

# Top Ten ways to **fail** an IR\$ Audit

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# Bill Barnes Bio

- BBA University of Notre Dame, CPA, CMA
- Arthur Andersen-Contractors, Mfg, Non Profit
- Abbot labs-Audit, Mfg, Engineering, Fin Report
- Coopers & Lybrand – Management Consulting
- Givens & Barnes
  - Audit, tax, accounting, accreditation reviews
  - Small businesses, non profits, individuals
  - Non profits are primarily associations (i.e. IKECA)

# Top Ten

1. Documentation of meals & entertainment
2. Personal use of company vehicle
3. Classification of employee vs. contractor
4. Failure to issue 1099s to contractors
5. Documentation of business trips
6. Personal use of cell phones
7. S-Corp distributions (if applicable)
8. Sloppy bookkeeping
9. Shareholder loans
10. Self-representation in an IRS audit

# Meals & Entertainment

Document, Document, Document...

- Business purpose of the meeting, examples:
  1. Discussed proposal with potential customer
  2. Discussed referral opportunity with customer
  3. Discussed contract renewal
  4. Discussed past performance with customer
  5. Discussed business development with employee
- Entertained Who?
  1. Name
  2. Title
  3. Company

See IRS Publication 463 ([irs.gov](http://irs.gov))

# Company Vehicles

- Work vans and trucks are almost always 100% business use vehicles
- Autos and SUVs are almost always not 100% business use vehicles
  1. Be sure to charge owners & employees for personal use of company vehicles
  2. Maintain & save logs for these vehicles. If no log, maintain & save date books (or outlook calendar)

# Employee vs. Contractor

- IRS prefers employees – taxes, benefits, etc
- If your “contractor” is deemed to be an employee, you may be required to pay any unpaid taxes
- Determination of employment status is a “facts and circumstances” test based on:
  1. Behavioral control (instruction & training)
  2. Financial control (investment, expenses, profit)
  3. Relationship (contract, benefits)
- Simple 2 page brochure at [irs.gov](http://irs.gov) “publication 1779”

# Form 1099

- Be sure to get a ***signed*** W-9 from all contractors
- Be sure to send 1099s to all those who qualify to get one
- You may be on the hook for their taxes if you do ***not*** send the 1099

# Business Trips

- Refer to slide on Meals & Entertainment
- Business purpose of trip – how will business benefit, what do you expect to gain
- Who did you meet with? Names, titles, companies , etc. What did you discuss? How long did you meet?
- Keep business separate from personal – i.e. spouse, etc.



# Cell Phones

- Has been a hot button
- “Family” plans. Be sure to remove an amount for personal use.
- IRS proposes 75% business use as a safe harbor
- See Internal Revenue Bulletin 2009-23 ([irs.gov](http://irs.gov))

# Shareholder Distributions

- Relates to Subchapter S Corporations only
- Tax strategy is to pay wages to owner (subject to FICA & Medicare @ 15.3%) and shareholder distribution (not subject to FICA & Medicare).
- Make sure to pay a “reasonable” wage to the owner. Be careful - don't pay too low a wage or nothing at all.

# Sloppy Bookkeeping

- Worst case scenario
- Example – IRS reviewed bank statements and took all deposits as income and disallowed ALL expenses
- Make sure you have separate business banks accounts, accounting software, professional assistance, backup for all revenue and expenditures

# Shareholder Loans

- Short term advances < \$10,000 ok
- Document the terms with a formal note
- Pay interest at IRS determined rates
- If not, IRS may consider this compensation

# Self Representation with IRS

- Get a qualified professional to assist
- Keeps credibility high
- Allows time and space to answer all questions
- Removes IRS from your work place
- Most agents also prefer this scenario