



Charles M. Pace, CPA
K. Brad Wooten, CPA

2809 Village Way
New Bern, NC 28562

P: 252.633.5096
F: 252.633.6901

APRIL, 2011

Would you like to receive our newsletter by e-mail? If you would like to receive our monthly newsletter by e-mail instead of or in addition to the paper copy please let us know by sending an e-mail to info@paceandwooten.com. Include your first and last name and the e-mail address you would like the newsletter sent to. Also state whether or not you would like to continue receiving the newsletter by mail as well as e-mail.

What are your chances for being audited? IRS's 2010 data book provides some clues. IRS has issued its annual data book, which provides statistical data on its fiscal year (FY) 2010 activities. As this article explains, the data book provides valuable information about how many tax returns IRS examines (audits) and what categories of returns IRS is focusing its resources on, as well as data on other enforcement activities such as collections. The figures and percentages in this article compare returns filed in calendar year 2009 and audited in FY 2010 to returns filed in calendar year 2008 and audited in FY 2009.

What are the chances of being audited? Of the 142,823,105 total individual income tax returns with a filing requirement, 1,581,394 were audited. This works out to roughly 1.1%, a bit higher than the 1% rate for the previous year. Of the total number of individual income tax returns audited in FY 2010, 473,999 (30%) were for returns with an earned income tax credit (EITC) claim, a decrease from the 35.64% of all audited returns for FY 2009.

Only 21.7% of the individual audits were conducted by revenue agents, tax compliance officers, tax examiners and revenue officer examiners; the bulk of the audits (about 78.3%) were correspondence audits. The percentages for FY 2009 were 22.8% and 77.1% respectively.

Following are selected audit rates for individuals not claiming the EITC:

... For business returns other than farm returns showing total gross receipts of \$100,000 to \$200,000, 4.7% of returns were audited in FY 2010, up from 4.2% in FY 2009.

... For business returns other than farm returns showing total gross receipts of \$200,000 or more, 3.3% of returns were audited in FY 2010, versus 3.2% in FY 2009.

... Of the returns showing farm (Schedule F) income, .4% were audited in FY 2010 versus .3% in FY 2009.

... For returns showing total positive income of \$200,000 to \$1 million, 2.5% of returns not showing business activity were audited, and 2.9% of returns showing business activity were audited; for FY 2009, these percentages were 2.3% and 3.1% respectively.

... For FY 2010, the audit rate for returns with total positive income of \$1 million or more was 8.4%, a substantial increase from the 6.4% rate in FY 2009.

Not surprisingly, examination coverage increases for higher income earners. For example, the percentage was .71% for those returns with adjusted gross income (AGI) between \$100,000 and \$200,000 (up from .67% for FY 2009), and 1.92% for those with \$200,000 to \$500,000 of AGI (up slightly from 1.86% for FY 2009). Exam coverage increased to 6.67% for those with at least \$1 million but less than \$5 million of AGI (up from 5.35% for FY 2008). Similarly,

Circular 230 Disclaimer: Any tax advice contained in the body of this material was not intended or written to be used, and cannot be used, by the recipient for the purpose of (i) avoiding penalties that may be imposed under the Internal Revenue Code or applicable state or local tax law provisions, or (ii) promoting, marketing, or recommending to another party any transaction or matter addressed herein. The taxpayer should seek advice based on the taxpayer's particular circumstances from an independent tax advisor.

coverage increased for those with at least \$5 million but less than \$10 million of AGI, as well as for those with AGI of \$10 million or more.

The audit rates for business returns were as follows:

- For all corporate returns other than Form 1120S, 1.4%, versus 1.3% for the year before.
- For small corporations with total assets of: \$250,000 to \$1 million, 1.4%; \$1–\$5 million, 1.7%; and \$5–10 million, 3%. For FY 2009, the percentages were, respectively, 1.3%, 1.8%, and 2.7%.
- For large corporations with total assets of \$10 million or more, the overall audit rate was 16.6%, up from 14.5% for FY 2009. The audit rate for these corporations increased with the size of the entity. For example, the audit rates were 13.4% for those with total assets of \$10–\$50 million (up from 10.1% for FY 2009); 16.1% for those with \$250–\$500 million (versus 15.8% for FY 2009); 45.3% for those with \$5–20 billion (down from 48.7% for FY 2009), and 98% for those with \$20 billion or more (down from 100% for FY 2009).
- For partnership and S corporation returns, the audit rate was .4%, the same as for the year before.

IRS's activity on other fronts. Here's a roundup of some of the other valuable information carried in the new IRS Data Book.

Math errors on individual returns. Of the roughly 10.5 million math error notices that IRS sent out relating to the 2009 return, 60.8% were attributable to the making work pay credit (MWPC), which was a refundable tax credit based on earned income and was available to taxpayers in 2009 and 2010.

Of the total math error notices, 9% were for tax calculation/other taxes (which includes errors related to self-employment tax, alternative minimum tax, and household employment tax), 4.9% related to exemption number/amount, 4.4% related to the EITC, 4.1% related to the standard/itemized deduction, and 1.3% related to the first-time homebuyer credit.

Penalties. In FY 2009, IRS assessed 27.1 million civil penalties against individual taxpayers, up from 26.387 million civil penalties assessed in the previous year. Of the FY 2010 assessments, the “top three” penalties in percentage terms were 57.3% for failure to pay, 27.3% for underpayment of estimated tax, and 13% for delinquency. On the business side, there were a total of 1,145,931 civil penalty assessments (up from 970,098 for the year before), and 42.1% of these assessments was for either failure to pay or underpayment of estimated tax.

Offers-in-compromise. In FY 2010, 57,000 offers-in-compromise were received by IRS (versus 52,000 for FY 2009), and 14,000 were accepted (11,000 for the year before).

Criminal cases. IRS initiated 4,706 criminal investigations in FY 2010. There were 3,034 referrals for prosecution and 2,184 convictions. Of those sentenced, 81.5% were incarcerated (a term that includes imprisonment, home confinement, electronic monitoring, or a combination thereof). By way of comparison, in FY 2009, IRS initiated 4,121 criminal investigations, and there were 2,570 referrals for prosecution. Of those sentenced, 81.2% were incarcerated.

The following estimated tax payments are due by April 15, 2011:

Individuals	1 st Installment
Corporate Income Tax Years Ending:	
December 31, 2011	1 st Installment
October 31, 2011	2 nd Installment
July 31, 2011	3 rd Installment
April 30, 2011	4 th Installment

Circular 230 Disclaimer: Any tax advice contained in the body of this material was not intended or written to be used, and cannot be used, by the recipient for the purpose of (i) avoiding penalties that may be imposed under the Internal Revenue Code or applicable state or local tax law provisions, or (ii) promoting, marketing, or recommending to another party any transaction or matter addressed herein. The taxpayer should seek advice based on the taxpayer's particular circumstances from an independent tax advisor.