

Tax Route

A DIVISION OF HOFFLER-SMITH, INC.

A Newsletter from TaxRoute and HofflerSmith, Inc.

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Why Tax Planning Works!

How Tax Planning Can Save You Money

Timing ... Options.... Smarter Choices. All planning involves looking ahead to reach a specific goal. To gain the most from tax planning it must be a consideration all year long.

Tax planning is not intended to help you cheat the government in some way or do anything against the IRS code. Every taxpayer has the right to arrange his/her affairs so as to keep taxes as low as possible.

Tax planning strategies usually involve determining **WHEN** is the best time to take certain actions with your finances; and/or determine the best way to report certain deductions or write-offs for your personal or business situation. Sometimes a transaction can be postponed without penalty, and it may be in your best interest to take advantage of that option.

Generally it is best to receive more income when taxes are low; and less income when taxes are high. If your income is such that you change tax brackets

frequently from year to year, you should definitely be consulting with a tax accountant to help you best manage these shifts. Making adjustments may help you postpone payment of tax or let you shift some income or deductions to a different tax year to at least lower your taxes.

Buying and selling property can create some tax planning opportunities. Retirement planning will involve decisions regarding tax and financial planning options.

Tax Planning for Your Business. Tax planning is critical for the business owner. A business owner needs to develop a strategy in regards to the timing of large purchases, and other payments. The business owner must also factor in depreciation. Will it benefit us to write-off the entire amount now, or to take a little out annually over the next several years. These considerations are paramount to ensuring the stability, growth and viability of your business.

You should strongly consider tax planning if any of the following

items fluctuate significantly from year to year: Income, Deductions, Income Tax Withholding, or Estimated Tax Payments.

Last Word of Advice: Be sure to consult with your tax accountant for planning purposes **BEFORE** you make a decision about any of the following:

- Borrowing money for any purpose;
- Paying off a loan;
- Contributing or taking funds from a retirement plan;
- Buying or selling any property;
- Retiring; getting married; negotiating a divorce;
- Making a large gift to a relative;
- Making an investment where your participation will be minimal;
- Changing your business structure to a partnership or corporation;
- Incurring business expenses as an employee;
- Holding an uncollectible note;
- Moving

These articles are intended to be general guidelines and information to the public. Be sure to consult with your tax professional regarding your specific situation.

Tax & Accounting Expertise You Can Count On.

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Questions or comments?
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TaxRoute Receives An Award From NABA Philadelphia Chapter

TaxRoute was honored at an award ceremony in April, 2006, by the Philadelphia Chapter of the National Association of Black Accountants (NABA). NABA and TaxRoute worked together in 2006 on their first joint project: NABA's Annual Volunteer Income Tax Assistance (V.I.T.A.) program. The V.I.T.A. Program is one where the members of NABA volunteer their time and expertise to prepare returns for low income individuals free-of-charge. The Philadelphia



Chapter of NABA has participated in this IRS-sanctioned program for the past 15 years. The program operated in three sites in Feb—March of last year. Last year's partnership with TaxRoute allowed the members of NABA the use of newer, user-friendly software, and the ability to monitor and track returns that were filed electronically. E-filing reduces errors, and allows for simpler tracking of submitted returns. TaxRoute plans to work with NABA on future projects that will benefit local PA and NJ communities.



What To Do If You Owe This Year

....there are some options available to you.

There are some options for you if you owe the IRS or the state this year. Many people find themselves in the situation where they owe the IRS or their state taxes. While this can be a startling, anxious, and stressful predicament for some, there are many people who have maintained this status for several years. Some common situations where this issue comes up can include:

- Not having enough taxes taken out of each paycheck during the year;
- Taking an early withdrawal from your retirement funds, and not having adequate taxes deducted at the time of the disbursement;
- If the IRS changes a return you have submitted to include additional income or

to disallow a deduction.

- If you fail to file your taxes, the IRS may file a tax return for you; this could result in you owing money to the IRS or the state.

TaxRoute Golden Rule: *If you have an issue with the IRS, do not sit on it. ALL situations are workable. However, the longer you wait, the worse the situation will be.*

File an Amendment for the Return. Consult with a tax accountant to review the return in question and determine if anything was missed, and if it would be beneficial to amend the return. This is often an option to consider for those returns that were prepared by the IRS. Very often they neglect to include all the deductions, etc., that will benefit you. Frankly, that's not their job, (and most certainly NOT their priority).

Make A Payment Arrangement. Work with your tax accountant to submit a reasonable payment plan schedule to re-pay the debt owed. Oftentimes a payment plan can be put in place to pay the IRS as little as \$50.00/month. The most important thing to remember about the plan you agree to is to STICK TO IT. Or contact the IRS to negotiate a new arrangement.

Allow Current/ Future Tax Refunds To Pay Off Any Debt Owed. Once the return is filed that shows a refund of let's say \$3,500, the IRS simply takes that refund to apply it to the balance owed. Many people use this as one of the less painful methods to pay off a debt to the IRS.

There could be more options available to you. Each taxpayer's situation is different. Be sure

Small Business Corner: Do I really need to incorporate my business?

➔ Incorporation offers some significant benefits to the small business owner. First of all, a small business will gain an enhanced image. Being able to include the abbreviation "Inc." at the end of your business name makes your business appear to be bigger and more established than a business that is not incorporated. This may prove to be a powerful marketing tool in terms of presenting oneself as established and trustworthy to your client base. Vendors oftentimes will require this as a condition of selling products to a small business. Banks often have similar requirements for opening a business account.

Myth #1 – "In order to claim my business on my tax return and take advantage of the business write-offs, I need to have my business incorporated." NOT TRUE. You may in fact file a Schedule C with your 1040 form as appropriate with or without being incorporated.

Myth #2 – "I don't have to incorporate my business because I do great work. I don't have

to worry about a possible lawsuit".

It doesn't matter that **you** think it's great work. Someone may be dissatisfied and want to sue. You can be sued by **anyone** (i.e. a customer, another company, a group) who may be upset, dissatisfied or even harmed by you or your work.

Most small business owners would benefit from incorporating as a Limited Liability Corporation (LLC), or in the case that there are multiple owners, a Limited Liability Partnership (LLP). With an LLC/LLP you, as the owner(s) are protected by a "veil" or a "liability shield". In the event that you or your business were sued by a dissatisfied customer, incorporation will protect your (and your family's) personal property and assets.

The damages or financial award to your customer could not exceed the company's total assets.

This means that your personal property

(house, cars, rental properties) would be off limits, and could not be used to satisfy a debt even if the amount awarded by the court exceeded the total net worth of the company.

Piercing the Liability Veil. If your company is guilty of gross misconduct, negligence, or intentional illegal activity, then this liability shield will not help you. In that instance the owners or specific people may be singled out and brought to court on charges. (We all remember the ENRON scandal, right?)

Nevertheless, it is recommended that most business owners consider incorporation as an LLC/LLP, primarily for the liability protection. Speak with your TaxRoute/HofflerSmith professional about your specific business situation.

Q & A

Q: If I take an early withdrawal of \$20,000 from my retirement, pension, or 401(k) will I have to pay out a lot in penalties and taxes?

A: Many taxpayers are opting for early withdrawals from their retirement savings. Planning is critical, and it's best to get answers to these questions BEFORE you make the withdrawal if at all possible.

The short answer is "Yes". First you will pay a 10% penalty on the early withdrawal which is usually deducted at the time of the disbursement.

Second, the amount you withdrew will be counted and included with your regular income. Then finally at tax time you will be taxed on the whole amount. Here's where it gets a bit tricky.

Example 1:

Disbursement	\$20,000
Regular salary	<u>\$12,000</u>
Total Annual Income	\$32,000

Adding the \$20,000 has changed your income/tax bracket. You'll be taxed at the \$32,000 which is

a higher rate. In this example, the person would no longer qualify for the Earned Income Credit.

When considering making a withdrawal from your retirement fund, be sure to consult your tax accountant. Planning can often make a big difference. There may be some steps you can take to offset an increase in taxes if you can make the time to plan ahead.



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