Willard J. De Filipps, CPA, PC
www.defilipps.com
A Quarterly Update of Essential Tax Information

DEALER TAX WATCH

Volume 13, Number 4 | Publisher: Willard J. De Filipps, C.P.A. | December 2006

DEALER TAX WATCH *OUT*

If you had called me personally to ask, "What's happening lately with IRS audits of dealers and dealerships that I need to know about?" ... Here's what I'd say:

#1. THE FOCUS OF THIS ISSUE IS ON TWO PRESENTATIONS AT THE AICPA AUTO DEALERSHIP CONFERENCE. It's been relatively quiet over the last few months ... However, a lot of excellent information was available at the AICPA National Auto Dealership Conference in Phoenix on Oct. 26-27, 2006.

Most of this issue of the *Tax Watch* is devoted to two major Conference update presentations ... one by the IRS Motor Vehicle Technical Advisor, Ms. Terri Harris ... the other, by attorney Rich Sox, who discussed dealer-manufacturer conflicts and issues. More about each of these a bit later... But, first, let's get caught up on some current IRS audit activity in the field.

#2. IRS AUDIT ACTIVITIES. Evidence of greater IRS audit activity is everywhere. Discussions with individual practitioners confirm this. Various Fall meetings of dealership CPA groups confirm this. And, Terri Harris, from the IRS, confirmed this in her presentation at the Conference.

It seems unanimous that these audits by the IRS are by no means being conducted by agents with uniformly high levels of experience. Nor are these agents looking into identical target issues on every audit. Some agents are examining selected technical issues relentlessly. Others barely give these issues a cursory glance or a nod. Despite the lack of IRS audit focus uniformity, we're comfortable making the following generalizations.

IRS target area - S corp. compensation. Where part of the IRS pre-audit activity involves a pair of human eyes scanning the tax returns, if a dealership is operating under Subchapter S and the tax return shows no deduction for salaries for officers, the absence of a deduction for officer compensation is very likely to trigger an audit. Why? Because the IRS is greatly concerned about the possibility of taxpayers playing games with payroll taxes.

One action that might possibly forestall an audit on this is preemptory disclosure. The suggestion is to attach an appropriate explanation or note in the tax return to justify the absence of a deduction for officers' compensation.

Many dealership officers are drawing salaries from other corporations or from management entities. If this is the case, explaining this in an attachment to the return may avoid an audit (at least, that's what one auditor told a CPA). We've also heard that some processing centers have routinely sent out computer-generated letters where the Form 1120-S

WATCHING OUT FOR

see **DEALER TAX WATCH OUT**, page 2