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TAX NEWSLETTER **January 2011**

Dear Folks:

1. As in the past, I remind you that as soon as you receive any information from any governmental agency or tax collector, before you call me, fax me the letter and if you do not have a fax please mail a copy of the letter to me. Too often I get a call from clients saying they just got a letter from the IRS and it turns out to be from PA and normally I can't even make sense of what the problem is without seeing the actual letter. Another problem is that many of my clients assume that I just automatically pick up all of the estimated payments that I advise you to make when I am doing your tax return. I do not make that assumption, then I find out my client has forgotten to make one or two payments or made changes in the amount of the payment. So if you do not list on the organizer or on some piece of paper how much you have made in estimated payments, I assume you made none. Therefore, you must list all of the estimated payments you made both for Federal and State. I do, however, pick up any overpayment from the previous year that I have applied to the next year.

2. Local Earned Income Tax – I am constantly in a battle with the local tax collectors on the 1% earned income tax. This applies to the City of Philadelphia and any other local municipality which has an earned income tax. The earned income tax is only supposed to be paid if you live in an area that does not have an earned income tax, then the earned income tax is only supposed to be paid on the amount of income you earned within the earned income tax jurisdiction. For example, if you live in the suburbs and work in and outside of Philadelphia, the Philadelphia income tax is only to be paid on those earnings which you make while you work within the city limits. So if you work out of your home half the time and in the city half the time, then you should only be paying earned income tax on half your earnings. You should get your employer to only report half as Philadelphia taxable. However, if you can't get your employer to adjust that with your withholding and it insists on withholding on 100% of your income tax, good luck with trying to get a refund from the City of Philadelphia or any other local municipalities. You have to get your employer to stop withholding on 100% and reduce it to only the percentage that you earned while within the taxing jurisdiction. That applies whether you work in the City of Philadelphia or you live in Chadds Ford and work in West Chester, Chadds Ford which has no tax but West Chester has a 1% tax. It also applies if you live in PA and work in DE or live in NJ and work in NYC. Whenever the earned income tax is higher in one jurisdiction than the other, it is always better to try to allocate your time to the lower jurisdiction.

3. Florida Residents: Of course everyone knows it is better to be a resident of Florida because Florida does not have an Inheritance Tax or a Personal Income Tax. So as long as you are not a resident in any other state over 183 days a year, you can classify yourself as a Florida resident. Now, of course, we all know how to establish a residency. Certainly a resident of Florida does not file their tax return out of PA or have a driver's license in PA or vote in PA, etc. There is not one item which makes you a resident but a combination of all items. I assure you one thing, if you file your tax return with a PA address, have a PA drivers license and vote in PA, have all of your credit cards registered in PA, have your passport issued out of PA, then in my opinion, you are a PA resident. By the way, the difference in income tax between a NY resident and a non-NY resident is significant so if you can establish that you are a Florida resident and or course you are, then in the case of NY or NJ, the savings can be substantial. Even for PA, the savings can be significant.

4. Contributions. I know most of my clients have been accustomed to the olden days when you could deduct cash contributions so that you always expect me to put down something for Church plate. That is no longer the case. Cash contributions are not permitted unless you get some kind of statement or letter from the donee organization. Therefore, unless you specifically put down a total of donations on your information you give to me, I am not allowed to deduct a guesstimated amount for cash contributions.

See Reverse Side

5. Statutory Employees. On my website there are articles and write ups about the difference between a ***statutory employee*** and a regular employee. A ***Statutory employee*** is somebody who gets a W2 but meets certain other criteria that would permit them to take business expenses directly against their income not as miscellaneous itemized deduction by which you lose 2% of your adjusted gross income in deductions. A ***statutory employee*** is a person over whom the employer exercises little control, is predominantly on percentage basis compensation, pays a substantial amount of their own expenses, and has no set office at their employers location. It has been impossible for me to get the comptrollers of most large companies to understand 1) the difference between statutory and common law employees and 2) that there is no downside to the employer in making such a designation. The employer still has to withhold all taxes, still has to include the employee for all benefit plans and still has to provide for vacation and holidays. So what I have decided to take upon myself this past year is to make a classification of a ***statutory employee*** myself and include a detailed explanation of what the client does in order to qualify as a ***statutory employee***. In one case, it was clear to me that my client was a ***statutory employee*** so I filed his tax return that way and saved about $8,000 in income taxes. My bet is that the IRS will send a letter inquiry and we will have to go into detail to convince them. But once I am successful, the initial work will be worth it because all future years will be permitted as a ***statutory employee***. If you can get your employer to classify you that way then it is really simple because they check off a box on your W2 that says ***statutory employee*** and then the IRS will raise no question about that. In that case, you must keep detailed records of your business expenses along with written evidence of your transportation – cost for driving your own vehicle.

6. Powers of Attorney. I'm running into more and more problems with banks not honoring our lawful and appropriate powers of attorney. Legally they have no right not to honor them and as a matter of fact, legally, they are the only powers of attorney that should be honored because a power of attorney in PA has to be done in a very specific way and the bank's powers of attorney is generally not the same and therefore, in my opinion, not totally proper and legally binding. This being said, if you do have a power of attorney that you are using for a relative or you're planning to use one, before that relative gets to a point where they can no longer sign another one, go to the specific bank they are using and make sure the bank will honor the power of attorney you have and if they are going to give you a hard time, take the path of least resistance and have their power of attorney executed. If you want a power of attorney, go to my website and get all the forms. There are various forms such as power of attorney, living will, simple will and some others on my website. The power of attorney to be proper in PA must be signed, dated and witnessed but only needs to be notarized if there is going to be any real estate involved in the use of the power of attorney. If there is real estate, you must be sure to fill in the address on page one.

7. Loan Modification. Recently I had the opportunity to help somebody get a loan modification. It is not an easy task but certainly worthwhile because the interest rate reduced and the loan payment dropped by about $600 per month. It's a crazy procedure but worth looking into. Typically because it is a governmental program, it has typical governmental regulations, one of which is that your monthly payments for interest, principal and taxes must exceed 41% of your gross income. Another, which is even crazier, is that most of the people who administer this do not know how to add 2 and 2 together, so if your parents are loaning you money to make the mortgage payments, they'll add that into your income. So make sure that if they are making loans to you to make the payments directly, DO not deposit them into your regular bank accounts because in a loan modification procedure they require four months of bank statements and if they see a deposit into your bank statement of $10-20,000 they add that in and consider it income. Then even worse, they annualize that. So a $10,000 gift will add $30,000 to annual income. So it is better that if your parents are loaning you money to make the payments, that they make the payments directly or you open up a separate bank account in their name so you do not have to submit it when you go for the loan modification. It is very tedious, time consuming and frustrating but can be exceedingly rewarding and therefore if you are having trouble paying your mortgage, don't pass it up. If you need help, get the forms from your mortgage company and contact me.

If you have any other questions regarding tax, legal, real estate or county matters, please feel free to contact me. If you do not want to receive this, please advise me to remove your name from my list.

Respectfully,

Donald J Weiss

Donald J. Weiss, Esq/CPA

See Reverse Side