Major Tax Myths - 4/17/2001
by Sanford Botkin

Sandy Botkin CPA. Esq.

I just had a tax seminar where we had 30 participants out of 30,000 mailings. Considering that I usually save people $5.000-$20,000 in new deductions, this low turnout was all the more perplexing. I decided to call up some people who did not attend and find out what was the problem. Astonishingly, there are a number of widespread tax myths that seem to impoverish most people and make the IRS more money than would be ordinarily due them. This article is a summation of some of the bigger, more widespread of these myths.

1.”If I don’t take every deduction, I will reduce my chance of an audit.” This is absolutely untrue. If you were to ask any former IRS agent they would tell you that you have only given some extra money to you “Uncle Sam” and won’t even get a thank you. If you really want to do this, make it a charitable contribution and take a deduction.

2. “I didn’t make a lot of money this year so I didn’t feel that I needed to attend a tax seminar.” This is also a big mistake. If knowledge of some unknown deductions creates a loss because the deductions exceeded your limited income from your endeavor, you may use the loss against any form of income that you have such as wages, dividends, interest, pensions and rents. If the loss exceeds your personal income, you can use it against a spouse’s earnings if you file jointly. Thus, you will never get divorced!

If the loss exceeds the income that both you and your spouse have earned, you can carry back all business losses two years and offset the last two years of tax that you paid into the IRS or to most states. Moreover, if that doesn’t cover all your losses, you can carryover all business losses twenty years and offset up to the next twenty years of earnings. Thus, even if you didn’t make a lot of money, tax knowledge will always pay you back. In fact, if your earnings were limited this year, it becomes even more vital since you can use the subsidy that you would get from the increase in your deductions even more than those that already have more money than they can spend.

3. “I heard that I had to have a profit or had to have a profit three out of the last five years.” This is only partially true. The tax law provides that if you run your business like a business and not like a hobby, you can use the losses as discussed above. If you are deemed to be hobby, your losses from your endeavor are limited to the income from the endeavor with no carry back or carry over. There is a presumption that if you have a profit three out of the past five years, you have a business profit motive. However, the important point about this widespread myth is that this is a presumption that can be rebutted. I have a whole chapter in my series “Tax Strategies for Business Professionals” and “Tax Strategies For Home Based Business” where I discuss this. However, basically you need:

- A five year projection of income and expenses, which will project an eventual profit
- A marketing plan
- A good tax organizer and good documentation
- Working your business at least 45 minutes a day, four to five days a week
- Attendance at training
- Consultation with experts
- Changing the way an activity is marketed from year to year especially if no profit is shown.

Thus, this presumption can be overcome with proper knowledge and some simple planning.

4. “My accountant takes care of my taxes” or “My spouse takes care of my taxes.” This may be the single biggest myth and wealth killer in the US. It certainly makes the IRS more money than any other myth. I

equate this with “my doctor takes care of my body.” Wouldn’t it be great if we could eat all the fattening foods that we want and never exercise, yet, once a year go to a doctor and get a form of “Roto Rooter” job? If you don’t know what to tell your accountant by December 31 or if your documentation isn’t right, there is very little that they can do for you. Sadly, accountants also have a conflict of interest when preparing our returns. They are subject to both a high standard for taking a deduction and are subject to high civil penalties. Thus, as many accountants have informed me, “they would rather not tell a client about a deduction that may be questioned if it results in any risk to the accountant.”

5. “<u>Keeping good records isn’t worth the time or expense</u>.” This is also a major mistake. I estimate that most people can be audit proof by keeping records that would take no longer than 3 minutes a week. This is about 150 minutes a year, which is about 21/2 hours a year. This may, at first, seem like a lot of time, but this would save approximately $4,000-15,000 in taxes. Even using the low-end figure, this averages to be about $1,333 per hour and it is <u>tax free. I bet that you don’t earn this in an hour!</u>

In short, tax knowledge can and will benefit anyone at any income. One seminar participant summed it up very well by saying,” The more you know, the less you’ll owe!” I couldn’t agree more.

Sandy Botkin is a CPA, attorney and former trainer of IRS attorneys nationwide. He lectures all over the nation on tax planning for self-employed and corporate taxpayers and can be seen in the big events with Donald Trump, Anthony Robbins and many others. He has been written up in Newsweek and in many other magazines. He is also a syndicated writer and noted author of this famed tape series “Tax Strategies for Business Professionals” and “Tax and Financial Strategies for Residential Real Estate.” To find out more about Sandy and his products, check out his terrific small business web site at: www.taxreductioninstitute.com or by calling his office at 301-972-3600 in Maryland.