

# HOW TO PREPARE FOR A CBT (SALES TAX) AUDIT BEFORE IT HAPPENS

THURSDAY, AUGUST 20, 2020

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## PRESENTED BY:

*Ellen Kera, CPA - Automotive Practice Co-Leader*  
*Tom Walsh, CMI*

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## YOUR PRESENTERS



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**Ellen Kera, CPA**  
Partner & Automotive  
Dealerships Practice  
Co-Leader



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**Tom Walsh, CMI**  
Principal, State and Local Tax



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## IN THE BEGINNING...

This is not just a sales tax audit, it incorporates the following:

- A. CBT - Corporate Tax Or Partnership Tax (For LLCs)
- B. GIT - General Income Tax
- C. S&U - Sales And Use Tax
- D. Tire Tax - \$1.50 fee imposed per tire including the spare sold as part of the vehicle. It also applies to the sale of new tires in connection with repair or maintenance service.
- E. DSF - Domestic Security Tax - applies only if you rent vehicles of no more than 28 days at the rate of \$5 per day. A motor vehicle is rented by the same renter per their agreement with the maximum rental fee of \$140 even if it extends over the 28 days.

The audit periods are either 3 or 4 years depending on the tax type.

Here are two samples showing initial correspondence from two different auditors.



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# SAMPLE #1



State of New Jersey  
DEPARTMENT OF THE TREASURY  
DIVISION OF TAXATION

RE: TAXPAYER ID NO :  
CASE NO :

**Dear Taxpayer:**

We will be auditing your accounting records. The audit will focus on payment and reporting of all tax returns you are required to file with the State of New Jersey. This audit may look at returns and other documentation for Sales and Use Tax, Corporation Business Tax, Gross Income Tax, and any other taxes and/or fees that the State requires you to remit.

More information about the New Jersey State Tax Audit process is available on our website at: <http://www.state.nj.us/treasury/taxation/pdf/pubs/misc/aud100.pdf>

### What do you need to do?

At your earliest convenience, please contact the auditor listed below to discuss your audit. You are entitled to have a representative (an accountant or attorney) appear with you or on your behalf at all meetings. If you want a person(s) to act on your behalf at any time without your presence, you must submit a completed Appointment of Taxpayer Representative form available at:

[http://www.state.nj.us/treasury/taxation/pdf/other\\_forms/misc/m5008r.pdf](http://www.state.nj.us/treasury/taxation/pdf/other_forms/misc/m5008r.pdf)

Upon completion of the audit:

- We will provide copies of the final work papers.
- The auditor will explain the calculation of any assessment or overpayment; and
- You will be given the chance to discuss any audit issues/questions with the auditor and/or the auditor's supervisor, at your request.

At this time, you should advise the auditor if you have any information that has a direct impact on the proposed adjustment(s).

After the audit, you will receive:

- A bill by certified mail; or
- A notification indicating no additional tax liability; or
- A notification indicating the amount of refund due to you.

In accordance with the Taxpayers' Bill of Rights, all amounts billed by the Division will include notice of the administrative appeal rights available to all taxpayers.

**If you have questions regarding this letter, please contact the auditor.**

IN REPLY REFER TO:

NJ DIVISION OF TAXATION  
NEPTUNE AUDIT B  
1828 WEST LAKE AVE, 3RD FL  
NEPTUNE, NJ 07753

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Creating Reconciliation Report...

Form NJ-IDR	State of New Jersey — Division of Taxation		Date of Request:
Rev. 06/2012	Information Document Request		
Name and address of Taxpayer:		Taxpayer ID #	
		Audit Case #	
		Request submitted to (name/title):	
		Request number:	1
Following are the taxes to be audited and the audit periods:		Received	Date
CBT-S	01/01/15 - 12/31/18		
GIT	01/01/16 - 12/31/18		
S&U	01/01/16 - 12/31/19		
TIRE	01/01/16 - 12/31/19		
DSF	01/01/16 - 12/31/19		
Description of documents and/or information requested:			
1. Trial balance for years 2015 - 2018			
2. General ledger for sample year 2018			
3. NJ-W2's and 1099's issued for years 2016 - 2018			
4. NJ-W3's issued for years 2016 - 2018			
5. Depreciation Fixed Asset schedule for assets placed into service during the audit period along with invoices, 01/01/16 - 12/31/19			
6. Expense invoices/paid bills for sample year 2018			
7. Sales invoices for sample year 2018			
8. ST-50's filed for 2018 along with back up documentation			
9. Copies of NJ CBT returns and Federal 1120's filed for years 2015 - 2018 with attached statements			
10. Tire report filed for 2018 with supporting documentation			
11. DSF report filed for 2018 with supporting documentation			
Please note additional information may be requested during the audit			
Information due by (date):		At next appointment <input checked="" type="checkbox"/>	Mail in <input type="checkbox"/>
Auditor Name:			
Office Address:			
153 HALSEY STREET, Box 47022			
NEWARK, N.J. 07101			
Phone: (973) 648-3900 Fax: (973) 648-3929			





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## SAMPLE #2



State of New Jersey  
DEPARTMENT OF THE TREASURY  
DIVISION OF TAXATION  
March 1, 2018

RE: TAXPAYER ID NO : B  
CASE NO : 1

Dear Taxpayer:

The Division of Taxation will conduct an examination of your accounting records and the supporting documentation as they relate to the tax returns you are required to file with the State of New Jersey. As a general rule audits cover all major taxes that are within the Statute of Limitations, such as Sales and Use Tax, Corporation Business Tax and Gross Income Tax, as well as ancillary taxes such as Litter Control, Spill Compensation or Petroleum Products Gross Receipts Tax if applicable. You will be contacted in the near future by a Division representative to arrange a meeting to begin the examination. A pamphlet with additional information about the New Jersey State Tax Audit process is available on the Division of Taxation website at "[www.state.nj.us/treasury/taxation/pdf/pubs/misc/aud100.pdf](http://www.state.nj.us/treasury/taxation/pdf/pubs/misc/aud100.pdf)".

At the initial meeting, or any subsequent meeting held during the audit, you are entitled to have a representative (such as an attorney or accountant) appear with you or on your behalf. If you want this person to act without your presence, you must submit a completed "Appointment of Taxpayer Representative" form which is available at "[www.state.nj.us/treasury/taxation/pdf/other\\_forms/misc/m5008r.pdf](http://www.state.nj.us/treasury/taxation/pdf/other_forms/misc/m5008r.pdf)".

Upon completion of the audit, you will be offered the opportunity of a post audit conference. At that time you will be presented with copies of the auditor's work papers and given an opportunity to discuss any audit issues or other questions you may have. Any information that has a direct bearing on the proposed adjustment should be made known to the auditor at this time.

After the post audit conference, you will receive either a bill by certified mail, a notification indicating no change, or a notification indicating the amount of refund. In accordance with the Taxpayers' Bill of Rights all underpayments billed by the Division will indicate in detail the administrative appeal rights available to all taxpayers. In the event an additional liability is determined and the taxpayer wishes to make payment, please ensure that the check is made payable to the New Jersey Division of Taxation.

In the event you have questions regarding this letter, please contact the auditor whose name and phone number are listed below.

Thank you for your anticipated cooperation.

IN REPLY REFER TO:

NJ DIVISION OF TAXATION  
TRENTON AUDIT-A  
P O BOX 289  
TRENTON NJ 08695-0289  
609-588-3867

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State of New Jersey  
DEPARTMENT OF THE TREASURY  
DIVISION OF TAXATION  
P O BOX 289  
TRENTON, N.J. 08695-0289

March 20, 2018

ATTN: Ellen Kera, CPA

Dear Taxpayer,

Enclosed please find Form NJ-IDR, Information Document Request ("Form NJ-IDR") which sets forth our specific requests for additional information required to complete the audit. Please review such Form NJ-IDR and provide all requested documents and information to the auditor listed below. Other items may be requested as the examination proceeds.

Thank you for your cooperation in this matter. Should you have any questions or concerns, please do not hesitate to contact me.

Sincerely,

Quakerbridge Plaza Office Complex  
Building 9, 3<sup>rd</sup> Floor  
Mercerville, NJ 08619  
(609) 588-3867

Enclosure: Form NJ-IDR

Phone: (609) 588-3333 Fax: (609) 631-4710

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## SALES

As we know, CDK, R&R, Dealertrack, and automate post the sales tax for each deal - but what they look for are the sales that do not have tax...what does that mean?

If a deal was posted with no tax, which they will see from the sales journals they ask for, they will ask you for the deal jackets.

### When are deals tax exempt?

- Wholesale
- Religious and charitable organizations
- Swaps
- Diplomats – only specific designations are in fact exempt.

One common mistake among clients is if they buy a car or truck from another dealer, more times than not, they are not paying tax when registering the vehicle.

The purchaser is the end user, therefore tax must be paid by the dealer

A common question to ask yourself - **who is the end user?** If the answer is **you**, then it is taxable. In contrast to items purchased to add to vehicles.



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## LOANERS AND DEMOS

### LOANERS

1. If the car is used exclusively as a loaner and the manufacturer reimburses the dealer for the cost of supplying the vehicle as part of the warranty agreement or other dealer-sponsored program, the charge to the manufacturer is exempt from sales tax. The manufacturer must provide the dealer with a properly completed Form ST-3. A trade-in credit may be claimed when loaner is replaced by another vehicle.
2. If the dealer contracts with a car rental agency to provide free loaners to customers and the customer are contractually entitled to a loaner, the dealer can rent the car exempt from tax by providing the rental agency with Form ST-3. However, if the customer is not contractually entitled to a loaner, the dealer must pay sales tax (including any special taxes) on the rental, to the car rental agency.
3. Dealers may also rent cars to provide a customer with a loaner at their discretion, rather than as part of the manufacturer's warranty or a dealer's contractual obligation. In this case, the use of the loaner would be considered a promotional use and subject to tax on the rental rate.





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## LOANERS AND DEMOS

### DEMOS

1. Tax shall be computed and paid monthly by the retail dealer as part of the regular monthly report of taxes due on the sale and use of taxable property or services if the vehicle is removed from stock and used as a demonstrator.
2. The basis for the tax shall be determined by multiplying .25 times the sum of the manufacturer's suggested list price of the motor vehicle plus \$500. If the motor vehicle is used, the basis for the tax shall be determined by multiplying .25 times the sum of the average retail price listed for the vehicle in the NADA Official Used Car Guide, or similar NADA official guides for other categories of used vehicles, for the year and month of withdrawal, plus \$500.
3. The Dealer is required to notify the Division of Taxation when a vehicle is withdrawn from stock for demo purposes. Form C-1003-ST must be completed and filed along with the sales tax return which covers the period during which the vehicle was removed from inventory.



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# ACCOUNTS PAYABLE – Out-of-State Purchases

Auditors will gravitate to certain accounts on the general ledger. These are the most frequently chosen:

- Advertising - service of creating and producing advertising should not be taxable, however final product may indeed be taxable.
- Out-of-state taxes - Many office managers are not aware of what expenses are taxable, and even today, many out-of-state vendors do not charge tax on invoices. Why?
- Policy
- Outside services
- Small tools and other supplies
- Travel and entertainment
- Fixed assets for the entire audit period
- Lead generators

More times than not services performed for the dealerships are taxable. Always double check with your CPA

The biggest surprise: non-original flooring. If you are renovating, or involved in an image upgrade, flooring is usually one of your changes. NJ can and will charge you tax on this even though it is part of a capital improvement because it is not the original floor.

I am frequently asked about the following:

- Detailing, washing, waxing - obviously you would post this to the vehicle, but the payment to the vendor is taxable if you are using an outside detailer
- Outside storage of vehicles (not on your lot)
- Printing or imprinting ETCH
- Machinery equipment, tools, supplies.
- Insurance
  - Gap Coverage (provided by lease company)*
  - Gap Coverage (provided by third party insurer)*
  - Credit life, health, unemployment insurance*
  - Etch*



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## PARTS AND SERVICE

- Resale certificates - Historically, these have been kept in the parts department. It is a better idea to keep them in the accounting office alphabetically. Make it a habit to check all vendors once a year and have them fill them out.\*
- Policy - Auditors have learned to look at this account. LOF's are taxable if you give to your customer free of charge but only the oil and filter is taxable. Labor is not. If the dealer is contractually obligated to provide the service at no charge, the dealer will not owe sales tax. Any item you give away free, makes you the end user and ultimately you will need to pay use tax.
- Service – similar to parts in that they will review your journals and see which R/O's have not been taxed. They will pull a random selection and you will have to pull them. Obviously warranty and most internals are not taxable.



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## FIXED ASSETS

- When assets are purchased for your business, they are taxable with the exception of certain capital improvements - **construction**.
- Furniture and fixture purchased during construction is not part of the capital improvement. You must pay the sales tax unless you know for a fact that the contractor purchased them on your behalf.





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## QUICK REFERENCE – Common Taxable Items

- Cleaning services
- Monthly Landscaping
- Supplies purchased over the internet that are not taxed on invoice
- Lead generators
- Out-of-state purchase for end user supplies
- Tools and supplies
- Uniform cleaning
- Free oil changes – parts only
- All policy work that is not subject to warranty
- Advertising production costs not taxable – the actual commercial or ad may or may not be.
- Mailers including postage



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# QUESTIONS?





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## CONTACT US



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**Ellen Kera, CPA**  
Partner & Automotive  
Dealerships Practice  
Co-Leader  
914.358.3401  
[ekera@citrincooperman.com](mailto:ekera@citrincooperman.com)



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**Tom Walsh, CMI**  
Principal, State and Local Tax  
212.225.9559  
[twalsh@citrincooperman.com](mailto:twalsh@citrincooperman.com)



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