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Rich Are Targeted in IRS Audit Offensive

By [LAURA SAUNDERS](#)

The Internal Revenue Service is stepping up audits of wealthier taxpayers as part of a multiyear effort to crack down on tax avoidance.

According to the agency's latest statistical report for the fiscal year ended Sept. 30, the percentage of taxpayers who were audited increased in every category of adjusted gross income above \$500,000, compared with a year earlier.

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The biggest jumps came at the top of the income ladder. About 18% of Americans earning at least \$10 million were audited in fiscal 2010, up from 11% in fiscal 2009, according to the IRS. For those earning \$500,000 to \$1 million, the audit rate rose to 3.4% from 2.8%.

Accountants and tax preparers said the IRS's heightened scrutiny of wealthier taxpayers is in sharp contrast to the agency's audit practices during the previous decade.

David Lifson, an accountant in New York for Crowe Horwath LLP, said the number of audits among his high-earning clients has "at least doubled, if not tripled" in the past two years. The audits often are "correspondence" exams in which a series of letters is exchanged. Such exams account for more than 70% of IRS audits of individuals.

"They are touching a broader group of high-income taxpayers, asking about one or two issues at a time," Mr. Lifson said. Common issues include high deductions for mortgage interest and charitable gifts.

In 2009, IRS Commissioner Doug Shulman announced limited amnesty for U.S. taxpayers with undeclared offshore accounts, as well as creation of the agency's Global High Wealth Industry group, known as the "wealth squad," to undertake detailed audits of the highly affluent.

The IRS announced in February another limited amnesty, with tougher terms, for undeclared foreign accounts. It ends Aug. 31.

Janet Hagy, a certified public accountant in Austin, Texas, with about 800 affluent clients, said she has handled more than a dozen audit cases in the past year, up from none in "four or five years" of the past decade. Those cases were resolved relatively easily, such as by substantiating capital gains or interest expense, she said.

The scrutiny can be much more intense.

In the process of setting up a comprehensive audit for one taxpayer with an income of more than \$10 million, the IRS tapped six agents and a lawyer with wide-ranging expertise, said Martin Press, a tax lawyer at Gunster, a Fort Lauderdale, Fla., law firm.

Battery of Questions

The agency also submitted a battery of detailed questions, including which magazines the taxpayer subscribed to and how deeply involved the client's wife was in the business.

Andrew Mattson, a certified public accountant at Moler, Nixon & Williams in Campbell, Calif., has a redacted copy of a nine-page document request from an IRS "wealth squad" in June 2010 that contained more than 60 detailed questions. Among the demands: details on assets transferred to children or relatives, hedge-fund or private-equity investments, asset appraisals and copies of compensation agreements.

Complying with such requests can cost at least \$10,000 in accounting fees, excluding legal fees, Mr. Mattson estimated.

Some accountants are trying to head off audits by the IRS.

James Guarino of Moody, Famiglietti & Andronico, a Tewksbury, Mass., accounting firm, said that if a client donates closely held stock to a charity, he provides a summary of key points in addition to the appraisal that is required by law.