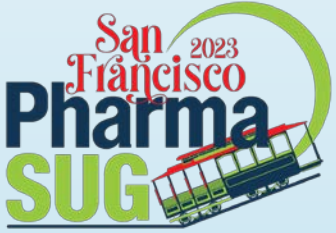


# IRS AUDITS – How to Beat Them



# Lawrence Pon

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- Mr. Pon received his BS in Business Administration from UC Berkeley and MS in Taxation from Golden Gate University in San Francisco

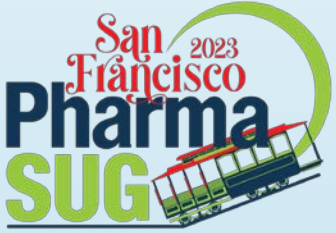
# IRS Audits

- ▶ When the IRS questions /adjusts your tax return
  - You have a balance due
  - You are due a larger or small refund
  - IRS has a question about your tax return
  - IRS needs to verify your identity
  - IRS needs additional information
  - IRS changed your tax return
  - IRS needs to notify you of delays in processing tax return

- ▶ Types of audits
  - Adjustment letter
    - CP-2000
  - Correspondent audit
  - In-person audit







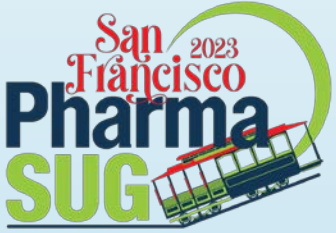
# Respond to the Notice

- ▶ Respond by the specific date
  - Minimize additional interest and penalty
  - Preserve your appeal rights if you do not agree
- ▶ IRS now has the new IRS Documentation Upload Tool
- ▶ Provide the requested information in the letter

# Examination

- ▶ Per the IRS
  - An IRS audit is a review/examination of an organization's or individual's accounts and financial information to ensure information is reported correctly according to the tax laws and to verify the reported amount of tax is correct.
  - The SB/SE Examination employees are to ensure consistent application of policy, procedures, and tax law to effect tax administration while protecting taxpayers' rights.



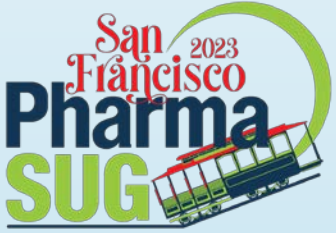


# Initial Contact

- ▶ IRS Letter 2205 – your tax return has been selected to be examined.
- ▶ Scheduling the appointment
  - Hold appointment within 28–35 calendar days of the first action of the case.

# IDR

- ▶ Information Document Request (Form 4564-IDR)
  - List of documents and information
  - If too vague or non-specific
    - Request a modification of the information being examined
    - Prove that it is not necessary for a proper examination



# Time and Place of Exam

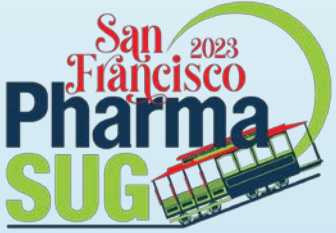
- ▶ Teleconference
- ▶ Meet at representative's office
- ▶ Prefer not at taxpayer's home or office
  - Taxpayer states **in writing** that the examination would unduly disrupt business operations or force it to close
- ▶ Avoid rescheduling appointments
  - **NEVER NO SHOW**

# Timely Actions

- ▶ Set expectations regarding timely actions and assistance if encountering problems
- ▶ Make sure the representative understands the Internal Revenue Manual provisions
- ▶ Problem solving

# Inspections and Probes

- ▶ IRS agent insists of an inspection of taxpayer's business premises and interior of the client's residence
  - Business tour required?
    - Tours should not disrupt business operations or interfere with taxpayer's interactions with customers
    - Per IRM, inspection of the interior of the home is not required
    - Consideration should be given to the cost effectiveness and practicality of conducting the tour
    - Consider alternative
      - Video, photo tours, floor plans



# Reasonable Determinations

- ▶ Substantiation for deductions
- ▶ Taxpayers have burden of proof
- ▶ Recordkeeping requirements
- ▶ Close approximation?
  - Reasonableness of expenditures
  - Reliability and accuracy of the taxpayer's records
  - General credibility of the taxpayers' statements in light of the entire record in the case

# Penalties

- ▶ Negligence penalty
  - Audit indicators of negligence?
  - Recognizing noncompliance
- ▶ The decision to assert penalties must have a legal basis in the IRC
- ▶ Taxpayers have the right to challenge the examiner's conclusion

# Negligence

- ▶ History of noncompliance
- ▶ Failure to keep adequate books and records
- ▶ Inadequate internal controls for processing and reporting business transactions
- ▶ Unreported or understated income
  - Combined with taxpayer's failure to offer a reasonable explanation
- ▶ Overstated deductions or credits
  - Claiming clearly improper or exaggerated amounts, unsubstantiated by facts or documentation
- ▶ Using deduction descriptions in such a manner as to conceal the true nature of the deduction
- ▶ Failure to explain items questioned by the Service



# Fraud

- ▶ Always intentional
- ▶ Intent to evade tax
- ▶ False explanations regarding understated or omitted income
- ▶ Large discrepancies between actual and reported deductions
- ▶ Concealment of income sources
- ▶ Numerous errors – all in taxpayer's favor
- ▶ Fictitious records or other deceptions

# Fraud

- ▶ Large omissions of personal service income
- ▶ False deductions, exemptions, or credits
- ▶ Failure to keep or furnish records
- ▶ Incomplete information given to the return preparer
- ▶ Large and frequent cash dealings
- ▶ Verbal misrepresentations of the facts and circumstances

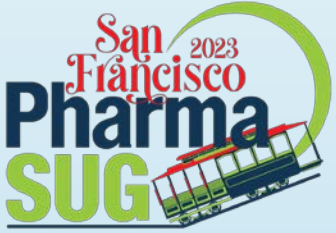


# Audit Conclusions

- ▶ No change
- ▶ Agreed
- ▶ Disagreed

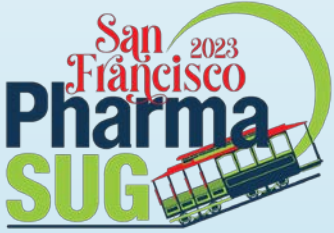
# Disagreed Case

- ▶ Group manager review
  - Discuss disputed issues
  - Attempt to resolve issues
  - Obtain agreement
  - Limit taxpayer burden



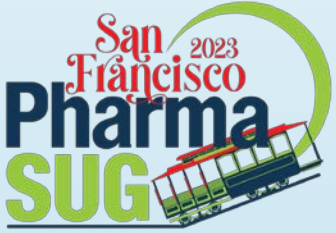
# Resolution Options

- ▶ Fast Track Settlement (FTS)
  - If eligible
- ▶ Formal appeal with Office of Appeals
- ▶ Pay the deficiency and file a claim for refund
- ▶ Receive a notice of deficiency and file a petition in the United States Tax Court



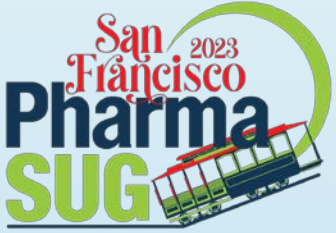
# Fast Track Settlement

- ▶ Expedite case resolution
  - Voluntary mediation program
    - Resolve tax dispute more quickly than traditional appeal
- ▶ Appeals mediator will facilitate settlement discussions
  - Since voluntary, the Appeals mediator cannot force taxpayer or IRS to participate or accept a proposed agreement
  - If unable to resolve dispute through Fast Track
    - Still have right to request traditional appeal or a conference with an IRS manager
- ▶ Goal is to resolve cases with 60 days Fast Track application accepted



# Fast Track Settlement

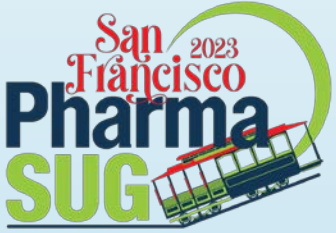
- ▶ Publication 5022 – Fast Track Settlement: A Process for Prompt Resolution of Small Business and Self Employed Tax Issues
- ▶ Form 14017 – Application for Fast Track Settlement
- ▶ Revenue Procedure 2017–25



# How to Avoid an IRS Audit

- ▶ Fill out all tax forms completely
  - Use the right forms
- ▶ File your tax returns on time
- ▶ Keep good records
- ▶ Do not lie
- ▶ Report all your income
  - Forms 1099
- ▶ Understand the tax rules
  - Claiming business losses?





# How to Avoid an IRS Audit

- ▶ Hot topics
  - Charitable contributions
  - Math errors
  - Basis of assets sold
  - Loss limitations
    - Passive losses
    - Partnerships
    - S corporations
  - Tax credits
    - Child tax credits
  - Home Office deductions
  - Business mileage and travel

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