

Audit?

We can help!



Business owner FAQs about IRS audits

IRS audit rates remain relatively low, but that's little consolation if the IRS selects your return for an examination. Although most taxpayers will never face an audit, business owners often have more complex tax situations that can attract IRS attention. The good news is that with proper preparation, detailed records and professional guidance, you can make the process far less stressful.

Am I at risk for an IRS audit?

The IRS accepts most returns as filed. However, your return may be selected for examination because of discrepancies identified by IRS systems, unusual reporting patterns, information reported by third parties or, in some cases, random statistical sampling.

Business owners should remember that an IRS examination may not be limited to a business tax return. Many small businesses operate as sole proprietorships, partnerships or S corporations (or as limited liability companies taxed as one of those structures). For these entities, business income, deductions and credits flow through to the owners' individual returns. As a result, IRS questions about business activities may arise during an examination of either a business return or an owner's individual return.

While there's no guaranteed way to eliminate your audit risk, the best way to manage an audit is to be prepared. Maintain organized records throughout the year, including

invoices, receipts, bank statements, payroll records, canceled checks and other documentation supporting items reported on your tax returns. Keeping complete records in a central location, whether physical or electronic, can make responding to IRS inquiries much easier.

Which issues does the IRS target?

Some returns are more likely to attract IRS scrutiny than others. Common issues that may lead to questions include:

- Significant inconsistencies between current and prior-year returns,
- Income reported on a tax return that doesn't match Forms W-2, 1099 or other information returns received by the IRS,
- Gross profit margins or expense levels that differ substantially from similar businesses in the same industry,
- Large or unusual deductions compared to income,
- Repeated business losses, and
- Mathematical errors or incomplete information on a return.

Certain deductions often receive closer scrutiny because they have strict substantiation requirements. Examples include deductions for vehicles, travel, meals and home offices.

Pass-through entities also present special audit risks. For example, the IRS may examine whether S corporation shareholder-employees are receiving reasonable compensation or whether owners have sufficient tax basis to claim losses and deductions. Proper documentation is essential in these areas.

How should I respond to an IRS notice?

If your return is selected for examination, you'll generally be notified by mail. The IRS doesn't initiate audits through email, text messages or social media. Be wary of unsolicited messages claiming to be from the IRS — these are likely scams.

Many audits involve a request for documentation supporting specific items reported on a tax return. In some cases, taxpayers may be asked to meet with an IRS representative at a local office. More complex examinations may involve a field audit conducted at the taxpayer's home, business or representative's office. However, most examinations are handled through correspondence rather than in-person visits.

If you receive an IRS notice, it will explain any discrepancies and give you time to respond. Carefully review the request and gather all documents relevant to the items in

question. If records are missing, you'll have to reconstruct the information using other available documentation.

If you're selected for an audit, call us as soon as possible. By involving us early in the process, our experienced tax professionals can help you:

- Understand the issues the IRS is examining,
- Gather and organize the necessary records,
- Communicate with the IRS on your behalf when appropriate, and
- Respond to the examination efficiently and effectively.

In most situations, the IRS has three years after a return is filed to assess additional tax, though longer periods may apply in certain circumstances. Because examinations often occur well after a return has been filed, you should retain finished returns and any supporting documentation for the appropriate period. As a general rule, you should hold on to tax records for at least six years after they're due or filed, whichever is later.

However, you should keep certain tax-related records longer. For example, keep records related to a bad debt deduction for seven years. And keep copies of your tax returns and other proof of filing indefinitely to document that you filed. (There's no statute of limitations for the IRS to assess tax if you didn't file a return or you filed a fraudulent one.)

Am I audit ready?

Don't let the possibility of an audit keep you up at night. Most IRS examinations are routine and manageable when taxpayers maintain accurate, detailed records and respond promptly to IRS inquiries.

If you receive an IRS notice, we can help you prepare for an examination and represent your interests throughout the audit process. Or if you simply want to strengthen your recordkeeping and tax compliance processes, contact us to assess your audit readiness and identify opportunities for improvement.