

2009-10-23: Tax Mistakes You Can Avoid

Consider the recent case of Treasury Secretary Timothy F. Geithner, whose nomination to that post hit a snag during confirmation hearings. According to published reports, Geithner disclosed that he had failed to pay more than \$34,000 in federal taxes over several years early this decade. What's more, Geithner faced questions about the employment papers of a former household employee. Obama transition officials said Mr. Geithner's failures were innocent mistakes or technicalities and Geithner's nomination was ultimately approved.

Here's a look at some common tax blunders.

Not reporting gambling income - If you receive money, prizes or awards of monetary value from winning the lottery, you are required to report this as income on Schedule A, line 28 of your tax return. Losses also are deductible, but only to the extent of the taxpayer's gains from similar transactions.

Not paying taxes on unemployment, wages, tips or other earned or unearned income - If you are out of work and receiving unemployment benefits, you have to pay taxes on the benefits. You either can instruct your state unemployment agency to withhold the taxes similar to how you would instruct your employer to withhold from a paycheck, or you have to pay quarterly estimated taxes on it.

Incorrectly reporting children's investment income - A child's investment income of more than \$1,800 must be reported on the parent's income tax return and taxed at the parent's income tax rate if the child was under age 18 at the end of 2008; was 18 years old at the end of 2008 and did not have earned income that was more than half the child's support; or the child was a full-time student 19 to 23 years of age and did not have earned income that was more than half of his or her support. You need to use Form 8615 to figure out the tax for a child's investment income.

Not paying the nanny tax - If you have household workers, you are required to withhold and pay FICA taxes if cash wages paid in 2008 totaled \$1,600 or more (\$1,700 in 2009). As the employer, you have to report and pay the required employment taxes for these domestic employees on Schedule H (Household Employment Taxes), with the tax amount then transferring to the appropriate line on your Form 1040 or 1040A.

Not reporting gifts given over \$12,000 - If you gave a gift to an individual in excess of \$12,000 in 2008 as a single filer or \$24,000 as a split gift by joint filers (\$13,000 and \$26,000, respectively, in 2009), you either have to pay taxes on the amount above this limit or apply it against your lifetime gift tax exemption (which currently is \$1 million). The tax on gifts ranges from 18 percent on taxable gifts below \$10,000 to 45 percent on gifts of \$1.5 million or more. If you don't report the gift, it is considered tax evasion. Gifts are reported on Form 709.

Being overly charitable to oneself with charitable donations - The IRS expects people donating items to use fair market value in determining the value of the items; for non-cash donations of more than \$500 a written description of the donated property must also be furnished. Additionally, cash donations of any amount now require proof, such as a cancelled check, credit card statement or receipt from the charity. Contributions of \$250 or more also require a letter from the organization specifying the name of the donor, the amount given and the date received.

Exaggerating expenses - Taxpayers who don't have proof of expenses they are deducting will be required to pay back taxes and interest on non-substantiated deductions. Depending upon the extent of abuse, the IRS may take other measures as well.

Not filing a tax return - Most people are required to file a tax return and even those who are not can benefit from doing so, for example, by having the chance to get a refund on taxes already withheld or to claim the earned income credit, additional child tax credit, first-time homebuyer credit or the recovery rebate credit. Income thresholds for those who must file range based on age and filing status. For single filers under age 65, returns must be filed if they earn \$8,950; returns must be filed for married couples under age 65 filing jointly if their income is \$17,900 or more. Tax returns are due on April 15. Taxpayers can file for an extension until October 15, but they must file the request (using IRS Form 4868) for an extension by April 15.

Filing an incomplete tax return - For most people, making an error on their tax return or not completing it means a delay in any refund they may have been coming and additional inquiries from the IRS. They may also be subject to additional payments and interest if it's determined they owe more taxes. However, if the IRS determines someone is intentionally filing an incomplete or inaccurate return, this is tax evasion and the IRS will pursue it as such.

Doing your own tax return - To be fair, doing your own taxes isn't a blunder. But it's very easy to miss your mistakes as Treasury Secretary Geithner recently discovered. Software is terrific but some things get missed and errors are made.

Failing to learn from the past - It's one thing to have your taxes prepared by a professional. But it would be a mistake if you failed to ask that professional to analyze your tax return for ways to reduce your tax bill going forward.