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2020 Audit Triggers

After a brief break during the height of the spring shutdown, the IRS is back at it, auditing certain taxpayers. Your financial situation has likely gone through some unexpected bumps in 2020, which means your taxes could be more complicated than ever for the coming tax season. Keep an eye on the following tax triggers for both individuals and business owners to avoid turning those complications into legal and financial hardships.

PPP loan fraud: For business owners who received a federal Paycheck Protection Program (PPP) loan this spring and misused it, the time of reckoning has come. More than a dozen criminal cases have been filed across 11 states involving PPP loan misuse. These first cases involve "blatant fraud" by small businesses and individual business owners, not large corporations. You may have heard that those who took out a PPP loan for less than $2 million won't be audited. But if the IRS suspects fraud, all bets are off.

High-net-worth activities: The Global High Wealth Industry Group (GHW) of the Large Business & International (LB&I) Division includes a team commonly called the IRS "Wealth Squad." These examiners are solely focused on conducting audits of taxpayers with around $1 million in liquid financial assets. This fall, they've been using data analytics to identify and audit high-net-worth-individuals who also own partnerships or other pass-throughs like disregarded entities and S corporations or trusts, or who own offshore accounts and foreign trusts. These entities require numerous different forms and filings throughout the year. Be sure to stay on top of those deadlines, particularly if you own foreign assets, for which the regulations are ever-changing.

Syndicated conservation easements: Designating conservation easements on a property can be a great way to preserve land while gaining a valuable tax break. But the IRS is cracking down on abuses of this practice by partnerships and individuals who have invested in something called syndicated conservation easements. Those who have taken part in syndicated transactions may have already received a time-sensitive ultimatum from the IRS (in the form of a settlement offer). The settlement requires a concession of the income tax benefits claimed by the taxpayer and imposes penalties.

Over-the-threshold deductions: The standard deduction threshold for individual income tax returns ($24,800 for married couples and $12,400 for individuals in 2020) put an end to itemized deductions for many taxpayers. Exceeding that amount may trigger an audit, particularly by claiming sizable charitable contributions, self-employment deductions, repeated business losses, or rental income losses. Some of these triggers are worth the risk if they result in substantial tax savings, but it's essential to maintain receipts and records for itemizing and to follow best practices.

Early retirement withdrawals: You may have heard that the CARES Act for coronavirus relief allows you to dip into retirement savings without penalty this year. That's only partially true. The Act enables early withdrawals from eligible IRAs and employer-sponsored 401k plans without the usual 10% penalty. But that's only if you or a family member have been officially diagnosed with SARS-CoV-2/COVID-19 and/or only if you can prove you've experienced adverse financial consequences from being quarantined, furloughed, or left without childcare due to the virus. Early retirement distributions are still a top audit trigger, and the penalties are steep, so it's critically important to follow guidelines closely.

Don't rest on the assumption that the IRS is too distracted to notice your returns in 2020. Remember that the IRS has three years from the time you file a return to audit it. If you neglect to file a return for a given year, there is no deadline for the IRS to audit. Be on top of your deadlines, and follow guidelines as closely as you can, to ensure this remarkable year doesn't come back to haunt you later.

Steven Bankler has more than 43 years of experience in the accounting industry. Steven's expertise lies in consulting, planning, tax, and asset protection as well as exit strategy services for closely-held businesses. He also provides litigation support (both as a testifying expert witness and consulting expert), business negotiations and estate planning. Visit www.bankler.com for additional tax strategy tips and to learn more about Steven Bankler, CPA, Ltd.