

THE 12 RED FLAGS THAT INCREASE THE PROBABILITY THAT IRS WILL EXAMINE THE RETURN

- A. Making too much money – While the overall exam rate is around 1%, if income is over \$200,000 the rate goes up to 3.7%. Returns with income in excess of \$1,000,000 will get a visit from the IRS 12.5% of the time.
- B. The IRS computers have gotten very good at matching 1099s and W-2s to the return. Make sure all forms are reported correctly.
- C. Large charitable deductions compared to the averages will raise the red flag. Several of the software packages today are set up to monitor those variances.

Adjusted Gross Income	Medical Expenses	Taxes	Interest	Charitable Contributions
\$15,000 to \$30,000	\$7,074	\$3,147	\$9,245	\$2,024
\$30,000 to \$50,000	\$6,153	\$3,830	\$9,055	\$2,189
\$50,000 to \$100,000	\$7,102	\$6,050	\$10,659	\$2,693
\$100,000 to \$200,000	\$9,269	\$10,798	\$13,734	\$3,757
\$200,000 to \$250,000	\$21,554	\$18,164	\$18,570	\$5,895
\$250,000 or more	\$37,143	\$50,267	\$27,865	\$20,930

- D. The home office deduction continues to be a major issue for IRS not because it is a complicated deduction but because many taxpayers have poor records; this may be remedied with the new standard deduction for 2013.
- E. Rental real estate losses have grown into an especially thorny issue in the past several years. If you are a “real estate professional” IRS continues to look at these returns more closely, make sure your time records are in good order.
- F. Nothing is more cherished than the business meals, travel and entertainment deduction, but the record keeping standards are high and IRS often strike gold when challenging M & E on the self-employed tax payer’s return.
- G. Claiming 100% of vehicle usage is sure to cause the auditor to take a second look. Keep complete records in this area. i.e. mileage log, receipts.
- H. Filing a Schedule C with large losses consistently makes the IRS think hobby loss. Businesses experience losses but if it looks like those businesses might be fun, get ready for the IRS challenge. A business plan should be put together for any business that is part-time or appears to have a significant element of personal pleasure.

- I. Businesses that are primarily cash income continue to be a favorite target of the IRS. In 2010 IRS published the Cash Intensive Businesses Audit Technique Guide. One of the best ways to equip your cash intensive business to survive an audit is to review the ATG and institute the controls IRS will be looking for to determine the correctness of income and expense.
- J. Foreign bank accounts are of significant interest to the IRS and over the past several years IRS has had a lot of success in getting foreign institutions to disclose account information.
- K. TIGTA recently told IRS that they are not using the \$10,000 currency transaction reports effectively, in a recent audit TIGTA told IRS that the transaction reports were an important indicator of unreported income and IRS agreed. Expect more focus on the part of the agency when they receive those reports.
- L. Look again at Item C. Taking itemized deductions that are comparably large to income. Keeping a record of legitimate deductions is important.