

AUDIT

"A DREADED FIVE LETTER WORD"



Compliments of

Every April, many taxpayers face the necessary filing of their income tax returns. Here are some facts regarding the Internal Revenue Service (IRS) and audits.

INTERNAL REVENUE SERVICE STATISTICS

So what is the value in calling the IRS? Consider these statistics from a May 2001 Treasury Department Report, Reference Number 2001-40-077:

- The IRS provided incorrect or insufficient answers to taxpayers 73 percent of the time.

According to IRS statistics reflected in an Associated Press article, things did not improve much in 2002:

- The IRS only answered 68% of the calls to their toll-free telephone numbers.
- Only 45% of the questions were answered correctly and completely.
- IRS employees gave wrong answers to 28% of the questions.

RESULTS OF A 2002 STUDY

- In a 6-month study, the IRS gave incorrect answers to tax law questions 43% of the time.
- Over 1/2 million taxpayers during this 6-month period probably received incorrect responses.

THE ODDS OF AN AUDIT

- The audit rate for 2002 was 0.57%, which equates to about 1 million tax returns. This is below the historical IRS audit rate of around 1%.
- The odds of an audit in 2002 were 1 in 65,000.

WHAT ABOUT §1031 EXCHANGES?

When it comes to IRC §1031 tax deferred exchanges, many taxpayers wonder if performing an exchange increases their chances of an audit. The answer is an unequivocal "no." Historically, the IRS has not audited investors who perform §1031 exchanges more than any other group of taxpayers.

A Qualified Intermediary should always recommend that taxpayers seek the advice of their personal tax and/or legal advisors regarding their tax deferred exchange and their specific situation. A Qualified Intermediary cannot provide tax or legal advice. Additionally, a Qualified Intermediary is generally not aware of the many other variables or financial planning issues that could be important. Examples of other issues include suspended losses or financial planning/title issues that often become important in second marriages.

The bottom line is that it is critical for an Exchanger to review their transaction with knowledgeable advisors and to feel comfortable that they have sufficient documentation and facts and circumstances to substantiate their intent to hold property for investment.



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