

## How Long to Keep Tax Records

### IRS often focuses on four audit areas

Keeping accurate records is the best way you can protect yourself in the event of an IRS audit. But how long do you have to hold onto your records?

There is no definitive answer. But at the very least, you should keep your records until the statute of limitations for the return expires. Normally, this is three years after the due date (including extensions) or two years after the tax is paid—whichever is later.

But the limit is six years if your gross income is understated by more than 25% of the amount shown on your return. Furthermore, there is no time limit at all if an income tax return is found to be false or fraudulent.

Therefore, conservatively speaking, you might hold onto tax records for as long as, say, ten years. Consult with your tax return professional.

What sort of tax records? The obvious ones include your 1040s, W-2s, 1099s, K-1s and receipts of business expenditures. However, watch out for other records that may be overlooked or discarded prematurely, especially in the following four areas:

1. Charitable donations: Under new rules that went in effect in 2007, you must have a bank record or written communication from a charity for any monetary contribution. You are also required to obtain a written acknowledgment for any single contribution of \$250 or more. Other special rules apply for donations of property valued over \$500. For donations valued above \$5,000, you must obtain an appraisal of the property.

Note that the cost of the appraisal itself is deductible as a miscellaneous expense but your unreimbursed miscellaneous expenses are only deductible to the extent the total for the year exceeds 2% of your AGI.

2. Investments: You should be able to document your gain or loss from the sale of all securities. In particular, it may be difficult to keep track of mutual fund sales. Be sure to supply your tax return preparer with all the relevant information. Because several methods may be used to calculate mutual fund gains and losses, this can make a big dollars-and-cents difference on your tax return.

3. Home sales: It is important to substantiate certain deductions (e.g., prorated mortgage interest and real estate tax paid up to the date of the sale may be deducted) to determine the “net” amount realized from the sale of a home. Similarly, detailed records of home improvement costs may help reduce your taxable gain when you sell the home.

4. Travel and entertainment expenses: Traditionally, the IRS pays extra-close attention to travel and entertainment expenses deducted by individuals because there are strict substantiation rules imposed by the IRS which are often unmet.

As a general rule, you must document the date, amount of the expense, the business purpose and various other details (depending on the nature of the expense). Note that receipts are required for items of \$75 or more.

It is worthwhile to repeat this: The best protection you can have in the event of an audit is to keep accurate and detailed records in an organized manner.