

ON YOUR SIDE

E-Bulletin

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*An informative presentation from your Pre-Paid Legal
District of Columbia/Maryland Provider*

TAX TIPS FOR THE COMING SEASON

With tax season upon us, your provider firm wanted to pass along a few tips on frequently asked tax questions we encounter. Please feel free to call us with your questions.

1. Discharges of debts are typically considered taxable income. The exception is when it is done in a bankruptcy circumstance or an otherwise adjudicated "insolvent debtor. The definition means that someone's debts exceed their fair market value of assets pursuant to IRC's Section 108. Reductions of debts more than \$600.00 can be subject to a taxable income and the creditor who reduced the debt by more than \$600.00 often will issue a 1099. This reduction of debt is typically considered taxable.

2. In order to receive a deduction or personal exemption for somebody that the taxpayer supports, the person being supported must be verified as a person that is in existence; they must have a social security number; and they must receive at least half of their support from the taxpayer. There are other conditions that must exist as well.

3. Deductions for work-related clothing requires that the clothing can only realistically be used in the course of employment. Clothing and accoutrements that can be worn realistically in ordinary social environments are almost never deductible. Com-

mon examples include nursing uniforms and doctor's scrubs; safety and utility gear; work uniforms; work specific costumes.

4. The home office deduction is a significant audit trigger. Proof of the home office deduction should be put into a conspicuous folder marked "Future Audit Documents" because a home office deduction is a frequent trigger for audits under current IRS procedure. The home office must be used more or less exclusively for a business purpose and there are other conditions that must exist.

5. Continuous running of a loss on a business is a major audit trigger. The IRS understands that some businesses lose money for one year or even more. However, when the business has been in existence for more than one year and the loss is more than nominal, it sends a red flag and could trigger an audit. The same standard exists for rental losses. However, given the current real estate climate, the IRS may be more willing to accept small rental losses in the landlord/tenant arena.

6. American citizens and lawful permanent residents are taxable on their worldwide income, even if that income is also taxed by a foreign government or is exempt from taxation by a foreign government. This may result either in double taxation or in

inconsistent tax treatment.

An example might be gambling winnings from Canadian casinos. Canada does not tax gambling winnings but Americans who win money at Canadian casinos will owe the United States Treasury taxable income. There are some credits, exclusions and treaties that modify this general rule. In general, if the United States taxes it, it will be taxed by any state with an income tax, which includes the State of Maryland.

7. Very few people can deduct medical expenses on Schedule A. The medical expense deduction is a major audit trigger and is subject to a very high standard that the medical expenses must exceed 7.5% of the adjusted gross income floor of the tax payer. Very few people can meet the existing standards.

8. Every tax season the tax protest movement seems to materialize and convince citizens that there are Constitutional arguments against Federal taxation. Regardless of what one wants to believe, the current state of the law is that these tax protestors are legally incorrect. There are very strict requirements that must be met to avoid taxation.

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