

## How to Clean Out Your Tax, Financial Files

MarketWatch

By Eva Rosenberg | MarketWatch – Thu, Dec 29, 2011 11:37 AM EST

LOS ANGELES (MarketWatch) — The end of the year is a great time to clean house, and to remove the detritus and accumulation of another year. What about tax returns or financial records? That's one of the common questions that comes to TaxMama®. My instinctive response always is: never!

Yet the big shredder truck is coming to our office to destroy records. We are destroying hard-copy client records that are five years or older. We did ask our clients if they wanted copies before turning them into confetti. Naturally, we have electronic copies of key files.

Have you ever seen one of those behemoth shredders? They're nearly as big as a municipal trash truck. The good ones (the ones we use) have cameras, allowing you to watch the shredding taking place. They come to our office and demolish 20 or 30 boxes in a half hour or less.

Why watch the shredding process? Is it really better than TV? Not really. It's a security measure we take when shredding sensitive client records. They contain enough information to allow for identity theft. That's why we don't have them pick up the records to shred later (an optional service). If you use a service to do your shredding, it's important that you watch the process until it's done. Otherwise, do it yourself.

The cost of using these mobile shredding services tends to be about \$100 for the first few boxes, then about \$5 or \$10 for subsequent boxes. If you don't have a ton of your own trash, consider inviting your friends, neighbors or business colleagues to share the truck and bring all the boxes to a central location — your office building, school, church, or social hall. This can be a great fundraiser and community clean-up event.

### **Don't destroy tax returns**

Never destroy copies of your tax returns or proof that you paid any balance due. If possible, keep both an electronic copy and hard copy of your returns. They don't take up that much room. You can fit 10 to 20 years of tax-return files into one or two 12" x 15" cardboard storage boxes.

Why say "never" on tax returns? After all, the IRS may audit you only for up to three years after you file, right? Well, not so right. If there is an error of 25% or more on your return, the IRS may audit for up to six years. When it comes to certain other errors, there may be no statute of limitations. States tend to have a longer open window because they assess taxes after an IRS audit.

Another problem that crops up often enough to consider is that government agencies lose tax records. TaxMama® hears from taxpayers who have been hounded by the IRS or their state for not having filed a return in a year when they know they have filed. Without a copy of the tax return from 10 years ago, how can you prove you've already filed and paid?

Speaking of states, people have become more mobile. Our jobs and careers often have us working in more than one state. More states have started implementing the Jock Tax concept. Read more: [The long arm of states' tax laws](#).

Why should you care? If you worked in a state several years ago and never filed a tax return, the statute of limitations has never closed. The same thing applies to partners in a partnership, LLC or S corp, where the business has income in several states. When you don't file a tax return to report income from the entity (whether publicly traded or privately held), the states can come after you forever.

How does having a copy of the tax return for that year help? Most state tax returns start with the federal information and give you credit for your federal itemized deductions. So you don't have to work as hard to prepare those unfilled state

returns when the states demand you file.

### **Save property records**

One of the big nightmares many people face is how to establish the basis (tax cost) of an asset held for decades when they sell it. This applies to real estate, stocks, retirement accounts, insurance policies, collectibles, etc. Keep all purchase records, improvement receipts, reinvestment records — and anything else related to the ownership of your assets.

Even if you don't organize your files, if you keep all the records in one place, you can sort them out when necessary. Better yet, try to keep the records organized, at least minimally. Use expandable files, labeled with each asset or asset type. Then, just drop papers into the file.

### **Save loan records**

Doesn't it feel great when you pay off a loan? Especially a mortgage. But when I see people on TV having a "burn the mortgage" celebration, I cringe. What if you need to prove you paid it off, years later? The Recorder's office does make errors. Or the bank may fail to file the final paperwork with the appropriate government or credit agency. Keep copies of major loans and their payoffs — real estate, vehicles, student loans, lawsuit payoffs, long-term credit-card balances, personal loans, family loans, etc.

Those records are also helpful when you need to prove that you made a particular payment. The very first time I shredded records (after keeping everything for over 20 years), I discovered that I'd destroyed the proof of a loan owed to me by a former boyfriend. Fortunately, he paid every dime, so we didn't need to end up before Judge Judy.

### **Keep warranties**

Warranties and service records have a variety of terms. They will provide parts and labor in the initial years after purchase. But some will provide longer-term support for the more expensive materials in computers, furniture, appliances, etc. They will also provide model numbers and valuable contact information to the company so you can get replacement parts, even after the warranty has expired.

### **Disaster strikes**

If you live in a disaster-prone area, consider keeping copies online of important personal and business records — and irreplaceable family photos. You won't have to struggle to reconstruct anything after your local earthquake, flood, fire or hurricane.

### **What can we toss?**

It sounds as if you must keep everything. Not so. After four to seven years, you can shred all of your bank records and credit-card records.

You can shred personal utility bills after a year or two. And business or rental utility bills after four to seven years.

Sort through the correspondence that you've saved. Aside from precious letters and cards, you can shred all correspondence that is unrelated to those must-save items above.

Definitely stop saving all the junk mail related to things you might buy someday. Toss the old magazines, unless they are collector's items (like the Playboy issue about Hugh Hefner's wedding to Crystal Harris, which was called off, alas). You can re-read those articles online.

Do you need all your old, out-dated reference materials? We finally tossed more than 25 years of IRS and California tax books. The IRS has 1913 to the present on one single disk. These materials were unreasonably difficult for me to relinquish. What are you holding on to from your profession that is now available on a single disk?

While you're at it, if you happen to run across old letters from friends, perhaps you can scan them and send a copy to your friends. They might enjoy the memories.

Eva Rosenberg, an enrolled agent, is the publisher of TaxMama.com, where your tax questions are answered. Rosenberg is the author of several books and ebooks, including “Small Business Taxes Made Easy.” She teaches a tax pro course at IRSExams.com and other tax courses at <http://www.cpelink.com/teamtaxmama>.

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