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No. 2022/053

November 15, 2022

TO COUNTY ASSESSORS AND INTERESTED PARTIES:

PROPERTY TAX RULE 192

State Board of Equalization (Board) staff has initiated a project to amend Property Tax Rule 192, *Audit Selection*. Enclosed is a draft of Rule 192 showing the proposed amendments in strike-out and underscore format.

Effective January 1, 2019, Senate Bill 1498 (Stats. 2018, Ch. 467) amended Revenue and Taxation Code (RTC) section 469 to provide County Assessors flexibility in meeting annual audit requirements. Beginning with the 2019-20 fiscal year, Assessors may meet the requirements of RTC section 469 by completing the four-year total of required annual audits within that four-year period.

As a result, Rule 192 is being amended to include language representative of County Assessors' options in meeting the annual audit requirements.

Interested parties are encouraged to participate in the rulemaking process for Rule 192. Suggested revisions to the draft, in the form of alternative text, should be provided to Alexander Fries at Alexander.Fries@boe.ca.gov or mailed to the above address by December 31, 2022. Upon reviewing the submitted suggestions, it is anticipated that this project will proceed as follows:

- If necessary, staff will meet with interested parties to discuss the language for the rule.
- The Board will hear presentations on issues regarding the language for the rule and vote to place the rule into the formal rulemaking process.

All documents regarding this project will be posted on the Board's website at www.boe.ca.gov/proptaxes/proptaxprojects.htm. If you have questions regarding this project, you may contact Mr. Fries at 1-916-274-3380.

Sincerely,

/s/ David Yeung

David Yeung
Deputy Director
Property Tax Department

DY:abf
Enclosure

Rule 192. Audit Selection.

Authority: Section 15606, Government Code.

Reference: Sections 106, 469 and 470, Revenue and Taxation Code.

(a) DEFINITIONS. For purposes of this regulation:

(1) "Personal property" means all property except real property.

(2) "Business tangible personal property" means personal property used in a profession, trade, or business, and shall include vessels and/or aircraft if used in a profession, trade, or business.

(3) "Trade fixtures" means any fixtures that are used in connection with a trade or business.

(4) "Farming" is a business. When conducting an audit pursuant to this section of a farming or ranching operation, the assessor must determine whether any racehorses taxable to the same taxpayer pursuant to Part 12 of Division 1 of the Revenue and Taxation Code have been underreported or escaped assessment.

(5) "Significant number of audits" means at least 75 percent of the fiscal year average of the total number of audits the assessor was required to have conducted from the 2002-03 fiscal year to the 2005-06 fiscal year, inclusive, on those taxpayers in the county that had a full value of four hundred thousand dollars (\$400,000) or more of locally assessable trade fixtures and business tangible personal property.

(6) "Taxpayers with largest assessments" means taxpayers that have the largest assessments of locally assessable trade fixtures and business tangible personal property in the county for the applicable year of audit selection.

(b) GENERAL PROVISIONS. The assessor must annually conduct a significant number of audits of the books and records of taxpayers engaged in a profession, trade, or business who own, claim, possess, or control locally assessable trade fixtures and business tangible personal property in the county to encourage the accurate and proper reporting of property.

(c) SIGNIFICANT NUMBER OF AUDITS. If the computation of the significant number of audits, as defined in subdivision (a)(5), does not result in a whole number, the number must be rounded before calculating the number of audits that must be performed on taxpayers selected from the pool of taxpayers with the largest assessments and the number of audits that must be performed on taxpayers selected from the pool of all other taxpayers in the county.

(1) Fifty percent of the significant number of audits must be performed on taxpayers selected from the pool of taxpayers with the largest assessments.

(A) This pool of taxpayers must be selected from a list of taxpayers in the county, ranked in descending order by the total locally assessed value of both trade fixtures and business tangible personal property.

(B) The qualified number of those taxpayers for inclusion in the pool must be that number equal to 50 percent of the significant number of audits multiplied by four.

(C) All taxpayers in the pool must be audited at least once within each four-year period following the latest fiscal year covered by a preceding audit and the audit may combine multiple fiscal years.

(D) The assessor is relieved of the requirement to audit the taxpayer at least once every four years if the assessor determines that the taxpayer's assessments are no longer large enough for inclusion in the pool. If such is determined, then the next ranking taxpayer not currently within the pool of taxpayers with the largest assessments must be added to the pool.

(E) The assessor is not required to audit a taxpayer that is fully exempt from property taxation under other provisions of law for purposes of the requirements of this section. Therefore, a taxpayer fully exempt from property taxation must not be included in the pool of taxpayers with the largest assessments.

(2) The remaining 50 percent of the significant number of audits must be selected by the assessor from among the pool of all taxpayers.

(A) These audits must be selected in a fair and equitable manner.

(B) These audits may be based on evidence of underreporting as determined by the assessor.

(3) If the significant number of audits is an odd number, the assessor must determine how to split the odd number audit.

(4) As long as the four-year total number of audits in each category are complete within a four-year period, the assessor may satisfy these requirements by auditing the four-year total of the significant number of audits at any time within that four-year period. The first four-year period begins with the 2019-20 fiscal year.

(d) OTHER AUDITS. Nothing herein shall be construed to prohibit an assessor from auditing the books and records of any taxpayer more frequently than once every four years.

(e) EXAMPLES. The following hypothetical examples illustrate the audit selection process.

Example 1: Prior to January 1, 2009, a county with a total number of mandatory audits of 800 during the 2002-2003 fiscal year to the 2005-2006 fiscal year was required to conduct 200 audits ($800 \div 4$) per year. This county's significant number of audits that must be conducted annually is 150 ($75\% \times 200$). Of the 150 annual significant number of audits, 75 ($50\% \times 150$) must be from the pool of the taxpayers with the largest assessments, and 75 ($50\% \times 150$) must be selected from among the pool of all other taxpayers in the county. The number of taxpayers with the largest assessments that must be audited on a four year cycle is 300 ($150 \times 50\% \times 4$).

Example 2: Prior to January 1, 2009, a county with a total number of mandatory audits of 61 during the 2002-2003 fiscal year to the 2005-2006 fiscal year was required to conduct 15 audits ($61 \div 4 = 15.25$, rounded) per year. This county's significant number of audits that must be conducted annually is 11 ($75\% \times 15.25 = 11.4375$, rounded). Of the 11 annual significant number of audits, 5.5 ($50\% \times 11$) must be from the pool of the taxpayers with the largest assessments, and 5.5 ($50\% \times 11$) must be selected from among the pool of all other taxpayers in the county. The

county assessor must determine how to split the odd number audit. The number of taxpayers with the largest assessments that must be audited on a four-year cycle is 22 ($11 \times 50\% \times 4$). Therefore, during a four-year cycle, the county assessor would be required to audit five from the pool of taxpayers with the largest assessments in the county and six from among the pool of all other taxpayers in the county each year for two years; and six from the pool of taxpayers with the largest assessments in the county and five from among the pool of all other taxpayers in the county each year for the remaining two years.