How Long Should I Keep My Tax Records?

By Doug Nelson, CPA, Vice President, Tax Manager

Is the financial paperwork piling up at your house? Despite the inconvenience, the truth is that many financial documents require long-term safekeeping. Holding onto your basic tax records for at least three years is the norm, and some should be kept indefinitely. Doug Nelson, CPA, Commerce Trust Company Family Office Services Director of Tax, takes a moment to discuss the latest requirements in saving your supporting tax documentation, and a few other items you may not have considered.

Q. How long should I hold onto my tax records?

The length of time to hold onto tax records varies depending on the type of return you file. In most cases you should plan on keeping your income tax return and all supporting documents for a minimum of three years following the date you filed or the due date of your return (whichever is later). You should keep gift tax returns indefinitely — your executor will need them as attachments to your estate tax return.

Q. Are there any exceptions to these rules?

The statute of limitations goes up to six years if income is underreported by more than 25%. There is no time limit if fraud is alleged, or a return is never filed. If you file a claim for a loss from worthless securities or a bad debt deduction, you should keep documents for seven years. Please note some states require a longer retention period. However, if you have the luxury of filing space, it never hurts to save income tax returns indefinitely in case the IRS comes back in the future and alleges an understatement of income or fraud.

Q. What types of tax records do I need to keep and why?

Here are three categories we consider important:

Income tax returns. Each year's return is very handy in preparing future filings. They are also necessary to file amended returns, for support on an audit by the IRS (or other taxing jurisdictions), or to assist your executor with the administration of your estate.

Government forms documenting sources of income. These items would include W-2 forms; 1099s; Schedule K-1s; Schedule C, E, and F items; etc. They assist in preparing future returns and provide support if audited.

Expenses and deductions. These records include statements on medical billings; estimated income tax payments; real estate and personal property tax payments; mortgage interest paid; charitable contributions; unreimbursed employee expenses; child care; Schedule C, E, and F items; etc.

Q. How long do I need to keep paperwork regarding my property?

Keep records regarding your property (i.e., home, investment property, securities, mutual funds, etc.) basis until the period of limitations expires for the year in which you dispose of the property in a taxable disposition. It is important to keep these documents because you need them in order to calculate whether you have a gain or a loss on the sale of the property, or to figure any depreciation, amortization, or depletion deductions. This includes the cost of purchase, improvements to a home and reinvested dividends to name a few.

Q. Where is the best place to store my documents?

The best place to keep documents would be in a fireproof safe. You should tell one other person the password, lock combination, or location of the key in case of an emergency. With today's technology, you may also decide to scan your documents and keep them locked in a file on a cloud service. (Keep in mind that the cloud service may go out of business.) The IRS accepts digital copies as long as they can be easily read. You can store many different years' returns on a thumb drive, or a CD or DVD locked in a safe deposit box. Please note that these electronic devices may also go bad over time and some media may become difficult to access as technology advances (ex. many laptops do not have a CD reader).

Q. What is the best way to dispose of tax records after the retention period has expired?

All paper statements should be shredded and old hard drives with personal data should be destroyed. Make sure to be careful when giving away a computer. Many organizations receiving computers have protocols for the secure destruction of confidential information stored on hard drives, so ask before you donate.

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Doug manages the West Region tax team for Commerce Trust Company. The tax team oversees the back office functionality of Commerce Trust as it relates to taxes, specifically consisting of forms 1099 and 1041 on accounts. They also interact with select clients by providing tax preparation, tax consulting, and estate planning services. Prior to joining Commerce in 2010, Doug was a senior manager at Hostess Brand, Inc., and oversaw the outsourced income tax function and personal property tax compliance and planning. Also, he utilized bankruptcy codes to benefit the company regarding tax savings and cash payment deferrals. Before that, he was with Cornerstone CPA Group as senior manager of the CPA component of a full-service firm and with Ernst & Young, LLP, starting at the staff level and progressing to senior engagement coordinator of the national tax compliance group. Doug has a bachelor of science degree in accounting from Missouri Western State College and a master of science degree in tax accounting from the University of Missouri-Kansas City.