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**WHAT TO EXPECT IN A
COMPUTER-ASSISTED
AUDIT**

**CALIFORNIA DEPARTMENT OF
TAX AND FEE ADMINISTRATION**

Introduction

The goal of all California Department of Tax and Fee Administration (CDTFA) audits is to determine whether or not the correct amount of tax has been paid during the audit period. To do that, we look at your sales and purchase records.

Since you keep your records in electronic form, we can more readily assess the accuracy of your tax reporting by examining the electronic records and dramatically reducing the volume of paper documents needed for the audit. We call this a “computer-assisted audit.” Sales and use tax [Regulation 1698, Records](#), permits the CDTFA to access all records, including electronic (machine-sensible) records and data you maintain. Computer data is considered part of the books and records.

We are providing this brochure to help you understand what to expect as we review your electronic records. If you have questions about the computer-assisted audit process, be sure to ask the staff whose name and phone number are written on the back of this brochure.

What is a computer-assisted audit?

In a computer-assisted audit, we examine your electronic records. You download data that we then analyze using specialized software such as ACL, VEdit, etc. We provide guidance and work with your information technology staff in order for them to download this data in a format we can use.

In an examination of records, we will likely utilize a Computer Audit Specialist (CAS) to assist the auditor in the completion of the audit. The CAS is specially trained in data systems and statistical sampling and provides technical support to our audit team. The CAS does not make decisions regarding the audit.

Typically, we request that you submit electronic data to us in a nondelimited, fixed width, and flat file format along with the record layout. Data is accepted in EBCDIC format or ASCII format. Data received in EBCDIC format is converted to ASCII format. With advanced notification and approval,

other formats may be accepted. We can work with most data systems to find the most effective manner to complete the audit.

What are the benefits of a computer-assisted audit?

Businesses usually find this method less time-consuming and more convenient than a conventional audit as a computer-assisted audit requires the retrieval of fewer source documents, such as invoices. This saves the time and expense of the taxpayer retrieving paper documents which minimizes the disruption to the business and reduces the time the taxpayer (and his or her employees) must devote to the audit.

In the end, we expect to have an audit which is more accurate and requires fewer resources by both you and our staff.

Are the tests, procedures, standards, and techniques the same as those for audits using paper records?

In general, yes. Since the objectives of the audits are the same, it follows that we will apply similar, if not identical, measures to both. In fact, a computer-assisted audit usually reduces the number of records we examine, as we can better identify the population being examined.

What will the auditor need to know about my electronic records?

Before starting any audit, we need to understand your business operations and record keeping procedures. For a computer-assisted audit, we will ask:

- What electronic records do you have? What format are they in?
- What periods are the records available for?
- What internal controls are in place to support your tax accrual system?

- How have you developed and implemented tax accrual system changes?
- Do you have records of individual sales and purchases?
- Have you changed accounting systems since the prior audit or during the current audit period?

We will also need to:

- Understand the accounting system and sales/purchasing processes.
- Identify information (files) that is maintained electronically.
- Determine relationships between files and any fields that link them together.
- Determine which fields in those files contain the needed information.
- Observe a system walk through. This will provide an opportunity for us to watch someone enter a sales or purchase invoice and obtain a screen print of what information is captured in the taxpayer's computer records. This will assist us in developing our test.

This will help us determine which fields (in which files) contain the information that will be needed for us to examine your records. The information is usually in several files and may be on a mainframe, network, or PC. The taxpayer's computer staff will be asked to create one composite file. A composite file is one file containing all of the fields needed to complete the audit. Composite files make the audit process go faster with fewer data problems.

We may ask you to provide table files that contain descriptions of codes or an electronic chart of accounts. These files may be kept on a PC in a word processing, spreadsheet, or database program.

How do you keep my records confidential?

You are protected by the state's confidentiality laws, which generally prevent us from disclosing any of the records we obtain in your audit, whether they are paper or electronic. In addition, before you provide copies of electronic business records, you and the auditor should agree on the following:

- Format of the records.
- Security measures we will use to protect the confidentiality of your records.
- What we will do with your electronic records at the end of your audit.

You may request that we perform all work on your premises and do not remove your electronic data.

What are the steps in a computer-assisted audit?

Step 1: Discussing your records at the preaudit conference

A preaudit conference is a meeting that may occur several months before the start of the audit to discuss the availability and production of records, including electronic records. Taxpayers (for example, owners, partners, or corporate officers) shall be invited and encouraged to attend the preaudit conference along with their representatives and appropriate information technology staff.

During the preaudit conference, the items to be discussed will include: general audit procedures, availability and access of records, computer-assisted audit procedures, relevant sampling issues, data transfer process, verification of data, security of data, timeframes for furnishing and reviewing records.

We will request only records and data that are relevant to the audit. We will ensure the transaction data is material to the audit and is used properly. We will take into account the nature of transactions and the ease with which data can be accessed and analyzed.

Step 2: Reviewing your computer system

In addition to understanding your accounting records, we will discuss other elements of your computer system, including:

- The software package used for your general ledger, sales orders, accounts payable, and fixed assets.
- Areas related to ecommerce such as electronic data interchange, procurement cards (credit cards) and electronic funds transfer.
- Availability of imaged source documents.

Step 3: Evaluating data integrity

The data you provide must be examined for accuracy and completeness. This is accomplished by reconciling the electronic data with your books and records. Selected accounts/sales in the data are totaled for a given time period (for example, one year or the audit period). The totals are compared with the totals from your books and records.

We will ask you to review your data and provide all additional records needed to reconcile any differences. Timing issues, manual adjustments to accounts, etc., may cause amounts to not match perfectly. Still, we expect the amounts to closely agree.

Step 4: Developing a sampling plan

Like audits that use paper records, computer-assisted audits attempt to identify the most accurate manner in which to sample your transactions. Before we sample your records, we will work with you to develop a sample plan. That plan will be documented on our [CDTFA-472, Audit Sampling Plan](#).

Please note that the information and methods described in the *Audit Sampling Plan* may change during the audit. We use the form to establish the most effective and efficient sampling plan; however, we continually evaluate the plan as the audit progresses and change it if necessary. We will discuss any proposed change with you.

Step 5: Selecting the sample

Using the method described in the *Audit Sampling Plan*, we will select the sample transactions to be reviewed. In many cases we can significantly reduce the number of source documents required based on information available in the electronic data. In order to select the most representative sample, it is not uncommon for us to reduce the population by stratifying (separating) accounts known to contain errors and reviewing those accounts on an actual basis. On the other hand, we also may include transactions recorded as occurring outside the State of California to verify the claimed (or netted) exemption.

Upon selection of the sample, we analyze the sample of the population. If the sample is not representative of the population, we immediately select another sample. This is done prior to reviewing any source documents. If requested, you may review our sample log to examine our sample selection.

Step 6: Evaluating the sample

After reviewing the sampled transactions, we will evaluate the results. See “What statistical sampling standards do you use” (below) for an explanation of our policy standards for the minimum number of errors and confidence level requirements. If this analysis shows that the transactions examined are not representative, our auditor and you may agree to one of the following options:

1. Increase the sample size.
2. Stratify (by dollar value, product line, or type of error).
3. Examine specific transactions on an actual basis.
4. Drop the test and accept reported amounts in that area of the audit.

Step 7: Computing error rate and total category error

In nearly all audits that use statistical sampling, we determine the dollar value of the errors found in a category (for example, sales) by using the results of the sampling. We take the error rate from the sample and apply that to the total dollar value of the sample to determine the total error amount.

What statistical sampling standards do you use?

Minimum errors

When a sample results in only one or two errors, the auditor must evaluate whether these errors are representative of the population. Such a low error rate may indicate that the sample is not representative. CDTFA policy is that for any stratum of transactions sampled there must be at least three errors. If we find

fewer than three errors, the auditor may decide to use one of the options described in Step 6.

Confidence interval

“Confidence interval” is one statistical measurement we use to measure the sampling error. It is the difference between the amount calculated in the sample and the error we would expect if we had examined all of the transactions. We compute our confidence interval using an 80 percent confidence level.

For more information

A complete explanation of our statistical sampling procedures is too lengthy for this publication. If you have any questions about the sampling methods used in your audit, please discuss them with the auditor or the CAS. You may also want to download or review [chapter 13](#) of our *Audit Manual, Statistical Sampling*, at www.cdtfa.ca.gov. The chapter explains our sampling practices and standards in detail. If you have any questions about your computer-assisted audit, please contact:

AUDITOR NAME

PHONE NUMBER

AUDIT SUPERVISOR NAME

PHONE NUMBER

COMPUTER AUDIT SPECIALIST NAME

PHONE NUMBER

For more information on audits in general, see our [publication 76](#), *Audits*. You may obtain one from your auditor, download or order a copy from our website, or request a copy by calling our Customer Service Center at 1-800-400-7115 (TTY:711). Customer Service representatives are available to assist you weekdays from 8:00 a.m. to 5:00 p.m. (Pacific time), except state holidays.

Taxpayers’ Rights Advocate: Call toll-free for help with disagreements you have been unable to resolve through normal channels. 1-888-324-2798.