



# Waldron H. Rand & Company, P.C.

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## Why You Shouldn't Fear an IRS Audit

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*From Waldron Rand's April 2012 Newsletter: Accelerating Business Success*

You think you've done everything right, submitted your tax returns on time, worked closely with your accountant and kept track of your expenses all year and then suddenly, you find yourself in receipt of a notice from the Internal Revenue Service (IRS) or State Taxing Authority... something is wrong. Your tax return is being reviewed. First thing you must do is stay calm. There's no need to panic since it's likely that this is either a random check or they simply need to confirm some data.

It's likely that you have never received a tax notice or experienced an audit so the fear of the unknown will play a huge role in how you react. You may be wondering, "What do I NOT know that they are going to find out?" It is the responsibility of the Federal and State Taxing Authorities to verify that all information presented is correct. Therefore, if you made your best effort to be honest in completing your tax returns, then even if you did do something wrong, you may not be penalized. Large penalties are typically incurred when the auditor can prove that the mistake was a willful act and you knew you were doing something illegal.

There are a variety of reasons why your returns might be reviewed. It could be a random check or you could have mistyped a number on a form or required documentation is missing. For example, if a 1099 form is missed and you filed a return on time, then the IRS might send you a notice – just to let you know that you missed the form and your return needs to be changed to include it. The auditor might seek backup information to support something that seems unusual like a high charity to income ratio or a sudden spike in your deductions. Standard compliance checks are performed on payroll and 1099s so if you are asked questions related to these topics, it may be a simple routine check based on computer matching.

From the taxpayer's perspective there is basically no difference between a State or an IRS review. There are, however, four different types or levels of reviews. The first two are pretty basic and can generally be handled by simply responding to the request. The last two audits are more complicated and definitely require representation from an accountant or a lawyer specializing in tax issues and representation.

- 1) **Notice** – With notices the auditor is usually looking for a response to some basic questions, like there is missing information on your return. To meet their needs, respond to their questions as soon as possible and make corrections to your filing, if necessary.
- 2) **Desk Audit** – In this case, the auditor will ask you to send them specific information or documentation. Once again, a quick response with the information they are seeking will

usually satisfy the auditor's needs. Depending on the outcome, changes may or may not be required on your returns.

- 3) **Issue Audit** – This is where it becomes more complicated. The auditor will request a meeting or a visit to your office (in the case of a business) and will provide you with a list detailing the information they are looking for. Generally these are either random checks or based on a specific item on your return. The review is usually focused on a certain area of the return. It's best to seek professional advice if you receive an Issue Audit notice.
- 4) **Project Audit** – This is a more complex audit where the auditor will request a visit to your office to review all of your documents. This is a major endeavor and can last 6 to 9 months. You definitely will need professional support managing a Project Audit. Typically the largest costs end up being your lost time and the cost for representation. Expect the auditor to review everything in detail, especially anything out of the ordinary. It is typical for companies with over \$10M in revenue to be audited every 6 to 8 years. As your annual revenues increase, your audits can become more frequent. Please note that S Corporations and partnerships are a current focus of the IRS.

### **Six Tips To Keep You Calm**

Below are six tips to help you get through the audit process:

- 1) **Respond Quickly.** Gather all documents as quickly as possible to support your tax return. Expect the auditor to ask for basic information (i.e., W-2s and 1099s for individuals and your general ledger, balance sheets and income statements for businesses). They will provide you with a list of the expected items.
- 2) **Seek Expert Advice.** Do not try to do this yourself. Always get expert advice from your accounting firm. The auditor and your accountant speak the same language. For more complicated audits you may need advice from an expert whose focus is tax law.
- 3) **Be Patient.** The IRS and State do not move quickly. It could be sixty days before they read your letter of response. They'll keep sending you collection notices so stay on top of this. Don't get frustrated.
- 4) **Appeals are An Option.** If you do not like the result of your audit, you do have the option to appeal. The decision of the auditor is not binding. However, going to tax court can be expensive and a long process, which will probably involve engaging tax attorneys. Decisions can be adjudicated on tax matters because it all comes down to the interpretation of the tax code.
- 5) **Cooperation is Critical.** Carefully review all of your information to see if there's something that you inadvertently missed. If you find something, let the auditor know immediately because self-disclosure always works in your favor. This sends a clear message that you are cooperating and trying to do the right thing. It's better to work with the auditor and not against them.
- 6) **Change Behavior.** If the auditor finds errors on your return you **NEED** to change your behavior. If sales or meal taxes were a concern, you can be certain the State will be scrutinizing this information carefully in the future so make sure you are doing this properly. They will be back to check on you.

Finally, we cannot emphasize enough the importance of addressing every tax notice you receive. If you can't respond with all the information, be upfront and let them know that you are working on gathering the information and will get it to them at a specific time. Do not ignore the request no matter how minor it may seem. They won't forget that you owe them information or a response.

### **About the Author, Anthony Librot, CPA, MSF**

Anthony (Tony) Librot provides accounting, audit, corporate tax, and management advisory services to a diverse client base in varying industries including real estate, hospitality, technology, and manufacturing. He combines his experience serving both public and privately held companies to provide value-added financial, operational, and tax advice. Prior to joining Waldron Rand in 2002, Tony worked at KPMG, LLP where he gained national firm experience serving Internet, communication, and software companies.

Tony holds a B.S. in Business Administration from Colby-Sawyer College and an M.S. in Finance from Suffolk University. He is a frequent speaker at industry group forums on topics relating to accounting and finance and is a guest professor at Colby-Sawyer College where he serves on the Colby-Sawyer President's Advisory Council. Tony is a member of the Dana Farber Leadership Council and the Accounting and Auditing Committee of the Mass. Society of CPAs.

### **About Waldron H. Rand & Company, P.C.**

Waldron Rand, located in Needham, MA, provides unmatched accounting, auditing, tax, and consulting services to individuals and privately held businesses in a wide range of industries throughout the U.S. and globally.

At Waldron Rand, our business, tax and assurance experts are more than scorekeepers. We take a holistic approach to working with clients. For more than 100 years, we have been providing partner-level service to help our clients manage challenges and seize business opportunities.

For more information or to personally speak with a partner, please call 781.449.5825 or email us at: [advice@waldronrand.com](mailto:advice@waldronrand.com).

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