



CALIFORNIA DEPARTMENT OF TAX AND FEE ADMINISTRATION

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EDMUND G. BROWN JR.
Governor

MARYBEL BATJER
Secretary, Government Operations Agency

NICOLAS MADUROS
Director

July 24, 2017

VIA INTERNET

Dear Interested Party:

The Compliance Policy and Procedures Manual (CPPM) and the Audit Manual are guides for the California Department of Tax and Fee Administration (CDTFA) staff in administering tax and fee programs. They are available to the public and can be accessed from the CDTFA web page at <http://www.boe.ca.gov/sutax/staxmanuals.htm>.

The Business Tax and Fee Division is proposing to revise CPPM Chapter 8, *Consumer Use Tax*, and AM Chapter 4, *General Audit Procedures*, to incorporate policies pertaining to the In-State Service Program.

The revision material is provided on the following pages for the convenience of interested parties who may wish to submit comments or suggestions. Please feel free to publish this information on your website or otherwise distribute it to your association/members.

If you have any comments or suggestions related to the proposed AM or CPPM revisions, you may contact the CDTFA at CPPM.RevisionSuggestions@boe.ca.gov. Your comments or suggestions must be received by the CDTFA no later than **September 25, 2017**, in order to be considered by staff. Thank you for your consideration.

Sincerely,

A handwritten signature in cursive script that reads "Trista Gonzalez".

Trista Gonzalez, Chief
Tax Policy Bureau
Business Tax and Fee Division

Interested Parties

July 24, 2017

bc: (via email)

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Compliance Policy and Procedures Manual

Chapter 8

~~Consumer~~-Use Tax

Business Tax and Fee ~~Department~~Division
California ~~State~~Department of
~~Board of Equalization~~Tax and Fee
Administration

This is an advisory publication providing direction to staff administering the Sales and Use Tax Law and Regulations. Although this material is revised periodically, the most current material may be contained in other resources including Operations Memoranda and Policy Memoranda.

Please contact any ~~Board of Equalization~~California Department of Tax and Fee Administration office if there are concerns regarding any section of this publication

CONSUMER-USE TAX

800.000

Use tax is a companion to California's sales tax and is imposed on the use, storage, or consumption of personal property in California. This chapter covers several programs administered by the California Department of Tax and Fee Administration (CDTFA) to ensure the proper reporting and/or collection of use tax.

CONSUMER USE TAX SECTION (CUTS) - GENERAL

800.005

~~The purpose~~ Sections 800.005 through 850.020 of this chapter ~~is to~~ provide information regarding the functions, procedures, and responsibilities of the ~~Consumer Use Tax Section~~ (CUTS).

The CUTS administers the Sales and Use Tax Law as it applies to the purchases of vehicles and mobile homes from persons not licensed or certificated pursuant to the Vehicle Code or the Health and Safety Code. In addition, the CUTS is responsible for applying the provisions of the Sales and Use Tax Law to purchases of vessels and aircraft when the seller is not required to hold a seller's permit by reason of the number, scope, and character of that person's sales. ~~CUTS also monitors and issues tax determinations for transactions where tangible personal property is purchased in a foreign country and personally hand-carried through U.S. Customs by California residents.~~

~~The information provided in this chapter does not apply to other types of property purchased for use in California. See CPPM 215.000 for information on Consumer Use Tax and Certificate of Registration — Use Tax permits.~~

USE TAX ADMINISTRATION SECTION (UTAS) 860.000

Sections 860.010 through 860.100 of this chapter provide information regarding the functions, procedures, and responsibilities of the In-State Service Program administered by the UTAS.

IN-STATE SERVICE (ISS) PROGRAM 860.010

The ISS program is administered by the ISS Group in the UTAS, and was implemented under the Tax Gap Initiative. The tax gap is defined as the difference between the amount of taxes owed and the amount of taxes paid to the state. The Tax Gap Initiative was intended to promote voluntary compliance through education and outreach, improvement of current programs, and implementation of new programs. The ISS program was started to investigate and collect use tax from service-based businesses that may not be aware of their reporting requirements. The ISS Group has teams located in Northern California (MIC 05) and Southern California (MIC EHS).

The ISS Group contacts in-state service business leads through a mailing campaign, requiring the taxpayer to: conduct a self-review of purchase records for a three-year period; register, file and pay any use tax due online; and submit supporting documentation for review and verification that the correct amount of use tax was reported.

SOURCES OF LEADS 860.030

The Employment Development Department (EDD) and Franchise Tax Board (FTB) provide information to the Data Analysis Section (DAS) to help identify service businesses operating in California. The type of information received includes the business name, address, phone number, NAICS code, business description, number of employees in California, entity type, FEIN, SSN, gross receipts, and cost of goods sold.

The DAS will match the business lead data to CDTFA records and remove any leads currently registered with a sales or use tax account. The DAS will forward the remaining unregistered ISS business leads to the ISS Group for further analysis, pre-screening, and selection of leads to assign to staff.

LEAD SOURCE CODES 860.040

To capture and identify the revenue resulting from ISS Group efforts, the Lead Source code “TGI” (Tax Gap In-State Service) is assigned to any sales and use tax accounts generated, any audit cases created, and any compliance assessments issued as a result of ISS Group efforts.

For new accounts, the Lead Source Subtype “EDC” (UTAS EDD Lead) will be assigned. For audit cases, the Lead Source Subtype assigned will depend upon the office receiving and conducting the audit. For example, an audit case generated and referred by the ISS Group to the San Diego Office (FH) will have the lead source “TGI FHC” assigned. (FHC = San Diego audit referral from the UTAS-ISS Group).

The Lead Source added at the account level will be for three years, by using the creation date of the account for the lead source “start-date” and creation date plus three years for the lead source “end-date.”

The Lead Source assigned for Audit Cases or Compliance Assessments should be added directly to the FO (Financial Obligation). Lead source “start date” and “end date” are not required when assigning a Lead Source to an FO.

Refer to CPPM section 230.070, *IRIS Lead Source*, for further instructions.

PROCESSING BY THE HEADQUARTERS (HQ) CASHIER SECTION 860.050

When a payment is received in HQ for a case initiated by the ISS Group and no existing account number can be found, the Cashier Section will issue an arbitrary account number. Any correspondence received will be forwarded to the ISS Group with a copy of the payment document.

RESPONSIBILITY OF THE ISS GROUP 860.060

CASE ASSIGNMENT PROGRAM - ISS DATABASE (CAP)

After the unregistered ISS business lead data is received from the DAS, the ISS Group will further sort, filter, and match the data to prior lead data to avoid duplication of leads. Each month a manageable amount of business leads are selected and assigned to staff based upon specific criteria, as determined by the ISS Group.

For the selected business leads, the information from the source file(s) is placed in the Case Assignment Program - ISS Database (CAP). The CAP database contains original lead information, assigned ISS Group employee name, letter mailing date, reporting periods under review, and multiple tabs and blank fields that allow the assigned ISS Group employee to capture information about the business as they investigate and communicate with the taxpayer. The CAP database allows staff to enter comments, send letters, record actions taken, indicate current status, set follow-up dates, and generate reports.

INITIAL CONTACT

Based on the lead data received from DAS, the ISS Group selects and assigns leads to staff to investigate and determine if the ISS business has use tax that may be due. Initial contact is made to the ISS business by sending a BOE-403-CL, *Tax Gap In-State Service Contact Letter* that explains what use tax is, how use tax may apply to its purchases, and how to comply with California Use Tax laws. Included with the contact letter is the BOE-403-CLW, *California Use Tax Worksheet*, used to calculate use tax due for the previous three calendar years and verify ownership of the business entity. The letter also references publication 110, *California Use Tax Basics*, and publication 217, *Use Tax Guide to Reporting Out-of-State Purchases*.

If tax is due, the letter and worksheet instruct the business to utilize the CDTFA's online services to register for a use tax account and file and pay use tax returns. All businesses contacted are required to complete and return the BOE-403-CLW, regardless of whether or not they owe use tax, along with the following documents: purchase journal/general ledger for the past year; a current asset depreciation schedule/asset listing; and their California Income Tax Schedule R, if applicable.

The ISS businesses have 30 days to respond to the contact letter. After 15 days, staff in the ISS Group will call to verify the initial contact letter was received and to answer

any questions the business may have. If a response to the letter is not received within 45 days from the inquiry date, a follow-up letter will be sent to the business.

DESK REVIEW

Based on the contact letter responses, the ISS Group will review the information provided for accuracy and understanding of use tax, and may do one or more of the following:

1. Assist in filing returns online for previously unreported use tax liability periods.
2. Place a delinquency withhold in IRIS, and corresponding comments in the Integrated Revenue Information System (IRIS) and the Automated Compliance Management System (ACMS), for any periods that require additional time to review or require additional assistance.
3. Request additional documents (for example, specific invoices or federal income tax return).
4. Create compliance assessments based on the completed *Use Tax Return Worksheets* and evidence of use tax due found within the required documents received or from other sources.
5. Issue account numbers for future reporting, for those who failed to register but provided information that shows they owe use tax.
6. Refer ISS Group leads to field audit staff for further investigation if it has been determined that additional use tax may be due or other questionable activities are noted.
7. Close the assignments if no account number (i.e., arbitrary or permanent) is required and no use tax liability is due.
8. Refer to field compliance staff unregistered in-state vendors selling to an ISS Group business lead using a BOE-142, *Request for District Investigation*.
9. Refer registered, questionable vendors to field audit staff for further investigation.
10. Refer to OH 1032 team unregistered out-of-state vendors selling to an ISS Group business lead.

When a service business does not respond within 30 days from the follow-up contact letter date, the ISS Group will conduct further research to determine if the business is still active, if the business address is valid, and whether or not there is a potential for use tax based upon the business industry.

The following actions may be taken by the ISS Group to resolve the business lead:

1. Locate business websites, conduct Internet searches, and conduct searches in the CLEAR system.
2. View state income tax returns requested using the BOE-1144, *Official Request for Return Information*, interagency information requested from EDD, FTB, and the Secretary of State which are tracked in the External Agency Tracking (EAT) system.

3. Perform a like business analysis for use tax potential.
4. Cross-reference other sources of information for potential for use tax (e.g., customs import documents, request to County Assessor for BOE-571-L, Business Property Statement, purchase history from known out-of-state vendors used).

Depending upon the results from the additional investigation/research of the business that has not responded to the initial contact, the ISS Group will take one or more of the following actions:

1. Resend the Initial Letter if a better address was found.
2. Make contact with the business/responsible person to further explain use tax and request the business respond to the initial letter immediately.
3. Create compliance assessments based on evidence of use tax due from Customs imports documents or actual purchase information from out of state vendors.
4. Refer the use tax lead to field audit staff for audit.
5. Close the assignment if the business is inactive or if it is determined that the assignment is not cost effective to pursue.

AUDIT REFERRALS

860.070

The ISS Group will select the leads to be referred for audit, create an account and an audit case ID using the audit selection reason code GAP, and assign the lead source TGI and the appropriate lead source sub-type to identify the field office conducting the audit.

Audit Referrals will be sent electronically and should include:

1. Memo or ISS “all-in-one referral form,”
2. Business lead contact information and business description,
3. Detailed reason for audit recommendation,
4. Evidence of use tax owed and/or supporting information of potential use tax owed,
5. Any transcribed income tax information, including gross receipts, COGS, assets, and other deductions,
6. Prior contact history between the ISS Group and the business (case history),
7. Copies of letters sent, and
8. Any other relevant information.

For audit tracking purposes, the ISS Group will issue arbitrary account numbers to those businesses that do not have an account with the CDTFA or did not obtain one during the desk review process. The audit case will be created on the arbitrary account. The ISS Group will conduct periodic follow-ups with the field offices to determine the status of in-process audits referred to the field offices.

1032 REFERRALS TO OUT-OF-STATE (OH) OFFICE

860.080

The ISS Group will review invoices, worksheets, purchase journals, and asset listings received from all ISS business leads and identify unregistered out-of-state vendors.

Utilizing the 1032 Desktop Application Program (1032 Database) that contains historical data of out-of-state vendors contacted by the CDTFA, the ISS Group will determine if the unregistered out-of-state vendor qualifies as a 1032 referral. If the vendor qualifies, the ISS Group will do the following:

1. Add the vendor to the 1032 Database to create a case.
2. Upload the source document with the vendor's address to the new case.
3. Research the vendor for possible proof of nexus and upload any relevant information.
4. Add the customer information to the case.
5. Add comments to the case and refer electronically to OH-1032 team via the 1032 Database.

The appropriate lead source code will automatically populate on the 1032 case for the appropriate UTAS program (ISS or Interstate Commerce Analysis Team (ICAT)). In the case of 1032 referrals from the ISS Group, the lead source is TGI OHE (OHE = OH Office 1032 referral).

SPECIAL TAXES AND FEES PROGRAM REFERRALS **860.090**

There may be occurrences when the ISS Group or the in-state field audit staff determine ISS businesses are purchasing items from outside of California for consumption and are not being charged appropriate special taxes or fees (for example, purchases of new televisions, computer monitors, portable DVD players, tires, fuel, lead-acid batteries, alcoholic beverages, and cigarette or tobacco products). Similarly, there may be cases where the Out-of-State Office compliance staff register out-of-state retailers who are engaged in business in California that also require registration under special taxes and fees programs.

In such cases, the ISS Group Supervisor, Principal Auditor, Out-of-State Compliance Supervisor, or designee, should send an email notification containing the name, address and telephone number of the ISS business or out-of-state retailer to the "BTFD-ISS Referrals" mailbox. The email notification should also include an account number and information concerning the description of items purchased, the quantity of items purchased, and the periods in which the purchases occurred, if available. The Registration and Licensing Section will forward the information to the appropriate staff for further investigation.

RESPONSIBILITY OF FIELD OFFICES FOR ACCOUNTS ISSUED BY THE ISS GROUP **860.100**

Field Compliance Staff

Field compliance staff will handle accounts with delinquencies and/or accounts receivable balances due for accounts with Taxable Activity Type SU, following the normal CDTFA policy and procedures unless there are comments entered by the ISS Group staff with specific instructions.

Field Audit Staff

Field audit staff will follow the procedures outlined in Audit Manual section 0408.45.

Out-of-State (OH) Field Compliance - 1032 Team

Upon receiving a 1032 referral from the ISS Group, the OH field compliance staff (OH 1032 Team) will generate a BOE-790, *Registration Questionnaire*, using the 1032 Database to send to the vendor. Through investigation and responses received from the out-of-state vendors, the OH 1032 Team will follow up on registration of any out-of-state vendors engaged in business in California. For 1032 referrals from the ISS Group that result in the registration of an account, OH staff will assign the Lead Source and Lead Source Sub-type code TGI OHE to the account.

PRELIMINARY ARRANGEMENTS

0403.10

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

BOE-80-A *Audit Engagement Letter – Confirm Start Date*

[BOE-80-AT Transfer Letter – Agreement to Transfer Audit to Representative](#)

BOE-80-B *Audit Engagement Letter – Agreement to Delay Start Date*

BOE-80-C *Audit Engagement Letter – Initiate Contact*

BOE-80-D *Audit Engagement Letter – 10-Day Follow Up*

BOE-80-DOH *Audit Engagement Letter – 10-Day Follow Up (Out-of-State)*

BOE-80-EOH *Audit Engagement Letter – In Area (Out-of-State)*

BOE-80-FOH *Audit Engagement Letter – Apology (Out-of-State)*

Forms BOE-80-A, [BOE-80-AT](#), BOE-80-B, BOE-80-C, and BOE-80-EOH **include contain links to** the following **enclosures** [publications and provide tax/feepayers with the CDTFA website address so the publications can be downloaded. For tax/feepayers who are unable to download the publications, information is provided on how to obtain them from the Customer Service Center:](#)

~~Form BOE-80-RU, Record Update~~

Publication 70, *Understanding Your Rights as a California Taxpayer*

Publication 76, *Audits*

Publication 17, *Appeals Procedures, Sales and Use Taxes and Special Taxes*

[When conducting use tax audits referred by the Use Tax Administration Section, In-State Service Tax Group \(ISS Group\), the BOE-80-TG series of "Audit Engagement Letters" should be used \(see AM section 0408.45\).](#)

~~Form~~ [The BOE-80-RU, Record Update, is provided as an enclosure with the BOE-80-A, BOE-80-AT, BOE-80-B, and the BOE-80-C. The BOE-80-RU is intended to help obtain the tax/feepayer's current registration information at the start of an audit. The auditor should verify the accuracy of the information provided by the tax/feepayer on Form BOE-80-RU and include a comment to that effect on Form in the BOE-414-Z program, Audit Assignment History.](#) A copy of Form BOE-80-RU should be included in the *Forms* subfolder of the audit case folder. To update the tax/feepayer's registration information on IRIS, a copy of Form BOE-80-RU should be sent to the ~~District~~ [Compliance Supervisor for sales and use tax accounts and to the Registration and Licensing Section's account maintenance mailbox \(BTFD-PCD Reg Maint Close\) for special taxes and fees accounts.](#)

Normally, the initial contact with the tax/feepayer will be by telephone. When the audit appointment results from a telephone contact, the appointment must be immediately confirmed by mail [or email](#) using Form BOE-80-A, *Audit Engagement Letter – Confirm Start Date*, with the ~~enclosures listed above~~ [BOE-80-RU enclosed. If distribution of the engagement letter occurs via email, a BOE-82, Authorization for Electronic Transmission of Data, must be on file.](#) If the audit will commence within a

GENERAL AUDIT PROCEDURES

week of making the appointment, the engagement letter and ~~enclosures~~ [the BOE-80-RU](#) may be given to the tax/[feepayer](#) at the start of the audit. If the audit appointment is with the tax/[feepayer](#)'s representative, the engagement letter and ~~enclosures~~ [the BOE-80-RU](#) should be sent to the tax/[feepayer](#), with a copy to the representative.

The auditor should grant reasonable requests by tax/[feepayers](#) to delay the start of an audit, but should be alert to detect attempts to forestall it. If excessive delay in the start date is agreed to, and a reporting period is about to expire, Form BOE-80-B, *Audit Engagement Letter – Agreement to Delay Start Date* should be used. Form BOE-122, *Waiver of Limitation*, covering a minimum of two quarterly reporting periods should be included [along](#) with the [BOE-80-RU](#)~~enclosures~~. (AM section 0215.15 provides guidance when a waiver of limitation should be requested.) If the audit is a result of a claim for refund filed by the tax/[feepayer](#), Form BOE-146, *Waiver of Credit Interest*, should be obtained.

* * * * *

Comments regarding contacts and attempts to contact tax/[feepayers](#), both oral and written, must be documented ~~on Form in the~~ [BOE-414-Z program](#). Copies of correspondence referenced ~~on in~~ the [BOE-414-Z program](#) should be included in the ~~audit~~-*Correspondence* subfolder of the audit case folder. It should be noted in the “books and records” comment of the Field Audit Report or Field Billing Order if any records were withheld or were not available. *The auditor’s comments must clearly state the effect the lack of records had on the amount billed.*

PURCHASES SUBJECT TO SALES OR USE TAX

0408.00

**AUDITS OF PURCHASES SUBJECT TO USE TAX
IN-STATE SERVICE PROGRAM**

0408.45

GENERAL

The In-State Service program is administered by the Use Tax Administration Section, In-State Service Group (ISS Group) and was implemented under the tax gap initiative. The tax gap is the difference between the amount of taxes owed and the amount of taxes paid to the state. The tax gap initiative was intended to promote voluntary compliance through education and outreach, implementation of new programs, and improvement of current programs. The purpose of the In-State Service program is to investigate and collect use tax from service based businesses that may not be aware of their reporting requirements. The ISS Group has teams located in Northern California (MIC: 05) and Southern California (MIC: EHS).

Through a monthly letter mailing campaign, the ISS Group contacts in-state service business leads, requiring the business to: conduct a self-review of purchase records for a three-year period; register, file, and pay online any use tax due; and submit supporting documentation for review and verification that the correct amount of use tax was self-assessed.

SOURCE OF INFORMATION

The Employment Development Department (EDD) and Franchise Tax Board (FTB) provide information to the Data Analysis Section (DAS) to help identify service businesses operating in California. The type of information received includes the following: business name, address, phone number, NAICS code, business description, number of employees in California, entity type, FEIN, SSN, gross receipts, and cost of goods sold.

The DAS matches the business lead data to CDTFA records and removes any leads currently registered with a sales or use tax account. The DAS forwards the remaining unregistered in-state service business leads to the ISS Group for further analysis, pre-screening, and selection of leads to assign to staff.

LEAD SOURCE CODES

To capture and identify the revenue resulting from the ISS Group efforts, the Lead Source code **TGI** (Tax Gap In-State Service) is assigned to any sales and use tax accounts generated, any audit cases created, and any compliance assessments issued as a result of the ISS Group efforts.

For new accounts, the Lead Source Sub-type code **EDC** (UTAS EDD Lead) will be assigned. For audit cases, the Lead Source Sub-type assigned depends upon the specific office receiving and conducting the audit. For example, an audit case

generated and referred by the ISS Group to the San Diego Office (FH) will have the lead source “TGI FHC” assigned. (FHC = San Diego audit referral from UTAS—ISS Group).

The Lead Source added at the account level will be for three years, by using the creation date of the account for the lead source “start-date” and creation date plus three years for the lead source “end-date.”

The Lead Source assigned for Audit Cases or Compliance Assessments should be added directly to the FO (Financial Obligation). Lead source “start date” and “end date” are not required when assigning a Lead Source to an FO.

(See AM section 0103.25, *IRIS Lead Source*, for additional information.)

RESPONSIBILITY OF THE USE TAX ADMINISTRATION SECTION IN-STATE SERVICE GROUP

Initial Contact

Based on the lead data received from DAS, the ISS Group selects and assigns leads to staff to investigate and determine if the in-state service business has use tax that may be due. Initial contact is made to the in-state service business by sending a *Tax Gap In-State Service Contact Letter* (BOE-403-CL) that explains what use tax is, how use tax may apply to its purchases, and how to comply with the California Use Tax laws. Included with the contact letter is the *California Use Tax Worksheet* (BOE-403-CLW) used to calculate use tax due for the previous three calendar years and verify ownership of the business entity. The letter also references publication 110, *California Use Tax Basics*, and publication 217, *Use Tax Guide to Reporting Out-of-State Purchases*.

If tax is due, the letter and worksheet instruct the business to utilize the CDTFA’s online services to register for a use tax account and file and pay the use tax returns. All businesses contacted are required to complete and return the BOE-403-CLW, regardless of whether or not they owe use tax, along with the following required documents: purchase journal/general ledger for the past year, a current asset depreciation schedule/asset listing, and their California Income Tax Schedule R, if applicable.

The in-state service businesses have 30 days to respond to the contact letter. After 15 days, staff in the ISS Group will call to verify the initial contact letter was received and to answer any questions the business may have. If a response to the letter is not received within 45 days from the inquiry date, a follow-up letter will be sent to the business.

Desk Review

Based on the contact letter responses, the ISS Group will conduct a desk review of the information provided for accuracy and understanding of use tax, and may do one or more of the following:

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1. Assist in filing returns online for previously unreported use tax liability periods.
2. Place a delinquency withhold in IRIS and corresponding comments in IRIS and ACMS for any periods that require additional time to review or require additional assistance.
3. Request additional documents (for example, specific invoices or federal income tax returns).
4. Create Compliance Assessments based on the completed *Use Tax Return Worksheets* and evidence of use tax due found within the required documents received or from other sources.
5. Issue account numbers for future reporting, for those who failed to register but provided information that shows they owe use tax.
6. Refer the ISS Group leads to field audit staff for further investigation if it has been determined that additional use tax may be due or other questionable activities are noted.
7. Close the assignments if no account number (i.e., arbitrary or permanent) is required and no use tax is due.
8. Refer leads on unregistered in-state vendors selling to an ISS Group business to field compliance staff using a BOE-142, *District Office Investigation Request*.
9. Refer leads on registered, questionable vendors to field audit staff for further investigation.
10. Refer leads on unregistered out-of-state vendors selling to ISS Group business to the OH 1032 team.

When a service business does not respond within 30 days from the follow-up contact letter date, the ISS Group will further investigate/research the business to determine if the address is valid, business is still active, and whether or not there is a potential for use tax based upon the business industry.

The ISS Group investigates the unresponsive business by doing one or more of the following:

1. Locate business websites, perform internet searches, or conduct searches in the CLEAR system.
2. View state income tax returns requested using the BOE-1144, *Official Request for Return Information*, interagency information requested from, EDD, FTB and the Secretary of State which are tracked in the external Agency Tracking system (EATS).
3. Perform a like-business analysis for use tax potential.
4. Cross reference other sources of information for potential for use tax (e.g., customs import documents, request to County Assessor for BOE-571-L, *Business Property Statement*, purchase history from known out-of-state vendors used).

Depending on the results from the additional investigation/research of the unresponsive business, the ISS Group will do one or more of the following:

GENERAL AUDIT PROCEDURES

1. Resend the Initial Letter, if a better address was found.
2. Make contact with the business/responsible person to further explain use tax and request the business respond to the initial letter immediately.
3. Create Compliance Assessments based on evidence of use tax due from Customs import documents or actual purchase information from out of state vendors.
4. Refer the use tax lead to field audit staff for audit.
5. Close the assignment if business is inactive or if it is determined that the assignment is not cost effective to pursue.

AUDITS OF REFERRALS FROM THE ISS GROUP SALES AND USE TAX PROGRAM

Depending on the response from the in-state service business, the ISS Group will select the leads to be referred for audit, create an account, create an audit case ID using the audit selection reason code GAP, and assign the lead source TGI and the appropriate lead source sub-type to identify the specific office conducting the audit.

Audit referrals are sent electronically and should include:

1. Memo or the ISS Group “all-in-one referral form;”
2. Business lead contact information and business description;
3. Detailed reason for the audit recommendation;
4. Evidence of use tax owed and/or supporting information of potential use tax owed;
5. Any transcribed income tax information, including gross receipts, COGS, assets, and other deductions;
6. Prior contact history between the ISS Group and the business (case history);
7. Copies of letters sent; and
8. Any other relevant information.

For audit tracking purposes, the ISS Group issues arbitrary account numbers to businesses that do not have an account with the CDTFA or did not obtain one during the desk review process. The audit case will be created on the arbitrary account. The ISS Group will conduct periodic follow-ups with the specific offices to determine the status of in-process audits referred to the them.

The audit period for these use tax audits will be the prior three calendar years unless otherwise determined by the Principal Auditor or designee. The ISS Group’s initial investigation requests the in-state service business review its records and self-report purchases subject to use tax that it made during the prior three calendar years. Despite the three calendar year timeframe, in cases where the in-state service business did not file a return, Revenue and Taxation Code section 6487 authorizes the CDTFA to mail notices of determination within eight years of the relevant period for which it proposes the amount to be determined.

The ISS Group adds the Lead Source code **TGI** and the respective Offices’ Lead Source sub-type code to the account and FO at the time the leads are selected for audit and

GENERAL AUDIT PROCEDURES

the FO is created for the audit period. The Lead Source and Lead Source Sub-type code are assigned to an account and FO by accessing the LSR ML, *Maintain/Inquire Lead Source Information*, screen in IRIS.

Audit staff performs audits on the use tax leads referred by the ISS Group to determine if use tax may be due. The appropriate BOE-80-TG series “Audit Engagement Letter” for the In-State Service Businesses Tax Gap Program should be used to confirm audit engagements or to establish contact.

- BOE-80-ATG, *Audit Engagement Letter - Confirm Start Date.*
- BOE-80-BTG, *Audit Engagement Letter - Agreement to Delay Start Date.*
- BOE-80-CTG, *Audit Engagement Letter - Initiate Contact.*
- BOE-80-DTG, *Audit Engagement Letter - 10-Day Follow Up.*

The BOE-80-ATG, BOE-80-BTG, and the BOE-80-CTG include links to the following publications and provide taxpayers with the CDTFA website address so they can download the publications. For taxpayers who are unable to download the publications, information is provided on how to obtain them from the Customer Service Center:

- Publication 70, *Understanding Your Rights as a California Taxpayer*
- Publication 76, *Audits*
- Publication 17, *Appeals Procedures, Sales and Use Taxes and Special Taxes*
- Publication 123, *California Businesses: How to Identify California Use Tax Due*

Audits will be conducted following general audit procedures set forth in this Chapter.

Audit staff should advise the Western States Office (OH) compliance staff, using the BOE-1164, *Audit Memorandum of Possible Tax Liability*, when an auditor discovers a business purchasing items subject to use tax from an unregistered, out-of-state retailer (see AM section 0408.19). A notation, “In-State Service Tax Gap” should be written in the comments and recommendation section of the BOE-1164 as a flag to the OH compliance staff that this referral was generated from an audit of an In-State Service Business lead. This will assist OH compliance staff in properly identifying and registering out-of-state retailers who are engaged in business in California resulting from TGI efforts. Alternately, audit staff may provide a list of unregistered out-of-state vendors discovered during the audit to the ISS Group, who will ensure the vendors are properly flagged and referred to OH.

Audit staff should be alert to recognizing transactions where the in-state business is remitting California use tax to an out-of-state unregistered retailer who is not billing the in-state business for the use tax. Auditors should utilize the IRIS CTS CS, *Client Search/Registration*, screen to determine whether such out-of-state vendors are registered to collect the use tax. When an auditor discovers that an in-state business is erroneously paying use tax to an unregistered out-of-state retailer, the auditor should immediately advise OH Compliance staff (see AM section 0408.23). The business should be informed of the responsibility for the payment of tax to the proper authority per Regulation 1685, *Payment of Tax by Purchasers.*

GENERAL AUDIT PROCEDURES

Audit Supervisors will follow the normal audit procedures when processing completed audits. The Audit Supervisor should also provide the ISS Group feedback as to the quality of the use tax leads received and suggestions for improvement. This can be done via e-mail to the referring ISS Group Supervisor.

1032 REFERRALS TO WESTERN STATES (OH) OFFICE

The ISS Group will review invoices, worksheets, purchase journals, and asset listings received from all ISS business leads and identify unregistered out-of-state vendors.

Utilizing the 1032 Desktop Application Program (1032 Database) that contains historical data of out-of-state vendors contacted by the CDTFA, the ISS Group will determine if the unregistered out-of-state vendor qualifies as a 1032 referral. If the vendor qualifies, the ISS Group will do the following:

1. Add the vendor to the 1032 Database to create a case.
2. Upload the source document with the vendor's address to the new case.
3. Research the vendor for possible proof of nexus and upload any relevant information.
4. Add the customer information to the case.
5. Add comments to the case and refer electronically to OH Office-1032 team via the 1032 Database.

The appropriate lead source code will automatically populate on the 1032 case for the appropriate UTAS program (ISS or Interstate Commerce Analysis Team (ICAT)). In the case of 1032 referrals from the ISS Group, the lead source is TGI OHE (OHE = OH Office 1032 referral).

SPECIAL TAX AND FEE PROGRAM REFERRALS

There may be occurrences when the ISS Group or the in-state office audit staff determine in-state service businesses are purchasing items from outside of California for consumption and are not being charged appropriate special taxes or fees (for example, purchases of new televisions, computer monitors, portable DVD players, tires, fuel, lead-acid batteries, alcoholic beverages and cigarette or tobacco products). Similarly, there may be cases where OH compliance staff register out-of-state retailers who are engaged in business in California that also require registration under special tax and fee programs.

In such cases, the ISS Group Supervisor, Principal Auditor, OH Compliance Supervisor, or a respective designee, should send an email notification containing the name, address and telephone number of the in-state service business or out-of-state retailer to the **"BTFD-ISS Referrals"** mailbox. The email notification should also include an account number and information concerning the description of items purchased, the quantity of items purchased and the periods in which the purchases occurred, if available. The Registration and Licensing Section will review the notification and forward the information to the appropriate staff for further investigation.