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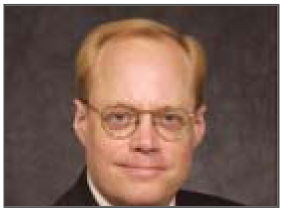

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How Long Can IRS Audit? It All Depends On You

In most cases, the IRS has three years after you file to audit. If the IRS shows up after that, you may be able to point out that the statute of limitations has run. It's better than hunting for receipts! But there are many special rules that can extend the purgatory.

First, the three years is ***doubled* to six** if you omitted more than 25% of your income. It's also doubled if you omitted more than $5,000 of foreign income. Even worse, the IRS has ***no*** time limit if you ***never*** file a return. The three years never starts to run.

There's no time limit if you fail to report certain foreign assets, even though the IRS has become much better at ferreting out foreign account information. This makes it all the more important for taxpayers to report foreign assets and accounts as required.

There's also no time limit on fraud. Fraud is the IRS's greatest trump card. You might think the IRS might assert fraud just to get unlimited time. Fortunately, though, the IRS has a high burden to show fraud. Here are other timing rules you should know.

(Photo credit: 401(K) 2013)

Extend? The IRS may contact you (usually about two and a half years after you file), asking you to ***extend*** the statute. Most tax advisers say you should usually grant an extension. Some taxpayers say "no" or ignore the request. Either usually leads the IRS to send a notice assessing extra taxes.

Amend? To amend a tax return, do it within three years of the original filing date. If your amended return shows an increase in tax, and you submit the amended return within 60 days before the three-year statute runs, the IRS only has 60 days after it receives the amended return to make an assessment. An amended return that does not report a net increase in tax does not trigger an extension of the statute.

Refunds. If you pay estimated taxes or have excess withholding but fail to file a return, you generally only have ***two*** years (not three) to get it back.

State Timing. Some states have the same three- and six-year statutes as the IRS. But some set their own time clocks, giving themselves even more time to assess extra taxes. In California, for example, the basic tax statute of limitations is four years. However, if the IRS adjusts your federal return, you are ***obligated*** to file an amended return in California. If you don't, the California statute will ***never*** expire.

Partnerships? Partnerships and LLCs generally don't pay tax themselves, even though they file tax returns. Rather, their partners or members pay the tax. Statute issues come up frequently with partnerships. For example, what happens when a tax notice is sent to a partnership, but not to its individual partners?

The audit or tax dispute may be ongoing, but you may have no personal notice of it. As a result there are numerous special rules for partnerships. In general, partnerships have a "tax matters partner" who gets notice.

John Doe Summons. Another set of rules says the statute of limitations may be "tolled" (held in abeyance) by an IRS John Doe summons. That is so even if you have no notice of it. It works like this.

Suppose that a promoter has sold you on a tax strategy. The IRS may issue a summons to the promoter asking for all the names of his clients and customers. While the promoter fights turning over those names to the IRS, the statute of limitations clock for his clients is stopped.

Bottom Line? Statute of limitations issues can be pivotal in tax cases. Of course, the difference between winning and losing often depends on records. The statute usually begins to run when a return is ***filed***, so keep certified mail or courier confirmation. If you file electronically, keep all the electronic data, plus a hard copy of your return. If you can successfully assert a defense based on the statute of limitations, you don't have to go further!

You can reach me at Wood@WoodLLP.com. *This discussion is not intended as legal advice, and cannot be relied upon for any purpose without the services of a qualified professional.*