

How to Prepare for a Tax Audit

There is no reason to be afraid of an audit if you have been ethical and truthful in your accounting methods. However, it is best to be prepared for an audit to make sure that it runs smoothly. Different types of audits require different preparation methods.

If a business is brought up for an audit by the IRS, there are several things you can do to prepare your business for audit. First, review the tax returns that are being audited. Make sure that you are ready to explain how you or your tax preparer came up with the figures in the return when you go into the audit. If you don't know how your tax preparer came up with the figures, or you have any questions, you should contact your tax preparer prior to the audit for any clarification needed so that you are thoroughly prepared for the audit.

Organizing records used to prepare your tax returns yearly is a great way to maintain proper accounting before an audit. However, if you have not organized your records as you filed year by year, now is the time to organize them for the audit. Make sure that the person performing the audit has access to all records used to prepare the tax returns. For the audit to go smoothly, these records should be organized in a logical fashion. In addition to making an audit quick and painless, this organization will lend you credibility with the auditor, thus making the auditor take things in stride if a small issue does arise during the audit.

Your audit notice should tell you what documentation the auditor wants to see during the audit. Typically, auditors may want to see bank statements, canceled income checks, receipts for expenses, and your financial records. If you have a smaller business, you are not required to maintain a formal set of financial records such as journals and ledgers. However, the auditor may request to see any financial records you do have, and see your bookkeeping system during the audit. If your bookkeeping system is on a computer or otherwise electronic, make sure you take a printout of your financial records with you. If you do keep a ledger and journal for financial records, the auditor is entitled to see them and you should bring them to the audit also. In addition, you should bring with you any prepared financial statements so that the auditor has a clear overview of your bookkeeping.

If you don't keep a formal set of financial records and you are missing a few receipts, take your appointment books, service logs, and diaries with you to the audit as well. The documentation in your appointment book, service log, and diary will substantiate your expense for deduction without a receipt, provided the expense can be proved to be reasonable based on the information in your

personal records.

If you have a home based business, you will also want to bring with you to your audit any usage logs of "listed property." This is anything that you use for business and home use. Usage logs show that you use these things for business purposes, thereby allowing you to take a partial deduction for that property during the audit if you have not already done so.

If you are in any doubt as to what information you need to prepare for your business tax audit, you should contact a certified public accountant to assist you and represent you to the audit representative.