

# WHAT TO SAVE, WHAT TO TOSS



According to the *Data Book* released by the IRS on March 24, the agency collected almost \$3.1 trillion in federal revenue and processed almost 240 million returns during fiscal year 2014. About 65 percent of all returns were filed electronically. Of the 147 million individual income tax returns filed, 84 percent were e-filed.

You might think those numbers suggest we are close to becoming a paperless society, at least when it comes to the IRS. That would be a wrong assumption. Even if you recently filed your 2014 tax return electronically, you probably printed out a hard copy for your files. Add that paper to the financial reports, bank statements, receipts and other documents you may have been holding onto for years and it's likely your filing cabinets and closets are overflowing with paper.

Do some cleaning, but you shouldn't just dump old tax records without thinking about the process. Some of the documents may still be needed in case the IRS ever comes calling.

## IRS Audits and Amended Returns

You should generally keep records supporting items claimed on your individual tax return until the statute of limitations runs out. Typically, that is three years from the due date of the return or the date you filed, whichever is later. So this year you can generally toss out your tax records for the 2011 tax year (return filed in 2012) and most paperwork you have left from that year and earlier years.

But keep your files for the past three tax years. This is because the IRS can audit your returns for a minimum of three years after you file. You can also file an amended return on IRS Form 1040X during this time period if you missed a deduction, overlooked a credit or misreported income.

But you are not necessarily safe from an audit after three years have passed. There are a couple of key exceptions to this general rule:

1. **The statute of limitations increases** to six years if the IRS has reason to believe you understated your income by 25 percent or more, and
2. **There is no time limit** if the IRS suspects fraud or you do not file a tax return.

## Various Retention Requirements

Keeping records for 3 years is the general rule. There are exceptions for certain records. In some cases, there is no easy answer to the question for how long you should keep specific papers. The IRS does not require you to keep records in any particular way. But here are some basic guidelines for individuals to follow:

**Completed Tax Returns** Some tax advisers recommend that you hold onto copies of completed, filed returns for your lifetime. The reason is so that you can prove to the IRS that you actually filed if there's ever a question about it. Even if you don't keep the returns indefinitely, you should hang onto them for at least six years after they are due or filed, whichever is later.

**Backup Records** Any written evidence that supports figures on your tax return, such as receipts, expense logs, bank notices and sales records, should generally be kept for at least three years.

**Exceptions** There are times when you may be entitled to more than the usual three years to file an amended return. For instance, you have up to seven years to take deductions for bad debts or worthless securities, so don't toss out records that could result in refund claims for those items.

**Real Estate Records** Keep real estate records for as long as you own the property, plus three years after you sell (or otherwise dispose of) it and report the transaction on your tax return. Throughout ownership of the property, keep records of the purchase, as well as receipts for home improvements, insurance claims, and documents relating to refinancing. These may help prove your adjusted basis in the home, which is needed to calculate the taxable gain at the time of sale, or to support calculations for rental property or home office deductions.

**Securities** To accurately report taxable events involving stocks and bonds, you must maintain detailed records of purchases and sales. These records should include dates, quantities, prices, dividend reinvestment, and investment expenses, such as broker fees. Keep these records for as long as you own the investments, plus the statute of limitations on the relevant tax returns.

**Individual Retirement Accounts (IRAs)** The IRS requires you to keep copies of Forms 8606, 5498 and 1099-R until all the money is withdrawn from your IRA accounts. Now that Roth IRAs have been added into the mix for some retirement savers, it's more important than ever to hold onto all IRA records pertaining to contributions and withdrawals in case you're ever questioned. If an account is closed, treat IRA records with the same rules as securities. Don't dispose of any ownership documentation until the statute of limitations expires.

**Issues Affecting More than One Year** Records that support figures affecting multiple years, such as carryovers of charitable deductions, net operating loss carrybacks or carryforwards or casualty losses, should be saved until the deductions no longer have an effect, plus seven years.

**\*NOTE\*** *One critical step to take when cleaning out financial documents is to shred them thoroughly before you toss them out.*

## Business Record Guidelines

### Employee Earnings

Maintain for at least 4 years to meet various state and federal requirements

### Employee Time Cards

Keep for at least 3 years if your business is subject to the *Fair Labor Standards Act* (engaged in interstate commerce).

### Personnel Records

Retain for 3 years after an employee has been terminated

### Employee Tax Records

Keep 4 years from the date the tax was due, or the date it was paid—whichever is longer

### Sales Tax Returns

State regulations vary. For example, NY generally requires sales tax records to be retained for 3 years, while CA requires 4 years.

### Business Property

Records used to substantiate the cost and deductions associated with business property must be maintained to determine the basis and gain (or loss) on the sale.