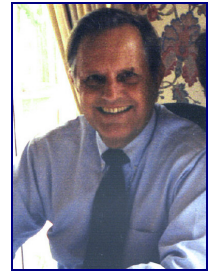


from Chuck's Desk

Affordable Business Services Inc.

www.affordabl.comIn This Issue

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Volume 9 No. 3

"from Chuck's Desk"

is published periodically during the year by Affordable Business Services Inc.
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I welcome any comments or suggestions you may have.
Please call or e-mail me at your convenience.

If you enjoy reading my newsletter, the highest form of compliment I can receive is a referral to your friends, family and business associates.

Chuck Donovan

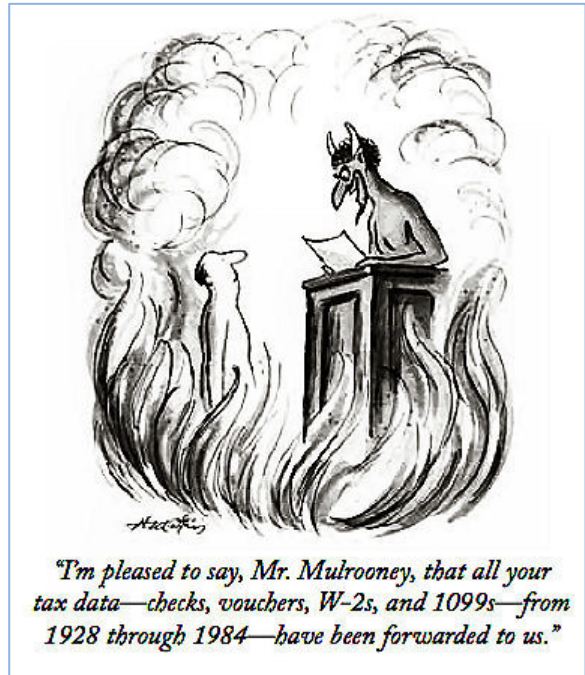
Saving Your Tax Records

I receive calls from people who say they are cleaning out their storage areas and have found years of past tax returns, some kept since the 1970s. They ask whether they need to keep the old ones and, if so, how many prior year returns should they hold on to.

I tell them they need generally to keep them for at least three years. Anything beyond the three year period they can destroy, but they always call back with further questions about the information they are digging out of storage.

There is considerable confusion about maintaining prior year filed tax returns and the supporting documents for these returns. Couple this with the fear that the IRS will ask about items in the old filed tax returns and you understand why there is a hesitancy to throw anything away.

So, let's review the rules and what information needs to be kept and for how long.

*Statute of Limitations*

Taxpayers are protected from the IRS by the Statute of Limitations. This limits the number of years during which the IRS can audit a tax return. When a limitation period has expired, the Service is legally prohibited from even asking a question about the return.

For filed tax returns - the statute of limitation for the IRS's assessment of additional taxes is **three years from the date the tax return must be filed.** This is April 15th of the year following the year of the return. For example, the year 2005 return must be filed by April 15, 2006. The IRS will have three years thereafter or until April 15, 2009 to assess further taxes.

For refunds - the statute of limitation, if a refund is due or an additional refund requested, is **three years from the date the return must be filed or two years from**

Affordable Business Services provides a complete range of tax, accounting, and consulting services to individuals and businesses at affordable fees.

Chuck Donovan started the firm in 1993 with a single principle in mind – to provide quality financial services that meet and suit his clients' needs. He has built a successful operation by combining personal attention and expertise with quick, accurate, friendly service.

The company's growth has been fueled by referrals from existing clients and peers. The hallmark of Affordable Business Services remains the individualized service that addresses clients' unique requirements small or large.

Chuck is a graduate of Dartmouth College and has a MBA in Accounting and Finance from American International College.

the date the tax was paid.

However, there are **exceptions to these rules** which are:

1. The statute of limitation is **six years** if **all the income is not reported** on the return and is more than 25% of the return's gross income.
2. The statute of limitation is **seven years** if a **loss from a worthless security** is claimed on the return.
3. **If a person does not file or files a fraudulent return**, there is **no statute of limitation period** and the IRS can come after the person at any time.



Returns Filed on Time

If you have filed your return on time and paid any taxes due, you need to keep the records only for three years. You must remember that, because a tax audit is a verification of the income and deductions items listed on the return, the records kept are not only the return itself but also the supporting and back-up information relating to the data on the return.

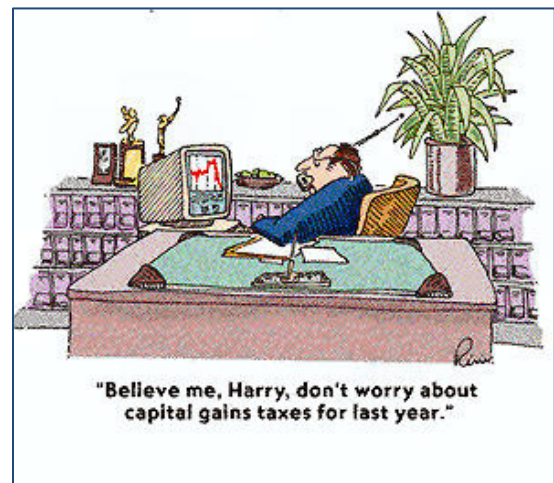
However, there are some other considerations that need to be looked at before any records are thrown away. **The three-year rule relates to all the information on the tax return.** Some of that the supporting and back-up information may concern transactions more than three years old. Among them are:

Capital Gains and Losses

Gains are reduced by the costs plus commissions; the costs of mutual funds include reinvested dividends and capital gains. A capital gain or loss is determined by subtracting the costs from the gains.

If a stock was bought over three years ago, the original bought ticket needs to be kept to support the cost appearing in the tax return. In addition, information occurring during the period between the purchase and sale of the stock, such as reinvested dividends, capital gains and stock splits, has to be maintained.

You will have to prove these numbers, should the IRS audit you. As a result, **keep this information about the purchase with the tax return records for at least three years after the return reporting their sales has been filed.**



Tax Returns

The IRS can not be relied upon to have copies of tax returns filed earlier than three

years ago. **It is a good idea to hold onto the returns themselves for about six years.** The supporting and back-up information for returns older than three years can be thrown away.

It is really a case of being safe rather than sorry.

Home Expenses



The cost records of your house and improvements on it should be kept until the home is sold. **It is just a good idea,** although most people will not have any tax problem when the sale occurs.

In a tax law passed in 1997 a profit on a home of less \$250,000 on a single return and \$500,000 on a joint one is excluded from income and not

taxable. However, if the profit exceeds either \$250,000 or \$500,000 depending on the return filed or if a person does not qualify for the full exclusion, there will be a tax. The records in this latter instance must be kept for the three years after that return is filed.

Business Records

The IRS is particularly interested in business returns and views them as prime targets for finding areas for the assessment of additional taxes. This applies not only to corporate returns but also sole proprietor ones.

The three year limitation period applies to business returns also. Since the IRS can go back at least six years if it believes income is understated and even longer if it thinks the return is fraudulent, it is critical to hold on to everything backing up every item appearing on a business return and not throw anything away.



It may be a long time to keep receipts, but they may be needed to validate the numbers.

W-2s, 1099s, Bank and Brokerage Statements

W-2s, 1099s, brokerage and bank statements are supporting and back-up information and need to be kept to prove the income until the three year limitation period passes. This also applies to checks, receipts, mileage logs, tax diaries and other documentation that substantiate the expenses appearing on the tax returns.

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Click on the Newsletters tab for the issues of the newsletter from 2002.

Do you need to be Incorporated?

We can provide you with Articles of Incorporation, Minute Book, Stock Certificates, and Tax ID and Small Business Election papers.

Do you need a Living Trust to replace your will?

We can provide you with a Living Trust that will eliminate probate and legal costs.

Do you need a Durable Power of Attorney for Health Care, a Living Will, and a Designation of Health Care Surrogate?

We can provide you with a complete set of documents that will put your mind at ease when medical situations arise.



Summary

A letter from the IRS, even a very friendly one at that, is life's worse experience, worse than a root canal. Having the right information with the right supporting and back-up information alleviates the experience. **Saving your records for the right period puts your mind at ease.**

Getting rid of the old records has the added advantage of freeing up space in your storage areas. These old records should be shredded, not torn up.

Should You Go to a Free Lunch?

There is nothing wrong with eating a free lunch the courtesy of broker or financial advisor. What is wrong is when you fail to understand or realize why the presenter is feeding you. Free lunches are nothing more than an opportunity for him to find you and target your money.

The lunches offer him a chance to make a hard sell presentation filled with recommendations covering specific investments such as equity-index annuities, reverse mortgages, viaticals, and life settlements. Rarely are the risks associated with the recommendations discussed. Instead they are presented as the greatest, newest, highest earning investments now available and suitable for every one in the audience.

He does not feel guilty about using the ruse of free lunch to entice you, so he can make a strong sales pitch – one that is not free and can be very costly to you. The lunch is a scam to pull you in.

You should also not feel guilty about attending, but need to carefully evaluate the recommendations to see if they are suitable for you before you sign up for a personal meeting with him. You can not take his word at face value. The real hard sell will take place when he has you alone in a meeting.



I admit I go to free lunches. I do so with the awareness of why I was being invited. **I am a potential prey** – someone who may be enticed by a hard sell presentation and could fall victim to its temptation. As a result, I listen carefully to what is being discussed, consider whether any of the proposals may be of interest, and review them thoroughly after the lunch.

I do not disclose any personal financial information during the lunch. I ask for a business card and tell him I shall give him a call in a week or so to set up a meeting. He does not like my not signing up immediately for a meeting. After all he wants to strike while the iron is hot.

But I know **there is no such thing as a “free lunch”**.