

# **SAN ANTONIO ESTATE PLANNERS COUNCIL**

## **PRACTICES BEFORE THE IRS**

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# IRS Individual Audit Levels Are Way UP

- For fiscal year 2006 total 1040 audits up 6%
- Field audits up 23%
- Audits of individuals with income over \$100,000 up 18% (2-1/2 times 2001 level)
- Audits of individuals with income over \$1,000,000 up 33% (1 in 16 were examined)

# Business Returns

- For fiscal year 2006 1120S audits up 34%
- Partnership Returns (1065s) up 15%
- Small corporations (1120) audit level was unchanged in fiscal year 2006
- Large corporations (1120s with assets over \$10,000) dipped slightly in fiscal year 2006

# Exempt Organizations

- For fiscal year 2006 audits increasing 43%

# Transfer Taxes

- Estate tax returns – for large 706's fiscal year 2006 audits dropped by 17%
- Gift tax returns – fiscal year 2006 audits dropped by 5%
- Issues:
  - Valuation of minority equity interest in closely-held entities (example – FLPs)
  - GRATs
  - Schedule J expenses

# Collection Activity

- For fiscal year 2006
  - Levies up 36% (3.74 million)
  - Liens up 20% (630,000)

# IRS Budget Increases

Fiscal year 2008 – the President is proposing a 6.3% overall Budget Increase

Big increases in:

Enforcement (\$440 million increase)

Information services

Business systems modernization

# Whistleblower Statute

- Section 7623(b) creates the first true tax whistleblower statute:
  - Reward is between 15% and 30% of total amount collected
  - Can be reduced to 10% for “less substantial contribution”
  - Applies to civil and criminal cases
  - Effective date December 20, 2006

# Simultaneous Criminal and Civil Examinations



# Burden of Proof Shift

- Section 7491 allows the burden of proof to shift to the government if:
  - Taxpayer produces “credible evidence”
  - Taxpayer has complied with any substantiation requirement, and
  - Taxpayer has cooperated with reasonable requests during audit
- Limitation: Does not apply to high net worth/high income taxpayer

# Individual Audit Targets

- Section 1031 exchanges
- Section 183 hobby losses (Section 469 passive activity rules)
- Listed transactions
- Executive compensation
- Unreported income (the “tax gap”)

## Individual Income Tax Underreporting Gap Estimates, Tax Year 2001

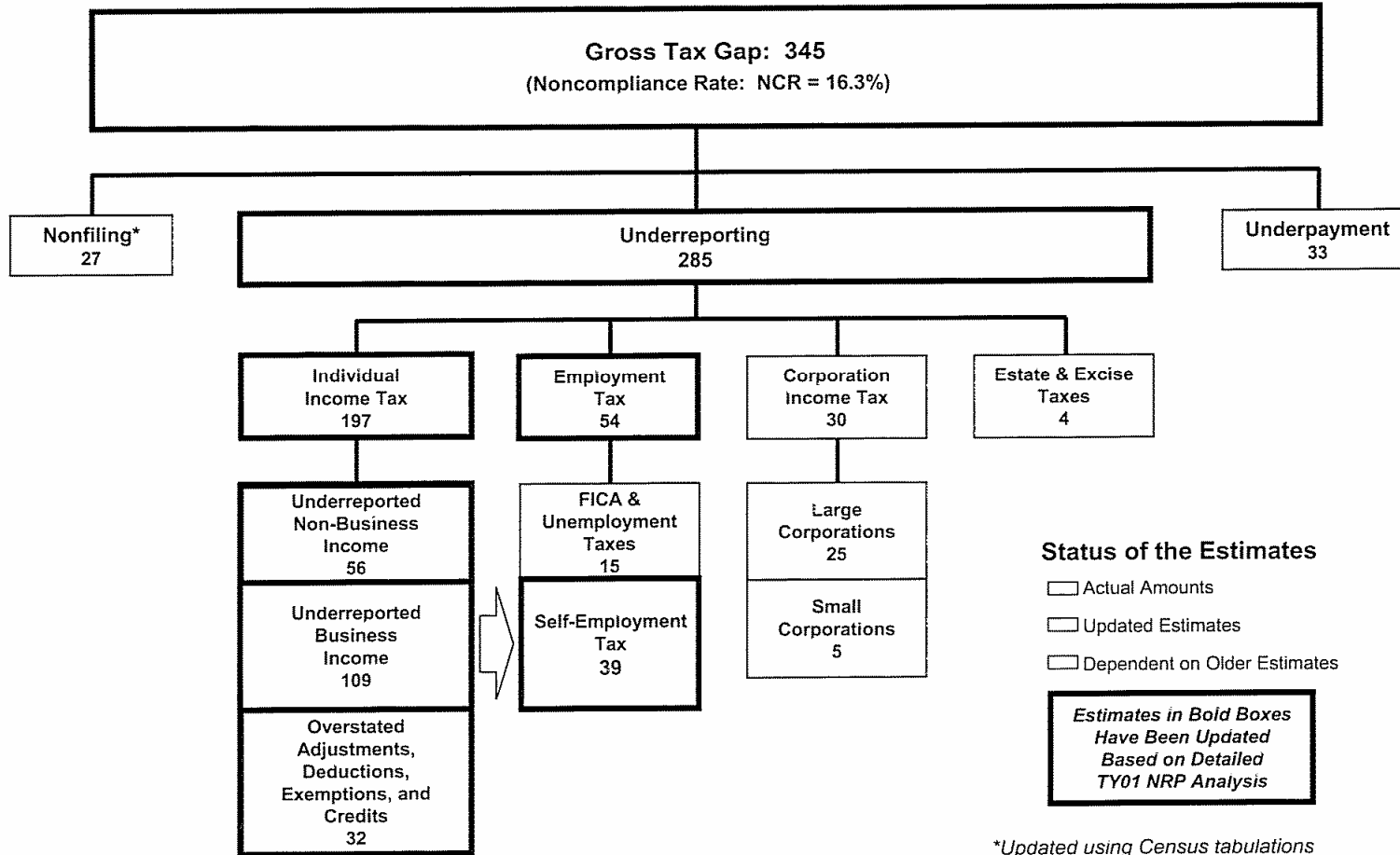
<i>Type of Income or Offset</i>	<i>Tax Gap (\$B)</i>	<i>NMP †</i>
<b>Total Underreporting Gap</b>	<b>197</b>	<b>18%</b>
<b>Underreported Income</b>	<b>166</b>	<b>11%</b>
<b><i>Non-Business Income</i></b>	<b>56</b>	<b>4%</b>
Wages, salaries, tips	10	1%
Interest income	2	4%
Dividend income	1	4%
State income tax refunds	1	12%
Alimony income	*	7%
Pensions & annuities	4	4%
Unemployment Compensation	*	11%
Social Security benefits	1	6%
Capital gains	11	12%
Form 4797 income	3	64%
Other income	23	64%
<b><i>Business Income</i></b>	<b>109</b>	<b>43%</b>
Nonfarm proprietor income	68	57%
Farm income	6	72%
Rents & royalties	13	51%
Partnership, S-Corp, Estate & Trust, etc.	22	18%
<b>Overreported Offsets to Income</b>	<b>15</b>	<b>4%</b>
Adjustments	-3	-21%
SE Tax deduction	-4	-51%
All other adjustments	1	6%
Deductions	14	5%
Exemptions	4	5%
<b>Credits</b>	<b>17</b>	<b>26%</b>
<b>Net Math Errors (non-EITC)</b>	<b>*</b>	

† NMP = Net Misreporting Percentage

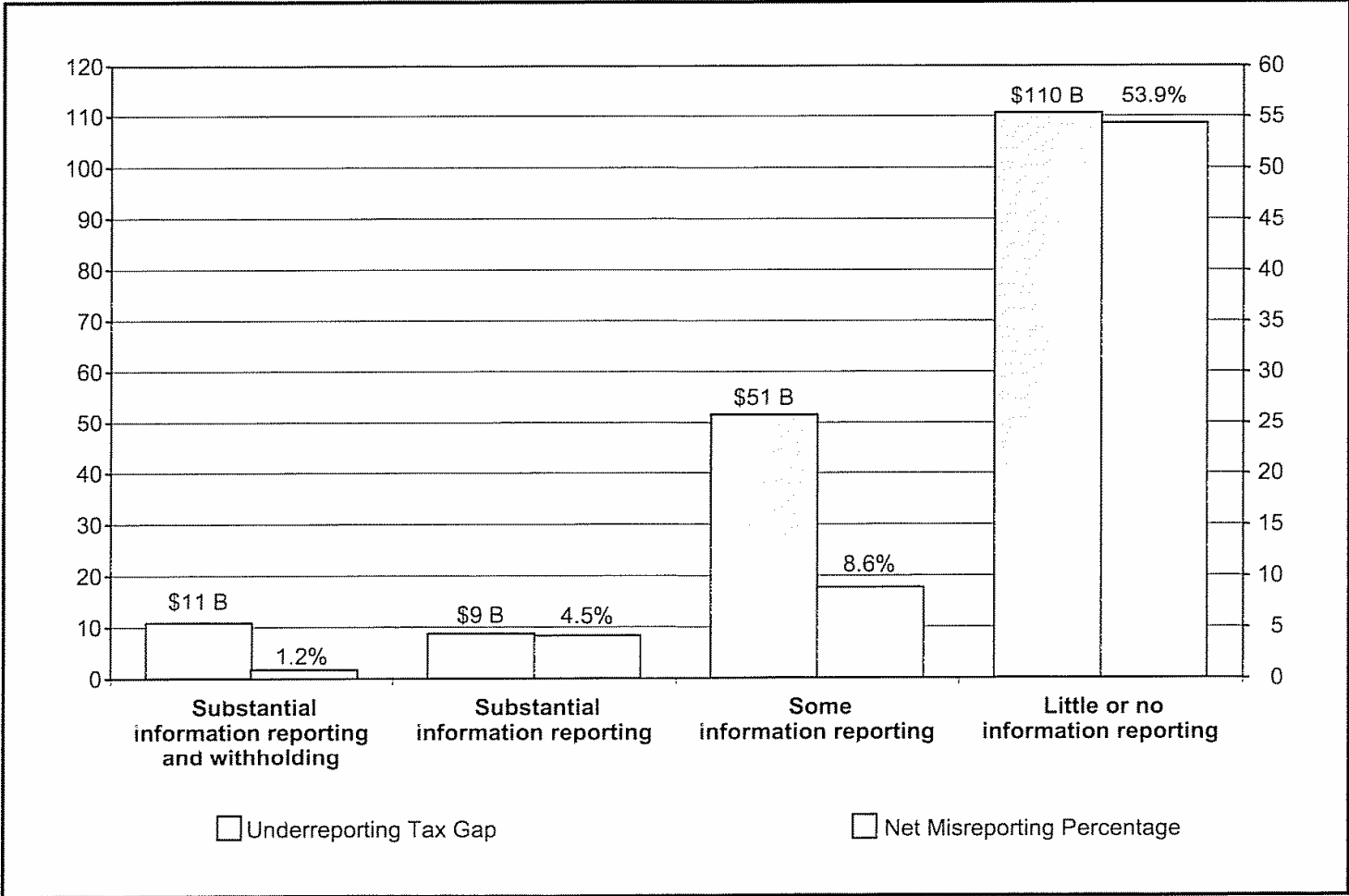
\* Less than \$0.5 billion.

# Tax Year 2001 FEDERAL TAX GAP

(in Billions of Dollars)



# Individual Income Tax Underreporting Gap



# Individual Income Tax Underreporting Gap Little or No Information Reporting

(Dollars in Billions)

