

Managing Income Taxes

As the year-end is approaching, many of you may be thinking about how you will do this year when it comes to income taxes. With proper planning and discipline, you can save on what taxes you are required to pay. Below are some suggestions on saving on your income taxes for 2006:

- Sign up for tax-free and tax-advantaged employee benefits at your workplace such as cafeteria plans and flexible spending accounts for health and dependent care. These accounts allow you to pay your out-of-pocket expenses with pre-tax dollars for medicine and dependent care.
- Save and invest the maximum amount possible in your employer-sponsored 401(k) retirement plan or at least up to the amount of your employer's matching contribution. Invest additional money for retirement in tax-sheltered accounts.
- Buy a home so you can record the interest and property taxes as itemized tax deductions. Later, if you sell, you can reap the benefit of the capital gains exclusion.
- Read and study to learn more about how to reduce your income tax liability. You are the best person to come up with ways to save money on your income taxes.

You might want to consider starting your own business in order to reduce your tax bill. Did you know that a sideline business can open many doors to tax deductions and income-shifting techniques? That's right! I never recommend spending money for a tax deduction, but if you're going to spend the money anyway, you should try to make it tax-deductible. Consider buying and managing real estate as an investment for the possible tax advantages it can bring. By having your own business, every dollar you spend in your attempts to make a profit becomes tax-deductible. You can deduct such expenses as an automobile, in-home office expenses, office equipment, educational expenses, and more. You can deduct salaries of employees, even if they are your children. The business does not have to be your primary employment. In fact, if you lose money on such a business, you can deduct those losses from your other income. The IRS says that you must do what a reasonable business person would do to make a profit. If your business does not meet the IRS test, they will classify the operation as a hobby and will require you to report the income, and will not allow the deductions. If you decide to start your own small business, be sure to make it something you enjoy doing. Be sure to keep detailed records, and take advantage of your deductions.

Source: Garman, E. Thomas, and Raymond E. Forgue. *Personal Finance*. Boston and New York: Houghton Mifflin Company: 2006.

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