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TAX GUIDE

FOR RECORDKEEPING

How long should records be kept?

Just how long you should keep records is partly a matter of judgment and a combination of state and federal statutes of limitations. Federal returns can be audited for up to three years after filing (six years if underreported income is involved), so all records substantiating tax deductions should be kept at least that long.

Here are recommended retention periods for various records:

Records	*Retention Period*
Cancelled Checks	7 years
Credit card receipts	7 years
Paid invoices	7 years
Bank deposit slips	7 years
Bank statements	7 years
Tax returns (uncomplicated)	7 years
Tax returns (all others)	Permanent
Employment tax returns	7 years
Expense records	7 years
Financial statements	Permanent
Contracts	Permanent
Minutes of meetings	Life of company plus 7 years
Corporate stock records	Permanent
Employee records	Period of employment plus 7 years
Depreciation schedules	Life of assets plus 7 years
Real estate records	Ownership period plus 7 years
Journal & general ledger	Life of business plus 7 years
Inventory records	7 years
Home purchase and improvement records	Ownership period plus 7 years
Investment records	Ownership period plus 7 years

Requirements for computer-maintained records are generally the same as for manually kept records.

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Tips for Recordkeeping

Tax records should be kept year-round, not hastily assembled just for your annual tax appointment. But which records are important, and how and why do you keep them?

Without tax records, you can lose valuable deductions by forgetting to list expenses on your return or having unsubstantiated items disallowed if you're audited.

Generally, returns can be audited up to three years after filing. However, if income is under-reported by more than 25%, the Internal Revenue Service can collect underpaid taxes up to six years later. In other words, you need good records to verify what you report on your tax returns.

Another money-saver: If your records are organized, your accountant will need less time to review your records. This may translate to lower tax preparation fees.

Which records are important?

- Records of income received
- Expense items, especially work-related expenses
- Home improvements, sales, and refinances
- Investment purchases and sales information
- The estate value of inherited property
- Specific uses of loan proceeds
- Medical expenses
- Charitable contributions
- Interest and taxes paid
- Records of nondeductible IRA contributions

How should you keep your tax records? Any way that is convenient for you that will allow you to give complete information on each item: how much? what for? when? where? why?

Recordkeeping for Businesses

The tax law requires all businesses to keep records to support the gross income, deductions, and credits claimed on their income tax returns.

What records? All businesses should have a permanent set of books which summarize individual deposits, disbursements, and items of adjustment. These records should be retained indefinitely. Permanent records also include those needed to prove the basis (cost) of depreciable assets.

Supporting documents may be needed to validate the journal entries if your returns are examined by the IRS. The general rule is that supporting documents should be retained at least until the statute of limitations for a tax year has passed.

The supporting documents the IRS reviews include bank statements, cancelled checks, payroll records, invoices, and the like. You should also retain documents supporting deposits which do not reflect income, such as loan documents. If storage is a problem, consider microfilming these documents.

What happens if your records are inadequate? If you fail to retain adequate records to support the items claimed on your returns, the IRS has authority to reconstruct your income using one of several methods, including estimating increased net worth, looking at bank records, or estimating the raw materials used in manufacture. Whatever method the IRS uses, you have the burden of proof if you dispute their estimate. Without adequate records, proving the IRS estimates wrong is difficult, at best. You could end up with an assessment for additional taxes, plus penalties and interest.

For additional information and recordkeeping suggestions which will fit your financial world, call us.