AUDIT OF TAXABLE SALES - 111

GENERAL - 111.1

A. The objective of auditing sales is to determine if the correct amount of New York State and local sales tax was collected and remitted on all taxable receipts. Auditing taxable sales encompasses many areas related to verifying reported tax due from sales. Field Audit Guideline Section 110 – Audit of Non-Taxed Sales deals specifically with determining if the vendor has properly accounted for non-taxed sales. This section provides a guide to audit methods used to determine if the correct tax has been reported and remitted on sales considered taxable by the vendor, in addition to determining any additional taxable sales and/or sales tax through the audit of the available books and records.

B. The auditor will be responsible for verifying:

1) Reported gross sales.

2) The use of proper jurisdictional tax rates and reporting the tax to the correct jurisdiction.

3) The use of proper tax rates for sales of services or products that have specialized tax treatment.

4) The vendor's mathematical accuracy of tax calculations and the proper recording and reporting of the calculated tax.

5) Tax accrual accounts or the taxpayer's method of accumulating tax due to ensure the remittance of all monies collected as taxes.

BASIS OF TAXABILITY - 111.2

A. New York State Sales Tax is a "destination tax". In general, the tax due on each sale is determined by applying the jurisdictional state and local (if any) tax rate to the total sale.

B. There are several exceptions to the preceding statement. Common exceptions include:

1) Motor vehicles taxed at the jurisdictional rate in effect at the owner's registered address (Tax Law Sec. 1117 and 1214).

2) Flowers by Wire (see Reg. 526.7 (e) (3), TSB-M-82 (31) S, DOS-83-10)

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3) Vending Machines (TSB-M-83 (33) S, DOS-85-09, TSB-M-97 (12) S, TSB-M-00 (6) S)

   a) Sales at $.10 or less (Tax Law Sec. 1115 (a) (13), Reg Sec. 528.14, TSB-M-97 (12) S)
   b) Bulk Vending Machine – (Tax Law Sec. 1115 (a) (13-a), Reg Sec. 528.14, TSB-M-97 (12) S)
   c) Off Premises Consumption – (see TSB-M-79 (1) S)

4) Admissions Charges (see Reg. 527.10)

   a) Permanent use of a Box or Seat – (see Reg. 527.10 (a) (2)), STB-92-2)
   b) Admission charge to a qualifying place of amusement TSB-M-05(5)S, TSB-M-06 (12)S
   c) Season tickets

5) Dues and Initiation Fees (see Reg. 527.11, TSB-M-95 (12) S, DOS-80-08, DOS-80-30, TSB-M-96 (16) S)

6) Room Rentals (see Reg. 527.9, TSB-M-91 (3) S, TSB-M-94 (4) S)

7) Mobile Homes (Tax Law Sections 1101 (b) (10) and 1101 (b) (11), Reg Sec. 544, TSB-M-81 (22) S, TSB-M-83 (24)& 24.1) S)

8) Race Horses (see Reg. 527.15, STB-92-14, TSB-M-95 (6) S)

9) Promotional Materials (see TSB-M-92 (4) & (4.1) S, TSB-M-94 (3), STB-94-04, TSB-M-97 (6) S)

10) New York City selected services (see TSB-M-89(21)S, TSB-M-95 (13) S)

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VERIFICATION OF REPORTED TAXABLE SALES - 111.3

A. A copy of a representative tax return within the reconciled period (see Field Audit Guideline Section 109 – Reconciliation of sales tax returns) should be requested from the vendor, examined and compared to the imaged copies or the data captured in the department's systems. The vendor should be asked to identify the source of the amounts used to compile taxable sales. This analysis of the tax return will aid the auditor in understanding the vendor's method of computing and reporting taxable sales and may alert the auditor to any weaknesses in the vendor's accounting or reporting system that may lead to errors. Unless the vendor's method of reporting is entirely erroneous, audit time may be saved by adapting the audit procedures to the vendor's reporting methods.

B. When verifying reported taxable sales, the auditor must determine that sales from all sources, such as separate departments, store locations, subsidiaries or related companies, have been recorded in the sales journal and on the sales tax return worksheets. In addition to verifying the inclusion of credit card sales, the auditor must verify that credit card transactions have been entered at the actual sales amount rather than the discounted amount received from the bank or Credit Card Company. Also, adjustments of general journal entries must be reviewed and verified as proper. All discrepancies must be recorded in the workpapers to support the audit adjustment.

AUDIT PROCEDURES - 111.4

A. In order to accurately verify taxable sales, the Auditor should:

1) Analyze sales invoices or other source documents within the period of review on which tax has been charged;

2) Verify the accuracy of tax collections within the review period as to amount and taxing jurisdiction based on point of delivery;

3) Trace selected source documents during the review period through the accounting system to journals and ledgers;

4) Record errors in the collection of sales tax on workpapers. Workpaper entries should include customer name, invoice number and date, taxing jurisdiction, taxable amount, tax collected and tax due.

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B. The following audit procedures are generally used in various audit situations.

1) Taxable Ratio Test (see Field Audit Guideline Section 207 – Taxable Ratio Analysis)
2) Mark-Up Techniques (see Field Audit Guideline Section 208 – Mark-Up Test)
3) Statistical Sampling (see Field Audit Guideline Section 205 - Statistical Sampling)
4) Audit of Computerized
5) Observation Audit Technique Records (see Field Audit Guideline Section 209 – Alternative Audit Methods)
6) Third Party Verification Records (see Field Audit Guideline Section 209.3 – Alternative Audit Methods)

TAX COLLECTED - 111.5

A. The audit of taxable sales should include verification of the accuracy of tax collected on individual transactions.

B. If the reconciliation of the sales tax return and verification of reported taxable sales reveals that the vendor is remitting taxes actually collected and computing taxable sales based on such collections rather than from sales records, a representative test of individual sales invoices, register tapes or similar record should be made to ensure that the appropriate amount of tax has been collected on individual transactions. Any discrepancies must be recorded in the workpapers to support the audit adjustment. (see Field Audit Guideline Section 206 - Projection of Test Results)

C. The auditor should also review individual sales invoices, register tapes, etc. to determine that erroneous over-collections have not been made. These are amounts collected in excess of the amount due. A common example of an erroneous over-collection is the rounding of tax to the next nickel. The vendor must remit all amounts representing erroneous over-collections in addition to the correct tax due on sales where the tax has been under-charged. The vendor is not permitted to off-set over-collection with under-collections. This test is performed by comparing the tax collected on individual transactions with the appropriate amount of tax due. All discrepancies must be shown in the workpapers to support the audit adjustment. Detailed procedures for performing an over-collection test are presented in Field Audit Guideline Section 217 – Test for Proper Collection of Tax.

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D, If the vendor is using an automated or electronic system for computing tax, the Auditor should analyze the system, and where possible, test the accuracy of the tax calculations by running dummy transactions through the register or other system. If the system proves reliable, an over/under-collection analysis normally would not be necessary.

CASH DISCOUNTS - 111.6

A. Cash discounts which represent a reduction in price, such as trade discounts are deductible when computing tax on receipts.

B. Early payment discounts which are granted by a vendor for prompt payment of an account are not deductible from taxable sales.

C. The following audit procedure should be used when auditing cash discounts:

1) The audit of cash discounts is performed after total sales and taxable sales have been verified, as any change made by the auditor in the vendor's classification of taxable and nontaxable sales will affect any cash discount deduction.

2) The vendor's accounting records are examined to determine the method of computing cash discounts. If the listing of sales invoices on which a discount was allowed is available, the auditor should verify the deduction in detail. Generally, however, sales are too numerous to list and the cash discounts would be audited for a test period. The period(s) used to test taxable sales would also be used for this test.

3) When reviewing cash discounts, the auditor must verify that:

   a) the discount was actually taken by the purchaser;

   b) the difference between the invoice price and the cash received is actually a cash discount and

   c) the discount applies to a taxable sale.

Any discrepancies found during this review must be recorded in detail in the workpapers as a basis for the audit adjustment.

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DELIVERIES BETWEEN LOCAL TAXING JURISDICTIONS - 111.7

A. As part of the audit of taxable sales, the auditor must determine that the proper local taxes have been collected. The procedures for verifying deliveries from one local taxing jurisdiction to another are generally the same as those for out-of-state deliveries, stated in Field Audit Guideline Section 110 – Audit of Non-Taxed Sales.

1) When auditing a vendor located in a jurisdiction having a lower rate than surrounding areas, the auditor should review sales invoices and related documents for transactions taxed at the lower rate to ensure that the property has not been delivered to jurisdictions with higher tax rates.

   Particular attention should be given to large consumer items; such as furniture and appliances which are not normally transportable by the consumer. Evidence of delivery would be the driver's log, delivery slips or directions to the purchaser's residence entered on the sales invoice. All discrepancies should be recorded in detail in the workpapers to support the audit adjustment.

2. When auditing a vendor located in a jurisdiction having a higher rate than surrounding areas, the auditor should verify that claimed deliveries into neighboring areas with lower rates are properly substantiated.

   Particular attention should be given to small but high priced items such as jewelry, furs, small appliances, stereo components, laptop computers, cameras, etc., which are easily transportable by the customer. Unsubstantiated deliveries must be recorded in detail in the workpapers in order to support the audit adjustment.

NO WRITTEN RECEIPTS - 111.8

A. If no written receipts are given to the customer, the "unit price" method is permissible provided certain conditions are evident. The unit price is the total amount of the item, including the sales tax, which is either rung up on a cash register or recorded in some other accounting for sales. Since the customer must be made aware of the inclusion of sales tax in the total sales price, every business establishment employing the "unit price" method must visibly display to all customers a placard stating that the price of all taxable items includes sales tax.

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B. The following procedure should be used in the audit of a vendor who gives no written receipts and is reporting sales tax based on the "unit price" method.

1) If the vendor is displaying a placard which states that the selling price includes sales tax, then the unit pricing method shall be accepted on audit.

2) If the vendor has no sign or an improper sign posted, and the accounting records and reporting methods reflect the inclusion of sales tax in the selling price, the unit pricing method will be utilized for the purposes of the current audit. However, the vendor must be advised that this method will not be recognized for subsequent audits unless the proper sign is posted. An entry must be made on the *Field Audit Record*, Form DO-220.5 that notification was made, showing the date and who was placed on notice. A letter should be sent to the taxpayer confirming the notification, and a copy should be kept in the audit folder.