

TO SHRED OR NOT TO SHRED

JUNE 2008

Should you fire up the gas powered shredder or not?

There tends to be a serious amount of confusion when it comes to the plethora of paper records required to substantiate the information Americans use for their tax returns. Record-keeping requirements have been growing, as evidenced by the recently expanded requirements for receipts supporting charitable contributions. All records of stock transactions, retirement plan distributions, charitable contributions, childcare expenses, partnership K-1s, and similar materials must typically be kept as long as taxpayers might need to produce them to support tax return disclosures. (Note: We have recently added the services of INautix to aide our clients in this.)

What to save and how long...

Federal Income Tax Returns: Most taxpayers can feel safe if they hold on to their records for five years. Assessment of federal income tax by the IRS must occur within three years of the later of the date that the return was actually filed or the unextended due date of the return. The assessment period, combined with the portion of the year that the taxpayer held the document prior to the date the return was filed, would equal no more than five years in most cases, even when a possible extension is included. Of course one needs to keep the cost basis of all property until sold than five years thereafter. A form 1040 might be subject to an audit for even longer periods under the circumstance that a taxpayer underreports income by 25%. For filers of fraudulent returns and for nonfilers, the statute of limitations runs indefinitely.

State Income Tax Returns: Many states have an income tax and their statutes of limitations differ from state to state. States such as California, Michigan, and Ohio have statutes that exceed the federal by a full year. We side on it is better to safe than sorry so we recommend keeping the state returns for seven years.