

## PAY LITTLE OR NO INCOME TAX LEGALLY

So you think the government is out to rob you of all your hard-earned money? Every time you hear the word "tax,

" you recoil in fear? Cheer up! It's not that bad--especially if you're a business owner. Tax expert Joe Trevison author of "The Secrets of The IRS by The Renegade Ex-Employee" says there is hope for all us saps who just hand over our paychecks to Uncle Sam. Read on for Trevison's tips on taking advantage of tons of business tax deductions--all within the letter of the law.

You say that home-based business is one of the few legal tax shelters left. What does that mean?

First of all, understand something: We have two tax systems in this country. [Many] times people think there's one for rich and one for poor. That is a huge myth. What the systems are is one for employees--people who don't know the rules, which are designed to take your wealth--and one for self-employed people, [the rules of] which are designed to create economic growth. The reason for that is, small business generates over 70 percent of the jobs in this country. So Congress passes good tax laws. And there are good tax laws--let me emphasize this--for small business.

Let's say your business generates a loss. If that loss exceeds the income from that business, you can use that loss against any form of income you have: interest, dividends, rents, wages, pensions, anything. Say you make \$50,000 in salary and you have a small business that creates a \$10,000 loss. You only pay tax on \$40,000. Let's say the loss exceeds your whole income. You can carry back all business losses in 2002 five years and actually get a refund from the last five years' federal and state income tax you paid. In 2003, by the way, that number is going down to two years. Or you can carry forward all business losses 20 years and offset the next 20 years of earning. So you never lose a properly documented business deduction.

What if your home based business is profitable? How can you still save on your taxes?

Trevison: By having a profitable home based business, you can set up a host of fringe benefits, many of which I include in my book. You can set up a self-insured medical reimbursement plan and write off all your deductibles, eyeglasses, co-insurance, pre-existing conditions. Usually that stuff has to exceed a certain threshold [7.5 percent of your adjusted gross income] to deduct anything. With a self-insured medical reimbursement plan, you get a deduction regardless. It's dollar for dollar.

What other deductions do people not typically know about?

Trevison: As an employee, you have to pay [taxes on everything]. As a self-employed person, you don't pay tax until all your deductions are over. So [if you're an employee making] \$60,000 a year, you've got to pay Social Security on 15.3 percent of \$60,000. You've got to pay income tax on \$60,000, regardless of your employee business expenses. [But] if you're self-employed--let's say you have \$40,000 of expenses on that \$60,000, you only pay tax on \$20,000. You pay tax on your net. See the difference?

So what are some things you can do? If you have a child and you want to send them to college, that isn't deductible. And if you pay for their wedding, is that deductible? The answer is no. But if you were to hire your children in your business and pay them [the same] wage you'd pay an assistant, that's deductible. And if they use that money to pay for their own college or their own wedding or their own car, aren't you in essence getting a deduction for those things?

And by the way, children under 18--if you hire them in a sole proprietorship business--are exempt from Social Security, Medicare taxes and federal unemployment taxes and the first \$5000 made in 2005 is exempt from income tax. Result? You get a deduction, and they get that money tax-free.

So to protect yourself, you need to do the same paperwork as you would a normal employee?

Trevison: Good point. You want to have things like time sheets or a tax diary showing what your kid did. So for example, you might say Matthew, my son, sorted files and made 3-by-5 cards for four hours on February 3. That shows what he did, when he did it and how long he worked.

You also want to pay by check--none of this under-the-table nonsense, because [checks] establish a payment from you to your child to your child's bank account. You want to have the appropriate paperwork done. There are W-2s you have to file once a year and 940s and 941s for unemployment and Social Security. But I recommend using a payroll service, because people don't want to do all this paperwork. They will do all the payroll, all the forms, all the filings. You also want to have a contract for services showing you hired your kids and what you're paying them, a normal contract like any other employee.

Does all this apply when you hire your spouse as well?

Trevison: Yes, it's all the same. Now for hiring your spouse, you can set up a self-insured medical reimbursement plan. I can deduct all my medical expenses, dollar for dollar--not because I'm paying medical, but because I'm providing a medical reimbursement plan for my employee, who I happen to be married to. And the IRS has approved this, by the way. It's not some loophole I thought up.

What are some other techniques for taking deductions?

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Trevison: A lot of people don't know that when you're in business, you can deduct your fun. IRS says in their regulations that you can deduct 50 percent of your fun and 50 percent of your [business associate's] fun if you talk business within the same 24-hour day as the fun. Say you invite a prospect over to go to a football game. You talk business over the phone and then pick them up two hours later. Is that talking business within the same 24-hour day? The answer is yes. Say we go to a restaurant and I talk to you in the car about our business or try to get referrals and then we go to a nice theater. Is that talking business within the same 24-hour day? The answer is yes.

You also don't need receipts for entertainment if it's under \$75 per expense. Now when you do entertain, the IRS requires certain documentation. So with entertainment, you have to write down what I call the four Ws and an H:

Who: name and occupation

Where: We went to Greasy Lloyd's restaurant.

Why: Why did you take that person out?

And here's one of the biggest mistakes self-employed people make. You must be specific in the documentation. The word "prospect" isn't specific enough. "Good will" isn't specific enough. Specific would be "try to get a referral" or "talked with a reporter about my book." Don't be general.

What: What was the date, and was it for breakfast, lunch or dinner?

And finally, how much. If you write down all five things, you'll never have to worry about an IRS audit again. If you leave out any one of the five, your deductions will be disallowed and the IRS will hit you with a 75 percent penalty, plus interest.

Why is it so important to make yourself aware of these things?

Trevison: What amazes me is, say you look at your credit card statement and there's a \$200 charge you never saw before. Aren't you going to call the credit card company and find out what's going on? And you might spend an hour on the phone doing that. Yet taxes are the number-one expense in this country. They exceed what most people pay for food, clothing, lodging and transportation combined. [But] 99 [percent of people] give it a 10-minute thought. And the reason is, there's a huge myth in this country. "My accountant takes care of my taxes."

What are some audit red flags that people need to avoid?

Trevison:: The number-one red flag is failing to report all your income. The IRS matches all those 1099s you get from your bank accounts, your stock brokerage companies,

whatever. If there's a mismatch--suppose you made \$30,000, but you only report \$28,000--then you're calling attention to your tax return.

The second thing you want to do is do not use cents in figuring out your tax return. Always round. Mathematical errors cause some of the biggest scrutiny of your tax return because things don't match up. If you use cents, you're just increasing your chance of making an error.

If you do your own tax return, for the most part, you increase your chance of being selected for an audit. The IRS figures if you do your own return, you don't know what you're doing, unlike accountants who might do hundreds of returns. People tend to make more mathematical mistakes when they do their own returns than accountants make.

Third major tip to reducing your chance of audit: Always, always send in your tax return with a return receipt. And if there's a check, send it registered mail or FedEx. There [have even been] cases where if you do send it FedEx [and it is lost], the IRS will waive penalties.

I'll give you another nice tip. Many times people call the IRS for information, especially during this time of year. The problem is, the IRS isn't bound to anything they tell you. However, there is one situation where you can call IRS and if you get a bad answer, they'll waive penalties. But you've got to get six things when you call them: The person's name, their badge number, the date of the call, the time of the call, the nature of the question and the answer. If you write down all six things and you get a bad answer that IRS relied on, they'll waive penalties.

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