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**April 2012**

## **Single Audit White Paper**

### **Scope of Paper**

This paper focuses on the issues involved in the implementation of a single audit for sellers. The paper was prepared by a workgroup consisting of members of the Streamlined Sales Tax Audit Committee and members of the Business Advisory Council. There was not unanimous agreement on all issues but the workgroup has attempted to present a workable plan to conduct a single audit. The paper addresses the issues with complying with a federal requirement for a “single audit,” as used in the federal legislation.

The implementation of a “single audit” may require changes to rules and audit practices in member states and could involve an amendment to the Streamlined Sales and Use Tax Agreement and legislation in some states. Ideally, the workgroup believes many of the issues presented in this paper could be incorporated into a rule to guide both taxpayers and the member states on the process used to conduct a “single audit.”

### **Background**

The present Main Street Fairness Act which was introduced in Congress (S.1452 & HR 2701) contains a provision for a “Single Audit”. Subsection (12) of Section 6 (part of the minimum simplification requirements) states “Audit procedures for sellers, including an option under which a seller not qualifying for the small business exception may request, by notifying the SST Governing Board, to be subject to a single audit on behalf of all Member States for sales and use taxes. The Governing Board, in its discretion, may authorize such a single audit.”

### **Single Audit Options**

The Audit Committee discussed three options for the single audit. Option one involves an Audit Core Team concept. Option two detailed having the Multistate Tax Commission (MTC) perform the audit for the member states and option three followed

the IFTA/IRP model where the base state performs the audit for all member states. A survey of member states revealed that an Audit Core Team concept is the preferred option.

**Following is a description of how the Audit Core Team concept would work:**

**SST Single Audit**

The attached flow chart proposes a process for managing a *single audit*. A number of issues need to be addressed before a single audit (which some states describe as more of a coordinated audit) could be completed on behalf of the member states.

The cooperation of all member states will be required to initiate a single audit. This type of audit will need to be managed much differently than current audits that member states conduct independently.

The workgroup envisions using the Audit Core Team audit concept utilized for the contract compliance audits of CSPs and the tax compliance audits of Model One Sellers transactions processed by the CSPs.

Since the Streamlined Sales Tax Governing Board does not have an audit staff, member states would need to provide Single Audit Team members in much the same way member states are providing Audit Core Team members for the contract compliance audits. Member states would have an obligation to ensure quality audit staff was assigned to participate in the single coordinated audit. Staffing the Single Audit Team might be an issue for some states which could result in the SSTGB hiring an audit staff.

The workgroup believes the single audit process should primarily focus on a seller's sales/use tax from sales to purchasers for the following reasons:

1. States' collection of sales tax from sellers is the most efficient mechanism for the states to collect the tax.
2. Audits on sellers are easier to conduct for both the taxpayer and the audit team.
3. If single audits are limited to remote sellers, consumer use tax is not an issue with the majority of states.
4. It may be difficult to track consumer use tax accruals.

There are some obstacles to limiting audits to sales and use tax that should have been collected from purchasers by the sellers:

1. Taxpayers may not want separate consumer use tax audits while under audit for sales tax.
2. Some states cannot audit sales and consumer use taxes separately without a law change.
3. States with statute of limitations issues may still have to incorporate a consumer's use tax audit for the same period.
4. States may not be agreeable to performing a single sales tax audit.
5. States may want to have the right to pick and choose which taxpayer audits to participate in; and
6. It may be more economical for the seller and some states to conduct the consumer use tax at the same time.

### **Requesting a Single Audit**

The workgroup discussed the process for requesting a single audit and envisions developing a request form to be used by the taxpayer that would list the criteria needed. The request for single audit form would be placed on the website to standardize this process.

Upon receipt of a request for a single audit, the Executive Director of the Streamlined Sales Tax Governing Board would send an acknowledgement notice to the taxpayer that the request was received and forward the request to the Streamlined Sales Tax Audit Committee. This acknowledgement will include a notice of the taxpayer's rights and an explanation of the single audit process.

When a taxpayer requests a single audit, the legal entities of the taxpayer subject to audit and the member states' participation would have to be determined. Some of the issues are:

1. Determining which business units and affiliated entities of the taxpayer would be part of the single audit.
2. Formulating a policy regarding the options available to member states for participation and, if a member state chooses not to participate, how that will affect a state's rights to conduct a separate audit.
3. Addressing additional unforeseen issues that arise in making a determination of whether a single audit can be performed.

The workgroup believes the SSTGB Single Audit Team should be the primary contact between the taxpayer and the member states during the audit process. The Single Audit Team would coordinate with the member states to establish the audit period and audit

timeline. This would allow the taxpayer an opportunity to plan their audit resources more efficiently. Below are some of the steps involved:

1. Along with an audit timeline the Single Audit Team would develop an audit plan to ensure that states are consistent in applying audit procedures. The audit plan would need to give states the ability to apply each state's tax law and required notices to taxpayers on what to expect during an audit. The audit plan and timeline would be worked out in agreement with the taxpayer.
2. The taxpayer would be required to provide data as specified in Appendix F (Audit Work Files) to the Single Audit Team. The Single Audit Team would then distribute to each State's representative their state specific data for review and to verify all transactions reported. Each State could do additional testing as each state deems necessary. The states would report back to the Single Audit Team their findings which the Single Audit Team would discuss with the taxpayer. This will help limit training required for state auditors while identifying compliance problems for member states.
3. Finally, the Single Audit Team would coordinate the issuance of each state's audit report and facilitate communications between the states and taxpayer. This would ensure the audit is complete for that time period for each SST state. Each state would issue its own assessment and the taxpayer would have the right to appeal with each state using that state's appeals procedures.

## **Issues**

### **Statute of Limitations**

Statutes of limitations for issuing assessments and refunds differ among the states. Thirty-five states (16 SSUTA states) have a three-year statute of limitations for assessments, nine states (six SSUTA states) have a four-year statute of limitations, one SSUTA state has a 3.5 year statute of limitations and one state has no statute of limitations.

The workgroup recommends states use the same audit period for a single audit. The workgroup recognizes if a taxpayer is in the process of being audited by a state that might limit their ability to participate in the single audit. This could apply as long as any portion of the current state audit is part of the audit period included in the single audit request.

Waivers could be an issue for some states if a three-year audit period is used. States should be able to continue to request statute of limitation waivers based on each state's established guidelines.

### **Other Member State Issues**

Several states are not able to issue more than one assessment per audit period; therefore, they cannot make a separate assessment for consumers use tax if the consumers use tax is not audited at the same time as sales tax. This may require some states to change their statutes. The Audit Committee surveyed the states on this subject and 18 states responded. There are eight states that are not able to issue an assessment for consumers use tax after a sales tax assessment has been made for the same period. Some of these states have indicated that it would be very difficult to change their statutes.

### **Exchange of Information Concern**

In order for the SST Governing Board to authorize a single audit on behalf of all the member states, the member states, including the Audit Core Team and Single Audit Team, must be able to share information. While there are several multi-state information sharing agreements, the workgroup suggests a special exchange agreement be put in place to cover the confidentiality and information-sharing requirements of all of the member states.

The uniform confidentiality and information-sharing agreement between all member states should include felony provisions for disclosure of tax information or audit parameters to unauthorized individuals and/or penalties for unauthorized disclosure of tax information to satisfy states that have these provisions in their statutes.

### **Appeals Process**

The workgroup discussed the appeals process when an assessment or refund is disputed by the seller and determined that the appeals should be handled on the individual state level. The audit would be conducted/coordinated through the Single Audit Team and the proposed assessment/refund would be billed by the individual state. Any protest or appeal of the audit findings would then be filed with the respective state and proceed through that state's protest and appeals process the same as any other taxpayer. Each state currently has a protest and appeals process in place, so there would be no difference between an appeal of a streamlined taxpayer and a non-streamlined taxpayer.

# Single Audit Request and Review

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