How to Successfully Deal with Correspondence Audits and IRS Notices

A review of the process, relevant IRM procedures, types of audit letters and notices, how to get help, and more

Practitioner and IRS Analyst Panel
Torie Charvez, Enrolled Agent
Barbara Doherty, Tax Attorney
Gail Murphy, Tax Policy Analyst, IRS
Susan Clark, Tax Policy Analyst, IRS

Moderator
Caroline Chen, Professor, SJSU

Introducing Practitioners & IRS Analyst Panelists

• Torie Charvez, Enrolled Agent
• Barbara Doherty, Tax Attorney
• Gail Murphy, Tax Policy Analyst, IRS
• Susan Clark, Tax Policy Analyst, IRS
Objectives

- Review:
  - Correspondence Exam process
  - Issue resolution
  - Case closure
Correspondence Examinations

- Efficient
- Broad compliance coverage
- Highly automated
- Campus operations

Correspondence Examinations

- IRS Audits webpage
  - www.irs.gov/audits
- EITC Central
  - www.eitc.irs.gov
Inventory Analysis and Selection

• Identify returns with high potential for a tax adjustments using:
  — Results of prior audits
  — Third party information
  — Entries on the return

• Referrals from:
  — Criminal Investigation
  — Preparer /promoter actions

• Non-filer conditions
Correspondence Examinations

- Defined scope
- Generally less complex
- Focus on documenting specific tax return entries

Common Examination Issues

- Refundable Tax Credits
  - Earned Income Tax Credit (EITC)
  - Child
  - American Opportunity

- Schedule A
  - Employee business expenses
  - Charitable contributions

- Schedule C

- Emerging issues
- Non-filing conditions
Common Initial Letters and Notices

• Initial contact letters, no examination report
  — CP 75/75A – Earned Income Tax Credit
  — CP 06/06A – Premium Tax Credit
  — Letter 566 – Most other issues

• Initial contact letters, examination report
  — Letter 1862
  — Letter 2194

Initial Letters and Notices

Enclosures

• Forms (listing requested documentation) and Questionnaires

• Publication 3498-A, The Examination Process (Audits by Mail)
Acknowledgement and Interim Letters

- Acknowledgment Letter 3500
- Interim Letter 3501

Common Follow Up Letters and Notices

- Letter 525/692 – Follow-up including the examination report
  - Form 4549
  - Form 886-A
- Letter 3219 - Statutory Notice of Deficiency, “90 Day” Letter
- Letter 555 – Follow up after Letter 3219 issuance
Resolve Disagreements and Reconsideration

- Resolve Disagreements
- Reconsideration

Correspondence Examinations - Key Points

- Respond to notices timely
- Ask for additional time to respond if needed
- Provide a complete and organized response
- Fax or mail documentation
- Work with IRS to resolve issues
- Reconsiderations
Correspondence Examinations - Future Initiatives

- Taxpayer Digital Communication (TDC)
  - Resolve correspondence examination in a secure online environment
  - Pilot launched in December of 2016
  - Documentation for audit issues can be directly uploaded instead of mailed

Practitioner Priority Service

- For expedited access to Correspondence Exam contact PPS:
  - Call 1-866-860-4259
  - At the voice prompt press or say “6”
Successfully Dealing with Correspondence Audits & IRS Notices

Practitioner Tips & Suggestions by Barbara Doherty, Tax Attorney

Practitioner Tips and Suggestions

• Disclose any actual or potential conflict of interest
• Weigh reliability of the underlying data
  • Taxpayer penalties
  • Potential preparer penalties.
• Consider if continued representation violates of legal and ethical considerations.
• Small business owners and rental property owners may not have enough data to withstand a large adjustment.
• After being engaged to represent the taxpayer complete Form 2848 Power of Attorney to include the year before the examination year and up to 3 years ahead of the current tax year.
Practitioner Tips and Suggestions

• Initial Response.
  • Call, fax or mail as indicated in the examination letter.
    • Consider if an experienced tax attorney, or criminal tax attorney, should be referred.
    • All the information you be providing are essentially statements and admissions
    • If there are gross discrepancies to the tax return, engage a legal tax professional immediately.

• Correspondence audit is the standard. Selected IRS field campuses are utilized for centralized examination and standard.

• Only with exceptional circumstances, would a return selected for a correspondence exam be transferred to a local office for an in person examination.

Practitioner Tips and Suggestions

• Taxpayer or representative should provide all requested information.
  • All materials should be printed, banded together with clear summary pages to indicate the detail therein.
  • Be very specific with what information is being provided and what income or deduction amounts you are requesting.

• Be prepared for several exchanges of information by fax or mail.
  • Not all the adjustments will be seen in an IRS response.
  • May have to request some adjustments a second or third time.

• Appeals cannot consider new information so a case will be returned to Exam for review of any new information.
Practitioner Tips and Suggestions

• Prepare research ahead of time if you know an item of income or expense will be contested.
  • Include the law and research subtlety in your correspondence.
  • On appeal, you can provide your legal analysis developed in your earlier writings.
• Always replicate the original return data.
• Amend any return information to isolate the additional tax with the changes you want, and later with the agreed examination changes.
  • Calculate the expected tax before the IRS provides the revised changes so you will know immediately if the agreed changes were processed correctly.
  • Estimate penalty and interest with a few quick multipliers.
  • Do not forget there are opportunities for penalty abatement.

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• Be prepared for an additional exchange of information by fax or mail.
  • Not all the adjustments requested may be seen in an IRS first response if there are many adjustments requested.
  • May have to request some adjustments a second or third time.
  • The more clear and simple your request is written and assembled, the better it may be interpreted by the IRS examiner.

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Internal Revenue Manual 25.1.2.3
(06-09-2015)
Indicators (Badges) of Fraud

• Omissions of entire sources of income
• Substantial unexplained increases in net worth, especially over a period of years
• Substantial excess of personal expenditures over available resources
• Bank deposits from unexplained sources substantially exceeding reported income
• Concealment of bank accounts, brokerage accounts and other property
• Failure to deposit receipts to business account, contrary to normal practices
• Substantial overstatement of deductions
• Keeping two sets of books or no books
• False statement, especially if made under oath, about a material fact involved in the examination
• Patterns of consistent failure over several years to report income fully
• Use of secret bank accounts for income
• Deposits into bank accounts under nominee names
Your Client got an IRS letter, now what? – Torie Charvez, EA

• Case Studies
  • Sample IRS Notices & Practitioner Responses

See separate file with materials.

Questions?