What Could Trigger an IRS Letter (Even If You're Doing Everything Right)

Nobody wants to hear from the IRS—especially not when you're running a business and juggling a million other things. But even honest, hard-working business owners can raise red flags without realizing it.

Let's break down the most common business income-related triggers we see—and what you can do to steer clear of unwanted attention.

Common IRS Red Flags for Business Income

Here are some of the most common income-related red flags the IRS might spot, and how to avoid them:

- **You forgot to include side income or payment app deposits.** Did you freelance a bit on the side or get paid through Venmo, Square, or PayPal? Those platforms now report income directly to the IRS. If you're only tracking what lands in your business bank account, you could miss something—and the IRS won't.
  - Example: Sarah runs a home bakery and sometimes takes Venmo payments for custom cakes. She forgot to log a few of those small payments. The total added up to $3,200—just enough to raise a red flag when her reported income didn't match what Venmo reported to the IRS.
- **Your deposits don't match your sales.** Let's say your sales report says you earned $120,000, but your bank shows deposits totaling $135,000. That mismatch could be from loans, owner contributions, or app transfers—but if it's not clearly documented, it might look like you're hiding income.
- **Big deductions with little income.** Big deductions with small revenue can raise red flags. For example, claiming $40,000 in expenses on just $10,000 of reported income? That's going to stand out. While there might be legitimate reasons—like startup costs or slow seasons—you need clean documentation to back it up.
- **Year-over-year inconsistencies.** Sudden drops (or spikes) in income without a clear reason could get noticed. Let's say, last year you made $200,000 and this year you reported $25,000 with no clear explanation, the IRS may come knocking. Unexpected spikes or drops don't mean you're doing something wrong—but they do need to be explained.
- **Mixing personal and business funds.** Depositing personal funds into business accounts (or vice versa) without proper documentation makes your financials messy and harder to defend if questioned. Keep your records tidy and label all transfers clearly to avoid looking like you're commingling funds.
- **Inconsistent reporting across documents.** What you report on your tax return should match your bookkeeping. Discrepancies between forms, reports, and filings can create unnecessary scrutiny, especially when they involve income.
- **Cash-heavy businesses not properly tracked.** If you run a business that handles a lot of cash (like hospitality, beauty, or retail), the IRS pays closer attention. Proper logs and consistent records are essential.

Why This Matters

It’s not about doing something wrong—it’s about looking like you might have. The IRS uses algorithms to spot inconsistencies and patterns. Sometimes, all it takes is one oversight to prompt a closer look.

Make Sure Your Numbers Add Up

If the numbers are inaccurate or things aren’t tracked clearly, it can appear worse than it is. And that’s where we come in.

Need a second set of eyes on your books?

We’ll help you clean things up and stay ahead of the curve—no stress, no surprises. Give us a call.