

5000 WORKING WITH TAXPAYERS

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5005 WORKING WITH TAXPAYERS

Establishing a positive working relationship with the taxpayer that is conducive to the effective and timely completion of the audit is critical in every audit assignment.

During the course of interaction with the taxpayer, considerable effort should be directed toward ensuring that:

- The purpose of the audit and the legitimate need for information requested are conveyed to, and understood by, the taxpayer.
- The evaluation of audit data and the resulting determination of tax liability are made in a fair and impartial manner.
- The audit progresses with a minimum of inconvenience to the taxpayer.
- The final audit recommendations are supported by both the facts and the law and are discussed with, and understood by, the taxpayer.
- Audit Issue Presentations Sheets (AIPS) should be issued to the taxpayer as soon as the auditor has completed the issue, rather than waiting until the end of the audit to explain the adjustment. (See **MAPM 5065** for discussion of AIPS.) AIPS should be used for all material adjusted issues.
- The auditor should always communicate the results of the audit in writing to the taxpayer, and provide the taxpayer with the opportunity to rebut any findings. Where appropriate, or when requested by the taxpayer, a closing conference may be conducted and the supervisor may attend.

The following are suggestions on receiving cooperation from taxpayers and tax representatives:

- Auditors should conduct themselves in a courteous and professional manner. Your tone in letters and on the telephone is very important. As the auditor, you want to be treated politely and with respect and so does the tax representative and taxpayer. Words such as "thank you", "sincerely", "your cooperation is appreciated", "look forward to your response", "you are correct with respect to..." "although I understand your argument...", and "if you have questions, please call..." convey this feeling.
- When the taxpayer is verbally abusive and uncooperative, be cooperative and professional. If you respond with an equally abrasive attitude, you will not gain cooperation. If you are cooperative, it is difficult for taxpayers to remain uncooperative.
- Timeliness in your audit sets the tone for all follow-ups in the audit, and your ability to effectively close the audit. For example, if you take six months to reply to the taxpayer, the taxpayer will not give your next request for information a high priority. You should set a comparable response timeframe (same as we require from taxpayers) and stick to it.

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Although we typically respond to taxpayers within 30 days, try replying within 10 days to two weeks. This shows the taxpayer that the case is a high priority to you, and the taxpayer will also respond timely.

- Always set the taxpayer's response date to a specific due date (e.g. June 15, 2002) to reply. A specific due date avoids the confusion that setting the response date at 30 days can cause (e.g. calendar days vs. workdays).

5010 AUDIT PLAN

Purpose

The purpose of the audit plan is to establish open lines of communication and to promote understanding of commitments made and agreements reached. The audit plan is a tool that provides a road map of how the audit began, how the audit is progressing, where the audit is going, and identifies key potential audit issues. It allows the auditor and the taxpayer to work together to resolve problems as early as possible in the audit process and establishes a partnership relationship. The audit plan helps ensure an effective and efficient audit that is less burdensome, less costly and less intrusive.

Taxpayer participation in the development of the audit plan is encouraged. The Franchise Tax Board staff should be receptive to the taxpayer's suggestions of "what are we doing well", and "what can we do to make it better?" By involving the taxpayer in the audit plan:

- Both parties will more efficiently manage the fact gathering and analysis process.
- It will allow the taxpayer to anticipate deadlines and provide alternative solutions to resolving issues, such as using alternative documents, and using agreed sampling methods where the records are too voluminous.
- It will alleviate any apprehension the taxpayer may have about what to expect, and foster communication and cooperation in the audit process.
- Issues to be included in the audit plan should be based on the materiality of the potential adjustment and balanced with the statutory requirement to determine the correct amount of tax. If potential for an audit adjustment is likely, the issue should be pursued if the materiality of the potential adjustment warrants the audit resources necessary to audit the issue. Materiality is a facts and circumstances test and you should consider, and discuss, the materiality of issues throughout the audit.
- Emphasize that the audit plan is a guide for the examination. It is subject to revision as progress indicates the need for more, less or different work than originally planned.

Components of an Audit Plan

- a. * * * * *
- b. * * * * *
- c. * * * * *
- d. * * * * *
- e. * * * * *

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Additional Information

Additional resources available to assist you in the development of the audit plan are listed in Exhibit B. Exhibit C is an example of a Team Audit Plan.

a. When Do You Use An Audit Plan?

All audits will use some type of audit plan, though the complexity of the audit plan will differ based on circumstances. For certain audits, e.g., single-issue audit cases, the audit plan might be a simple Scope Sheet. A more formalized, detailed, audit plan should be used on:

- Cases which are either large and/or contain sensitive audit issues; or
- At the advice of the audit supervisor; or
- At the request of the taxpayer; or
- As a result of the auditor's judgment.

b. When Is The Audit Plan Developed?

The audit plan sets forth the road map for the audit and therefore would be completed as a preliminary step. Upon completion of the preliminary audit procedures and scope, the auditor should prepare a draft audit plan.

- The draft audit plan may be sent to the taxpayer with the letter confirming the initial appointment in order to initiate discussions during the opening conference.
- The draft audit plan should be discussed and reviewed with the taxpayer during the opening conference.
- After the opening conference, the lead auditor, the supervisor and assigned team members should finalize the draft audit plan incorporating changes made as a result of discussions with the taxpayer.
- If there are significant changes to the draft audit plan and the supervisor was not present at the opening conference, the lead auditor should submit the audit plan to the supervisor for review and approval before finalizing.

c. Who Develops The Audit Plan?

In a team audit, the lead auditor should prepare a preliminary draft of the audit plan, with team members providing comments, and submit the plan to the immediate supervisor for review and approval. The supervisor and program manager might also provide input on planning, the role of the team members, involvement of the supervisor and/or industry specialist, or anything vital to management's role and approval. In addition, the input provided by the taxpayer at the opening conference will also be considered.

d. What Should Be In The Audit Plan?

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The following items are typically included in the audit plan although not necessarily all-inclusive. Additions or deletions from the audit plan should be done on a case-by-case basis.

Items common to all audit plans include:

1. Audit Scope

The audit scope shows the years being examined, MSA office conducting examination, results of prior years, how examination began, etc.

2. Purpose Of The Audit Plan

The purpose is to provide a working tool to monitor the progress of the audit, to open lines of communication and establish a partnership relationship with the taxpayer.

3. List of Key Personnel

Key Franchise Tax Board staff and taxpayer personnel, including representatives, should be identified showing their addresses and telephone numbers. If applicable, the role and responsibility of each FTB audit team member should be explained.

It should be confirmed that the taxpayer personnel identified in the audit plan are authorized to provide the Franchise Tax Board with records or enter into preliminary and final discussions with the Franchise Tax Board relative to issues or other items of interest.

4. Timeframes

Establishing timeframes and adhering to them is critical in successfully completing cases on a timely basis. Throughout the audit process, these timeframes serve as benchmarks against which progress can be measured. Timeframes should be established for:

- Estimated starting date and estimated completion date.
- Expected response time frames on IDRs, AIPs and correspondence.
- Schedule of tentative field appointments.
- Status Conferences - to periodically meet and discuss audit issues, emerging problems, how the flow of information is progressing, and the general status of the audit.
- Waivers - Current statute of limitations and policy for managing the SOL throughout the audit.

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5. Status Of Federal Audits

The status of any federal audit, if known, should be included in the plan. Periodic follow-ups during the audit may be needed to ascertain the current status of the federal audit.

6. Amended Returns Filed By The Taxpayer

It should be ascertained from the taxpayer whether any amended returns have been filed of which the auditor may not be aware. In addition, knowing about any anticipated amended returns that might be filed by the taxpayer is helpful in managing the audit process.

7. Audit Issues

Known audit issues and the potential tax effect should be identified and set forth. The taxpayer should be informed additional issues may arise and changes may be made during the course of the audit.

8. Audit Procedures

Procedures should be set forth for issuing IDRs, AIPS and the closing letter.

9. Audit Logistics

Numerous logistic issues to be discussed with the taxpayer should be included in the plan. These might include:

- Location of the audit records.
- Taxpayer's record retention policy.
- Availability of photo copying equipment and procedures for photocopying.
- Adequate accommodations - audit room, storage of taxpayer's records, telephones, rest rooms, cafeteria facilities, etc.

10. Amendments To The Audit Plan

The audit plan is a guideline for conducting an examination and can be amended throughout the on-going audit process as circumstances warrant. Any amendments to the original audit

plan must be acknowledged to the taxpayer in writing and/or be provided in an amended audit plan issued to the taxpayer.

The audit team should be receptive to any suggestions by the taxpayer that would expedite the audit process and/or facilitate the taxpayer's task of complying with the audit team's information requests, without the loss of audit quality.

e. Delivery Of The Completed Audit Plan

The audit plan should be signed and dated by a senior member of the taxpayer's staff, preferably an officer, the senior tax manager or the representative. The auditor should document the delivery of the plan in the PASS file.

The audit plan should be signed and dated by the auditor and the audit supervisor. In some cases, it may also be appropriate to get Program Manager approval.

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Reviewed: January 2006

5015 OPENING CONFERENCE

Purpose

The purpose of the opening conference is to establish the groundwork necessary to conduct an effective and efficient audit. The opening conference establishes lines of communication and helps build a partnership between the auditor and taxpayer. During the opening conference you will introduce the participants of the audit; agree on a general audit plan; discuss audit processes and procedures; agree upon expected timeframes; and start developing a rapport with the individuals that will be working on the audit.

Components of the Opening Conference

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- m. * * * * *
- n. * * * * *
- o. * * * * *

Additional Information

Additional resource material that will help you in planning and conducting your Opening Conference can be found in Exhibit A.

a. Introduction of Personnel

- It is important that personnel be introduced and both parties understand the other's organizational structure. Items that assist in accomplishing this include:
 - The taxpayer should be provided the names and telephone numbers of the audit supervisor, program manager, MSA Field Operations Manager and Bureau Director. The auditor should explain the reporting lines.

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- Organization and understanding of the tax department.
 - Knowing the organization of the tax department helps you understand the reporting lines within the taxpayer's corporate structure. If possible, obtain an organization chart showing reporting lines through the Vice President of Taxes or similar position along with phone numbers.
 - It is also helpful to understand the employment history of those assigned to work on the audit. Employees that have prepared the return as opposed to joining the company after returns have been filed may be more familiar with filing positions taken and location of records.

b. General Discussion

The general discussion should be relaxed and informal. The purpose of the general discussion is to open communication and to begin forming a professional relationship with the taxpayer's staff. This is an opportunity to:

- Provide a copy of the Statement of Principles of Tax Administration if it was not already provided with the contact letter.
- Provide the taxpayer with a copy of the audit regulation or refer them to it for more detailed information about the conduct of the audit.
- Emphasize our expectation of completing the audit within two years from the initial contact in accordance with the audit regulation. A more detailed discussion of the estimated completion date should be done in conjunction with the audit plan.
- If appropriate, discuss questions you have on the general history of the taxpayer. Are there unusual activities during the audit years? Is the taxpayer undergoing current changes that might impact your audit?
- Determine other "environmental" issues that the auditors should know about such as whether the company is in the process of shutting down their tax department and outsourcing. People are proud of whom they work for and can provide insight into the uniqueness of the taxpayer and what they view as important.

c. Audit Plan

(See Audit Plan Section for details)

The purpose of the audit plan is to formalize the groundwork necessary to establish open lines of communication and to promote understanding of commitments made and agreements reached. The audit plan is an audit tool that provides a work document, a road map, of how the audit will progress and identifies key potential audit issues.

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- The draft audit plan may be sent to the taxpayer with the letter confirming the initial appointment. It should be discussed and reviewed with the taxpayer during the opening conference.
- A major component of the audit plan to be discussed is audit timing. This should include the estimated completion date, timing for IDR responses, follow-up procedures, AIPs response times, etc.

d. Discussion of Major Audit Issues

Auditors should inform the taxpayer of the potential audit issues identified during the scoping process. Possible items that might be discussed are:

- Recurring audit issues - Determine the status of recurring issues if the prior audit determination is being protested or was changed during the protest and appeal process. Discuss if there has been a change to the statutory treatment of these items since the last audit. Consider whether the examination of recurring issues can be limited on agreements to facts developed in prior audits. This should be done only when the prior audit development of the issue was comprehensive and after determining what current development is necessary to ensure that the facts in the prior audit are applicable to the current years. If this is feasible, it should be discussed with the taxpayer.
- New audit issues - You might be able to discuss specific issues, for example a sale of an operating division or product line reported as non-business income. However, for other issues, a more general outline can be provided.
- The taxpayer should be informed that additional issues might arise from the review of information in support of the tax return.
- Ask the taxpayer if they have changes or issues that they want to submit for consideration. The earlier that you discover potential claim issues, the easier it is to adhere to your audit timeline.

e. Tax Return Preparation

Obtaining information on how the return was prepared will provide valuable information on how to address issues and identify where knowledge might reside within the taxpayer's organization.

- Who prepared the return? If they are not the same people you are dealing with, are they still available for questions or information?
- Was the tax return prepared by the taxpayer or outsourced?

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- What part did the tax department prepare? What part did the divisions prepare?
- What instructions were issued to people who prepared parts of the return? Are the return preparation guidelines available?
- How was apportionment information compiled?
- Where are the tax preparation workpapers located and what lead time is needed to obtain them?
- Are the tax preparation workpapers stored electronically? If so, in what format? Can they be exchanged electronically?
- Have State or Federal amended returns been filed? If so, what is the status of these amended returns?

f. Status of IRS Audits and Audits by Other States

- Establish what years the IRS has audited. What is the status? If appropriate, discuss with the taxpayer how they would like to convey any final federal determinations that occur during the course of your audit.
- Determine whether the RAR for the most recent IRS audit has been submitted to the Department.
- Discuss any outstanding controversies at the federal/state level. Do any of the years/issues affect your audit cycle?
- Have any other states audited the years under examination? You may be able to save yourself, and the taxpayer, time and effort by obtaining copies of audit work performed by other UDITPA states.

g. Company Records

Company records provide the foundation for factual development. Knowing the following can greatly assist in obtaining needed information:

- What are the taxpayer's recordkeeping practices? What areas of the taxpayer's organization have responsibility for the records you need to examine?
- What electronic records might be available and in what format are they?
- What is the taxpayer's record retention policy?

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- What documents have actually been retained? It can be helpful to obtain the document that lists the actual records maintained in storage. Actual documents in storage as opposed to the taxpayer's record retention policy may vary.
- Generally, how long will it take to retrieve documents from storage?

h. Information Document Requests

(See Information Document Request Section for details)

The Information Document Request is an important tool used to obtain the necessary information in a timely manner from the taxpayer. All requests for information will be documented on an IDR. A master IDR Log will be maintained to track all issued IDRs and to provide a clear focus for the status of IDRs. Copies of the Master IDR Log can also be shared with the taxpayer so all parties have a common understanding of the expectations. During the opening conference, the auditor should:

- Discuss the general response timeframes and follow-up process for IDRs. It is important that an understanding be established on the importance of meeting timeframes in order to complete the audit timely. Taxpayers should be informed that it is our practice to issue an IDR, one follow-up, and then, if necessary, a formal demand for the information citing possible application of the failure to furnish information penalty.
- Discuss the general format of the IDR and explain the use of the single question as opposed to single issue IDR. If appropriate, discuss if the taxpayer would like to review the draft IDRs before they are issued.
- Establish who will receive the IDRs and who may be contacted to secure additional records or information.

i. Audit Issue Presentation Sheets (AIPS)

(See Audit Issue Presentation Section for details)

The purpose of the AIPS is to communicate the specific audit issue, the facts developed, the relevant law and the audit recommendation on the issue. The issuance of AIPS provides the opportunity to conclude and resolve issues on an ongoing basis. The AIPS is an important tool that keeps the taxpayer fully informed about the audit and the FTB's position on each issue. During the opening conference, the auditor should explain:

What an Audit Issue Presentation sheet contains.

- That AIPS will be issued as soon as issues are completed. Auditors will not wait until the end of the audit to provide this critical information flow.
- That all adjustments will be explained through the use of the AIPS process.
- Taxpayers are requested to respond to the factual write-up as presented in the AIPS. It is understood and expected that the taxpayer may disagree with the application or conclusion of the law but at a minimum, we should strive to obtain agreement with the factual understanding.
- The timeframes appropriate for responses.

j. Status Conferences

(See Status Conference Section for details.)

Status conferences should be held to measure actual progress with planned benchmarks. It is critical that all parties continually monitor the success of the audit. These conferences provide an opportunity to make needed adjustments to keep the audit on track with the planned completion date.

- During the opening conference, the auditor and the taxpayer should develop a plan for when status conferences will be held and what will be expected of each party at the status conferences.
- The status conference should be used to keep the communication process between the taxpayer and the auditor open.

k. Waivers

The Audit Regulation sets forth the expectation that the audit will be completed within the normal statute of limitations or two years of initial contact. However, there may be some situations where waivers are appropriate. It is the auditor's responsibility to assure the statute of limitations has not expired. During the opening conference you should:

- Determine if there is a federal waiver and if so, the status.
- Explain how waivers, if necessary, will be handled throughout the audit. See MAPM 9050 through MAPM 9110 for information on handling waivers during the audit.

l. Scheduling Future Audit Appointments

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Planning the entire audit process through the expected completion date is essential if the audit is to be successfully completed on time. This planning process encompasses anticipated field visits that will be needed to complete the audit. This approach provides a partnership endeavor with the taxpayer so both parties understand the expectations and resources that will be needed to complete the task.

- Audit examinations are generally expected to be completed within the normal statute of limitations and within two years of audit contact. Therefore, the first contact should occur within two years of filing of the original tax return.
- In order to keep the time frame for completion of the audit within the agreed completion date, the auditor needs to establish future audit appointment dates with the taxpayer. The auditor and the taxpayer should work out a timeline identifying future audit appointments, black out dates, review time, etc. It might be helpful to work backwards from the expected completion date to get a better perspective of the commitments needed in order to meet the 2 years completion date.

m. Photocopying

Photocopies of taxpayer records may be needed to support the facts as set forth in the audit report. Only relevant portions needed for the specific issue need to be photocopied. It is helpful to:

- Establish what procedures the taxpayer would like for photocopying of records or documents. If the taxpayer requests that its staff does all photocopying; address follow-up procedures if there are any problems.
- In cases where the auditor photocopies documents, if the taxpayer requests, the auditor shall provide a copy of any documents photocopied for the audit file.

n. General Items (office space, etc.)

Some taxpayers assign permanent space to auditors until the audit is completed or for the duration of a field visit. If an auditor is provided with an office, the auditor should find out who has access to the office, if keys will be provided and what hours the auditor can enter the office. Taxpayers might be limited in the space that they have available for auditors; however, it is appropriate to request adequate working space in order to work efficiently and protect the taxpayer's records.

- If temporary space is assigned, the auditor might want to request a locking file cabinet to store records or make an agreement with the taxpayer that records will be made available at the beginning of the first day of each field visit.

- For security reasons, many taxpayers require that an auditor obtain and wear an identification or access badge. The badge might provide entry access into the taxpayer's building and certain office areas. Auditors are not authorized to sign any confidentiality agreements in order to obtain an access or identification badge. The auditor should inform the taxpayer that any information provided is confidential and protected by Section 19542. If the taxpayer wishes to take its case to appeal or litigation, it may seek a protective order from the SBE or the courts in order to protect proprietary or otherwise secret information from disclosure to the public. Section 19504 gives FTB a right to examine the information without precondition or restriction. Therefore, FTB will not enter into any agreement, which could potentially restrict our ability to use information to which we are entitled.

o. Position Letter/Closing Conference

(See Position Letter Section and Closing Conference Section for details.)

During the opening conference, the auditor should discuss both the position letter and closing conference (if planned), so that the taxpayer knows what to expect.

- Position letters can simply make reference to the AIPS that have already been provided to the taxpayer and can also be used to send any remaining AIPS to the taxpayer.
- Complete copies of AIPS already provided to the taxpayer do not need to be duplicated with the position letter unless modified or requested by the taxpayer.

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5020 CORRESPONDENCE

Correspondence may be initiated as a result of:

- Scoping returns for potential audit issues.
- Audit inquiries into ownership, unity, business vs. nonbusiness income, etc.
- Claims filed for corporations by amended returns.
- Correspondence received.
- General questions received from corporations, their representatives, or accounting firms.
- Correspondence or returns referred from other sections or units.
- Tax Clearance or Post Dissolution Audits from the Tax Clearance and Post Dissolution Units.

Often, inquiries may be handled by telephone. Auditors are encouraged to use the telephone to answer taxpayers' correspondence and to obtain additional information or clarification. Telephone communication is an efficient and economical alternative when the taxpayer has questions that are relatively simple and will not require multiple contacts. This is true, particularly in the area of Tax Clearance cases, which should be handled quickly due to their high priority status. The * * * * * or the Public Contact Memo form FTB 6622 (PASS) should be completed for each contact.

You must get authorization from your supervisor before calling a taxpayer who is located outside of this country.

INITIAL CONTACT

The purpose of the audit must be established and communicated to the representative when the initial contact is made. See PASS for a listing of available initial contact templates.

When the auditor sends an initial contact letter or appointment letter, the auditor should enclose the California Franchise Tax Board Statement of Principles of Tax Administration and Mission & Values (form FTB 7899A) and the Notice of Audit (form FTB 1015). Other forms that may be given to the taxpayer are the Frequently Asked Questions About Your Tax Audit (form FTB 1015B) pamphlet, and the California Taxpayers' Bill of Rights (forms FTB 4058 and 4063) pamphlets.

The names and telephone numbers of the auditor's supervisor and manager must be given to the taxpayer early in the audit. The initial contact letter provides a practical means of distributing this information. Other alternatives are:

- List the names and telephone numbers on the letterhead of other early correspondence.

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- Add a "cc" section with the information on any early correspondence.
- The information can be included in paragraph form in any early correspondence.
- The auditor can hand out the supervisor's and manager's business cards.
- The supervisor and/or manager can attend the opening meeting.
- The information can be included on the audit plan.

Any of these are acceptable means of disseminating the information. The auditor is allowed to use discretion in terms of what works best for the particular circumstances of the audit.

For field audit cases, the initial contact is followed up with a letter, confirming the field appointment, the opening conference with the taxpayer's representative, and requesting records to conduct the audit. Single question Information Document Requests (IDRs) can be utilized by enclosing these initial IDRs with this letter, where appropriate.

See the Multistate Audit Technique Manual, **MATM 2710**, for examples of general items to request in the initial information document request.

CORRESPONDENCE NOT REQUIRING A REPLY

Occasionally, correspondence is received that will not require a written response. These are generally statements of information or comments of the taxpayer that should be filed in the corporate folder. Write "no reply necessary" on the turned-up lower right corner of the document prior to filing. If there is no corporation involved and information is not useful to any other areas of our department, keep the document for a short period of time, (in case of any further contact) then destroy it per departmental guidelines.

AMERICANS WITH DISABILITIES ACT - Requests for alternative formats

If you should receive a request from a taxpayer, or a taxpayer's representative, for an alternative format (e.g., large print, Braille, or videotape) please contact *****.

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5030 INFORMATION DOCUMENT REQUESTS

Purpose

The purpose of an Information Document Request (IDR) is to gather the relevant facts necessary to address the audit issues in a timely and efficient manner. Written requests provide a record of communication between the auditor and the taxpayer and avoid possible misunderstandings that could result from verbal discussions. All requests for information should be documented on an IDR and will use the single question format as the primary vehicle for requesting information. A Master IDR Log will be maintained to track all issued IDRs and to provide a clear focus for the status of IDRs. Copies of the Master IDR Log should also be shared with the taxpayer so all parties have a common understanding of the expectations.

Components of Information Document Requests

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- b. * * * * *
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Additional Information

Additional resources that can assist you with the preparation, followup, and management of IDRs are listed in Exhibit E.

a. Requests for information

- In most instances, requests for information should be in writing, and should only contain a single question per individual IDR. The IDR should specify the agreed date for the taxpayer to respond.
- The general format of the IDR is the single question as opposed to single issue IDR. This format assists the taxpayer if questions need to be distributed to different departments, provides for better organization in monitoring and following up on IDRs and provides for better organization of the audit workpapers. In the event that an IDR request is unanswered or incomplete, use of the single question format allows the auditor to send a follow-up request using the same IDR but modified to reflect the History Section. Separate IDRs make it easier to document the history of a request (i.e.,

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date of the original request, follow-up dates, extensions granted, etc.) in the event a penalty is assessed.

- Verbal requests for documents should be formally incorporated into a written IDR. Verbal requests that are completed while you are at the audit location may all be included in a single, completed-items IDR at the end of the field visit. Any verbal requests that are still outstanding at the end of the field visit should be transferred to single question IDRs and provided to the taxpayer with specific response dates.
- Information document requests should generally be numbered sequentially when they are provided to the taxpayer. They should retain the same number when they are reissued or followed up on (unless the nature of the information request has changed). Auditors may assign numbers differently in order to facilitate team audits, but it is imperative that the taxpayer understands the numbering system.
- If requested by the taxpayer, it is appropriate to discuss drafts of IDRs before they are formally issued.

b. Time Frames

- Normally response times to IDRs are a maximum of 30 days from the date of delivery. Requests for extensions of time should be based on the applicable facts and circumstances keeping in mind the benchmarks that must be reached in order to timely complete the audit. Dates to respond to an IDR should be reasonable, but it should be understood that responses must be timely in order to complete the case within the two-year expectation set forth in the Audit Regulation.
- The auditor should work with the taxpayer to arrive at a mutually agreeable date when a response is expected. Auditors are expected to adhere to comparable timeframes for reviewing taxpayer responses.
- 30-day contact - Reg. 19032(b)(5)(C)(1) provides that as a general rule the auditor should contact the taxpayer within 30 days of receiving a response to an IDR. At that time, the auditor should (1) issue additional IDRs; (2) issue an AIPS or position letter; or (3) notify the taxpayer that additional time is needed and provide them with a date for future contact. This is consistent with past audit practice. All taxpayer contact must be recorded in the Event Log.
- Telephone Contact - All telephone contact with taxpayers regarding extensions of IDR due dates, scheduling of field visits, or other matters affecting the progress of the audit, must be followed-up with a brief letter summarizing the auditor's discussion.

If the taxpayer requests an extended due date for an IDR via the telephone, the granting of the request should be treated as the second request for information. Granting of the

extension will be communicated to the taxpayer through the issuance of a follow-up IDR with the History section reflecting the extension granted. If information is not provided by the extension date, the next step in the process is the issuance of the Formal Demand.

- Reg. 19032(a)(6) states that the timeframes in the regulations are intended to provide an orderly audit process and cannot be used to limit the taxpayer's right to provide information. This does not mean that the taxpayer has an unlimited amount of time to provide requested information. However, if the taxpayer does provide information while the audit is still open, even if it is after the time period set in the IDRs, the information must be analyzed and applied to the audit findings.

c. Requesting Relevant Information

- Request for information must be explained to the taxpayer in terms of legitimate audit need. Discussion of the applicable laws, regulations, and department policies is also essential. Requests for information should always be discussed with the representative to find out exactly what corporate records will best satisfy audit verification objectives.
- When issuing IDRs, discuss the content with the taxpayer. Make sure that the taxpayer understands what is being requested, and discuss whether the information being requested will resolve the issue or whether alternative information should be provided. This may eliminate the need for additional IDRs on the same subject.

d. Tracking IDR Status

- All cases will contain a Master IDR Log which, at a minimum, identifies each IDR number, date issued, subject matter of information requested, expected response date from the taxpayer, actual response date and any applicable comments. In addition, re-issued IDRs will also be recorded in the Master IDR Log.
- The Master IDR Log is the focus document that provides all interested parties an immediate assessment of the status of all issued IDRs.

e. Timely Follow-Up

- The Audit Regulations require the initial IDR and one follow-up before the issuance of the Formal Demand. If cases are to be completed within established timeframes, seldom will it be beneficial or efficient to exceed this expectation.
- Tracking the status of IDRs is the responsibility of the Lead Auditor. Timely follow-up of unsatisfactory responses should be made according to the timeframe agreed with the taxpayer and included in the Audit Plan.

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- On the re-issuance of an IDR due to an incomplete response or no response, a History Section should be included on the bottom of the IDR. This section should indicate the original issue date, follow-up dates and other applicable information. At a glance, all parties should be able to understand the "track record" of the IDR and its status.
- If the requested information is not provided by the agreed date, the auditor should follow up by re-issuing the IDR with the History Section added. The follow-up IDR may be attached to PASS cover letter Forms FTB 1512 or 1522, if desired.

f. Formal Demand For Information

- When a taxpayer fails or refuses to furnish information in a timely fashion, a Formal Demand may be required. Audit Regulation §19032 provides for the issuance of the Formal Demand after the second IDR follow-up request for information. This is appropriate when a response to a request for information is unreasonably delayed, incomplete, refused or ignored. The auditor is expected to convey the consequences, in writing, to the taxpayer. The History Section on the IDR provides a written record of the attempts to obtain the information.
- Penalties for Failure to Furnish Information will be assessed if there is a reasonable need for the information requested given the relevant circumstances of the audit.
- PASS Forms 1512 and 4973 may be used as the formal notification process and modified to meet the specific case needs.
- See MAPM 8040 and 8050 for a full discussion of the steps necessary to assess the failure to furnish information penalty.

g. Audit Workpaper Requirements and Techniques

- The use of the "tickler" feature in PASS is a valuable tool. See PASS Help for additional information on how to use this effective method for reminders on needed follow-ups.
- For team audits, auditors will need to coordinate methods of generating IDRs, numbering and logging IDRs and presenting the history on unanswered IDRs.

h. Draft Correspondence vs. Separate Issue Folders

To provide for efficiency and effectiveness in issuing IDRs, auditors are given the option of using Draft Correspondence or a separate issue folder to prepare IDRs.

- If IDRs are issued from a separate issue folder, a separate issue folder called "IDRs and IDR Master Log" will be maintained. This folder will contain the Master IDR Log and a separate electronic copy of each issued IDR and follow-up. In addition, a hard copy will

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be maintained of each issued IDR. This method also allows the supervisor or Lead Auditor an opportunity to review and approve the IDR before it is finalized and issued to the taxpayer. This method may be preferable on a large case because it provides the ability to segregate IDRs from all other correspondence and thereby keep the files more manageable.

- If IDRs are issued from the Draft Correspondence file, a separate issue folder called "Master IDR Log" will be maintained that contains the Master IDR Log. Copies of the IDRs will, of course, be in the Sent Correspondence after issuance and hard copies are not required.
- Some auditors also keep a copy of the pertinent IDRs in the appropriate program item sections. Some have noted that this step may add additional time to complete the audit. We must bear in mind that others, such as reviewers, hearing officers and attorneys, will be using the audit file. The additional time may be more than offset by a better-organized file for these users.

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5050 FOLLOW-UP & KEEPING THE AUDIT CURRENT

When the requested information is not readily available, the auditor and representative should discuss a response timeframe. The auditor and representative should agree upon a specific date, generally within 30 days, but this should be determined on a case-by-case basis, as long as the audit is progressing to the scheduled completion date. Should the information not be provided by that date, the auditor should promptly follow up on the request. It is the auditor's responsibility to keep the audit process going and to prevent unnecessary delays requested by the representative. As a general rule, field audit activity is not delayed as a result of any of the following pending actions:

1. Court decisions on prior years,
2. Board of Equalization decisions on prior years,
3. Protest decisions on prior years,
4. IRS examinations of prior or current years,
5. IRS appeals.

If a representative cites one of the above reasons for delaying the audit, the auditor should explain that we do not delay audits for that reason. If the representative refuses to cooperate in commencing or continuing the audit, the auditor should consider the use of a formal demand for information, FTB 1513 (PASS). See **MAPM 8040** for a discussion of the penalty for failure to furnish information.

Failure to follow up on deadlines sends a message to the taxpayer that the auditor is not serious about the request and will possibly accept less than what was requested. It also establishes an unacceptable pattern that could impact the auditor's credibility and ultimate recommendations.

The auditor should keep the supervisor and/or lead auditor aware of the status of the audit when continual follow-ups are necessary. A verbal follow-up to the taxpayer, with written confirmation (letter or FAX), of the discussion is usually the most effective method for obtaining information and providing documentation for the audit file.

PASS TICKLERS

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There are two types of ticklers: Notification Ticklers and Document Ticklers. Both types can be set for following up on correspondence * * * * *

* * * * *

If the taxpayer does not reply by the tickler date, the auditor should send a follow-up letter or demand letter and attach a copy of the letter previously sent to the taxpayer.

See **PASS Help** for more information on setting ticklers.

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5055 Status Conferences

Purpose

The purpose of the status conference is to measure expectations against benchmarks and to expedite the audit process. The status conference should be used to keep the communication process between the taxpayer and the auditor open. Items to consider include:

Components of Status Conferences

- a. * * * * *
- b. * * * * *
- c. * * * * *
- d. * * * * *
- e. * * * * *
- f. * * * * *

Additional Information

Additional resources that will help you plan status conferences are listed in Exhibit D.

a. Frequency of the status conferences

It is a good audit practice to hold meetings periodically throughout the course of the audit. They may be held during the weeklong field audit appointments, or on a periodic basis (no less than bi-monthly). If it is critical that an issue be resolved immediately a separate meeting should be established.

b. Information Document Request (IDRs)

Although communication methods other than the status conference are used to follow-up on IDRs, the conference provides a good communication mechanism to assist in a smooth-flowing fact gathering process. During the status conference, the auditor should:

- Review outstanding IDRs and new requests. This can be accomplished by providing the taxpayer with a copy of the Master IDR Log.
- Time frames for IDRs should be reviewed for outstanding and new IDRs. If problems are occurring on meeting the time frames, solicit the taxpayer's cooperation in coming to a resolution of the problem.

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- Materiality - Any questions the taxpayer has regarding the materiality of an issue that is the subject of an IDR should be addressed.
- Follow-up requests on outstanding IDRs need to be communicated, with specific time frames for completion. The taxpayer should understand that non-compliance could lead to a failure to furnish penalty and a request for subpoenas.
- Any verbal discussion with taxpayer should be followed-up by a written confirmation of what was agreed to during the meeting.

c. Audit Issue Presentation Sheets (AIPS)

A review of outstanding and new AIPS can be accomplished by providing the taxpayer with a copy of the Master AIPS Log. Other aspects that can be addressed include:

- Discussing and trying to reach agreement on the facts related to the audit issue or describe what facts are still not agreed to, even if there is disagreement as to the application of the law.
- Discussing follow-up requests on outstanding AIPS, with specific expectations for completion. The auditor should inform the taxpayer of the benefits of providing their position to any proposed adjustments. Taxpayer-provided comments should be incorporated into a revised AIPS, if appropriate.
- Providing follow-up written confirmation of any agreements or understandings that resulted from the meeting.

d. Scheduling of Audit Appointments

Review any dates that were previously established and make any additions, deletions, or adjustments to keep the audit moving towards completion. If an appointment is needed at a location other than the corporate office of the taxpayer, the scheduling of such appointment should be directed through the taxpayer.

e. Resolution of Disputes Related to the Conduct of the Audit

Any disputes concerning the conduct of the audit should be addressed with the taxpayer immediately. If the dispute is not resolved between the auditor and the first line taxpayer representative, assistance at the next level should be requested. If the audit supervisor or next level manager of the taxpayer identified in the audit plan is unable to resolve the issue, the taxpayer has the alternative to request Program Manager or Bureau Director assistance to resolve the case. The auditor is also not limited in going to the taxpayer's next level or above to

resolve any disputes. All avenues of resolution should be explored in order to maintain the quality and integrity of the audit process.

f. Need for Authorization for Single Billing

If the taxpayer has filed on a separate return basis or failed to include various subsidiaries in a unitary combined return, and it appears that the audit will be recommending combination of such subsidiaries, you should discuss with the taxpayer the need to obtain a signed Authorization for Single Billing.

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5060 TAXPAYER FAILS TO RESPOND TO AN AUDIT

Auditors should first follow the formal demand for information procedures to obtain the audit information.

Also see **MAPM 8040** for the Failure to Furnish/File after Demand penalty.

ADMINISTRATIVE SUBPOENAS

An administrative subpoena may be necessary in some cases where the representative refuses to cooperate in furnishing information. A subpoena should be considered for significant issues where failure to furnish information is an issue. The designated program specialist in Technical Resource Section should be consulted by the supervisor or manager for guidance in these cases.

Audit staff should also identify cases where legal support may be necessary to determine and conduct any, necessary depositions to preserve testimony and/or discover such as subpoenas duces tecum, to preserve documentary evidence.

5065 AUDIT ISSUE PRESENTATION SHEETS (AIPS)

Purpose

The purpose of the Audit Issue Presentation Sheet (AIPS) is to communicate to the taxpayer and all other users the specific audit issue, the facts developed, the relevant law and the audit recommendation on the issue. The issuance of AIPS provides the opportunity to conclude and resolve issues on an ongoing basis. The AIPS is an important tool that keeps the taxpayer fully informed about the FTB's position on each issue. All audit adjustments should consistently be set forth in an AIPS format.

A Master AIPS Log will be maintained to track all AIPS and to provide a clear focus for all adjustments made. Copies of the Master AIPS Log may also be shared with the taxpayer.

Components of Audit Issue Presentation Sheets

- a. * * * * *
- b. * * * * *
- c. * * * * *
- d. * * * * *
- e. * * * * *
- f. * * * * *
- g. * * * * *
- h. * * * * *
- i. * * * * *
- j. * * * * *
- k. * * * * *

Additional Information

Additional resources to assist you in preparing and managing AIPS are listed in Exhibit F.

a. Draft correspondence vs. Separate Issue Folder - AIPS

To provide for efficiency and effectiveness in issuing AIPS, auditors are given the option of using Draft Correspondence or a separate issue folder when preparing and storing AIPS.

- If AIPS are issued from a separate issue folder, a folder called "AIPS and AIPS Master Log" will be maintained. This folder will contain the Master AIPS Log and a separate electronic copy of each issued AIPS and revisions. In addition, a hard copy will be maintained of each issued AIPS. This method allows the supervisor or Lead Auditor an

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opportunity to review and approve the AIPS before it is finalized and issued to the taxpayer. This method may be preferable on a large case because it provides the ability to segregate AIPS from all other correspondence and thereby keep the electronic file more manageable.

- If AIPS are issued from the Draft Correspondence file, the Master AIPS Log will be maintained in a PASS issue folder called "Master AIPS Log". Copies of issued AIPS will be in the Sent Correspondence Folder.
- Some auditors also keep a copy of the pertinent AIP in the appropriate program item section.

b. Tracking AIPS

The PASS Master AIPS Log is maintained to track the status of AIPS and should be used as a reference during status conferences with the taxpayer. The Master AIPS Log is created in PASS within the issue folder "Master AIPS Log" using the PASS Template FTB 9911a. This template may be modified to meet the auditor/case needs.

c. Numbering the Audit Issue Presentation Sheets

For ease of reference, AIPS should be numbered sequentially at the time they are issued. Auditors may assign numbers differently in order to facilitate team audits, but it is imperative that the taxpayer understands the numbering system so that they are not looking for "missing AIPS" which have not yet been issued.

For example, if team members will be checking out different pieces of the PASS file, AIPS numbers might be assigned to individual issues early in the case and completed as each issue is finished. If using this technique, all the assigned AIPS numbers should be listed in the AIPS log for recordkeeping purposes, and the Date Issued filled in when they are mailed to taxpayers.

Alternatively, each team member might find it easier to use his or her initials along with sequential numbering (e.g. ABC-1, ABC-2, DEF-1, DEF-2.) This methodology often helps the taxpayer identify which team member to respond to on the particular AIPS.

d. Preparing the Audit Issue Presentation Sheet

The PASS AIPS template FTB 1541A should be used when preparing the AIPS and can be modified to meet the specific case needs. Generally, a separate AIPS should be used for each issue with the following sections set forth:

- **Issue** - An introductory paragraph setting forth the issue and how the item was originally reported in the return helps the reader with a broad understanding prior to jumping into a list of facts.

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- **Amount of Proposed Adjustment, Year and Approximate Tax Effect** - The specific amount of the proposed adjustment should be set forth along with the approximate tax effect. Supporting schedules will also be provided for amounts reflected on the AIPS. This adjustment amount will be the source of the number directly transferred to the Principle Audit Schedules at the end of the audit. Since supporting schedules are provided with the AIPS, they need not be duplicated again when the Principle Audit Schedules are provided at the end of the audit.
- **Summary of Facts** - The statement of facts should be limited to information developed without analysis, commentary or conclusion. Workpaper references to documents and sources of statements should be included in the factual write-up and also provided to the taxpayer without redactions.
- **Application of the Law/Authority** - Relevant statutory, administrative and case law should be applied against the stated facts.
- **Conclusion** - Stated conclusions should be based on the relevant law and facts.

"Draft AIPS" can be used to communicate the facts developed on an issue at a specific point of time to the taxpayer with the understanding that the application of the law and conclusions will be forthcoming. For example, the taxpayer could be asked to confirm the accuracy of the listed unitary facts and whether any additional facts need to be considered. Application of the law and the auditor's conclusion would follow any submission of additional facts or corrections.

e. Taxpayer Response to AIPS

Upon the issuance of AIPS, the taxpayer will be given an opportunity to clarify facts and provide rebuttal arguments to the legal analysis and conclusions. Taxpayers should be encouraged to respond as this can result in the resolution of the issue at the lowest level and minimize time and costs for both the FTB and the taxpayer. At a minimum, attempts should be made to obtain the taxpayer's position with respect to the facts. On the last page of the AIPS, check-box options are provided for the taxpayer's response. The taxpayer can also respond in a separate letter if preferred. Additional items to consider include:

- The taxpayer is requested to provide agreement or disagreement with the facts, application of the law and the adjustment. The taxpayer should be encouraged to provide a response; however, there is a box on the AIPS that the taxpayer can check indicating that a decision is withheld.
- Advise the taxpayer that agreement to the facts and/or interpretation of law does not preclude protest or other administrative rights (the template also contains this statement).
- Taxpayer's responses need to be addressed either in a revised AIPS, subsequent correspondence, or in the position letter as opposed to simply including them in the audit package.

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Response times will vary depending upon the difficulty of the issue and the amount of discussion between the auditor and the taxpayer in advance of issuing the AIPS. Generally, the Audit Regulations provide for a maximum of 30 days for a response to an AIPS. However, auditors may use discretion and consider complexity in allowing less or more time than 30 days as set forth in Audit Regulation §19032(a)(6)(A).

f. Revising Audit Issue Presentation Sheets

Once an AIPS has been issued and the taxpayer has a clear understanding of the proposed adjustment, the taxpayer might provide additional documentation and/or rebut the legal arguments presented in the AIPS. This may necessitate issuing a revised AIPS and providing a copy to the taxpayer for response. A revised AIPS should be issued when:

- Additional material facts are provided.
- A different section of the law is applicable other than the one(s) stated in the original AIPS.
- The adjustment amount is revised due to documentation provided or revised interpretation on the state of the law.

The revised AIPS should use the same numbering as the original AIPS with some indication that it is a later version. (For example, AIPS #14 becomes AIPS #14 (Revised XX/XX/XXXX)). The Master AIPS Log should reflect that a revised AIPS has been issued. Do not delete reference to any original AIPS that have been issued to the taxpayer. There should be a record of all copies that have been provided to the taxpayer.

If the auditor determines that a revised AIPS does not need to be issued in regards to a taxpayer's response, the taxpayer's responses need to be addressed either in subsequent correspondence, or the closing letter as opposed to simply including them in the audit package.

g. Withdrawing Audit Issue Presentation Sheets

While every effort is made to make a correct determination before the issuance of an AIPS, there are times when an AIPS will need to be withdrawn. In some cases, the taxpayer might provide additional information after being provided with the AIPS. If the taxpayer fully supports a position, the AIPS should be formally withdrawn. This process can be done by using the original AIPS, adding a section at the beginning of the document that provides a brief explanation of the reason for the withdrawal and providing a copy to the taxpayer. The withdrawn AIPS would also retain the same number as the original AIPS. A copy of the withdrawn AIPS should be provided to the taxpayer. In addition, the Master AIPS Log should be updated to reflect that the AIPS has been withdrawn.

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h. Issuing AIPS on No-change Issues

The purpose of the AIPS is to communicate with the taxpayer and other users issues that are being adjusted. In order to maintain a focused file that maximizes benefit to other end-users, AIPS will be limited to communicating only adjusted items. (withdrawn AIPS would, of course, remain part of the AIPS file). However, we should notify the taxpayer of issues for which we have requested information but are not making an adjustment.

i. AIPS and the Principle Audit Schedules

The AIPS provide the sole basis for the construction of the Principle Audit Schedules. Therefore, the adjustment amounts in the AIPS should reconcile with the numbers in the Principle Audit Schedules. References within the Principle Audit Schedules only need refer the user to the specific AIPS number.

j. AIPS and the Position Letter

At the close of the audit, any new AIPS not previously provided to the taxpayer should be included with the position letter. If the taxpayer requests another complete set of all the issued AIPS, they should be provided. Otherwise, the AIPS provided throughout the audit process are sufficient and reference can be made to them. In addition, a copy of the Master AIPS Log should be given to the taxpayer to assist in confirming the accountability of all AIPS issued.

k. AIPS and the Audit Narrative

The AIPS should be attached to the Audit Narrative as Exhibits with the position letter. The Explanation of Adjustments section of the narrative can then be substantially shortened.

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5070 CONCLUDING THE AUDIT WITH THE TAXPAYER

Prior to making an audit proposal, the results of the audit should be discussed with the representative. This discussion is in terms of tentative proposals based on the information obtained. If there is disagreement, the basis for positions can be informally discussed and the need for additional information determined. The representative should be given the opportunity to submit all facts in support of their position. This information should be evaluated before an audit proposal is made. The representative should be made aware of all possible audit adjustments prior to submitting the final schedules. The auditor should issue an Audit Issue Presentation Sheet (AIPS) during the audit for each material adjusted issue, as soon as each issue is completed, as opposed to waiting until the end of the audit.

IMPORTANT: It is essential that the auditor and representative agree on the facts regarding the audit issues, even if the taxpayer does not agree with the auditor's conclusion or adjustment. See **MAPM 6040**, Narrative Report "Statement of Representative" for a complete explanation of this requirement.

DISCUSSION OF PROPOSALS

When final schedules are submitted to the representative, the auditor should discuss the proposed adjustments with the representative and, when possible, reach an agreement. An informal conference can be held with the representative and audit supervisor on any dispute that the auditor believes might be resolved without requiring the filing of a formal protest.

In the event the auditor's schedules are changed, either by the supervisor or at the review level, the auditor must notify the representative of the revision and provide revised schedules to the taxpayer. This will reconcile the audit adjustments to the NPA.

A discussion with the representative may prevent the return of the file for additional information after a protest is received. Cases may be returned to the field office to determine the validity of the protest, particularly if there is information that was not obtained or made available during the audit.

If the representative does not agree with the proposed adjustments, the protest procedures should be explained. Ideally, the representative will provide the auditor a position statement identifying the basis for their disagreement. Protests received in the field should be forwarded to Sacramento Office, Protest Control Desk, immediately. The auditor should call the Protest Control Desk to notify them that the protest is being forwarded. (See **MAPM 11000** for more information on protests.) Agreement or disagreement should be noted on the FTB 6430, Audit Report and FTB 6431, Narrative Report.

Prior to writing a position letter, the following steps are recommended:

1. Define the Problem or Issue

The first step in writing a position letter or answering correspondence is to define the problem or issue. In many instances there is only one problem, even though the taxpayer has raised several questions.

2. Determine the Essential Facts

After the problem has been defined, determine the essential facts that should be given to the inquirer. Be cautious not to include issues that are unrelated to the problem at hand.

3. Organize the Facts

Sort the essential facts into a logical sequence. Usually it is best to get to the heart of the problem in the first paragraph, rather than stating our position or affirming our previous action. In the latter instances, the taxpayer may only skim the rest of the letter and not pay any attention to our explanation.

4. Preparing the Letter

Letters should be concise, clear, tactful, complete, and to the point. Use complete sentences. Abbreviations should not be used unless they are previously identified such as: "California Revenue and Taxation Code (CR&TC)." Also, remember to update the address information in the PASS address book, as well as BETS, when you receive more current information from the taxpayer.

Note: The auditor should also request written confirmation from the taxpayer of where the notice should be mailed. This address may differ from the "primary" address in BETS. (****)

WRITTEN EXPLANATION OF ADJUSTMENTS/POSITION LETTER

After the auditor has gathered all the facts, organized the facts in a logical order, researched the law governing the issue, and made a determination, a letter presenting the auditor's findings should be mailed/ issued to the taxpayer (Explanation of Adjustments). In order to avoid redundancy, the auditor may prepare a letter and attach copies of the AIPS as enclosures, when appropriate. The letter should:

- Clearly identify the issue
- Outline all the information reviewed (facts)
- State the governing law

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- State the auditor's determination (conclusions) based on the facts and the governing law (analysis)
- Provide schedules showing the computation of the adjustments (see **MAPM 6020**).
- State the audit determination is subject to review
- Allow the taxpayer to rebut, clarify and/or present additional facts
- Provide the taxpayer with the option to pay the additional tax in order to stop the accrual of interest.

Even if the taxpayer does not agree with the auditor's findings, the auditor should at least try to get the taxpayer to agree on the facts.

The auditor should make a reference to the position letter in the Audit Issue Section in addition to clearly stating the final recommendation for such a case. A copy of the position letter should become a part of the official file for each case.

A closing similar to the one that follows should be used:

This is your opportunity to provide any additional information that you wish to be considered in regards to the proposed adjustments. If you disagree with these adjustments, provide us with specific reasons why you disagree. Include appropriate substantiation, citation of applicable law and any case authority. Additional information submitted by (the auditor fills in a specific date XX/XX/XX) will be reviewed. We suggest that you do not amend the return(s) under examination, as that will only delay the completion of this audit.

Please reply by (the auditor fills in a specific date XX/XX/XX). To ensure proper handling, please attach a copy of this letter to the front of your reply. Mail your reply to:

Franchise Tax Board
ATTN: 347:HW:XXX (xxx=auditor's initials)
PO Box 1468
Sacramento, CA 95812-1468

If you have any questions or concerns please contact me at the telephone number listed below.

PASS paragraphs contain a similar closing paragraph titled "P25560 – Closing." To insert PASS paragraphs into correspondence, see **PASS Help** for "using PASS paragraphs."

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5080 POSITION LETTER

Purpose

The purpose of the position letter is to notify the taxpayer that the fieldwork on the audit is complete and provide the taxpayer or representative with the results of the audit. The position letter should include all AIPS not previously provided and the Principle Audit Schedules. The position letter should be issued in advance of the closing conference, when possible, in order to give the taxpayer an opportunity to prepare for the closing conference.

Components of Audit Issue Presentation Sheets

- a. * * * * *
- b. * * * * *
- c. * * * * *
- d. * * * * *
- e. * * * * *

Additional Information

Additional resources to assist you in preparing the position letter are listed in Exhibit H.

a. Items To Be Addressed In The Position Letter

The position letter should summarize the Audit Issue Presentation Sheets (AIPS) that have previously been provided to the taxpayer and those that are enclosed in the final report. It should tie the adjustments to the attached Principle Audit Schedules.

It should include an explanation of any adjustments for which no AIPS have been issued, such as adjustments that result from other audit adjustments or Computations. Examples include the alternative minimum tax, limitations on tax credits, and NOL carryover.

If applicable, the position letter should explain any administrative items, such as identification of suspended corporations, explanation of the application of pending payments, proposed actions on outstanding claims, etc. It should also include an offer to the taxpayer to pay the proposed assessments to avoid accruing additional interest on additional tax due.

The position letter should state that the audit is subject to review both by the auditor's supervisor and by Technical Resource Section (TRS). The review might disclose the need for more documentation, or changes to the auditor's recommendations. If the supervisor or

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reviewer requires changes to the auditor's report, the auditor will notify the representative of the revisions. The timeframes for closing the case and issuing any notices should be included.

When the taxpayer and representative disagree with audit's recommendations, the taxpayer and representative should be informed of the protest, appeal, and settlement process in the position letter.

Request for Authorization for Single Billing - If taxpayer has filed on a separate return basis or failed to include various subsidiaries in a unitary combined return, and the audit has recommended combination of such subsidiaries, the taxpayer should be asked to complete and sign an Authorization for Single Billing if a single billing is needed or requested by the taxpayer.

The auditor should also request written confirmation from the taxpayer of where the notice should be mailed.

b. Items To Be Included With The Position Letter

Documents, schedules, and any other information needed to explain the audit adjustments should be provided to the taxpayer throughout the course of the audit with the AIPS. Various documents and information that provides the taxpayer with a reference for reviewing the final audit schedules or completed case results should be provided to the taxpayer with the position letter. These documents may also assist the taxpayer in making changes to subsequent period returns, with post-audit activities including payment of additional taxes, protest action and preparation for potential, subsequent audits. The following is a list of items that can be provided to the taxpayer with the position letter if not previously provided.

- Principle Audit Schedules and supporting Audit Schedules.
- Tax effect by issue.
- Master AIPS Log.
- Copies of any newly issued AIPS, revised AIPS, and, if requested, previously issued AIPS.
- Copy of any work papers, reconciliations of as-reported amounts to revised amounts, or any other information the taxpayer will need to understand the proposed adjustments

c. Taxpayer Response Time To Position Letter

The taxpayer should be provided with a reasonable amount of time to respond to the position letter. Response time may be coordinated with the scheduling of the closing conference, if appropriate. The amount of time will vary with the complexity of the audit and the number of newly issued AIPS included with the position letter. With AIPS issued throughout the audit, the taxpayer should already have had an opportunity to address each issue individually. The

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auditor should work with the taxpayer to agree on an appropriate amount of time for the taxpayer to respond. The following are general guidelines for response times to a position letter that should be included in the audit plan and discussed during the opening conference:

The Audit Regulation initially sets a response time at a maximum of thirty (30) days. If a significant number of AIPS are included with the position letter, this timeframe could be extended to include a 30-day response timeframe on the AIPS and an additional 30-day response time for the position letter.

Extensions may be allowed if the taxpayer requires additional time, however, the overall goal is still to complete the case within the prescribed timeframes.

It is important that the case be closed and submitted for TRS review with at least 4 months remaining on the statute of limitations. This may cause a need to shorten the general response time or request a short-term extension of the statute of limitations. If a taxpayer requests an extension to reply to the position letter, the auditor's agreement may be predicated on receiving the signed waiver.

d. Responses by Taxpayer

- **Written Response Provided** - If the taxpayer provides a written response, the auditor should acknowledge receipt of the response in writing and address the points raised in the response.
- **Additional Information or Documentation Provided** - If additional information or documentation is provided with the response, the auditor should analyze the information to determine if it has an effect on the previously issued AIPS or on any proposed audit adjustments. If it does have an effect, a revised AIPS and audit schedules should be issued. If it does not have an effect, the taxpayer should receive a response indicating that we have considered the information, but that no change is being made to our determination.
- **If the taxpayer's response or the additional information or documentation mandate an adjustment to an AIPS or revision to the Principle Audit Schedules**, revised AIPS and schedules should be sent to the taxpayer. The individual circumstances will determine whether the taxpayer should then be given additional time to review the revised AIPS and audit schedules.
- **Verbal Responses at Closing Conference** - If the taxpayer provides a verbal response at the closing conference, the auditor should summarize the response and provide a written copy to the taxpayer for verification.

- No Written Response Received From Taxpayer - If the taxpayer does not provide a written response to the closing letter, the auditor should note in the audit narrative their understanding of the taxpayer's position on each of the audit issues.

e. Position Letter As Exhibit to Narrative

Attaching the closing letter, the taxpayer's position letter and subsequent letters of rebuttal as exhibits to the Audit Narrative may substantially shorten the Audit Narrative. The effectiveness of this technique will depend on the complexity of the case and the number of closing letters and rebuttals.

NOTE: ((* *)) = Indicates confidential and/or proprietary information that has been deleted.

Reviewed: January 2006

5090 CLOSING CONFERENCE

Purpose

A closing conference should be held to discuss any items not already covered in the Status Conferences and to review the final audit results. It should include an explanation of the review process and the process for issuing any applicable notices, and rough timeframes so that the taxpayer has an idea of when they should receive any notices. An explanation of how the taxpayer will be notified of any changes during the review process should also be covered. A closing conference should be held on all large cases, cases where the taxpayer requests one or on any other case where the auditor finds it to be an effective communication tool with the taxpayer.

This is also an excellent opportunity to obtain feedback on what worked well in the audit process and for obtaining suggestions from the taxpayer on things that could be improved.

Components of the Closing Conference

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Additional Information

Additional information regarding for planning and conducting a closing conference are listed in Exhibit G.

a. Planning the Closing Conference

- **Timing the Conference** - The timing of the closing conference might vary with the type of audit conducted. A meeting can be held with the taxpayer on the last day of the fieldwork, explaining that a closing letter with audit schedules is to be provided. Alternatively, the closing conference might be conducted at a later date after the taxpayer has had time to review the audit closing letter and audit schedules.
- **Position Letter** - A position letter should be issued to advise the taxpayer that the fieldwork on the audit is complete. The position letter should be issued in advance of the closing conference when possible, in order to give the taxpayer an opportunity to prepare for the closing conference.

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- **Audit Issue Presentation Sheets (AIPS)** - Notification of the resolution of audit issues should be made during the course of the audit through the use of AIPS issued at the time the analysis related to each issue has been completed. Copies of the AIPS can be provided as attachments to the closing letter if requested by the taxpayer in preparation for the closing conference. At a minimum, you should plan on discussing any AIPS that the taxpayer has not yet responded to.
- **Preliminary Principle Audit Schedules** - Preliminary Principle Audit Schedules that incorporate all of the proposed audit adjustments should be prepared and sent to the taxpayer for review before the closing conference, if possible. Preliminary audit schedules are subject to changes and corrections.

b. Agenda for Closing Conference

The auditor should prepare an agenda for the closing conference with input from the taxpayer and provide copies to each person in attendance. The items below are suggested topics for the closing conference.

- **General explanation of proposed adjustments** - The taxpayer should already have a good understanding of the proposed adjustments as communicated through the AIPS and the closing letter. This conference provides an opportunity to clarify any remaining issues the taxpayer might have. If the taxpayer has not responded to the AIPS, the importance of having at least an agreement or disagreement as to the audit's facts and conclusions should be discussed.
- **Flow of Proposed Adjustments** - The auditor should review the audit schedules to ensure that the taxpayer understands how the adjustments flow through the schedules.
- **Notices** - Explain what the taxpayer can expect in the form of notices. This is a good time to discuss an Authorization for Single Notice if appropriate.
- **Handling new information that the taxpayer wants to provide** - If the taxpayer makes a request to provide additional information or documentation at this time, address how this information will be incorporated into the audit package and how any resulting changes will be handled.
- **Review Process** - Explain the review process by the audit supervisor and by the Technical Resource Section (TRS). Provide estimates of the dates when the audit will be submitted for review to the audit supervisor, forwarded to TRS for review and when issuance of notices can be expected. (The Audit Regulations provide a guideline that any notices should be issued with 90 days of the closing of the case and submission to TRS.)
- **Protest, Appeal, and Settlement** - If not already included in the closing letter, provide an explanation of the taxpayer's protest, appeal, and settlement rights. (See MAPM 6070).
- **Status of Federal Audits** - Update any developments on the status of federal audits and the issuance of any subsequent Revenue Agent Reports.

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- **Subsequent Audit Cycles** - Discuss subsequent audit cycles that might be pending. Inform the taxpayer if you know that another office will be doing the audit. If appropriate, discuss the estimated start date of the next cycle.
- **Other** - Seek input from the taxpayer on the audit process. Discuss what worked well and what improvements could be made. Provide the taxpayer an opportunity to discuss any items he/she might have.
- **Address** – Obtain confirmation from the taxpayer of where notices should be sent. This address may differ from the "primary" address in BETS. * * *

c. Goals of the Closing Conference

The auditor should be able to determine the following by the end of the closing conference:

- Whether the taxpayer agrees or disagrees with each of the AIPS and Principle Audit Schedules.
- Whether a formal protest will be filed. If so, attempt to obtain, and document, a full understanding of the taxpayer's position or request that the taxpayer provide the position prior to submitting the case for review.
- Whether the taxpayer will need additional time to review the audit findings or audit schedules. Agreement should be reached between audit and the taxpayer as to the amount of additional time the taxpayer needs and has for review. Extensions should be considered consistent with the timing requirements of Audit Regulation 19032.
- Whether a waiver is needed in order to provide the taxpayer with additional time for review. If the taxpayer intends to submit additional information and/or documentation following the closing conference, the auditor should advise the taxpayer that a statute of limitations waiver might be necessary to review any supplemental information.
- That the taxpayer understands what the process will be for communicating any changes made to the audit adjustments during the review process.

d. Who Should Attend the Closing Conference

- Whenever possible, the audit supervisor should attend with the auditor/audit team. The audit supervisor may want to introduce the lead auditor for the next audit cycle during the closing conference.
- Through the course of the audit, the auditor will have learned the names of the taxpayer's staff that is involved with the audit process. At a minimum, the auditor should request that the person who primarily handled the audit (e.g. tax manager, tax director, CFO) should attend along with his or her direct superior.

e. Documenting the Closing Conference

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A summary of the closing conference should be put in writing for the audit file and a copy should be mailed to the taxpayer.

f. Letter To Taxpayer When Case Is Sent To Technical Resource Services

In some cases, it might be appropriate to provide the taxpayer with additional notification about the handling of the case. If it has taken some time to compile the audit case and/or for supervisor review due to workload constraints, you might want to notify the taxpayer when the case leaves the local office.

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