THIENEL LAW LLC

THE ULTIMATE GUIDE TO SURVIVING A FEDERAL TAX AUDIT IN 2023

A free resource from Thienel Law, LLC

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Introduction

Steve Thienel

If you are reading this, you may have just received notice that one or more of your tax returns are going to be audited. While this can be a stressful time, please -- **Don't Panic!**

"Don't Panic" are probably the first two words I say to anyone that comes into my office to meet with me about an IRS tax audit. You will read those words throughout my book, and I encourage you to take those words to heart.

Being nervous about an IRS audit is understandable. A simple piece of correspondence with the word "audit" from the IRS can cause even a seasoned tax professional to be a little nervous when the audit is being conducted on their personal tax returns. However, the reason that I advise my clients not to panic is that a tax audit is more about numbers and documents than trials and prison. Only people who have committed serious tax crimes might need to panic a little bit (and hire a fantastic tax attorney).

The average person facing a tax audit simply needs to be prepared. Being prepared and organized are two concepts you will also notice throughout this book. IRS auditors want two things — answers and documentation. If you can provide the answers they need with the documentation to verify the information you are providing; your tax audit should go smoothly. Of course, that assumes you are not in the category above in which you have tried to hide something or defraud the government. If so, don't panic yet and call my office immediately so we can plan a strategy for helping you.

Otherwise, I wrote this book to help individuals like you who may be facing an audit learn more about the IRS audit process and how to protect yourself during the process. I encourage you to read the information contained in the book, but also caution you that the book is not a substitute for legal advice. Each situation is unique; therefore, nothing you can find in any book about tax audits can substitute for the advice, support, and guidance you can receive by meeting with me in person.

I hope you find the information in this book helpful and I look forward to speaking with you personally if you have questions about an IRS tax audit.

Steve Thienel

Chapter 1

What is an IRS Audit?

Filing tax returns with the Internal Revenue Service (IRS) is a yearly requirement for most adults and businesses in the United States. As the old saying goes, "Nothing is certain except death and taxes." The quote is usually attributed to Benjamin Franklin as he was writing about the durability of America's new Constitution.

Today, those words still ring true, and the quote is repeatedly used when discussing the IRS and taxes. Before we dive into specific information about how you can survive a tax audit by the IRS, it may help to have a general overview of an audit and the types of audits used by the IRS.

What is a Tax Audit?

The Internal Revenue Service (IRS) is the agency charged with processing and reviewing personal and business tax returns for the federal government. Thousands of employees work for the IRS in different departments, including the audit department. On average, the IRS audits over one million tax returns each year. However, it does not mean that an individual or a business has committed tax fraud or other crime because their return or returns are under an IRS audit. The IRS flags tax returns for audit for a variety of reasons including:

- ✓ Failing to report income
- ✓ Claiming excessive losses
- ✓ Errors in mathematical calculations
- ✓ Issues related to business income or loss
- ✓ Claiming excess charitable donations
- ✓ Issues related to dependents claimed on the return
- ✓ Returns that relate to other individuals being audited, such as business partners
- ✓ Randomly chosen tax returns for auditing

I discuss the reasons why your tax return may be chosen in Chapter 2 in more depth. In this chapter, I discuss IRS tax audits in a broad overview before delving into each topic in the succeeding chapters.

In the simplest terms, an IRS tax audit is a more detailed review and examination of your tax return or tax returns. You can be audited for one year or multiple years. After the audit begins, the auditor could request a review of additional tax returns based on the information the auditor discovers during the audit.

An auditor may ask for the documents you used as the basis for your income and deduction claims – be sure to keep those on hand for at least 5 years.

During the audit, the IRS auditor reviews your financial records, including all sources of income and evidence of all claimed exemptions and deductions. In some cases, an IRS tax audit may be limited to one or two specific issues. The purpose of the review is to determine if the information you reported on your tax returns was reported correctly and accurately according to the tax laws. Another purpose is to ensure that based on the correct information, you paid the required taxes under the applicable Tax Code.

Types of Tax Audits

There are three main types of tax audits that the IRS conducts. These include: tax audits by mail, in-office tax audits, and field audits.

Tax Audits by Mail

Most of the tax audits conducted by the IRS are conducted entirely through the mail. Correspondence audits are often used when the IRS has questions about a specific issue with your tax return, or it needs additional documentation to verify the information reported on your tax return. The IRS representative provides you with a detailed list of the information and/or documentation that the IRS requires for the audit. The auditor provides a deadline for you to submit the requested information and documentation to the IRS.

In most cases, submitting the information and documentation is all that is required to complete the audit. You may have a brief telephone conversation with the auditor to discuss the information and documentation you provide in response to the IRS request, but you should not be required to meet with the auditor in person unless other issues arise during the audit.

In-Office Tax Audits

Some audits are conducted in an IRS office. In-office tax audits are used in cases in which the IRS requires a more detailed explanation of an issue. The auditor believes the information required cannot be gathered from requesting an answer in writing or a copy of a receipt or other document. In most cases, the auditor provides a detailed list of documentation for you to bring to the meeting. Although it is not required, you also have the right to bring an accountant or tax attorney with you to the meeting.

> *"Most IRS tax audits are conducted entirely through the mail."*

Field Audits

Field audits are the types of audits that most people think about when they read or hear the words "IRS Audit." They imagine IRS agents storming their home and office seizing documents and electronics. This scenario does not happen in a typical IRS field audit. However, field audits are the types of audits used when the IRS identifies a major problem or red flag with a tax return.

You will typically deal with a single auditor who will provide a list of requested documents in advance so you can be well-prepared.

Even though field audits are the most daunting and time-consuming types of audits, a single auditor usually conducts the field audit unless the audit involves a large corporation. During the field audit, the auditor comes to your home or business to conduct an in-depth review of your financial records. The audit may take several days and require your full attention during those days. In most cases, the auditor provides a list of information and documentation in advance of the visit so that you can prepare for the audit.

Again, you are not required to have a representative present during a field audit; however, it can be a great advantage to have your accountant, tax preparer, and/or tax attorney present during the audit. In addition, working with a tax professional or tax attorney to prepare for an IRS field audit can also reduce some of the stress you may experience and reduce the risk of additional issues arising during the audit.

Having an experienced tax professional by your side during an audit can help alleviate stress and streamline the process.

The key to any IRS audit is not to panic and to seek legal counsel from an experienced tax law attorney if you have questions or concerns about the audit or your legal rights under the Federal Tax Code.

Surviving a Tax Audit

It may seem as if the purpose of an IRS tax audit is to find evidence of fraud or tax crimes that can get you into trouble. However, most audits are conducted because the IRS requires additional information, or you were randomly selected for an audit. Regardless, you need to treat an audit by the IRS very seriously, even a correspondence audit. Your actions throughout the audit process can have a significant impact on the outcome of the audit. Most audits result in a change in the tax return that was originally filed, but that does not mean you committed a crime. For most people, the result is a payment owed to the IRS for taxes, penalties, and interest.

In the next few chapters, I review why you may be chosen for an audit and how that reason could impact the audit. I also review how to prepare for an audit and some of the things that you can do to reduce your risk of being audited in the future. The key to any IRS audit is not to panic and to seek legal counsel from an experienced tax law attorney if you have questions or concerns about the audit or your legal rights under the Federal Tax Code.

Chapter 2

How Does the IRS Choose People for an Audit?

When you receive a notice of an audit by the Internal Revenue Service, your first instinct may be to think that the IRS is out to get you. However, that is not the case. An IRS agent is not sitting in a room somewhere searching through returns to target certain people. The IRS selects tax returns to be audited for a variety of reasons.

Choosing Tax Returns for Auditing

The software the IRS uses to flag returns for auditing identifies tax returns that could have potential errors or incomplete information. In addition, other programs used by the IRS randomly select tax returns for auditing. If a return is flagged for an audit, an experienced auditor reviews the return. The auditor may accept the return, and you never know that you came very close to receiving an IRS audit notice. However, if the auditor notices anything questionable, the return is assigned to an examining group for auditing.

In Chapter One, we referenced a few of the reasons why a tax return could be audited. In this chapter, we review those reasons in more detail, including learning about IRS audit triggers that could be the cause of your IRS audit.

> "One of the common reasons for IRS audits is mismatched information."

Potential Reasons for an Audit by the Internal Revenue Service

In this section, we discuss some of the reasons the IRS might target your tax return for an audit and how you might avoid an audit by changing the way you prepare your taxes.

Information Reported by You Does Not Match Information Reported by Other Sources

One of the common reasons for IRS audits is mismatched information. If your tax return contains information that does not match the information reported by other sources, you may receive an IRS CP2000 Notice. The CP2000 Notice is not a notice of an audit. It is a notice requesting additional information because the information on your return does not match the information reported to the IRS from employers, financial institutions, banks, and other sources of income. If you follow the instructions on the form to correct the information on your return or establish that the information reported to the IRS was inaccurate, the IRS may not proceed with an audit.

However, the IRS may determine that it needs to perform an audit because your explanation was not sufficient, or another issue arises that supports the decision to perform an audit. Mismatched information is a huge trigger for tax audits because this indicates to the IRS that you underreported your income and potentially owe additional taxes. Therefore, always review your W-2s, Form 1099s, and other statements you receive from any financial sources for mistakes, and then make sure the information is accurately reported on your return.

> "Mismatched information is a huge trigger for tax audits because this indicates to the IRS that you underreported your income."

Always know who you are doing business with – an audit of their activities can trigger an audit for YOU!

Potential Reasons for an Audit by the Internal Revenue Service

Related Tax Returns

Another reason why your tax return may be audited is if another person you are financially associated with undergoes an audit. For example, if you receive a Schedule K-1 from a partnership and a partner or the partnership is audited, your tax return may be audited too. The IRS may not believe that you reported anything incorrectly or failed to report information, but it is conducting the audit of your tax return to ensure information reported is accurately reported across any returns that affect another return.

IRS Triggers

Many of the other reasons why your tax return may be flagged for audit fall under the category of "triggers." Triggers are things on your tax return that may increase the chances of your return being flagged by the software the IRS uses to analyze certain aspects of tax returns. Some of the common triggers that can flag a return for an audit include:

- **Large Charitable Donations —** If you make significant donations to charity, you need to have written evidence of those donations. The IRS looks carefully at returns with large charitable donations when the donation equals a high percentage of the person's income. The agency also flags donations when the amount claimed does not match the type of donation (i.e. $5,000 for clothing to Goodwill).

- **Schedule C —** Being self-employed can increase your chance of being audited; however, there are items that you report on Schedule C that may increase the chance of an audit even more. For example, if you report too many losses on Schedule C, your return may be flagged for an audit. Claiming a home office deduction and excessive entertainment/travel expense are also areas that the IRS reviews very carefully. In addition, claims for expenses that are obviously not related to your business (i.e. claiming a large deduction for cleaning supplies when you are a writer).

- **Using Round Numbers —** Very rarely do all your deductions and expenses end in "0" or "5." However, some taxpayers round numbers to the closest amount by 5s or 10s. You may not be adding but a few dollars to round up your expenses, but by doing so, you may increase your chance for an IRS audit.

Potential Reasons for an Audit by the Internal Revenue Service

IRS Triggers (Cont'd)

- **Higher Incomes or Very Low Incomes —** It may not seem fair, but as your income increases, so does the chance you may be audited. There is absolutely nothing you can do to reduce this risk unless you want to reduce your income. On the other hand, if you substantially reduce your taxable income through deductions, you could also increase your chance of an audit for having a suspiciously low income.

- **Claiming Dependents Twice —** If you claim a dependent that is claimed on another return or claim a dependent that filed his or her own tax return, the IRS will investigate. The IRS is very good at matching social security numbers. You may or may not be audited, but the risk of an audit increases when dependents appear on more than one tax return.

- **Using Large Amounts of Cash —** If you use cash to make a major purchase, usually over $10,000, be prepared for an audit. Some institutions are required to report transactions involving cash in the amount of $10,000 or more. Operating a cash business in which your clients do not issue Form 1099s to you for services can put you on the IRS radar too.

- **Foreign Accounts or Assets** — Taxpayers who have assets or accounts in a foreign country attract the attention of IRS auditors too. While there is nothing you can do about this, you can make sure that you comply with all reporting requirements and have sufficient documentation to prove you complied with all tax laws.

- **Above Average Itemized Deductions** — Taxpayers who itemize deductions can lower their tax liability. However, if your itemized deductions are higher than average or higher than expected for someone in your income bracket, your return may be flagged for an audit.

- **Using a Tax Preparer with Questionable Ethics.** The IRS knows which tax preparers have reputations for filing "aggressive" tax returns. If you were attracted to your tax preparer due to the preparer's reputation for obtaining oversized refunds for his clients, then the IRS likely will be attracted to you for the same reason.

Speaking with a tax attorney early on in the process can often clear up issues without a full-blown audit.

Can You Avoid an Audit by the IRS?

There are many more triggers that could potentially prompt an IRS audit, including some triggers that tax professionals may not realize are on the IRS radar. However, if you have questions about whether something increases your chance of an audit, you should speak with a tax attorney or other tax professional. Even though you cannot completely control whether your tax return may trigger an audit, you can be prepared with organized documentation if your return does contain one or more known triggers for audits.

Chapter 3

What Happens During an IRS Audit?

Receiving a notice from the Internal Revenue Service (IRS) that you are under a tax audit can be very intimidating and frightening. As I said in the introduction, “Don’t Panic!”

It may be difficult not to panic a little bit at the thought of an IRS agent combing through your financial records, checking every entry on your tax return, and searching for evidence of tax crimes. However, most auditors are not approaching your audit as if you are a criminal who broke the law or committed tax fraud. Auditors are searching for explanations and documentation. Even if you made a mistake on your tax return, the auditor is not going to handcuff you and take you away. You most likely will be required to file an amended return to correct the mistake and pay any taxes owed plus interest and penalties.

To help alleviate some of your fears about being audited by the IRS, we are going to review what happens during a typical audit in this chapter. Remember, each audit is different. The information below is a general overview of what happens during a basic IRS audit. A tax attorney can help you understand your rights and responsibilities based on your unique situation.

Field Audits by the IRS

We will discuss a field audit since these types of audits are usually the most time-consuming IRS audits that also cause substantial anxiety for many taxpayers.

You will receive written notice from the IRS if your tax return is chosen for an audit. In some cases, the agency may request information or documentation before the field audit. It is crucial that you read the notice carefully to ensure you comply with each instruction in the notice.

If you are instructed to contact the IRS by a certain date, you must do so, or you could face an automatic determination of taxes owed and other penalties.

If the notice instructs you to submit records by a certain date, you need to ensure the documents are mailed in time to make it to the IRS office before the deadline. The notice is your first chance to demonstrate to the IRS auditor that you are treating the audit process seriously and you are cooperating with the audit.

Many taxpayers choose to contact a tax attorney when they receive the notice of an audit. Remember, you have the right to have your tax attorney, CPA, or other tax professional at the field audit.

The Day of the Field Audit

On the day of the field audit, an IRS Revenue Agent comes to your home or office to meet with you and review your financial records. These agents are highly-trained and typically have more knowledge and skill in accounting and tax laws than other agents. In many cases, the auditor provided a list of documents and information the auditor wants to review during his or her visit with the notice or in subsequent letters. You need to make sure that you have all documentation requested by the auditor organize and ready for his or her review.

Be Organized and Have Documentation Ready

Organizing the documentation and labeling it in the same order as the request for information can make the audit proceed smoothly and more quickly. Examples of documentation that you may be required to submit for review include, but are not limited to:

- ✓ Bank records
- ✓ Investment statements
- ✓ Statements for other accounts that produce interest or dividends
- ✓ Your copies of 1099s, W2s, or other earning statements
- ✓ Profit and Loss Statements
- ✓ Balance Sheets
- ✓ Receipts or other evidence of your deductions, expenses, and exemptions
- ✓ Records for contributions to charities, retirement accounts, and other non-taxable funds

Read Your Audit Notice Carefully!

Typically, the notice includes the dates covered by the audit. For instance, you may be required to provide copies of all bank statements from December 2016 through January 2018 if your 2017 tax return is being audited. It is imperative that you replace any documents that are missing. For example, if you need proof of charitable contributions, but you cannot locate the receipt from the non-profit organization, immediately contact the non-profit to request a duplicate copy. You should use the list of documentation provided to you by the auditor before the visit as a checklist. You must make sure that every item on the list is checked off and ready for inspection by the auditor.

During the Audit

During the audit, the IRS agent may ask questions about the documentation. For this reason, it is usually in your best interest to have a tax attorney and/or your accountant with you during a field audit. For businesses, the auditor may interview employees and tour the business.

Field audits can indicate a serious problem with your tax returns. When an auditor chooses to come to your home or business to conduct the audit, the auditor may suspect tax fraud and wants to view your home or business while conducting the audit. Therefore, consulting an experienced tax attorney in advance of the field audit is usually in the taxpayer's best interest.

Audit Basics

The audit could last just one day, or it could go on for several days or weeks depending on the taxpayer and the volume of information to review. For most individual taxpayers, field audits typically last between two to three days. However, field audits for businesses could take one to two weeks to complete depending on the size of the business and the scope of the audit.

At the Conclusion of the Field Audit

The auditor generally takes copies of documents back to the IRS to complete the audit and prepare a report. There is nothing for you to do after the conclusion of the field audit but wait until you receive the findings of the audit from the IRS.

Are In-Office Audits Different from Field Audits?

In-office audits are conducted in the same manner as a field audit, but you must go to the local IRS office to meet with the auditor. It is your responsibility to bring all documents requested by the auditor to the meeting. In some cases, the auditor may request additional follow-up information after the first meeting. As stated above, field audits tend to be more intrusive and may indicate a more serious issue with a tax return. In the next two chapters, I discuss in more depth how you can help yourself during a tax audit and the potential outcomes of the audit.

Chapter 4

What Should I Do to Help Myself During an IRS Audit?

Don't Panic! I cannot stress this particular tip enough, so I say it often, and I even put the phrase at the beginning of the book's title. You cannot change the fact that you are being audited by the Internal Revenue Service (IRS). Panic is an emotion that you do not need to focus on at this moment. Your focus should be on preparing for the audit. Therefore, one of the first questions to ask yourself is, "Do I need to hire a tax attorney to represent me during the audit."

As an experienced tax attorney, my response is, "Yes, you need to consult with a tax attorney immediately." Does consulting with a tax attorney mean that you need an attorney? Not necessarily. If you meet with an honest, reputable, experienced tax lawyer like myself, he will review your case and give you an honest opinion about your chances of winning the IRS audit with and without an attorney. Remember, I said that you should definitely "consult" with a tax attorney as soon as you receive an IRS tax notice, but I did not say you needed to hire an attorney immediately.

What is the Single Most Important Step You Can Take to Protect Yourself?

One of the most important things you can do for yourself if you are being audited is to become educated about the IRS audit process, your legal rights, and the steps you need to take to protect yourself during the audit. I cover some of those topics in this book; however, each situation is unique and to provide legal advice to a specific person without reviewing that person's situation would be unwise.

Use the information in this book as a guide; however, contact my office immediately if you receive an IRS tax audit to schedule a consultation and case review. My goal is to help you survive the IRS audit with the least amount of stress for you while keeping as much money in your pocket as possible. To further that goal, I might advise you that you may want to consider representing yourself if you are dealing with a very small amount of money or a simple error on your tax return that can be easily corrected.

Protecting Yourself During an IRS Audit

For example, if you forgot to include income from a Form 1099 that totals $750, you may owe additional taxes, interest, and penalties after the audit, but the amount may be small if you admit your mistake to the auditor and file a corrected return. Another example of a simple mistake may be transposed numbers on your tax return. You stated your income was $74,589 when the W-2 from your employer states your income as $75,489. Again, admitting your error in transposing the numbers can result in a corrected return and a small amount owed in taxes, interest, and penalties.

However, if the issue being investigated by the IRS auditor is complex, or the issue could lead to additional questions or problems, I will advise you to hire a tax attorney to represent you during the audit.

Welcome Back to "Don't Panic"

Another reason you may need to retain a tax attorney to handle your audit — you are frightened and nervous about the audit to the extent that you cannot be levelheaded, and you could end up incriminating yourself. Think about the IRS audit like a deposition or a courtroom. The agent can use any information you disclose to the agent against you. Furthermore, any information that the agent gathers can be forwarded to the criminal investigative unit for the IRS without your knowledge or consent.

Without an attorney, your anxiety about the tax audit may give the auditor an advantage. IRS agents and auditors are highly-trained professionals who understand the audit process and the tax laws related to the issue being investigated. An experienced auditor could get you to answer questions that you may not need to or want to answer. However, your tax attorney knows better than to answer that question. Therefore, acting on your behalf, your attorney may respond that you need to research that question and get back to the agent with a detailed explanation.

I am not advocating that we do anything wrong, but I am in favor of taking additional time to think carefully about our response to certain questions so that we do not provide the auditor with information the auditor did not request. In some cases, the auditor may have been fishing for information the auditor could use against you and drop the request or never follow up on the request if we request additional time to respond.

You deserve to have a trained and experienced professional acting on your behalf to level the playing field.

IRS auditors and agents are trained professionals with years of experience; therefore, you are at a disadvantage. Don't you deserve to have a trained and experienced professional acting on your behalf to level the playing field? I believe you do and I know you have the legal right to representation.

Tips to Remember If You Decide to Represent Yourself at Your IRS Audit

If you choose to represent yourself during your IRS audit, there are a few key points that you need to remember to help you survive the audit:

Organize Your Records — You do not want to show up for the audit with a shoebox full of paper. If you are not organized, you allow the agent to thumb through your documents looking for information. By being organized, you can hand the auditor the documentation requested and nothing else.

Ask for More Time — You want as much time as possible to prepare for the audit. You may need to request missing records or track down documentation to support the information on your tax return. Request to postpone the audit for at least a few weeks if possible to give yourself ample time to prepare.

Find Out the Reasons for Your Audit — You have the right to know why the IRS is performing an audit. Knowing the reason for the audit may help you prepare for the audit or reconsider your decision to handle the audit without an attorney.

Promptly Respond to All IRS Communications — Every letter you receive from the IRS provides clear instructions about how and when to respond. You must respond by the deadline; however, responding as quickly as possible can demonstrate that you are willing, ready, and capable of participating in the audit.

Avoid Hosting the IRS Agent — It is better for you to go to the local office than to have the IRS agent at your home or place of business. If the auditor demands a field audit, call my office immediately because field audits can be very complex and could result in additional issues and problems being raised during or after the field visit.

Only Answer What is Asked — Treat the audit as if you were testifying in a courtroom. Be polite and cooperative, but only answer the question the auditor asks. Listen to the question carefully, ask for clarification if necessary, and keep your answer limited to the information required to answer that specific question.

Understand Your Legal Rights — If you choose not to hire an attorney, you need to research your legal rights regarding the audit. You can find information about your legal rights in IRS Publication 1 – Rights as a Taxpayer.

Chapter 5

What Happens After the Audit is Complete?

Congratulations! You made it through your audit by the Internal Revenue Service. Now, what happens? Do you need to do anything? The answers to those questions depend on the outcome of your IRS audit. However, until you receive the letter from the IRS informing you of the outcome of your audit, there is not much you can do except wait. For some people, this task may be the most difficult part of the entire audit process.

Even though I cannot speed up the IRS, I can explain some of the potential outcomes of an audit. In addition, I will discuss some of the options that may be available to you once you receive the notification of a decision by the IRS.

If The IRS Needs Additional Information

Don’t Panic! A letter from the IRS requesting additional information or another meeting does not mean that something terrible is wrong. It means the agent needs more information or documentation to complete the audit. As before, try to remain calm, read the letter carefully, and organize the documentation requested.

I would strongly urge that you contact my office to review the letter to make sure that nothing appears to be out of the ordinary. In many cases, the agent is following up on an issue to ensure the agent has sufficient information and documentation to back up the agent’s conclusions. However, as with any notification from the IRS during a tax audit, it is best to obtain legal counsel before proceeding to protect your legal rights and best interests.

IRS Tax Audit Outcomes

After the IRS agent completes the audit, the agent prepares a report and you are notified in writing of the outcome of the audit. The letter from the IRS will inform you of its findings and your rights regarding the audit. In general, there are three ways that the IRS audit can be concluded.

1. No Change

The auditor reviewed the information and documentation provided and does not find any reason for the information on your tax return to be changed. There are no other steps that you need to take regarding the audit. However, you should keep all documentation, including all correspondence from the IRS, stored in a safe location in the event you need the information in the future.

2. Changes Are Required and You Agree with the Changes

The audit discovered errors in your tax return that required the return to be changed. The IRS will send you several forms and notices explaining the changes it alleges are necessary to correct your tax return. Unfortunately, the IRS never does anything the easy way.

The IRS will not simply send you a letter explaining the mistake, how the mistake was corrected, and how much money you owe. Instead, you receive a thick packet of letters, forms, and explanations that are complex and difficult to understand without training in tax law and IRS procedures. The IRS requests that you sign and return the documents if you agree with its findings from the audit.

You must be careful! Signing these forms and returning the forms to the IRS signifies that you agree to the proposed changes and acknowledge that you owe the additional taxes shown on the amended tax return. Depending on the facts and circumstances of your case, you could also acknowledge and agree to other terms if you sign the forms. At this point, if you have not retained an attorney, I strongly urge you to consult with a tax attorney before you sign any of the documents. However, please contact an attorney quickly because you are under a short deadline to respond to the IRS. Your failure to respond may result in an automatic acceptance of the audit results.

3. Changes Are Required and You Disagree with the Changes

If you receive your packet from the IRS and you do not agree with the proposed changes, you have several options available. Again, the IRS does not make any procedure simple. It would be easy if the IRS had only one option for appealing a decision. Instead, you must understand the various options available to you based on the audit's findings. Sorting out the options is only the first challenge you face if you disagree with the IRS audit findings.

Below are several options that might be available to you based on the findings of your specific audit and other factors relevant to your case. Since each case is different, all the options below may not be available for you to utilize if you disagree with the IRS findings.

Fast Track Settlement — This option is a newer option for settling a dispute with the IRS. If you choose this option, your case is assigned to an Appeals officer who acts as a mediator to settle the dispute.

Appeal the Decision — If you disagree with the findings in the IRS letter, you have 30 days to file an appeal when you receive the IRS audit decision letter (often referred to as the 30-day letter). Once the IRS receives your request for an appeal, an IRS appeals officer is assigned to the case. A hearing is scheduled approximately 60 days after you file your appeal. The Appeals Officer will examine any evidence and documentation you present and listen to your arguments as to why the auditor's decision is incorrect. At this stage, you may be able to settle the matter with the Appeals Officer, or you might need to proceed with tax litigation.

90-Day Letter and Tax Litigation — If you cannot settle the matter through the appeal process or you receive a 90-day letter, you have the option of tax litigation. A 90-day letter is usually sent to the taxpayer at the end of an audit when the IRS determines you owe more money in taxes. A 90-day letter may also be sent if you missed the deadline to appeal in the original IRS letter or you have exhausted your options for appeals. Judges instead of juries typically hear lawsuits filed in tax court.

A Tax Attorney Can Help If You Disagree with an IRS Audit Result

IRS auditors and agents are highly-trained, experienced government employees. They understand these forms inside, outside, and upside down. IRS employees and agents know exactly at which step in the process most people make mistakes. However, these agents are not your friends, nor do they provide legal advice. For a trusted advisor who will protect your best interest and fight for a just outcome, you need to retain a tax attorney.

Now What?

The above options may not be the only options available to you if you disagree with the audit findings. In addition, the above discussion is a brief overview of the options you might have available. The specific requirements required to implement each of these options can be very detailed and require numerous forms to be filed with the IRS. Dealing with the IRS can be a difficult process. If you represented yourself during your audit, now may be the time to consult with a tax attorney if you are not going to pay the additional taxes, interest, and penalties assessed against you because of the audit.

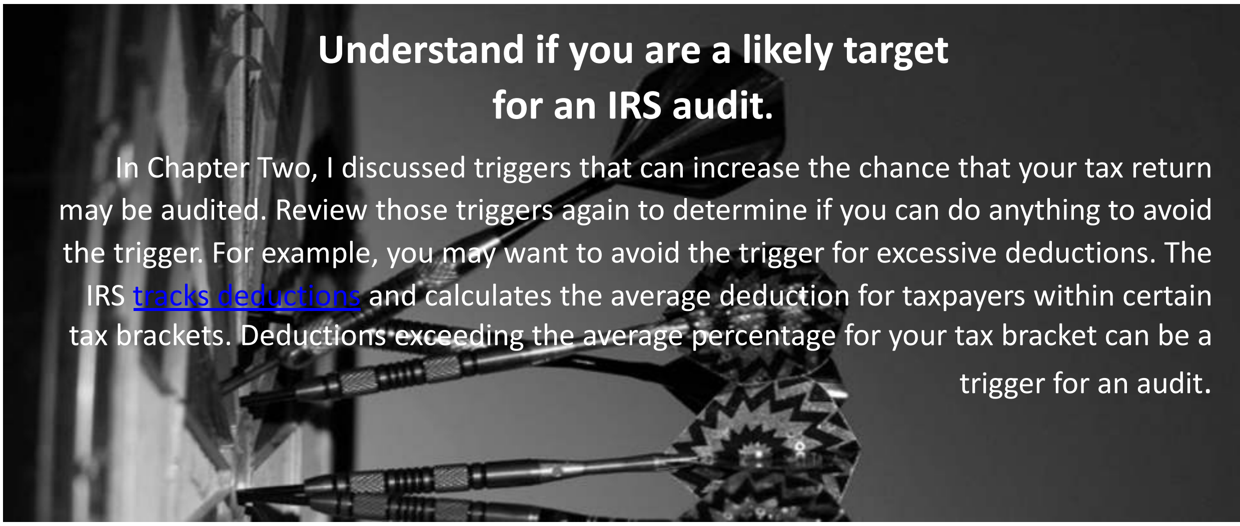
Chapter 6

How Can I Avoid Audits in the Future?

In this final chapter, I want to discuss some tips that might be beneficial for avoiding an Internal Revenue Service (IRS) audit in the future. However, keep in mind, with millions of taxpayers being audited each year by the IRS, there may be no way for you to statistically avoid an audit at least once during your lifetime. In addition, I also want to discuss some tips that can help you to be prepared in the event of an IRS audit.

Tips to Avoid an IRS Audit

Remember, the IRS is unpredictable; therefore, what may work today may not work next week. However, these tips can also help you avoid other finance-related problems with your personal finances or your business finances.



Understand if you are a likely target for an IRS audit.

In Chapter Two, I discussed triggers that can increase the chance that your tax return may be audited. Review those triggers again to determine if you can do anything to avoid the trigger. For example, you may want to avoid the trigger for excessive deductions. The IRS tracks deductions and calculates the average deduction for taxpayers within certain tax brackets. Deductions exceeding the average percentage for your tax bracket can be a trigger for an audit.

✓ Incorporate your Business.

Being self-employed increases your chance of being audited. Consult with a tax attorney to determine if incorporating your business could be a benefit for tax purposes. You may also benefit in other ways, including liability protection.

✓ Try to head-off the audit.

If you anticipate information on your tax return may trigger an audit, file a written explanation and include IRS forms related to the issue, worksheets, receipts, and other documentation to justify the item. The system may still flag your return, but the IRS auditor reviewing the flagged return may clear the flag once the information attached is reviewed and verified.

✓ Avoid filing amendments & corrected returns.

It is always your goal to operate under the radar of the IRS when filing tax returns. Drawing attention to your tax returns can also result in unwanted scrutiny. Therefore, review your return several times for accuracy before filing the return. Filing amendments and corrective returns can trigger flags for a closer review.

✓ Always triple check the math.

Calculation errors and line errors are some of the most common problems found on tax returns. Triple check all calculations, numbers, and line entries for accuracy before filing your tax return.

✓ Use exact numbers.

As discussed in the section on triggers, perfectly rounded numbers in increments of 5 and 10 can attract unwanted attention. Avoid rounding to the nearest 5 or 10 when preparing your tax returns.

Check personal information and sign all forms.

This mistake is simple, but it could cause an IRS agent to look closely at your tax return. You need to make sure that your personal information is correct, especially your name and Social Security Number. The names of your dependents and their Social Security Numbers must also be correct. Also, do not get into such a rush that you forget to sign and date each page that requires a signature.

File completed returns.

Do not leave any questions unanswered or forget to file a form. All lines should be completed, even if the entry is a "0" or a dash to indicate the information requested on that line is not applicable to you.

Hire an accountant or tax preparer.

It is tempting to save money by preparing your own tax returns. However, if your return is more complicated than a 1040EZ, consider hiring a professional to prepare your tax returns.

Understand changes in tax laws.

It is easy to make an honest mistake if you are basing your deductions and expenses on outdated tax law. Make sure that you consult a tax professional to ensure the steps you are taking now to prepare for next year's tax return are not based on outdated tax law.

> When completing your tax returns, be honest. Report all income and do not overstate deductions and credits. You may not be able to avoid a tax audit, but if you are honest when filing your return, you are better prepared if your return is audited.

Do not report zero income or business losses every year.

The IRS knows that you need to make money to survive. If you utilize deductions and business losses to reduce your adjusted gross income (AGI) too low, the IRS could become suspicious and begin reviewing your tax returns for several years to determine if there is a pattern.

Helpful Tips to Prepare for an Audit You May Not Know is Coming Your Way

For some individuals, there is nothing they can do to avoid an audit. Some tax returns are audited by random choice, so we may say those individuals just had a bit of bad luck that day. For other taxpayers, their tax returns contain one or more of the "triggers" that we discussed in Chapter Two that increase their chance of being selected for an IRS audit. Check out these tips that can help you prepare now for something you hope will never happen to you or anyone close to you:

✓ Track large money transfers.

Large financial transfers, especially cash, catch the attention of the IRS. Make sure that you have a detailed paper trail for all large financial transfers between any type of account.

✓ Document Schedule C expenses.

If you are self-employed, or even if you claim a work-related business expense, you need a receipt or other documentation to prove the amount you claimed for a deduction. Personal scanners and online financial software can help make this process easier and more organized.

✓ Document large deductions.

The IRS tracts the average deductions based on each income bracket. If you have large deductions, you need detailed documentation to substantiate the deduction. Be prepared to file copies of that documentation with your tax return as discussed above to help avoid an IRS audit.

More Helpful Tips…

- ✓ **Be very organized.** Being organized is one of the key factors in surviving an IRS audit. When tracking expenses and preparing tax returns, you need to keep everything organized into categories. Online software can make organization easy and quick. In some cases, you can store the copies of your receipts and other documentation as a file attachment to the applicable entry.

- ✓ **Have multiple backup copies.** Whether you are maintaining hard copies of your tax documents or you have all your information and documentation electronically preserved, you need multiple backups in case you lose the original copy.

- ✓ **Maintain detailed income documentation.** Issues related to reporting income are a common reason for tax audits. Regardless of whether you are a W-2 employee, self-employed, own a business, or work odd jobs for cash, you must keep a detailed record of all income. Remember, income includes more than salaries and wages. You need statements for interest-bearing accounts, stocks, annuities, bonds, and any other account that generates income.

The key to being prepared for an audit that you hope never arrives is being organized. The second key factor is to maintain detailed documentation of every financial transaction. The more documentation you have, the better chance you have of surviving an IRS audit successfully. So, if in doubt, store it in a file instead of tossing it out.

A Couple More Thoughts...

Protect your identity. Identify theft can also trigger a tax audit. Review your credit reports from all three credit reporting agencies at least once a year for mistakes or suspicious activity. Consider signing up for a fraud monitoring service, but research the service first to ensure it is a trusted, reputable company.

Document Major Purchases or Transfers. In some cases, a tax audit could involve the purchase or transfer of a large asset. If you sell or purchase a home, boat, or other expensive asset, you need to keep detailed records of the transfer with the tax documents for the year of the transfer, even if the transfer is not required to be reported on the return, just in case any questions arise during an audit.

Wrapping it all up…

Did you panic? I hope not. The IRS tax audit process through the end of the actual audit is not too complicated to understand. You receive notice from the IRS that one or more tax returns are being audited. You are informed of the date, time, and location of the audit and the documentation that you will need to provide to the auditor. Nothing to panic about so far.

During the audit, the IRS agent asks questions, gathers information, and reviews documentation. The agent copies certain documents and the audit is concluded. It does not seem there is a reason to panic yet.

In a few weeks, you receive a notice stating you owe more money in taxes, penalties, and interest because you made a mistake on your tax return. The notice is accompanied by a large packet of documents that appear to be the Japanese version of instructions for a child's bicycle. Is it time to panic yet? No, but it is time to call my office.

There are cases in which I advise clients that they do not need my assistance with an IRS audit. The error with the tax return is straightforward, and they already understand they will owe a bit more in taxes, penalties, and interest. However, as I also explained, I believe that it is prudent to seek the advice of a tax attorney when you receive a notice from the IRS about an audit. Consulting with an experienced tax attorney allows you to get answers to your questions and learn about your options. If it is a simple matter, you can handle it yourself, but it is best to understand what you are facing before diving into an IRS audit without an attorney.

If you intend to appeal an IRS audit decision, I strongly urge you to call my office. Appeals of audit decisions involve very short deadlines and numerous requirements. The rules and the law governing the appeals process can be confusing. Without an experienced tax attorney, your appeal could be dismissed or denied.

As I draw this book to a conclusion, I feel I must say it again, “Don’t Panic.” Being audited by the IRS is typically not as horrible an experience as you may believe. If you have any questions or concerns, I am always available and glad to help.

Call today to schedule a consult.

About Steve Thienel

Steve is a tax attorney with decades of experience consulting with individuals and businesses to ensure their tax issues are addressed with minimal stress. From tax preparation and compliance to assisting with audits and IRS conflicts, Steve Thienel is your partner in tax matters.

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