PROJECT DESCRIPTION: The current audit nominating process requires a minimum of five months and in some cases eight months to complete. The process should be streamlined to more efficiently and more quickly secure a list of audit candidates. Also, the current process does not always result in a list of candidates that are of interest or value to a number of states. This project will review both the steps in the nominating process and the criteria that are used to develop and consider audit nominations that are placed in inventory. We are looking at the process as it is used to create an inventory of audits for both the sales and income tax programs.

We would appreciate your responses to be from the perspective of your state. We would also appreciate knowing if any of your comments pertain to income or sales tax programs specifically:

1.   In the current process, what criteria do you consider when you submit a nomination?

When nominating a taxpayer for audit there are several factors that we consider:

> A. Is the taxpayer registered with the department for Sales and Use Tax purposes or does the taxpayer have sufficient nexus to require them to collect and remit taxes to the State of Alabama?
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> B. We consider the time and cost savings in terms of travel expenses associated with nominating the taxpayer as opposed to sending a Foreign Audit Specialist to conduct the same audit.
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> C. Has the taxpayer been recently audited by the department and whether it is a company that is scheduled to audit by the Department?
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> D. When nominating a taxpayer for audit we consider the complexity of the audit. For example, if the taxpayer has a direct pay or multiple tax accounts then we will consider auditing this taxpayer because it requires special attention by the Department.

National corporations with filed tax return problems/corrections by return sections accounts

> Income – Multi National companies who have not been audited by the Department in the last 3 to 5 years, or longer where we have identified issues on the return or other financial filings.

Income – We first look to see if the audit has already been assigned and being worked by one of our audit staff. Next we look to see if the taxpayer as operations in many states and it would have broad appeal to other states. Are there issues where we think a uniform approach might be better. Also, a major criteria for us is if we feel we might have difficulty in getting information from the taxpayer and, knowing our, subpoena power would be limited.

Sales – Multi National companies who have not been audited by the Department who are in an industry where reporting mistakes may be high. i.e large deductions.

Sales - Since Minnesota has auditors throughout the United States our first criteria is to select an audit that is in an open territory (not otherwise assigned to our out-of-state staff). A list is generated based on open territories then a review is completed to determine if there is high MN withholding, a variance in gross receipts for income tax returns to sales tax returns, and if any sales or use tax has been remitted. An internet search is also completed to determine if there are any other business locations throughout the United States that other participating states would be interested in.

I nominate large companies reporting sales and use tax in Arkansas and non-filer companies that I believe have nexus with Arkansas for sales and use tax. I try to nominate companies with operations in the states that are members of the MTC audit program.

Location of taxpayer. Size of audit , presence in our state, prior audit history and assessment potential. Cost/Benefit of sending auditors overnight to conduct audit.

- Whether it is more than just a North Dakota or regional issue. We would generally only nominate national companies with issues that would be relevant for other states.
- What is our own ability to get to that audit (based on priority). Would generally be one that is not a highest priority audit. Our own staffing levels might be a factor, but probably only a minor one. Our highest priority audits would be those that would have a large North Dakota presence, but likely not as relevant for other states.
- Nexus issues and placing a taxpayer on a combined report are issues we think the MTC auditors are well equipped to handle, and more efficiently as they can cover the issue for multiple states generally without the repetitive effort.
- Has there been a prior North Dakota audit of that taxpayer to indicate what the likely outcome would be.

    All of these considerations are taken together.

2.   In the current process, what criteria do you consider before you will vote for an audit nomination as a "priority"?

    A. If the taxpayer is a major corporation that has not been audited in the past and it is unlikely that the taxpayer will be scheduled for audit in the near future due to scheduling conflicts, we will recommend the taxpayer for priority audit.

Likely large assessment but currently not assigned to our audit staff.

    Income – A presence in the State, and whether the Department has not audited the company in recent years.

    Income - Do they have Nexus and are filing?

Do we think the taxpayer has some questionable issues that should be addressed?

Do we feel that the MTC auditors may have more expertise in handling the potential issues and/or taxpayer?

Sales – A presence in the State, whether taxpayer is in a category where the Department feels there is a need, and whether the Department has not audited recently.

Sales- Minnesota votes on MTC audits as a priority if the audit is in an open territory, has not been previously audited, and upon initial review appears to be a worthy audit.

An audit nomination would be a priority if the nominee is a non filer in Arkansas and the nominee appears to have activity within Arkansas and Arkansas does not currently plan to audit the nominee.

Do we currently have an audit in progress on taxpayer. Do we have the potential for a large assessment that we would want to keep internally and the same criteria as stated in #1 above.

We generally will participate in every audit unless we have already started an audit ourselves. Whether it gets rated a priority will be based on the criteria from our response in #1. After reviewing the returns of a potential audit candidate, if there are no apparent material issues and if it does not have a relatively large North Dakota presence, it will be rated a lower priority.

3. What is your philosophy about MTC audits and the audit program – how do you see them helping your state's audit program?

A. The MTC audit program is viewed as an extension of our Department because it insures greater audit saturation through highly trained and skilled auditors. The state benefits because travel related expenses are greatly reduced while at the same time revenues are increased and taxpayer compliance is insured. In addition the program facilitates the sharing of information between member states.

As an audit asset with great experience

For both Sales and Income – It's an additional source of manpower to conduct audits.

Income – We don't think there is enough sharing among states on new and/or different schemes taxpayer's are using to lower their tax bills. For example many States have gone to a single factor (Sales) to apportion income. We have found many taxpayers trying to find ways to inflate total Sales everywhere or decrease in State reported sales. This is just one example. What do other States see in this area?

Sales - MTC audits can help our state with auditing businesses in open territories and can help determine if a business has Nexus within our state.

The MTC audit program has been very beneficial to Arkansas. I see the program as an extension of our office—additional audit personnel to help with compliance.

The MTC can conduct out of state audits we don't necessarily want to do and bring in some revenue for the State , sharing of information and audit approaches as well as an extension of our audit program

The MTC audit staff is able to cover a lot of audits that we would not otherwise get to, or choose to do, either because the potential recovery is low or unknown. Because most of the audits are national companies, we believe we are really able to leverage the MTC audit program to do those, as those companies often have a smaller presence in North Dakota, but still might be deserving of some audit attention. The two audit issues we feel the MTC is best equipped to deal with are unity and nexus. Because those standards are fairly uniform among states, they are areas in which we continue to nominate companies.

4.   What are the good points about the current audit nominations process?

A. The State of Alabama is given the option of nominating taxpayers for audit which insure greater audit saturation throughout the continental US.

 Input/view from other jurisdictions

Each member gets the opportunity to nominate, discuss, and vote their priorities.

Sales - Every state gets to select audits based on their own audit criteria and the process for nominating businesses is fairly easy.

The basic structure of the process.

The number of candidates to vote on seems to be about the right size of selection.

5.   What are the aspects that you are concerned about, or that should be considered for improvement?

A. Many of the taxpayers that are nominated by MTC have minimal business activity in the state of Alabama. Maybe if MTC would request or accept a list of companies that the member states would prefer to audit it would be more beneficial.

Audit issues and the difference in the States' tax code

An earlier nomination and voting schedule. While SC has not been with the MTC audit program very long, I have found that a large percentage of the selected companies have already been audited by the Department in the recent years. An earlier selection period would give our auditors and selection team the ability to put MTC selected audits on hold for the MTC and move on to other audits. This would essentially allow the Department to gain a bigger benefit by participating in more audits.

MTC needs to ensure that the selection process works for all states. Minnesota has a high audit coverage and it is sometimes difficult for MTC to select an audit that will meet Minnesota's needs.

Front load the data so that the inventory is always being refreshed and the next audit being done is always the next best audit to do.

Income – I would like to see something what TEI does. They sit around tables and discuss what topics the states audited for, what were the arguments put forth and what was the outcome. MTC could take a prior audit and discuss what each State did with the audit, learn what arguments taxpayer put forth (I think we might find out what different arguments tp used in each state) and how did the settlement offers differ. This might help us in forming better settlement agreements.

Sales - After all of the states have turned in their nominations, it is very time consuming to research and fill out the forms for every nominated business. If a state knows that they are not going to participate in an audit maybe they should not have to fill out the form to save time. There are also some inaccurate FEINs given which makes it difficult to locate the taxpayer in question.

I am concerned about what happens when state personnel changes occur. I believe there should be some written guidelines or a handbook for the person actually preparing the nomination documents. I would like to know specific criteria and expectations of the MTC. (and there may be some, but I don't remember any being passed on to me.) I don't know how it works in the other states but the process was never fully explained to me and I have been submitting nominations for over ten years.

The timing from nomination to voting to actually beginning the audit takes too long. need for streamlining of process.

Perhaps there can be some audits where the voting includes consideration for whether the states / issues involve relate to "separate company" states versus those that would be combined reports or eligible to be combined. There could be an instance where separate company states may really have a good candidate, but the combined states vote in such a way those candidates aren't selected, or vice versa.

I think the recent discussion on efforts to improve the nomination process has been good. Discussing the criteria that states should be using was apparently good, because we had assumed all states were already using what we would consider "common sense" considerations, but perhaps not all were or were weighting considerations differently.

Perhaps the nominating state can provide a bit more information or more specific information about why it believes the company would be a good audit candidate.