subject to tax. Excess tax reimbursement also occurs when a retailer uses a tax rate higher than the rate imposed by law.

We have filed a claim for refund with the State Board of Equalization for the excess tax collected. Once we receive a refund from the Board, we will refund the money to you. Please indicate if you would like the amount sent to you or credited to your account.

send the refund to me

credit my account

Please acknowledge receipt of this notice by completing the information below, and returning it to our office promptly. Keep a copy of this form for your files. In accordance with Sales and Use Tax Regulation 1700, the Board of Equalization will not issue a refund for this tax to us until we have your signed acknowledgement that we are obligated to return the overpayment of sales tax to you.

The validity of all refund claims is subject to review and approval by the Board of Equalization.

COMPANY NAME

BY (print name)

SIGNATURE

TITLE

DATE

TELEPHONE

()

Sincerely,

[Name]

[Title]

Date

State of California

Board of Equalization

M e m o r a n d u m

To : Chief of Field Operations (or)
Collections and Third District Operations Manager

Date:

From : District Administrator

Subject : Report of Suspected Money Laundering Activity

An <investigation/audit> of <taxpayer name, permit number> by <auditor/tax representative>, disclosed information which indicates possible money laundering activity as defined under various provisions of the Penal Code.

During the period from <mm/dd/yy> to <mm/dd/yy>, there were money transactions that appear unrelated to the normal business operations of a <type of business> with sales of money orders, travelers checks and/or check cashing operations.

The total amount of all transactions was <dollar amount>. The average transaction amount was <dollar amount>. Each transaction was made in the form of <cash, money orders, etc.>. A summary of these transactions is attached.

The detected activities took place at <business address> and funds were deposited in <list bank(s)> during the period from <mm/dd/yy> to <mm/dd/yy>.

Date