



# Sales Tax Audits

Best Practices

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Materials

**NC State & Local** TAX CONFERENCE

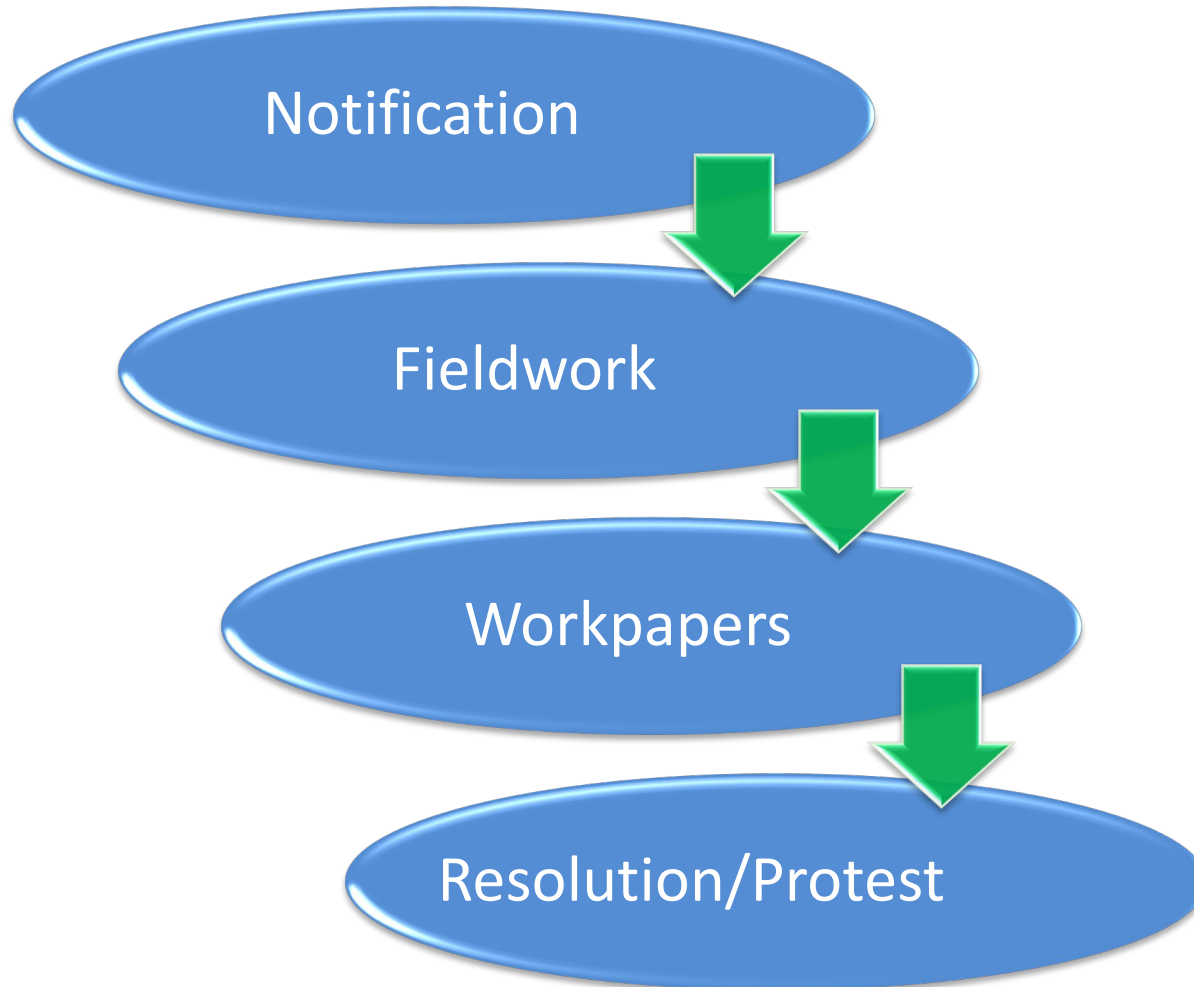
# OBJECTIVES

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- Overview of sales and use tax audit cycle
- Strategies to lead and steer the audit
- Understanding options for conducting the audit
- Remedies if documentation can't be obtained
- Mitigation of future exposure
- Q&A Discussion

# Sales & Use Tax Audit Cycle

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# Sales & Use Tax Audit Cycle

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Notification

Pre-Audit

Audit Questionnaire

Statute Waiver

Opening Conference

# BEST PRACTICE TIP #1

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Is there any possible way to avoid this audit?

# Sales & Use Tax Audit Cycle

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Fieldwork

Information Requests

Source Documents

Plant Tours

# BEST PRACTICE TIP #2

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Know your business!

Know your customers' business!

Know your vendors' business!

# BEST PRACTICE TIP #3

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A picture can be worth a thousand invoices!



# BEST PRACTICE TIP #4

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No state or federal income tax returns!

No apportionment workpapers!

# Sales & Use Tax Audit Cycle

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Workpapers

Version 1 - ok

Version 2 - better

Version 3 – good

Version 4 - great

# BEST PRACTICE TIP #5

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Deadlines are important

You can also set your own!

# Sales & Use Tax Audit Cycle

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## Resolution

No change / findings!

Pay tax and interest

Protest / Appeal

Recap and Repair

# BEST PRACTICE TIP #6

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Don't just be glad to get the audit over with  
Make improvements / changes / analyses

# SALES & USE TAX AUDITS

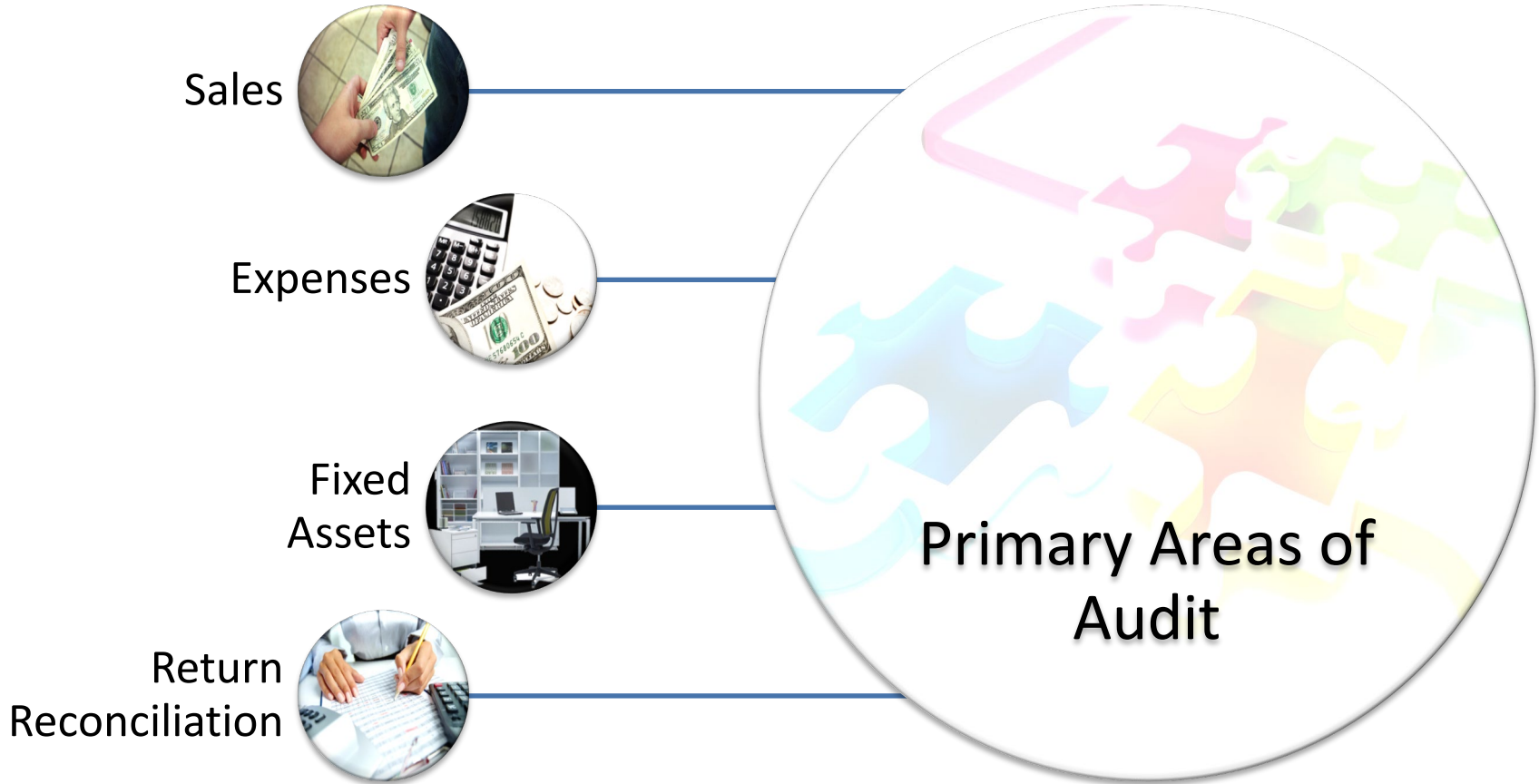
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- Audit period is usually 36 to 48 months
- Preparation is very time-consuming
- Large volumes of data are pulled and examined
  - Customer invoices
  - Tax exemption certificates and support
  - Vendor invoices
  - Credit card purchases
  - Capital project information
- Sales tax audits can take from 1-3 years to complete.



# Overview of the Audit Process

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# Sampling

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## Audit Sampling

In reality, a small portion of the invoices are actually reviewed

Types of sampling

Block  
Statistical  
Hybrid

An error rate is determined and projected against the entire population

Small errors can equal big assessments

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# BEST PRACTICE TIP #7

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Reduce the population!

Reduce the risk!

Put a fence around known issues!

# Audit Management

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# SALES & USE TAX AUDITS

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## Focus on Accounts Receivable

- All sales are taxable unless proven otherwise.
- Taxpayers have a legal requirement to correctly collect and remit sales taxes from sales made to taxable customers.
- If an Exemption Certificate is not obtained in a timely manner, is incomplete or not available, a seller is liable for the uncollected taxes.
- Taxes assessed for invalid exemption certificates during an audit are rarely recovered from customers.
- Audit review of sales is rarely done in detail; some sampling methodology is used – help guide this selection!

# BEST PRACTICE TIP #8

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It never hurts to ask!

Consider alternative evidence!

Did your customer pay use tax?

# SALES & USE TAX AUDITS

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## Focus on Purchasing

- **All purchases are taxable unless proven otherwise.**
- Liability is not extinguished until one party pays the tax
- Review “codings” carefully and try to provide legends and explanations
- Unless completely necessary – stay away from legal contracts
- Auditors tend to like to do asset reviews in detail

# BEST PRACTICE TIP #9

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Likely best to avoid Fixed Asset Depreciation Schedules

# SALES & USE TAX AUDITS

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## IDEAS TO CONSIDER

- Voluntary Disclosure Agreement (VDA)
- Managed Audit
- Managed Compliance Agreement
- Direct Pay Permits
- Bringing Audits to Current Period with Estimates

# SALES TAX AUDIT BEST PRACTICES



# QUESTIONS