



## Tax Tips You Can Use July 2011

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During the recent tax season, the most commonly asked question was how long to keep tax records. Although the IRS has an entire publication (552) about record-keeping that is great for bedtime reading, this article will give some practical advice about how long to keep your tax records.

There is a common myth that all tax records should be kept for 7 years. That is not true. The IRS generally only audits the last three open years. For most of us, the current open years are 2008, 2009 and 2010. However, if you have not yet filed your 2010 return, your open years are 2007, 2008 and 2009, even though it is June of 2011. I tell my clients that since their definition of three years and the IRS definition of three years are probably different, they should keep the last four years of tax records. That is not the end of the story and there are several exceptions to this guideline.

The first exception is that the IRS can audit six years of returns if substantial underpayment of tax is found. If you are audited and the IRS finds a pattern of underpayment of tax by 25% or more, they can, at their option, audit another three years, in addition to the three open years. If the taxpayer has committed tax fraud, the IRS can go back as far as it wants to, as in the case of Al Capone. Also a taxpayer who does not file a return, never starts the three year clock. If you file a late return, the three years for audit of that return starts on the date it is filed.

The other exceptions have to do with more practical considerations. First, a taxpayer should keep the records for all capital assets being depreciated for as long as the item is on a tax return that could be audited. Rental houses are depreciated over 27 and 1/2 years. That means that the purchase papers for a rental house should be kept as much as 32 years. This is not a joke. A taxpayer with a farm under audit was asked to submit the original bills for tractors, animals, a barn and fencing that were purchased as much as 10 years before the return being audited. I recommend that taxpayers keep a separate file for capital assets for each business, rental, or farm so that asset purchase information does not get thrown out after four years.

Another important guideline is that any taxpayer who has not yet filed for Social Security should keep all W-2's and other earned income information, like schedule C's, along with the first two pages of their 1040 until they do file for Social Security. A person's earnings record is used to calculate their SS benefit. The record can have errors and the only way to prove that is to have the original documents. I know the records can be changed in error, years after the fact, because it happened to me. In 2004, I received my annual statement and found the record for 1985, which had been correct on the prior year statement, was now zero. With my W-2 and the 1040 for 1985 (remember, I AM a tax preparer). I was able to have the Social Security agency quickly fix the error. As a note, in a recent seminar, a Social Security trainer mentioned that the Social Security Administration plans to stop mailing out the annual notices. The information will be available on line, but only with a password the taxpayer must obtain.

Knowing what records to keep is important, but just as important is to insure that records to be destroyed are properly handled. Never throw tax records in the trash. These records have social security numbers, birth-dates and a wealth of private information that ID thieves could use. The records should be shredded, burned (if available), or emulsified so all information is obliterated.

The Jacksonville Tax Lady, LLC can be reached at 541-899-7926 and is located in beautiful, historic Jacksonville at 610 N. Fifth Street across from the Pony Espresso.

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