

“TAX TALK TODAY”[®]

Surviving the IRS Audit

TUESDAY, MARCH 10, 2009

Brought to you by the IRS and produced by L&M Production Design Group, based in Alexandria, VA, “Tax Talk Today”[®] is a free, live, monthly interactive Webcast aimed at educating tax professionals on the most contemporary and complex tax issues. Now in its seventh year with over 500,000 viewings, the award-winning series airs monthly at www.TaxTalkToday.tv and programs are archived on the site for one year after each episode. For additional information or to inquire about sponsorship opportunities, please contact Paul Lamonia at (703) 642-6505 or Lamonia@LMpdg.com or visit www.taxtalktoday.tv.

(Music.)

PHYLLIS GRIMES: This is “Tax Talk Today,” the tax show for the tax pro. Today’s program: “Surviving the IRS Audit.” Hello, I’m Phyllis Grimes and welcome to “Tax Talk Today,” a series of programs brought to you by the Internal Revenue Service. The “Tax Talk Today” series provides you, the tax professional, with the opportunity to interact directly with representatives of the IRS and practicing professionals on current tax issues.

In addition, viewing the “Tax Talk Today” series is an easy way to earn continuing education credits. For today’s program, you will earn one CPE credit. You can purchase CE credits through the “Tax Talk Today” store. You will need the course number, which is given at the end of the program, so don’t forget to jot it down. Also, we want your questions throughout today’s program, so please e-mail your questions to questions@taxtalktoday.tv. Any questions not answered on the program today will be posted to the “Tax Talk Today” Web site under resources.

If you have not already done so, visit the resource section of our Web site. We have posted an outline for today’s program, as well as additional valuable information. Now, let’s get on to today’s program, “Surviving the IRS Audit.” On today’s program, we will hear our expert panelists discuss a topic that most of your clients hope to avoid – the prospect of an IRS audit. Panelists will discuss what you can do to prepare your client for an audit without striking fear in their hearts. We will also include what happens before, during and after the audit as practitioners and IRS staff talk about the audit from both sides of the desk.

Now, let’s join our first panel. Today’s moderator is Les Witmer. Les brings to “Tax Talk Today” 23 years of experience with the IRS, and is currently a communications consultant in Atlanta. Joining Les is Nancy Como, small business/self-employed examination policy senior program manager for the Internal Revenue Service and Barbara Fiebich, small business/self-employed examination policy senior program manager for the Internal Revenue Service. The complete bios for our guests are on the “Tax Talk Today” Web site. Les?

LES WITMER: Thanks, Phyllis. You know, when people think of audits or think of the IRS in the context of audits, there’s a certain amount of fear that is there. And at the same time, there’s probably misconceptions about the IRS and the IRS audit process. One of them is that everybody stands the same chance of being audited. That’s not really the case; it depends on the audit. Nancy, why don’t you outline for us the different types of audits?

NANCY COMO: Well, there’s several ways a return can be selected for audit. And the first way is what we call computer scoring – it’s sort of a random selection. And this is termed DIF, or Discriminate Information Function. The IRS evaluates tax returns based on IRS formulas, and this is based on deductions, credits, exemptions with norms for taxpayers in each of the income brackets. The second way is through what we call the National Research Project,

or NRP. And what this is, is it collects data we measure for payment, filing and reporting compliance.

Now, another way that we have is for our local and national projects. And what we do with this is, we look at – we pinpoint particular areas – and this is areas of noncompliance that we might see that are a lot higher than other areas that might be noncompliant and we try to have isolated projects. Another way that you can be selected for audit is information matching. And a good example of this, as you know, you can get a 1099 in the mail, whether it be for interest, it could be something you did – some subcontracting on the side. We'll match those 1099s to your return, and if we see that it wasn't reported on your return, you may get a letter in the mail asking you to explain it or actually pay the additional tax for forgetting it.

And the last one is a related return. Let's say a partnership was pulled in for audit and there were adjustments to that partnership. You were involved in that partnership and you received a K-1, we may have to either send you a letter, pull you in also for audit, because there will be adjustments, also, to your individual return.

MR. WITMER: Okay, so the selection process can go anywhere from just one item that you need to substantiate to a full-blow audit, line-by-line with, say, the National Research Program.

MS. COMO: Exactly.

MR. WITMER: Okay. Barbara, taking that into account, then, what are the types of audits? How are they actually conducted? What are we talking about here?

BARBARA FIEBICH: Well, Les, we have three general types of examinations, and all of them are geared towards determining the correct tax liability. First, I'd like to talk about the correspondence audits, which, as the name suggests, are conducted by mail, generally with one of our campuses. And these are audits where the examination can be conducted just by looking at the information that a taxpayer or that a practitioner mails in to the person conducting the audit.

The second type of audit that we have is an office audit. And those involve a little more complex returns – maybe a couple of additional issues that would be examined – and they're conducted in one of our local field offices by a tax compliance officer. And generally, these involve the review of documentation. And oftentimes, a face-to-face interview with the taxpayer or practitioner is needed in order to determine the correct tax liability.

And the third type of examination that we have is the field examination. And these are conducted by revenue agents, oftentimes at the taxpayer's place of business or, occasionally, at the practitioner's office. And these involve businesses where there may be a complex set of books and records that need to be analyzed or reviewed. And a face-to-face interview is usually required to be able to understand the nature of the business, the items of income and deductions that are shown on the return – to be able to make that correct tax liability determination.

MR. WITMER: Okay. Nancy, what if the practitioner feels that the type of audit that's been selected isn't really conducive to showing or substantiating the area? Can they change?

MS. COMO: Absolutely. We always want to be flexible and work with the taxpayer and/or the practitioner. And the taxpayer does have the right to transfer an audit, depending on the conditions. A very good example of this is when you have a Schedule C business and you have moved, possibly, to another state and you receive an audit letter. You can call in to where the letter – the phone number it gives you – and discuss it with the examiner, explaining that, possibly, you know, that you would like to have this transferred.

Another example: You may get a correspondence – what Barbara talked about – the correspondence audits, where you get a letter in the mail saying we would like to make an adjustment to, let's say, a small business return. But the practitioner feels that, well, there's a great deal of records involved in this and it would be very burdensome to them and/or the taxpayer and we wouldn't want to do that. And their request is, can I come into my local office and have the exam there so I can show the verification? We want to work with you; we want to take everything into consideration before those decisions are made. But definitely, we are understanding under those circumstances.

MR. WITMER: Okay. Speaking of understanding, what happens if – for the field audit or an office audit, you have an appointment and you're scheduled to come in at that time – what happens if something urgent, or for some reason, they can't make that appointment? Can the practitioner request a change?

MS. FIEBICH: Certainly, Les. The practitioner can request a change, and we frequently see this, especially now, during the tax season, when practitioners are very busy meeting with their clients and preparing tax returns. And a goal that we have – and a goal that the practitioners have on behalf of their clients – is to conclude an examination as expeditiously as possible. And I can think of three different scenarios and offer a couple of suggestions to handle each.

Now, if the date is particularly inconvenient, the practitioner may be able to hold the meeting the day before or the day after it was originally scheduled, and that won't immediately extend the course of the examination. Another situation happens where a taxpayer or a representative may have gathered most of the books and records needed to conduct the audit, but don't have every last piece of information that they think they might need. In a case like that, it might be acceptable to begin the examination with the books and records that are available, and then schedule a follow-up appointment to review the additional documentation, which may be necessary.

The third situation is during filing season. And we often get requests to postpone examinations until after April 15th or even beyond that. And again, that can add an extended period of time to an examination. And what we would do in that situation is ask our TCOs – our tax compliance officers – or our revenue agents to work with the practitioner to minimize the impact that an examination would have on their day-to-day operations, such as, they can agree to meet first thing in the morning, the examiner can work on the books and records all day and then have a close-out at the end of the day, which will allow two things to happen simultaneously.

One goal that we have for, particularly, our revenue agents is that the initial appointment be held within 14 days of the first work being done on the case file. And we recognize that that's not always possible, but in the event that it extends beyond 45 days, we ask our group managers to get involved in that case to help that initial appointment take place as quickly as possible.

MR. WITMER: I'm sure you get a lot of requests to move them out of the filing season. You couldn't do that for everyone – just wouldn't be about to do that – but some of the alternatives that you've offered seem very good. Nancy, what about, okay, for the – again, for the audit where you either need to go into the office or a field audit – who should come to that audit? The taxpayer, the taxpayer's representative – what is the IRS point of view here?

MS. COMO: Well, when these are business returns, it's often beneficial to have the taxpayer at the audit because they know the workings of that business. But when a practitioner is representing a taxpayer, we ask that the practitioner be prepared to explain how the return was prepared, how the business operate, income, expenses – we're looking for all those things to be explained. And when that doesn't happen, it may be necessary that we ask the practitioner to bring the taxpayer in so that can be explained. It makes it run smoothly. We don't want to consume any time of the practitioner and the service – it also becomes costly to the service to extend the audits beyond a certain period of time.

MR. WITMER: Okay. Any time we've ever talked on "Tax Talk Today" about audits, one of the questions that comes up is, why am I audited on the same topic, or for the same issue, year after year? But the IRS does have a program to deal with that, right?

MS. COMO: Oh, absolutely. When this occurs, that you have had an audit, you have had adjustments in one, two, three years in a row, we will continue to audit your return until the return comes out to be correct. When the circumstance is that you have had a corrected audit and there are no adjustments, or you possibly even have gotten a refund and now, in the subsequent year, you do get an audit letter, then you can contact the examiner.

And what you would do then – explain the situation. We may ask you to provide whether it be the final letter or the audit report that showed there were no adjustments and/or a refund. And we would be glad, then, to work with you then and cancel the audit. If you already had an appointment made, we may have to postpone it until we validate everything that's been submitted and make sure everything is complete.

MR. WITMER: Okay. On our January program for the filing season, we had a small business/self-employed commissioner on who talked about the economic times and the fact that the IRS has some procedures for people who might be having trouble paying their taxes this year. Does that apply to the audit situation as well, if the individual has a balance due because of the audit?

MS. FIEBICH: Les, it certainly does apply to the audit situation, and we recognize that these are difficult times. And assisting taxpayers in meeting their tax obligations is part of our core mission. And in this regard, we have reminded our examiners of the flexibility that they

have in considering collectability and conducting their audits. So for example, at the beginning of the audit process, during the pre-audit stage, an examiner will consider the collectability of that particular tax return. And if, based on the facts and circumstances of that taxpayer's case, they may decide not to examine that return or they may decide to limit the scope of that examination.

And then, at the conclusion of the examination, if there is a deficiency, we will ask the taxpayer to pay that deficiency. That's part of our standard audit procedure. However, if the taxpayer is not able to fully satisfy their obligation, there are certain avenues that they can pursue to help themselves in that situation. And the first is an installment agreement, which allows the taxpayer to pay off their deficiency in monthly installments. The second avenue that they have is the offer and compromise program, and there they would work with folks from collections in possibly settling their tax liabilities for less than the amount that is determined. The third is working with our collections program, and they have additional avenues that they can consider in helping a taxpayer resolve their tax liabilities.

MR. WITMER: Okay. Interesting news. Okay. Thanks for sharing that overview of, basically, the audit process. And we'll be talking with our practitioners about many of these topics and probably some more. But first, let's hear from Phyllis with the headline news.

(Music.)

MS. GRIMES: Here are the top stories from the IRS. Tax provisions in the American Recovery and Reinvestment Act of 2009 – A-R-R-A. The IRS is working closely with Congress and the administration on the new economic stimulus legislation, the American Recovery and Reinvestment Act of 2009, and will implement tax-related provisions of the new program as quickly as possible. Most taxpayers will not have to make any changes to their 2008 tax returns, due April 15th. The changes in the law will largely impact 2009 tax returns, filed next year in 2010.

There are a few limited areas in the legislation that could impact 2008 tax returns. Some first-time homebuyers may qualify and can choose either to claim the credit on their 2008 or 2009 federal tax returns. In addition, small business changes in the net operating loss provisions could affect 2008 tax returns. IRS.gov links to this information are posted on the "Tax Talk Today" resources page. Additional details will be available on IRS.gov as soon as they become available.

E-file accuracy: Most tax professionals know the benefits of using tax preparation software. However, one benefit often overlooked is greater accuracy. Preparing taxes electronically allows tax professionals the opportunity to prepare more accurate returns. The use of software also enables tax professionals to detect and resolve errors and inconsistencies before actually e-filing a client's return. Tax professionals who e-file have the additional benefit of IRS-performed error checks. This further decreases the chance of human mistakes.

Errors or questions on e-file tax returns generate almost immediate notification to the transmitter. Paper returns have a higher error rate, can trigger an error and generate an IRS

notice. Notices may take weeks to resolve. So send the return electronically to expedite the filing process and it may also avoid the chance of later IRS inquiries.

For more information about e-file accuracy, see the tax professionals section of the IRS Web site at irs.gov. Check irs.gov for practitioner news and information. As we mentioned during the January show, the May 12th show is the last live program of “Tax Talk Today.” Archives of shows will be available through September 30th 2009. The IRS offers a broad range of resources and communication mediums to deliver key messages in tax information to you, the tax professional, and will continue to provide you with quality service.

Have you seen the new online small-business resource guide or checked out the new tax professional video and audio presentation page on irs.gov? There is an upcoming phone forum on cancellation of debt in which you may be able to earn one CPE credit. We’ve placed these links on the resource page. Visit irs.gov for updates on upcoming phone forums, audio and video presentations and future developments on communicating up-to-date tax information to you.

Now let’s continue our conversation on “Surviving the IRS Audit.” Joining our panelists are Al Thomson, an enrolled agent based in Arlington, Virginia; and Cynthia Jeanguenat, an enrolled agent from Virginia Beach, Virginia. Les?

MR. WITMER: Thanks, Phyllis. Welcome to both of you. Well, the way we’re sitting here, we’ve got the IRS here and the practitioners there. Is that indicative of the way an audit goes? Al, is an IRS audit confrontational?

AL THOMSON: It can be, but it really shouldn’t be. I think it’s important for the practitioners to recognize that the auditors are there to do a job. The parameters of the audit have been set out, usually with the initial notice, and as enrolled agents, attorneys, CPAs, professional practitioners, we are there to represent our clients and to resolve the issue.

MR. WITMER: We heard a lot from Nancy and Barbara about the audit process. Maybe what we need to do here to generate a discussion is maybe for you all to take us through some of the things that you do as practitioners when a client comes walking in the door with – or calls you and says, uh-oh, I got this letter from the IRS. What are some of the things that you look – what’s the first thing you do, Cynthia?

CYNTHIA JEANGUENAT: Well, once they’ve received that initial contact and they come to talk to us, during that initial interview, we are going to be asking a lot of questions. Our objective is to know that taxpayer better than the IRS. And what we also want to determine at that initial meeting is what records that we have to substantiate, you know, what is being requested, what records do we have to obtain, for instance, bank statements, credit card statements, those types of things. What records could be reconstructed? And the best example of that would be mileage logs, for instance.

And we also want to try and ascertain what might be negotiable during the audit itself. So, in other words, we are going to really be conducting an audit with that taxpayer in the initial

interview to try and determine, you know, where we stand. Some of the other administrative things that we're going to take care of at that initial meeting are going to be, we're going to ask them to sign a Form 2848, power of attorney, so that when we can talk to the person, the examiner or the agent, and also that will allow us to pull the transcript so that we have the same information they have.

The other thing we are going to ask them to sign is an engagement letter. And what that is, is it will spell out the terms of what we're going to do as an enrolled agent, what are the expectations, what are the fees? In other words, that will really cover the scope of the representation portion. And then, of course, we are also going to ask them for a retainer at that point.

So, you know, really, when we are preparing and interviewing and taking care of all of this, we really are doing the same as an attorney will do for a court case. We are going to – keywords: research, organize and prepare so that when we get to the audit – and of course we want to be able to instill in the taxpayer the need to meet the deadlines if we have materials we have to get – so that we're ready. That's the bottom line.

MR. WITMER: That's an interesting point. You mentioned deadlines. What's the timeframes here? I guess, ideally, you'd want the taxpayer to notify you as soon as they've heard from the IRS, but that's probably not always the case, is it?

MR. THOMSON: No, it tends to depend on whether or not it's a client that you've prepared the return for. If you've prepared the return, generally, they call you right away. But if it's someone who you have not prepared the return, they've been referred to you, often they'll procrastinate, hope that the audit will go away, not pay attention to the letter.

At some point, they realize they need to prepare for the audit and contact us. And so, in those two different scenarios, it really is a pretty wide gap of what we need to do in the amount of time we have to prepare before the scheduled audit.

MR. WITMER: Now, Nancy, I ran across in the resource page something on mutual commitment date. Maybe we should explain a little bit, what is a mutual commitment date and how does this fit into this process that Al and Cynthia are talking about?

MS. COMO: Well, this is what the service has created. It actually begins as a discussion between the taxpayer and/or the practitioner along with the examiner. And what we're trying to do here covers the roles and responsibilities of the parties involved in the audit. Now, what this will state is the time it takes to provide all of the additional records and set a tentative date for completing the audit based on information known at the first appointment.

Now, what we're striving for here is we're coming up with the date of when the final report will be issued; in other words, the report that's either going to show whether there is a no change of refund or adjustments made to the tax return. And the optimum word here is "mutual." We want this to be agreed upon by the examiner and – the practitioner and/or taxpayers, that we're all in agreement to make it a more cooperative effort.

We definitely think that becomes a more productive setting.

MR. THOMSON: It's also important to recognize the mutual part addresses the fact that interest and penalty can continue to accrue to the taxpayer while the audit is pending. And so it's important to have an agreement that you're going to move forward expeditiously as soon as you're able to properly prepare the records for presentation.

MR. WITMER: So a speedy result is – for both, everybody needs that. We've gotten some questions in already from our viewing audience so let's go to a few that might apply to where we are right now: “Does the IRS have the right to specify where an audit will take place? We have clients in other cities around the state/nation. Example: A client of ours is selected for an audit whose business is in Austin, Texas. The nearest IRS office to our location is Lubbock, Texas. The auditor assigned is located in Austin. Can the IRS require the audit to take place in Austin, therefore requiring us to travel a full day's travel?” What's the situation there?

MS. FIEBICH: Les, the Treasury regulations provide guidance on setting the time and the place of the examination. And that is something that the IRS has the responsibility of determining. Now, given that particular scenario and any scenario where the location of the audit is in question, would be based on the facts and circumstances and what the regulations say.

Now, given that particular situation, where the taxpayer is located in Austin, the practitioner is located a distance away from there, the books and records, I'm assuming, are maintained in Austin as well, that the location of that audit would be in the Austin office where the letter was initiated; however, given that the examiner would work with the practitioner to minimize the disruption to their schedule and to maximize the efficiency of the audit.

MR. WITMER: One of the things that was mentioned in the first segment was that – I think Nancy was talking about the fact that the IRS would really like to talk to the taxpayer during that time. From the practitioner point of view, what do you all want to do in that situation? Do you have – do you go with your client or how does that work?

MS. JEANGUENAT: No, they are hiring us, the representative, to represent them. And the preference is to definitely leave – to go without them and speak to me.

MR. THOMSON: I don't think I've ever had a taxpayer accompany me to an audit. My job is to make sure that I know the information that the IRS is looking for to understand the records, understanding the operation of the business and to focus on the questions that are raised in the audit.

MS. COMO: I think that's, again, just being prepared, the practitioner being prepared in a professional manner where they're providing us all of the needed information. Then the taxpayer is not necessary during the audit. But, again, when those situations arise, it may be necessary to go past, to ask to see the taxpayer, to possibly ask them exactly how the business is operating at the place of business and, under those circumstances, although they are not often, we do have to have those kind of provisions in place.

MR. WITMER: It depends completely on the situation.

MS. COMO: Exactly.

MR. WITMER: Okay, let's go back to the process again. In gathering the documents, you said you actually audit your taxpayer. In doing that, what are some of the problems that come up? How do you deal with that? If you prepared the return, you probably have a lot of that information. But, if not, what are you looking for as far as record-keeping to substantiate it?

MS. JEANGUENAT: Much depends on what they already have. And, again, if we've prepared the return, chances are we have copies. But we may need to ask for some of those originals back. It's going to depend also on what are the items that are being requested. And I think, again, some of the problem comes in – and I had a case where the client had called or written to tell the credit-card company – and the credit-card company sent statements but for the wrong year. So, you know, now you have to do this again and try and get that taken care of. The banks, they might give you wrong checks. You have to resubmit.

So I think for what we require, it depends on what's being asked for.

MR. THOMSON: It varies from case to case, but, obviously, if you have good original documentation, you're in good shape. If you don't or it's someone you haven't prepared the return for, in that initial interview with them, I'm looking for a clear idea of whether or not whoever prepared the return prepared it correctly. There may in fact be mistakes on the return; it happens. And if it does then you'd want to address those straightforwardly with the IRS.

You may have a situation, though, where someone has good records but is missing a few pieces. And, in that instance, as we prepare, in our firm, an audit book, we prepare page by page, item by item documentation for the items that have been requested. But we may find that something is missing; it just isn't readily available, it was never kept in the first place.

A good mileage log would be something that might be a problem. But if we go in and we document that the major items that have been raised at audit, the records are clearly there, it's well-documented, it balances, there's generally reasonable consideration given to the fact that that's a pattern or practice there that shows that you probably have good records and probably have not exceeded the reasonable amount for the deduction you've taken.

MS. FIEBICH: And Al brings up a good point here about being prepared and presenting the records to the examiner. And our examiners have discretion when they're setting the scope of the examination. So, generally, they'll begin looking at the largest most unquestionable items to begin with. And if you're able to work through those issues and the documentation is provided and everything is checking out okay, if the examiner was planning on looking at additional issues, based on the condition of the records for the largest items, they may decide to limit the scope of the examination and not look into those items – which is to the benefit of the taxpayer and to you as well because we're concluding the audit even quicker than we normally would have and it's a benefit to both of us.

MS. COMO: I think that just sums up what the facts of why being prepared for the audit and coming in with your records in order is a benefit to both the service and to the taxpayer and practitioner.

MR. WITMER: Okay, here are some more questions that are coming in: “For years, I had told my clients to keep a written log of automobile mileage. This includes beginning and ending mileage on the vehicle used, dates of usage and miles, explanation of the purpose of the mileage. During an audit on this, why would an examiner also want third-party records?”

MS. JEANGUENAT: Third-party records would be auto repairs that were done, oil changes – and, again, I’m assuming that’s what they were talking about when they said “third party.” And when you take your car in for an oil change, you know, they give you the little sticker and, on that, they mark your pedometer rating. And what it is, is if you have some odometer reading proof of that from some points in that year, it justifies the mileage that was claimed for business. It’s just another way to prove that that mileage matches the actual use of the car.

MS. COMO: And just from the service’s point of view, when we are asking for the third party, it may be for either what is presented at the time or the type of business that you are running maybe isn’t conducive to what you’re trying to say that I travelled this place, this place and all of these different places – it’s not making sense. We may want to go back and validate some of the information that you gave us to make it all – because there are exceptions to every rule and we want to take that into consideration. But that would be why we’d go for third party.

MR. THOMSON: But there are also – sometimes it’s simply not a clear understanding of what – if I get a request from an auditor for something that seems unusual to me, I want to engage in a dialogue there to see what is it you’re really looking for? Are you questioning the specific number or is it that you don’t understand this cost within the context of the operation of this business?

MS. COMO: Exactly. And that dialogue has to take place.

MR. WITMER: Okay. Here’s another question: “A client’s company is being audited. I provide several detailed lists of expenditures. I received additional requests for information. It seems like a lot. How much can they ask for?”

MS. FIEBICH: Examiners will request information to determine the correct tax liability. And, as a practitioner, if you feel that the request for the information is overly burdensome or you have additional information or a substitute for the information that’s being requested, again, engage in a dialogue with the examiner to really nail down exactly what needs to be reviewed to determine that correct tax liability.

MR. WITMER: Okay. It seems like we’re talking a lot about what we might say the norm, you know, this is what the ideal situation for both the practitioner or for the IRS. I’m sure there are cases where that’s not the situation – maybe either a new examiner or possibly a

practitioner that doesn't have the experience. In those cases, when, say, it's not moving as smoothly as possible, what can the practitioner do, say, for a – in regards to the auditor?

MS.COMO: Of course we ask the practitioner, again, to schedule the appointments timely, bring in the correct verification of the books and records. But when they have done everything they have been asked and they still become extremely frustrated or feel that the audit is taking too long, they need to go to the next step or the next level here and they need to ask to speak to the examiner's manager.

The reason being is we don't want to consume the time of the practitioner and/or the taxpayer and it also becomes costly to the service to allow an audit to drag on. We want to get this done as quickly as possible. Every field examiner is told that they must give their manager's name and phone number at the initial appointment of the audit. When this doesn't happen the practitioner should definitely ask that question, that the information be provided to them and, that way, if it does occur – and we hope it is not often – but that the next step is able so they can take – so we can resolve things as quickly as possible in a professional manner.

MR. THOMSON: It's really important you should use a checklist. We've developed one in our office to make sure that we're gathering information we need when we first begin that audit. We want to make sure we have the names and numbers of anyone we're going to deal with at the service and particularly, the audit manager. And we're providing our information so that we're accessible as well.

MR. WITMER: Okay, let's reverse that. The practitioner is maybe newer or inexperienced and the auditor is having, maybe, a problem and again feels that it's not running as smoothly as it should. What can be done in that regard?

MS. COMO: Well, in that case, what the service has to do then is – we again, don't want to consume the time of the taxpayer and we don't want it to be costly to us – we do all means to contact the practitioners, forward letters of what we're requesting. If that is the case, then we will go then and try to contact the taxpayer by using bypass procedures.

Please keep in mind, this is very rare that we have to do this and we must elevate this requirement up to get the higher-level signature to have this approved to be done. But that is in place in case those situations happen. But again as, I think, as Al has stated several times, that professionalism is so important and when you do come in to represent your clients, if that is there then we will not have these kinds of problems.

MR. WITMER: And probably experience is an educational process for both sides. Here's another question: "Part of my job is to do the 2106 audits; where can I get more information on technical and procedural issues?"

MS. COMO: We have a very, very extensive Web site with lots of information on it. Everything from, you can see our internal revenue manual, which is all of our procedures of how we conduct audits in there. You can find publications that will talk about all kinds of Schedule C expenses, including auto expenses if that is what you're interested in. We have audit technique

guides, which actually explain how we audit particular businesses and there's a variety of those out there. So there's an entire – various – I probably haven't even covered any – I don't know if you can think of any from – you've gone on our Web site of all things you use.

MS. JEANGUENAT: Well, and again, the importance is of becoming educated and finding those resources. You know there's a lot of other companies that put out tax literature and resource literature that we use, so the point is, you know, to know and look everywhere you possibly can, you know?

MR. WITMER: Just a point here: Those audit guides and the links to the IRM and the IRS information is all on our resource page. So if you haven't checked that out, please do. Here's another question: "I am not an enrolled agent, but I studied and prepared tax returns for clients for over nine years and have represented clients over the telephone by power of attorney. What can a non-enrolled preparer do to help their client during an audit?"

MR. THOMSON: Well, quite honestly the recommendation I would make is to refer the client to someone who is an enrolled agent or another Circular 230 practitioner. The ability of an un-enrolled preparer to represent their client at audit is somewhat limited in that they can provide information and represent their client, but an un-enrolled preparer is not permitted to go beyond that process.

So it's possible that you'll have someone who is working with a client, you get to the end of an audit, you have a disagreement, you don't have an agreed-upon outcome, and the practitioner – in that case, the un-enrolled practitioner – cannot continue with an appeal. They're not permitted to represent a client at appeals, whereas an enrolled agent, an attorney or a CPA, can. And that experience really a large part of both the training and the practical reality of our practice.

MS. JEANGUENAT: And I think that it needs to be understood that there's a big difference between who can provide information to the IRS and who can represent the taxpayer; there's a big difference there.

MR. WITMER: So someone who's prepared the return or has knowledge of that return, the IRS is going to accept that information from them, they just can't represent during the audit the way an enrolled agent, CPA or tax attorney can.

MS. COMO: And I think you've listed several things you cannot – they cannot extend the statute. They cannot – if it would go to collection, where they're collecting – they can't represent in collection, and there are a lot of limitations there, and that is something to keep in mind for the taxpayer.

MR. THOMSON: It's an opportunity, though, to work together, you know? If you have a practice – a professional practice – and you have a client who needs representation in an audit, the prospect of working together with an enrolled agent, I think, is very possible, yeah.

MR. WITMER: Okay. "One of my clients is being audited for 2006 to 2007; however, the audit has been dragging on since November of '07. What can we do to accelerate the final findings without seeming to be pressing?"

MS. COMO: Yeah, you know and I talked about a little bit earlier about getting the things to move along quickly. You can always contact the manager; we don't want delays in the audit. And we want to make sure that things won't cause a burden on to the practitioners. And you can always take that approach.

MR. WITMER: Okay.

MR. THOMSON: Sometimes though, you are dealing with a situation where the auditor has a workload, where, you know, if there is a legitimate reason that an appointment has to be rescheduled, it may be being rescheduled five, six, seven weeks out. If that happens twice – for very legitimate reasons, not for purposes of delay – you can have a very elongated process evolve.

And I think that it's important – again, recognizing an interest penalty can be accruing in the event there is an additional tax – if you're in that situation and the auditor is not able to work you in, to go ahead and call the audit manager.

MS. COMO: That is very important.

MS. FIEBICH: That is true, and also in a perfect audit situation, at the conclusion of one appointment, the examiner should be scheduling a follow-up appointment or if they're issuing an information document request, having a due date on that. And, you know, adhering to that follow-up appointment or providing the information by the due date requested really helps with the planning and scheduling to avoid unintentional delays. And I agree that talking with the group manager, although it can seem a little bit adversarial, is a real important mechanism in getting cases moving along and helping with that planning and scheduling process.

MR. WITMER: It brings up an interesting question: Is there a psychological impact here? If they go to the manager, how does that, you know, how does that work? If I'm the examiner and all of a sudden, they want to talk to the manager, does that impact on the examiner?

MS. COMO: Absolutely not, and we want to emphasize here, our agents are trained in a professional manner to definitely work with the taxpayers. It's not like we want every practitioner to run under every little circumstances and it will not, you know, in any way, shape or form have any kind of effect onto the audit itself. Our goal here is to have, possibly in many situations, that it could be where they just need a third party to maybe hear both sides and move it along quickly.

MR. WITMER: Okay, let's get to – we talked about the audit report. What can the practitioner do if they get the audit report and don't understand it, or if there's some questions there? What takes place there?

MS. FIEBICH: Sure, let me address that. The tax law is very complex, so if a practitioner receives an audit report and they don't understand the adjustments or why the adjustments are being made, their first contact is going to be with the examiner who conducted the audit. And having a discussion will usually provide that level of understanding that they need.

If that doesn't work, the practitioner can also have a three-way conversation with the group manager and the examiner and, again, that often provides the resolution or the understanding that the practitioner is seeking. However, once the practitioner has an understanding of what the adjustments are and why they're being made, if they don't agree with those adjustments, they have a couple of avenues that they can pursue.

The first one would be an informal conference with the group manager. And again, that oftentimes leads to a resolution of the issue. If at that level, an agreement can't be reached, the case can go to our appeals division, and they would file a protest. Now, if there's a small deficiency, the protest is fairly simple; it basically just states that you don't agree with the adjustments and that you would like your case transferred to the appeals office. If there's a larger deficiency involved, the protest is just a little bit more complex in that you need to provide a little more background about the adjustment and the tax law and why you think the decision should be made in a different manner.

And the third avenue which we have is to issue a notice of deficiency. And normally, in a regular audit, this will not be the conclusion at the examination level. And a notice of deficiency is basically the commissioner's determination of an income tax liability and it's the beginning of the litigation process. And if a taxpayer or practitioner gets a notice of deficiency, they would respond to that by filing a petition with the United States Tax Court. And after our council responds to that petition, the case is then sent over to appeals for an opportunity to resolve the case again.

MR. THOMSON: It's important to keep track of the time. I mean, these are very time-sensitive matters. If you're at the end of an audit and there's still an unresolved – it is not a settled audit – you really have to stay on top. It is an area where you're placing your client in jeopardy of the deficiency notice or, if failing to file a petition, then having very little recourse. So it's important to stay right on top of that case. I find that appeals is a good avenue to go and that it gives you some time to additionally address it, as we talked about, with a third party.

MS. COMO: I think with some of the points we've talked about though, it's important to meet the deadlines all the way around, and to maintain the level of communication is the other factor.

MR. WITMER: Normally, I would imagine that once the audit report's coming out, that there's isn't too many surprises if you've had an ongoing dialogue and the examination was run smoothly. Is that the case?

MR. THOMSON: Normally, yeah, my experience has been that if you're on top of what's going on and it's clear what – it isn't that you don't understand what the decision is; it's that you may disagree with the findings, yeah.

MR. WITMER: Here's one, I don't know if the IRS, if you'll have an exact answer, but it just came in: "What percentage of IRS audits that are performed at the taxpayer's place of business result in a no-change audit?"

MS. COMO: You know, unfortunately, I don't think we have an exact number to – I'm not sure we even have the exact measurement for that.

MR. WITMER: And again, I guess what should be pointed out is, you talked about the selection process. And again, it might be a misconception that people have, but unless it's an NRP audit, there's a chance that something's out of line and there's a chance that you either have to substantiate it or you're going to be faced with additional tax.

MS. COMO: Right, and we talked about this, that you can have the random selection of returns which is one of those things. I think the important thing about that question is where it states, it doesn't make a difference if it's at the place of business or if you're coming into the audit. There's no different chance as far as that that's going to make it better or worse about the audit.

MR. WITMER: Okay, good point, I'm glad you picked that up.

MR. THOMSON: The client's question is, why me? What happened? If you've prepared their returns, they are coming to you and they assume you're infallible, of course. We're human and there are mistakes made and you take responsibility for them. But the why me, it may be something as simple as, the operation of the business, in a totally legitimate, totally well-documented fashion has some deduction that's out of the realm of the norm for a similarly situated business. And that draws the attention of the service and it's questioned.

MR. WITMER: Okay, we've talked on "Tax Talk" before about a pilot program that the IRS has – fast track settlement. Maybe we should spent a little bit of time talking about how that's going and what it is.

MS. FIEBICH: Okay, the fast track settlement program is a pilot which originally was launched in 2006, and was recently extended to run through the end of 2010. And basically what this pilot is, it is an opportunity for the resolution of un-agreed issues at the group level without using the traditional appeals method, which I just talked about. And what happens is, at the conclusion of an examination, generally before the 30-day letter is issued, a taxpayer or practitioner can request to be a part of the fast-track settlement program. And right now, this is currently being piloted in eight different areas in the country, including Philadelphia, central New Jersey, Laguna Niguel, Riverside, California, Chicago, Houston, St. Paul, Minnesota.

And what happens, there is a trained mediator from our appeals office will meet with the practitioner, the revenue agent or the tax compliance officer and the group manager to use

mediation techniques to help resolve that issue. And one of the real benefits of this is that it resolves those issues much more quickly than would be possible through the traditional appeals process, and it reduces the burden on the practitioner and on the taxpayer as well.

MS. JEANGUENAT: Barbara, since Al and I are in Virginia, is there a rollout date for that program?

MS. FIEBICH: Sure. During these next two years, we're going to be studying the pilot to see if there's way that we can make the program even better. And at the conclusion of that we're going to determine whether or not to modify and to expand and to roll out the program nationally.

MR. WITMER: Okay. Here's another question that's come in: "Can you tell me, how does the fed-state program exchange work concerning audited information?"

MS. COMO: The fed-state program is a program that we've been doing for a quite a few years now where it's taking data that the states have in their – for example, their revenue departments, as the IRS keeps in theirs – and what we do is exchange that data, as long as there's an agreement between the state and the federal government. A good example of that is if the IRS completes and audit, there's adjustment to that return and we have an audit report, we will, if there's an agreement with the state, exchange that audit report with the state and then, in turn, they will then do the adjustments on the state tax return and send a letter out.

The benefit is, the taxpayer isn't going to have to come in for a whole other complete state audit here if the adjustment is made based on what the federal adjustment was. And that saves time for the practitioner, the taxpayer, and most importantly, for the states. And when, also, the state does adjustments, they will forward it on to the IRS.

MR. WITMER: From the practitioner's point of view, do you deal with that separately? I think, Cynthia, you mentioned an engagement letter when you first meet; does that come up at that point, or is that something that is done separately? I mean, what Nancy's saying here is, a lot of the states, apparently, just piggyback onto the fed audit and go from there.

MS. JEANGUENAT: And in many cases, that's true. And the difference in the states, of course, is that each state department of taxation or revenue, you know, functions a little differently. But usually, at the initial visit with the audit, you really – of course, we're all hoping for a no-change, so I wouldn't really have a stipulation in the engagement letter that would address the state. However, once the results were completed and the IRS audit was over, we would have to, of course, look at that.

MR. THOMSON: You have a responsibility to inform the client that they have an additional tax liability if you're aware of that. You can't force them to file an amended state return, but it's likely that they're going to get an audit letter or a change letter from the state as well.

MR. WITMER: Okay. Here's an interesting question: "What's the focus of this year's audit?" I think we've talked before about the examination process on previous "Tax Talk Today" programs. There is an audit plan, or examination plan. What is that and how does that work?

MS. FIEBICH: Sure. There is an examination plan for the service-wide in general, and in small business/self-employed, we ensure that we have balanced coverage in that we provide audit coverage for all the types of returns that we examine, including individuals, corporations, s-corporations and partnerships. So we want to make sure that we examine taxpayers in all of these broad categories.

And then, within that, we're trying to focus on the most noncompliant taxpayers. So in particular, we'll have programs that deal with abusive tax schemes, offshore credit card cases, non-filer programs – and Nancy talked a little bit earlier about some of the compliance initiative programs that we have as well.

MR. WITMER: Okay. Nancy, I know that you do post-surveys of the audit program. I'm not sure that people involved would consider themselves customers – a customer survey – but what are some of the findings that you get out of that? What are some of the areas that people reply to?

MS. COMO: You know, I'm really glad you brought that up, Les. We do a taxpayer satisfaction survey to taxpayers that have completed an audit. And you know, the difference is that when you have a – you either receive a refund or have a no-change, the results are a little bit better than those that have adjustments on their return. (Laughter.)

But taking that into consideration, we take the results of the survey – we make it very important. It's a big emphasis of what we do within our examination process. To highlight some of the issues that come up that we're focusing on is probably the greatest area that we seem to come up over and over again is the timeliness of audits. That's important to taxpayers and it's important to us. And we're constantly looking at our process and emphasizing to our examiners the importance of – again, as we've talked here today – of completing the audit.

Another area – and again, I think this was brought up – about understanding the audit adjustments. Again, we get a lot of feedback that I got this report in the mail and I don't understand why there were adjustments and what these are about. I thought the audit was over. Again, we want to make sure our examiners are clearly communicating what the adjustments are to both the taxpayer and, if a practitioner is representing them, to the practitioner as well.

MR. WITMER: Okay. "If an audit begins with the IRS requesting documentation for itemized deductions, during the audit can the scope be changed to include other portions of the return?" That's a question that comes frequently, I think, when we're talking about audits.

MS. FIEBICH: Certainly, and the scope of an examination can be either expanded during the course of the examination or contrasted as well. So, if during that initial review of the

Schedule A, if the examiner finds something else that is warranting examination, they can and they have the authority to expand the audit to include those items.

MR. THOMSON: That sometimes comes up where you have the taxpayer present and there's a question that the taxpayer doesn't understand or they may go on about how they travel and do this and do that, and that's one of the reasons that I prefer not to have a taxpayer present during an audit. It's an opportunity for chit-chat that may raise questions for no reason other than the taxpayer's just chit-chatting and it leads to additional questions from the audit.

MR. WITMER: Okay. Here's another one let's see if we can get to quickly: "Can an amended tax return be presented during the audit?"

MS. COMO: Absolutely, absolutely. You would walk in and state that I would like to show you – I made these errors on the return – if it happened to be issues that we were already looking at and you're saying I've already known I've made these mistakes and I, you know, would give you an audit adjustment report then. It could be a little bit of work for the taxpayer to go and complete an amended return versus go through the audit, but you know, if they want to come in up front, they're going to save themselves a lot of time as well if they know those errors were made on the return.

MR. WITMER: All right. We're out of time. We're not going to be able to get to all the questions that came in, but like always, we will post the questions and answers on our resource page on Tax Talk Today, so check that out. Good information, and hopefully, we've provided some information out there to take surviving the audit more into the process and the fact that it is give and take and people need to be prepared on both sides of it. So hopefully, we've presented that. Thanks for a very interesting discussion on the audit process. But before we close out, let's go back to Phyllis.

(Music.)

MS. GRIMES: That brings us to the end of today's program, but mark your calendars for Tuesday, May 12th, 2009 for "Specialty Taxes: Estate and Gift and Employment Taxes." Remember that you will be able to view today's and other "Tax Talk Today" programs by going to archives on our site. And you can download a podcast of the programs from the home page of "Tax Talk Today" by clicking on audio podcasts. Podcasts may also be found under archives. Additionally, written transcripts of our program are available on our site under news.

Now, to receive your CE credit for viewing today's program, click on your account and fill out the evaluation form. And we want your feedback, so please send your comments to mail@taxtalktoday.tv.

There is one remaining live program scheduled in May and program archives will be available through September 30th. So tell your colleagues to watch "Tax Talk Today." I'm Phyllis Grimes, and we'll see you in May. Thanks for watching.

(Music.)

The "Tax Talk Today" series is brought to you by the Internal Revenue Service.

(END)