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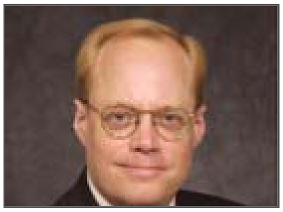

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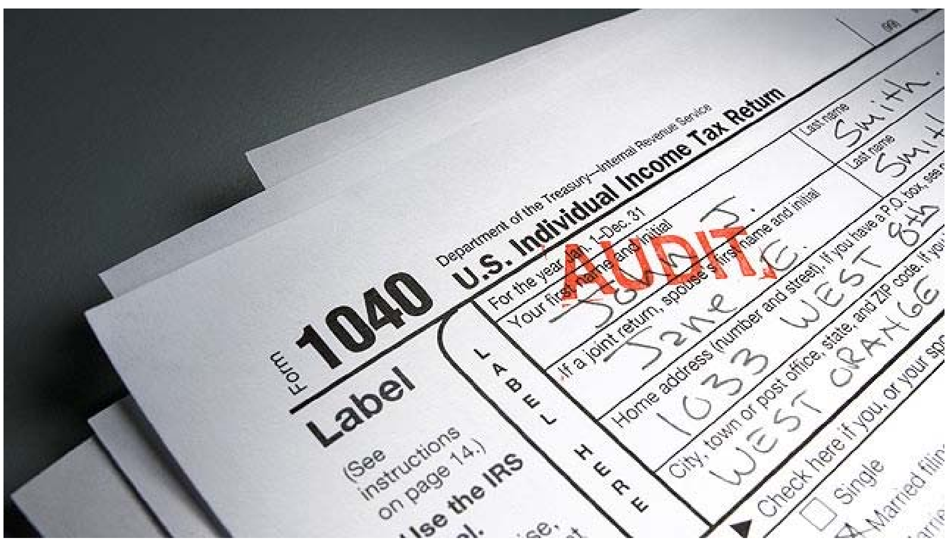
IRS Audit Period Just Doubled From Three Years To Six Years For Many

No one wants to be audited, and knowing how long your tax return can be attacked is important. Most people know that the IRS statute of limitations is *usually* three years. But there are many exceptions that give the IRS six years or longer. And one of those six year exceptions just got bigger, *way* bigger, despite the U.S. Supreme Court.

The three years is doubled to six if you omitted more than 25% of your income. That is called a substantial understatement of income. But for years, the debate has been over what it *means* to *omit more than* 25%. The IRS argues it isn't just gross income we're talking about.



- Example: You sell a piece of property for $3M, claiming that your basis (what you invested in the property) was $1.5M. In fact, your basis was only $500,000. The effect of your basis overstatement was that you paid tax on $1.5M of gain, when you should have paid tax on $2.5M.

The issue came to a head in 2012. The Supreme Court in *U.S. v. Home Concrete & Supply, LLC* dramatically cut back on IRS reaches into six year territory. The Supreme Court held that overstating your tax basis was not the same as *omitting* income. The Supreme Court said 3 years was plenty for the IRS. Some observers thought the Supreme Court might try to find a way to allow the IRS to go for six years. Nope, the High Court stuck to three years.

But Congress just gave the IRS the last laugh. H.R. 3236, the Surface Transportation and Veterans Health Care Choice Improvement Act of 2015, *overrules* the Supreme Court. Now, the tax code says: “An understatement of gross income by reason of an overstatement of unrecovered cost or other basis is an omission from gross income.” The change applies to tax returns filed after July 31, 2015. It also applies to previously filed returns that are still open.

Can you shorten the audit period by filing your return early? Normally no, the IRS audit clock starts running on the *later* of your actual filing or the due date. So, if you file in January and your return is due April 15th, the audit clock starts to tick on April 15th. The time periods can be downright frightening in some cases. The IRS has no time limit if you never file a return. For unfiled tax returns, criminal violations or fraud, the IRS can take its time. In most criminal or civil tax cases, though, the practical limit is six years.

Still, some taxpayers can end up in audit purgatory. For example, if you miss some tax forms, the IRS can audit forever, and occasionally they do try to reach back 10 or more years. It’s also doubled if you omitted more than $5,000 of foreign income (say, interest on an overseas account); the IRS can audit up to six years from your original filing. International information returns, such as Form 3520 for gifts or inheritance from foreign nationals, or Form 8938 for overseas assets, give the IRS three years from filing those forms.

If you’ve ever been audited by the IRS, you may think going back three years is bad enough. But once an assessment is made, the IRS collection statute is normally 10 years. Incredibly, in some cases the IRS can go back 30.

In *Beeler v. Commissioner*, the Tax Court held Mr. Beeler responsible for 30 year-old payroll tax penalties. Hiring a payroll service is often an good move, but even that may not insulate you. It’s one reason some say your newest tax fraud threat is your payroll tax. Flat tax, anyone?

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