Tax Watch

BROWNEDWARDS
certified public accountants

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SAVE OR SHRED?

You may have breathed a sigh of relief now that the April 18 deadline to file your taxes (or request an extension) has come and gone. However, if your office is strewn with reams of paper consisting of years' worth of tax returns, receipts, canceled checks, bank and brokerage statements, and other financial records, you probably want to get rid of what you can. Follow these retention guidelines (for both individuals and businesses) as you begin to clean up after another tax "season."

Guidelines for individuals

As a rule of thumb, you should retain records that support items shown on your individual tax return until the statute of limitations runs out — generally three years from the due date of the return or the date you filed, whichever is later. That means you can now generally throw out records for the 2013 tax year if you filed the return for that year in April of 2014.

Bear in mind that, in some cases, the statute of limitations extends beyond three years. If you understate your adjusted gross income by more than 25%, for example, the limitations period jumps to six years. And there's no statute of limitations if you fail to file a tax return or file a fraudulent one.

You can also file an amended return on Form 1040X during the general three-year statute of limitations period if you missed a deduction, overlooked a credit or misreported income.

Here are guidelines for specific documents:

Tax returns. Consider holding on to copies of your tax returns as filed indefinitely. That way, you can prove to the IRS that you actually filed. At the very least, hang on to them for at least six years after they are due or filed, whichever is later.

Real estate records. Keep these records for as long as you own the property, plus three years after you dispose of it and report the transaction on your tax return. In addition, retain receipts for home improvements, relevant insurance claims and documents relating to refinancing. These help prove your adjusted basis in the property, which is needed to figure the taxable gain at the time of sale of a personal residence, or to support calculations for rental property or home office deductions.

Stocks and bonds. To report taxable events involving stocks and bonds, retain detailed records of purchases and sales. These records should include dates, quantities, prices, dividend reinvestments and investment expenses, such as broker fees. You should hold on to these records for as long as you own the investments, plus the three-year statute of limitations for the relevant tax returns.

Traditional and Roth 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. For Roth IRAs, hold on to all IRA records pertaining to contributions and withdrawals in case you're ever questioned. If an account is closed, treat IRA records the same as records for stocks and bonds. Don't dispose of any ownership documentation until the statute of limitations expires.

Guidelines for businesses

If you own a small business, be aware that the record-retention guidelines are slightly different than for individual tax purposes. The IRS recommends keeping employee records for three years after an employee has been terminated. In addition, maintain records that support employee earnings for at least four years. This timeframe should cover various state and federal requirements.

Timecards specifically must be kept for at least three years if your business engages in interstate commerce and is subject to the Fair Labor Standards Act. However, it's a best practice for all businesses to keep the files for several years in case questions arise.

Here are guidelines for specific business-related documents:

Employment tax records. Keep four years from the date the tax was due or the date it was paid, whichever is longer.

Travel and entertainment records. For travel and transportation expenses supported by mileage logs and other receipts, keep supporting documents for the three-year statute of limitations period.

Sales tax returns. Because regulations vary state by state, please check with us for the correct guidance. For example, New York generally requires sales tax records to be retained for three years, while California requires four years, and Arkansas, six.

Digitizing your records

The IRS permits you to store tax records electronically, so long as the system you use meets IRS standards. For example, your system must provide reasonable controls to ensure its integrity, accuracy and reliability, as well as detect and prevent tampering. In addition, a retrieval system should include an indexing system, inspection and quality assurance measures, and the capability to reproduce legible hard copies.

You can retain the documents you need by scanning the originals and storing them on an external hard drive or some other medium. There are also Web-based services that will store electronic records, virtually eliminating space constraints.

When in doubt, don't throw it out

It's easy to accumulate a mountain of paperwork from years' worth of tax and financial records. The good news is that guidelines are available as to what you should keep and what you can discard. And if you're still unsure whether you should retain a document, a good rule of thumb is to hold on to it for at least six years or, for property, at least three years after the tax return reporting its disposition is due or filed. Contact us with any questions.