Taxes

Being self employed, what sort of deductions can I take?

To be deductible, a business expense must be both ordinary and necessary. An ordinary expense is one that is common and accepted in your trade or business. A necessary expense is one that is helpful and appropriate for your trade or business. An expense does not have to be indispensable to be considered necessary.

If I have a large capital gain this year, what can I do?

If you have a large capital gain this year from an investment, it may be advisable to hold onto the investment until next year to put the gain into next year's taxes. You may also want to sell off any investments that you have that are losing value at the moment to claim your losses.

What investments can I make to help defer taxes?

The interest gained from state and local bonds is usually exempt from federal income taxes. These investments generally pay back at a lower interest rate than commercial bonds of similar quality.

Since Treasury Bonds are similarly exempt from state and local income tax, they can be a particularly good investment for those who are in high tax brackets and live in high-income-tax states.

What retirement plans are available to aid in the deferral of taxes?

You have the ability to invest some of the money that you would have paid in taxes to add to your retirement fund. Many employers will offer the opportunity to defer a portion of your earnings and contribute them directly to your retirement account. Some of them may even match a portion of your savings. If this is the case, it is always advisable to save at least the amount that your employer will match. This will give you an automatic 100% gain on your money.

If you are self-employed, look into getting a Keogh, SIMPLE or a SEP IRA.

What other ways can I defer this year's income?

If you own your business you may want to postpone sending certain invoices to ensure that you will receive payment in the following tax year...

Record Keeping for Taxes

What do I need to keep for tax reasons?

It is a good idea to keep all of your receipts and any other records that you may have of your income and expenses. These will come in very handy if you are audited. It is best to hold on to these records for at least 7 years.

How should I separate and organize these?

It is advantageous to categorize your expenses:

- Income
- Exemptions
- Medical Expenses
- Taxes
- Business Expenses
- Education
- Travel
- Auto

How long should I hold onto these documents?

It is recommended that you keep these documents for three to four years. Check the Retention Guide on this site for additional details.

How long should I keep old tax returns?

If you are audited, it is very likely that the auditor will ask to see the last few tax returns. It is recommended to keep these tax returns forever.

An added benefit of keeping your tax returns is that you can see what you claimed last year, allowing you to adjust for the current year.

What other records should I keep?

If you purchased goods that you plan to sell later, you should keep the receipts to calculate your gain or loss on it correctly.

- Anything regarding the property you own and any fixes and repairs that you perform.
- Receipts for any jewelry or other valuable collector's items
- Records for capital assets, stocks, bonds and such

What recordkeeping system should I have?

If you are an employee of a company, your system needn't be complex - you can keep your records separated in folders.

If you are a business owner, you may want to consider hiring a bookkeeper or accountant. Check the Financial Guide for Business on this website.

Education Expenses

Are there available tax breaks for my children's education?

There are many different ways to use tax breaks for the higher education of your children. Be aware that you can only receive one type of relief for one item. It is best to consult with a professional to determine which would be the most advantageous.

What is the education tax credit?

You must make a choice between two types of tax education credit.

- The American Opportunity Tax Credit will work for the first 4 years of college for at least full-time study.
- The Lifetime Learning Credit applies for as long as the student studies, but the percentage of savings per year decreases drastically.

What is a Coverdell (Section 530)?

An education IRA is different than a standard IRA in these ways:

- Withdrawals aren't taxed if used for qualified education expenses.
- Contributions can be made only up until the point that the client reaches 18, and all funds must be distributed by the time that they are 30.
- Contributions are not tax deductible

How can I best use the Coverdell (section 530)?

It is possible to have various 530 accounts for the same student, each opened by different family members or friends. There is no limit to the number of people that can open an account like this for a child.

The account can be transferred to another family member at any time. If the original child decides against going to college or is granted a scholarship, another family member can still utilize the money that has been saved.

What is a qualified tuition program?

The Section 529 is a college savings program available in most states. Money is invested to cover the costs of future education. These investments grow tax free and the distributions may also be tax-free.

What differentiates the Coverdell Section 530 and the Section 529?

The Section 529 allows for much larger yearly investments, whereas the Section 530 currently only allows for $2000 annually.

The choice of investments in the Section 529 is extremely conservative and limited while the Section 530 allows for many different options.

The Section 530 is a nationwide program while the 529 varies from state to state.

The Section 530 will let you use its funds for primary and secondary education, while the Section 529 can only be used for secondary.

Can I take money from my traditional or Roth IRA to fund my child's education?

Yes, you can take distributions from your IRAs for qualifying education expenses without having to pay the 10% additional tax penalty. You may owe income tax on at least part of the amount distributed, but not the additional penalty. The amount of the distribution that is more than the education expense does not qualify for the 10% tax exception.

What tax deductions can be used for college education?

There is a limited deduction allowed for higher education and related expenses. In addition, business expense deductions are allowed, without a dollar limit, for education related to the taxpayer's business, employment included.

Is student loan interest tax deductible?

In certain instances, yes, although deductions need to adhere to a few guidelines. The deduction is also subject to income phaseouts.

- The deduction ceiling is $2,500.
- If you are a dependant, you may not claim the interest deduction.
- You need to be the person liable for the debt and the loan must be purely for education.

Can I deduct for education that helps at the workplace?

If you are receiving this education to maintain or improve skills at your current job, yes, but not if it is to meet the minimum requirements.