TAXGUIDE for recordkeeping

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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 underreported 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.

Individual recordkeeping

Which records are important? Here's a list of the most common records you need to keep:

- Records of income received.
- Expense items, especially work-related expenses.
- Home improvements, sales, and refinances.
- Investment purchases and sales information.
- The tax basis of gifted and inherited property.
- Specific uses of loan proceeds.
- Significant, unreimbursed medical expenses.
- Charitable contributions.
- Interest and taxes paid.
- Records on nondeductible IRA contributions.

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

Business recordkeeping

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

That means you need a permanent set of books for your business to summarize individual deposits, disbursements, and items of adjustment. Permanent records also include those needed to prove the basis, or cost, of capital assets. You can choose any system that suits your business, and you'll want to retain the books and records indefinitely.

In addition, you may need supporting documents to validate journal entries if your tax returns are examined by the IRS. Supporting documents include bank statements, cancelled or substitute checks, payroll records, invoices, and loan documents. As a general rule, keep supporting documents at least until the statute of limitations for a tax year has passed.

If you fail to retain adequate records to support the items claimed on your returns, the IRS can 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 wrong is difficult, at best. You could end up with an assessment for additional taxes, plus penalties and interest.

Tax records should be kept year-round, not hastily assembled just for your annual tax appointment

Record retention

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

Recommended Retention Periods

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

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

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