PERSPECTIVE

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Haven't Filed Your Taxes Yet?

By Robert W. Wood

This year, individual tax returns are due on Tuesday, April 18 — not last Saturday, April 15. These few extra days don't matter to people who already filed, and to those who always go on extension. But if you are in neither camp, should you rush to file on time, or should you go on automatic extension?

Few deadlines are more dreaded than April 15 (well, 18 this year). Still, this can seem like a tough decision. A common question is whether succumbing to the allure of an extra six months increases or decreases your odds of audit. How could it do the latter?

First, like tearing off a band aid, you may not *want* to delay filing. You may even feel guilty if you take advantage of an automatic six-month reprieve. But millions of extensions are processed every year. It's easy.

Everyone with an April 18 deadline can get *six extra months* by filing (electronically or by mail) a tiny form. It does not even require a signature. You need to pay what you owe — the extension is to *file* your return not to *pay* — but in my view, there are often good reasons to take the extension.

Many people are obsessed with IRS audit risk. Audits are worrisome and expensive, and opinions vary widely on how to avoid them. What's worse, there are many old wives' tales about what does or doesn't trigger them. But what about the time of filing? Many believe that filing at or near a deadline reduces audit risk.

A crush of other filers, as often occurs on April 15, logically may reduce the chance that your return will stand out from the millions of others. Even if that is true, that logic may also apply to the crush of tax returns filed on extension Oct. 15. Some say you increase audit risk by going on extension, while others say you actually decrease it.

There is no official data, and the IRS is predictably mum. The IRS does release data about audit rates based on income levels, types of tax returns, and similar criteria. They do not, however, release data about whether going on extension increases or decreases your chances.

Still, there's a reasonable case to make that an extension may actually decrease your audit risk. The best reason to go on extension is if you need time to consider proper reporting, get professional advice, and file an accurate return.

File accurately so you don't have to amend later. After all, amended returns are more likely to be scrutinized, so file once accurately if at all possible. Going on extension encourages reflection, which can make your return when filed more solid.

Moreover, the passage of time means that you are sure you have all those pesky Forms 1099 and Forms K-1. You may be waiting for Forms K-1, gathering documents or seeking professional advice. If there are debatable points on your return, such as whether a litigation recovery is ordinary or capital, get some professional advice.

But, even if you have all your forms and are ready to file on time, what if you receive a Form K-1 or 1099 *after* you file? The earlier you file, the greater the risk you will receive corrections. Going on extension makes it less likely that you will be surprised by a tardy corrected Form K-1 or 1099.

Sure, most Forms 1099 come in January, with stragglers in February. However, I have seen Forms 1099 show up in May. And Forms K-1 are even more notorious stragglers. What's worse, you may receive all your Forms K-1 in time for an April 15 filing. Then, right after you file your return — or sometimes months later — you get amended K-1s!

Will the IRS go on the amended K-1s, or the ones you filed? Must you amend your return, or should you? This can make for some big worries, and can increase your audit risk significantly.

An extension to file is automatic. The IRS doesn't have to approve the extension; there is no discretion involved. You just get the extra six months, period. Extensions used to be four months, with two additional months only if you had a good reason. Now, automatic extensions are six months.

Again, though, the extension is to *file*, not to *pay*. Often, the question how *much* to pay is a tough one. You can ballpark it, or try to calculate it to the penny. And you may have to estimate on some things.

For example, suppose you don't know if a payment is capital gain or ordinary income. You can pay based on either one, estimating conservatively or liberally. You'll either owe more or be due a refund when you file in October.

Finally, bear in mind that if you do get substantive tax advice, your tax lawyer or accountant may speak practically about audit risk or even audit triggers. Some things are obvious, such as mismatches of Form 1099 information. But if your tax advisor opines that you have strong — maybe more-likely-than-not — arguments for a particular tax position, consider what that means.

Your tax advisor is required (by IRS rules) to *assume* that you will be audited. That is, a tax opinion cannot be based on the audit lottery. A more likely than not opinion means that, if the IRS or a court were looking at the transaction or issue, there is a better than 50/50 chance the IRS or court would agree with you.

Your *actual* chance of audit might be only 5 percent. But if you are audited, you'll be glad you have backup. No client who ends up audited will be comforted to know that they only had a 5 percent chance of audit, if they end up being in that 5 percent.

In sum, go on extension if you need the time. You can mail a Form 4868, ask your return preparer, use commercial software, or do it yourself electronically. For more guidance, IRS tax topic 304 covers extensions of time to file your tax return.

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