Auditing Convenience Stores
VALTA Panel Discussion

Convenience Stores
& Car Wash Equipment Update

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Before we start-

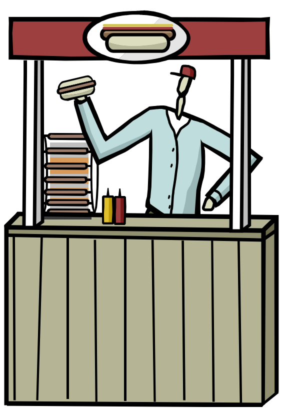
- Be Consistent Treat all Taxpayers equally
- The authority is in the code
- Use the same process for every audit
  - Have an audit program (VALTA site)
    - www.valta.org
  - Have an interview document (LAP)
  - Listen carefully
    - Document the taxpayer statements

Important Audit Tips!

- Keep the end in mind: COURT/APPEAL
- Correspondence sheet
  - Document everything
  - City Attorney
  - Helps when testifying in court
- Stamp for Audit work papers
  - Easy guide to stay on task
  - Evidence in court – *purpose of this document*
- Interview with a second person present
  - Two testimonies in court

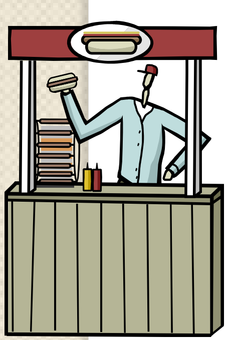
Audit Trigger

- Why am I auditing this taxpayer?
- In my case - *Hot Dogs (nesting puzzle)*
  - Failure to file meals taxes
  - A site visit
  - As I stood in the store watching the sub shop cook food, the owner said, "I am not selling prepared food."
  - What is your office policy for non-filers?
  - Based on your local code.



Businesses within a business..

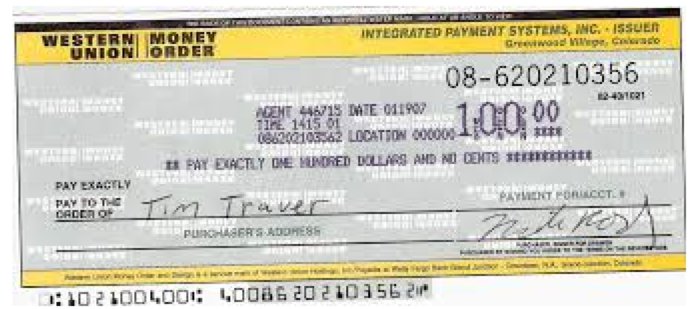
- Each of these income sources have unique criteria
- RETAIL
  - Gen Merchandise
  - Gas/Fuel
  - Cigarettes excise tax/tax stamps-trafficking
  - Sub Shop-prepared food-excise taxes
  - Car Wash (May be PERSONAL SERVICE license or ancillary to retail.)



Businesses within a business..

- Each of these income sources have unique criteria

  Commission Sales



  - Western Union
  - Money Orders
  - Check Cashing MSB Registrant
  - U-Haul Agent
  - Lottery
  - EBT Cards –

    A new challenge

Income Streams

Retail Income Streams:

- General Merchandise
- Gas/Fuel Sales
- Cigarettes-tax stamps
- Prepared food –excise tax
- Car wash (may be service)

Commission Income Streams:

- Western Union
- Money Orders
- EBT Cards
- Check Cashing
- U-Haul Agent
- Lottery
- EBT Cards –undercover $

Audit Objectives

- Compliance
- Proper Assessment
    - Excise Taxes –Trigger
    - BPOL
    - BPP

Examination of Income

- “The examination of income is a mandatory audit issue. Examiners must determine whether the taxpayer reported the correct amount of income. The depth of the examination of income and the techniques used are dependent on the facts and circumstances of the case. Generally, consideration should be given to tax return information, the reliability of the taxpayer’s books and records, the outcome of the Minimum Income Probes, and the resolution of Large, Unusual Questionable income issues.”
- http://www.irs.gov/Businesses/Small -Business-&-Self-Employed/Cash-Intensive-Business

My Case- Very little records

What do you have to work with?

-"…oops, all of my records were in the back of my car (I was going to the Accountant to get my taxes done) and someone ran into the back of us and swoosh …..they went everywhere."

I started with Bank Statements

Annual Deposits $5.4M

Sample Results:

All of the deposits represent check cashing activity!

Questions:

Where is the sales income being deposited?

Answer:

In another, undisclosed, bank account.

Subpoenaed the records

“Z” Tapes reveal a little

Server – MB
Date: 1/1/2013
Academy Restaurant
In: 16:30 Out: 23:30 – 7 hours
Table Count: 27
To Go: 0
Avg Ticket: 32.94

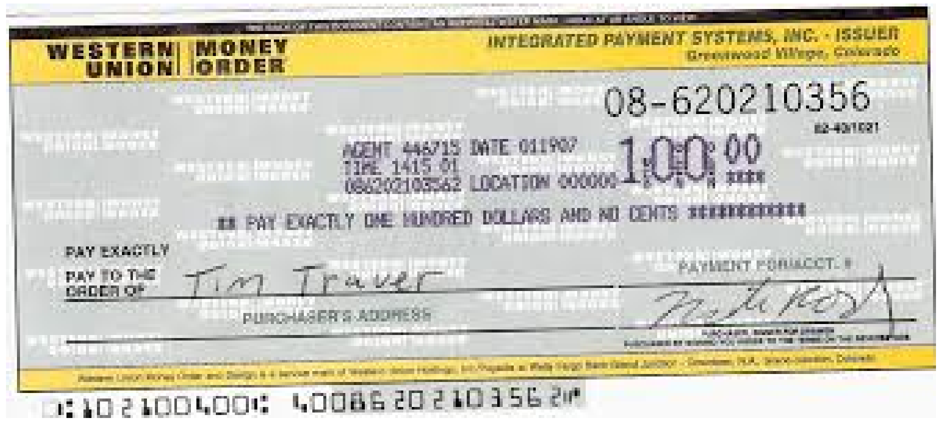
Food Sales	644.35
Bar Sales	185.00
Gift Certificates Sold	50.00
Tips Collected	61.43
Sales Tax	60.13
Gift Certificates Redeemed	50.00
Cash	276.00
VISA/MC	314.84
AMEX	363.50

- “Z” tapes were provided for some months.
- Key months were missing
- The data did not match the commission percentages indicated in the interview with the taxpayer for check cashing.
- Match the cigarette sales with the monthly reporting by supplier (COSTCO)
  - Suppliers are required to keep track of sales by store

Business #1 Lottery Sales

- Virginia Lottery
- A/R 1-804-692-7628
  - Must be Approved to sell
  - Their code requires a separate bank account
  - $ commission on lottery sales vary
  - The purchase is not swept from the bank account until the seal is broken on rolls/etc.
  - $ commission varies based on many criteria
  - Annual lottery sales – public information

Business #2 Western Union & Money Orders



- Who administers? Corporate
  - EMAIL customeradvocatedept@westernunion.com
- How does it work? Electronically deposits and withdrawals “net” through bank account.
- The commission is based on ……

Business #3 Gas Vendor

- BPOL net of taxes
  - Look at contract
  - Who pays the taxes?
- How does the store pay for the gas
  - Cash sales
  - Credit card sales –electronic payment to supplier
  - May be commission only. (Gas owner gets separate license, and store is comm. merch.)
- Call vendor or get copy of contract
  - Verify the process

Business #4 Check Cashing

- Must Register as a Money Services Business (MSB) through FinCEN (Financial Crimes Enforcement Network)
- www.fincen.gov then download list of authorized MSB’s.
- Commission on check cashing is at owner’s discretion
  - In my case his percentage fee did not match the “Z” tapes or the bank statements

Business #5 EBT Cards

- Replaced Food Stamps
- United States Dept. of Agriculture oversees through Virginia DSS
- Very corrupt (according to USDA source)
- Each recipient receives an EBT debit card
  - If the recipient shares PIN # anyone can use
  - Including the convenience store owner

-Suspected fraud in that owner buys EBT card from recipient.

-How do we assess fraud?

My BPOL Audit Results-small convenience store

- $6M plus deposits into bank account for check cashing only
- No record of daily operating deposits
- Daily 4-8 deposits; 4-8 cash withdrawals
- Large sums of cash withdrawn same day $8K-50K???
- 2nd Bank Account discovered
  - Summonsed records through court
- Underreporting of gross receipts and meals taxes
- Appears Fraudulent activity using EBT cards
  - Involve our Community Response Team
  - Possible FBI (U.S. Treasury) case –only if in millions of $

Added RESULTS

- Statutory Assessments
- Why so much cash? HAWALA
- Community Response Team case
- Police Investigation
- Possible FBI probe

What about BPP?

Special considerations may apply:

- Equipment often owned by another party
  - Original store/real estate owner often owns BPP and contracts out the store
  - Gas equipment may be leased from oil co./vendor
  - Other vendor/owners (ATM, tenants, etc.)
- Car wash equipment – NEW for 2013!
  - Treated as M&T as of July 1, 2012. *Code of VA §58.1-3508.5.*

Code of VA §58.1-3508.5

Separate classification of machinery and tools used directly in cleaning motor vehicles.

- Machinery and tools, including repair and replacement parts, used directly in cleaning motor vehicles by a motor vehicle cleaning business shall constitute a classification for local taxation separate from other classifications of machinery and tools as defined in § 58.1-3507. The governing body of any county, city, or town may levy a tax on such classification of property at a different rate from the tax levied on other machinery and tools. The rate of tax and the rate of assessment shall not exceed that applicable to the general class of machinery and tools.
- *Acts of Assembly, 2012, in force as of July 1, 2012. Not retroactive.*

Car wash equipment as M&T

To get this classification, equipment must be

- used directly in cleaning motor vehicles
  - Wash equipment (in "the tube")
  - May (?) include computer POS equipment used to run the machine (usually specialty equip)
    - Is it "used directly" if it runs the equip that actually touches the car? We say yes. Others may differ.
- by a motor vehicle cleaning business
  - *Is a gas station/convenience store also a "motor vehicle cleaning business" -- Yes!*

Car wash equipment as M&T

What is a "motor vehicle cleaning business"?

- Any business which offers a car wash for sale, even if ancillary to other sales.
  - Independent washes
  - Gas station car washes
  - Some detailers may qualify
- NOT one that washes only its own cars
  - Rental car companies
  - Car dealers
  - Repair shops

Car wash equipment as M&T

Notify known and potential car wash businesses of the change.

Joseph A. Horbal, MCR
Commissioner

Patricia J. Howell, MDCR
Chief Deputy Commissioner

Timothy M. McPeters, MDCR
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MEMORANDUM

To: Owners of car wash equipment used in a car wash business

From: Joseph A. Horbal, MCR, commissioner

Date: September 12, 2012

Re: New legal treatment of **car wash equipment** as **machinery and tools**, to be filed for 2013 on **Return of Machinery and Tools** for separate property tax.

Dear car wash equipment owner:

In their 2012 session The Virginia General Assembly amended the law, establishing car wash equipment as a class of "machinery and tools" for local taxation. This is a change from its previous treatment as business tangible personal property, and it affects your property tax filing requirements for 2013 and later.

House Bill 298 was passed and ratified, amending Section 58.1-3508 of the *Code of Virginia* to add §58.1-3508.5, which declared "[m]achinery and tools, including repair and replacement parts, used directly in cleaning motor vehicles by a motor vehicle cleaning business" to be a separate class of property defined within "machinery and tools" and assessed and taxed as such.

This law took effect on July 1, but the change will not affect your property tax reporting until the 2013 filing period. Starting with 2013, you will separate the car wash equipment from the other business tangible personal property that you have previously filed on one form. You will file both the **Return of Machinery and Tools** (for the car wash equipment) and the **Return of Business Tangible Personal Property** (for all other business tangible personal property).

In January, when you would normally receive your Return of Business Tangible Personal Property ("BTPP"), you will also receive a Return of Machinery and Tools ("M&T"), on which you will file the car wash equipment. You will NOT include it on the Return of Business Tangible Personal Property for 2013 and later. As is already the case with your BTPP returns, the M&T return must include an itemized list of the items reported on it. This will, of course, help to ensure that the equipment is filed on the proper return.

The instructions will be on the form, and should be self-explanatory. The assessment method will be similar to what you are used to, but the assessment will be lower, as M&T assessment factors are lower. And, while tax rates for 2013 will not be set until then, the tax rate on M&T is also generally lower.

If you have any questions, please feel free to call my office.

Happy auditing!