



State of California  
Franchise Tax Board

# Audit / Protest / Appeals

(The process)

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### Mission of the Franchise Tax Board

Our mission is to provide the services and information to help taxpayers file accurate and timely tax returns and pay the proper amount owed. To accomplish this mission, we develop knowledgeable and engaged employees, administer and enforce the law with fairness and integrity, and responsibly manage the resources allocated to us.

### Statement of Principles of Tax Administration

The primary function of Franchise Tax Board is to administer the Revenue and Taxation Code. Tax policy for raising revenue is determined by elected officials.

It is our duty to correctly apply the laws enacted by the Legislature; to determine the reasonable meaning of various Code provisions, and to perform in a fair and impartial manner.

Interpretation of the Code is the heart of administration. It is the responsibility of each person in the Franchise Tax Board, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when the true meaning of the statute is ascertained and applied.

We must also apply the law in a reasonable and practical manner. Issues are raised when they have merit, and are never raised arbitrarily or for trading purposes. Employees are encouraged to raise meritorious issues. We also exercise care not to raise an issue or to ask a court to adopt a position inconsistent with an established Franchise Tax Board position.

We believe in treating our taxpayers with courtesy and considerateness. As such, administration should be reasonable, vigorous, and timely. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

## Introduction

We use a self-assessed tax system where it is your responsibility to accurately compute and report your tax liability on your tax return. Under the authority of the California Revenue and Taxation Code (R&TC), the Franchise Tax Board (FTB) developed audit programs to effectively and efficiently verify the correct tax amount owed to the state of California. Our goal is to complete an audit within two years of our initial contact with you, four years from the date you filed your tax return, or within a reasonable period as guided by audit circumstances.

### Audit Objectives

We strive to effectively and efficiently determine the correct tax amount based on an analysis of relevant tax statutes, regulations, and case law as applied to your facts. The procedures and techniques we use to timely complete an audit depend on the case circumstances.

We can carry out our audit objectives and complete the audit more quickly with your cooperation, effective communication, and agreement.

### Audit Process

- › Identify tax issues.
- › Gather, evaluate, and document information.
- › Determine the correct tax amount under the law.

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Each audit follows standards and resource considerations for:

**Legality** - Ensure audit activities and conclusions agree with established laws and legal interpretations.

**Objectivity** - Examine all relevant, available facts fairly, and without bias.

**Timeliness** - Conduct and complete audits with a minimum of inconvenience to taxpayers.

**Supportability** - Adequately support recommendations with facts and law.

## **Our Auditor's Standard of Excellence**

- › Correctly apply and administer the tax laws.
- › Conduct audits:
  - › Within the limits of the law.
  - › With sound administration, minimal delay, courtesy, and respect.
  - › With minimal burden and cost.

## **Before the Audit**

When we receive your tax return, we must determine whether we should accept your tax return as filed, or start an audit. In order to make this decision, our auditors review the following items:

- › Federal and state tax returns.
- › Prior audit history.
- › Income exclusions and deductions.
- › Public information.
- › Internal Revenue Service data.

## Audit Procedures

### Desk or Field Audit

We may conduct desk or field audits. Most often, we perform a desk audit through written letters and secure emails. In contrast, a field audit takes place at your residence, place of business, or another location that facilitates the examination of your tax documents. The auditor reviews the complexity of your tax return and chooses the most effective and efficient manner to conduct the audit. In general, we perform a desk audit for audits involving simple tax issues which require few supporting documents. Complex tax transactions and large corporation tax returns typically require field audits.

### Field Audit Location

A field audit generally takes place at the location of the original books, records, and source documents. In the case of a sole proprietorship or business entity, this location is usually your place of business. We can conduct field audits at an FTB office, or your representative's office, if you do not have the appropriate work area or time available at your location.

### Designated Representative

You have the right to have someone represent you during the audit. (for example, a certified public accountant, enrolled agent, tax attorney, etc.). To designate a representative, complete FTB 3520, *Power of Attorney Declaration for the Franchise Tax Board* and provide it to the auditor. Go to [ftb.ca.gov](http://ftb.ca.gov) and search for **Power of Attorney** for specific instructions on how to complete and file this declaration.

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### **Initial Contact Letter**

- › Explains that we selected your tax return for audit.
- › Identifies the issues under examination.
- › Provides the names and telephone numbers of the auditor and supervisor.
- › Requests the name and contact information from you or your designated tax representative.

For field audits, the initial contact letter also asks you to provide information to schedule an audit appointment. When appropriate, the auditor may also request information or documents with the initial contact letter.

### **Audit Appointments**

The auditor works with you to schedule convenient times and locations for your audit appointments. Throughout the audit, the auditor reviews deadlines with you and makes adjustments to keep the audit moving towards timely completion.

### **Audit Plan**

This plan establishes open lines of communication to promote understanding of commitments made and agreements reached.

We strive to:

- › Provide a road map of how the audit begins, progresses, and ends.
- › Identify key potential audit issues.
- › Make the audit less burdensome, less costly, and less intrusive.

We encourage your participation and input during the development of the audit plan, which may reduce your concern about what to expect during the audit.

Your participation contributes to:

- › Efficiently managing fact gathering and issue analysis.
- › Solving problems timely and awareness of deadlines.
- › Providing alternative solutions to issues, such as offering different supporting documents.

## Opening Conference

The auditor may choose to hold an opening conference or you may request one.

This conference sets the groundwork necessary to conduct an effective and efficient audit. It establishes lines of communication, and helps build a partnership between you and the auditor. During the opening conference, the auditor will:

- › Introduce the audit participants.
- › Agree on a general audit plan.
- › Discuss audit processes and procedures.
- › Agree upon expected time frames.
- › Start developing a rapport with the individuals working on the audit.

The auditor's supervisor may attend as needed or at your request.

## Information Document Requests

Information Document Requests (IDRs) serve to gather the facts and documents necessary to understand and verify the items you reported on your tax return.

These written requests provide a record of communication between you or your representative and the auditor, and avoid possible misunderstandings that could result from verbal discussions. The auditor should make sure that you or your representative:

- › Understand our requests.
- › Provide the necessary information to substantiate the items you reported on your tax return.



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Failure to respond to the IDR does not relieve you of your responsibility to substantiate the items reported on your tax return. When the requested information is not readily available, you or your representative should discuss a reasonable time frame for a response with the auditor.

The auditor maintains and updates a master IDR log and provides a copy to you upon your request.

## **Audit Issue Presentation Sheet**

An Audit Issue Presentation Sheet (AIPS) details adjustments we propose to make to your reported tax. An AIPS includes a discussion of the facts, the relevant law, and the proposed adjustment. When examining several issues, the auditor may choose to prepare and distribute an AIPS for each individual issue upon completion of the examination of that particular issue. As such, you may receive several AIPS documents at various points throughout the audit process.

The auditor maintains and updates a master AIPS log, and provides you a copy.

## **Status Conference**

If needed, we hold status conferences to:

- › Review the audit plan.
- › Discuss how the audit is progressing.
- › Efficiently manage the fact and information gathering.
- › Work together to solve problems timely.

## **Closing Conference**

We hold a closing conference to:

- › Discuss any items not already covered in status conferences.
- › Review the final audit results.
- › Outline the technical review process.



- › Explain how we notify you of any changes made during the review process and how we issue notices.
- › Provide rough estimates of time frames.

Depending on the complexity of the audit, the auditor may choose to hold the closing conference in person, by telephone, or by letter.

### **Resolution of Disputes**

At any time during the audit process, you can contact the auditor's supervisor or manager to express your disagreement with any proposed tax changes and to work toward a resolution. We provide the names and telephone numbers of the audit supervisor and manager in our initial contact letter.

### **End of the Audit**

At the end of your audit, we provide you with the results in writing. We issue one or more of the following, as applicable:

- › A *No Change* letter that states we accepted your tax return as filed and you do not owe additional tax.
- › A *Notice of Proposed Assessment* that shows the additional tax we believe you owe.
- › A *Notice of Overassessment or a Notice of Proposed Overassessment* that shows the refund we owe you.
- › A *Notice of Proposed Adjusted Carryover Amount* that shows how we reduced a carryover item which did not result in any additional tax for the tax year we examined.

If you do not agree with our proposed adjustments, you may be able to file a protest or appeal. The auditor informs you of your protest or appeal rights, as applicable, either in a closing letter or during the closing conference. Written information about your protest or appeal rights will also accompany the audit notice, when applicable.



## After the Audit

If you receive a *Notice of Proposed Assessment* and agree with the proposed change to your tax as a result of the audit, there are various payment options available. Our free online Web Pay allows you to authorize payment from your bank account. For more information, go to **ftb.ca.gov** and search for **payment options**. For a fee, you can pay using major credit cards. Call 800 2PAY TAX (800.272.9829) or go to **officialpayments.com**.

We will update your account to reflect the audit changes. Do not submit Form 540X, *Amended Individual Income Tax Return*, or 100X, *Amended Corporation Franchise or Income Tax Return*.

### Interest Charges

Interest continues to accrue from the date of the *Notice of Proposed Assessment* to the date we receive your full payment. However, we will not charge any additional interest if we receive your payment in full within 15 days of the date on the notice. You do not lose your right to protest the proposed audit adjustments if you make a payment.

Filing a protest or appeal without making payment of the additional tax will not stop the accrual of interest. Due to workload constraints, it may take several months to resolve your protest and the accrual of interest will not stop during this protest period. The only way to avoid additional interest charges is to make a tax deposit or pay the liability in full within 15 days of the date on the notice. If we withdraw or reduce the amounts on our notice following your protest or appeal, we will pay interest on the tax deposit or on any overpaid amount as the law allows.

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## Notice of Proposed Assessment Protest Process

If you disagree with our proposed assessment, you can file a written protest with us by the **protest by** date shown on the front of the accompanying notice. If your protest is not postmarked or faxed by this date, the assessment will become final and we will bill you for the amount due, including penalties and interest.

### Your Protest Letter

Your written protest must clearly state what you are protesting and must be postmarked or faxed by the **protest by** date shown on the front of the accompanying notice.

Include the following:

- › Your name and address.
- › Your social security, taxpayer identification number, or business entity number.
- › The amounts and taxable years you are protesting.
- › A statement of facts.
- › Your explanation of why you believe our assessment is wrong.
- › Evidence/documentation that substantiates your position.
- › Your signature or your authorized representative's signature.
- › Your daytime telephone number or your authorized representative's name, daytime telephone number, and mailing address.
- › A copy of the *Notice of Proposed Assessment* we sent you.
- › A completed FTB 3520, *Power of Attorney Declaration for the Franchise Tax Board*, if you want someone to represent you during the protest process. Go to **ftb.ca.gov** and search for **power of attorney** for specific instructions on how to complete and file this declaration.

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Mail your protest to:

PROTEST SECTION MS F340  
FRANCHISE TAX BOARD  
PO BOX 1286  
RANCHO CORDOVA CA 95741-1286

**To expedite your protest**, fax it to 916.364.2754.

### **The Protest Process**

The protest process is informal. It is the first step in the administrative and judicial review process where you can dispute proposed audit adjustments. It provides an opportunity for you to discuss your concerns with an FTB staff member assigned to resolve your protest, known as a hearing officer, and provide any additional documents or information to substantiate your position. The hearing officer reviews your position and evidence to ensure that the changes made during the audit were correct and in compliance with the law.

After we receive your protest letter, we will mail you a letter to confirm we received your protest and we will take action as soon as possible.

The hearing officer determines the correct amount of tax based on the evidence that you submit and the law. The protest process does not include negotiating a revised tax amount. A separate settlement process allows for negotiating tax. Get FTB Notice 2007-2, at [ftb.ca.gov](http://ftb.ca.gov) for more information on FTB's settlement process.

We will hold a protest hearing if you request one in your protest letter. You or your authorized representative may attend the oral hearing to present your position on the audit issues and provide additional documentation or supporting tax law. We generally conduct hearings at an FTB field office nearest to you, and we work with you to schedule the hearing at a mutually convenient date and time. Hearings may also be conducted by telephone or video conference.

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After we consider your protest and make a final decision, we will send you a *Notice of Action* (NOA) that documents our findings.

If you agree with the change to your tax as shown on the NOA, there are various payment options available. Our free online Web Pay allows you to authorize payment from your bank account. For more information, go to [ftb.ca.gov](http://ftb.ca.gov) and search for **payment options**. For a fee, you can pay using major credit cards. Call 800 2PAY TAX (800.272.9829) or go to [officialpayments.com](http://officialpayments.com)

If you disagree, you may appeal to the Office of Tax Appeals (OTA) within 30 days of the date the NOA was mailed to you.

## Office of Tax Appeals Appeal Process

Office of Tax Appeals is a separate government agency that handles all personal and business entity income tax appeals. For more information on how to file an appeal, go to [ota.ca.gov](http://ota.ca.gov).

When you file an appeal within 30 days of the date of the NOA, you are given an opportunity to provide additional supporting information and file a brief in support of your position. FTB is given the same opportunity, asking OTA to sustain its position. You may also request a hearing before OTA.

Following OTA's consideration of the law and facts in your appeal, it will issue a decision in writing and either you or FTB may request a rehearing within 30 days of the decision. A rehearing is an opportunity for OTA to hear the appeal for a second time if there were mistakes of law or errors made in the original appeal or if new evidence has been discovered. If no rehearing request is made, OTA's decision becomes final in 30 days.

You may also file an appeal if you have filed a claim for refund and we have not acted on your claim within six months. The law does not specify a time limit for filing an appeal following FTB's failure to act on your claim for refund. However, if FTB denies your claim in writing before you file such an appeal, the 90-day period would then apply. The 90-day period would start from the date of the denial notice.

If you miss the due date for filing an appeal of a tax assessment, your only recourse would be to pay the amount due and file a claim for refund with FTB.

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### **Superior Court Action**

If you do not agree with OTA's decision and the tax liability remains unpaid, you can pay the tax liability and file a claim for refund. If FTB denies your claim, you can file an action against FTB in California Superior Court within 90 days.

After the California Superior Court makes a decision, either you or FTB may file an appeal of the decision to the California Court of Appeal.

### **Taxpayers' Rights Advocate**

The Taxpayers' Rights Advocate's Office is available to provide an independent review of your unresolved tax problems. We strive to ensure that your problems are handled promptly and fairly and that you have the highest confidence in the integrity, efficiency, and fairness of our state tax system.

### **Your Rights as a California Taxpayer**

You have rights as a taxpayer when working with us.

The following publications explain your rights. To view or download these publications, go to [ftb.ca.gov](http://ftb.ca.gov) and search for **FTB 4058** and **FTB 4058C**.

#### ***FTB 4058 - California Taxpayers' Bill of Rights Information for Taxpayers***

This publication provides a basic overview of your rights and includes the major provisions of the 1988, 1997, and 1999 California legislation.

#### ***FTB 4058C - California Taxpayers' Bill of Rights – An Overview***

This publication describes the R&TC provisions of your rights.

- › If you have not been able to resolve a problem during prior contacts with us, or you are suffering a hardship as a result of our action, you can contact Executive and Advocate Services by:

Website: **ftb.ca.gov**

Telephone: 800.883.5910

Fax: 916.843.6022

Mail: EXECUTIVE AND ADVOCATE SERVICES MS A381  
FRANCHISE TAX BOARD  
PO BOX 157  
RANCHO CORDOVA CA 95741-0157

- › If you have comments about how we can provide better service to the taxpayers of California, go to **ftb.ca.gov** and search for **advocate**.

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## Internet and Telephone Assistance

Website: **ftb.ca.gov**

Telephone: 800.852.5711 from within the United States  
916.845.6500 from outside the United States

TTY/TDD: 800.822.6268 for persons with hearing or speech impairments

For general information:

Website: **taxes.ca.gov**