Eight Money Myths – Busted

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We financial animals like our rules, yes we do. Some are quite useful, such as every debit must have a matching credit to ensure the survival of our species. But I believe some "rules" should be taken out of the box and dusted off periodically to see if they have outgrown their purpose. So…are these "rules" or urban legend? You decide but please read with an open mind! I'm not asking that you agree with everything I write, just that you consider what might be helpful to your situation.

Myth #1: You never want to get a tax refund back from the government because (heaven forbid) all you've done is given Uncle Sam an interest-free loan!

Buster: No, I'm not a double-agent for the IRS! Many people like getting their refunds on April 15, and I'm not so hard on them for doing so. Yes, they are loaning money to the government and receiving no interest on their loan. However, the only thing worse than making an interest-free loan to the government is owing income taxes on April 15 and having an empty saving account! For people who tend to spend every paycheck before it clears the bank, withholding extra taxes may be the only way to put aside a few thousand dollars. If that's what gets it done, I have no qualms with forgoing the nominal interest they *may* earn on their savings account. At least when it's sitting in the U. S. Treasury, you are forced to leave it there until you file your income taxes. Cash under the mattress may not be around next April 15th!

Buster: Children can earn up to the threshold standard deduction without having to pay income taxes so they don't need to file an income tax return.

My take: Sometimes you need to report income in order to take advantage of available tax benefits; a Roth IRA contribution is a great example. Children often begin making money mowing lawns and babysitting at a very young age. Consider filing a tax return and contributing to a Roth IRA for them, even if it's only $1,000. Saving $1,000 each year beginning at age 10 for 35 years, assuming an average 8% return (quite possible when investing aggressively at a young age) would yield over $200,000 by age 45 on an investment of $35,000. (The benefits are even better if you own your own business and can hire your children – but that's a topic for another column.)

Myth #3: You should begin claiming Social Security benefits as early as possible.

Buster: At least consider the benefits of waiting until age 70, if possible. You'll boost your benefits by 8% for each year you delay drawing, which is a wonderful return these days. Of course, if you or your spouse expects to die relatively early, you might want to begin drawing sooner. An exception to the exception is if you and your spouse are several years apart in age, in which case the younger spouse may want to begin claiming early to boost household income while the older spouse delays claiming until age 70. As you can tell, this is a topic that has no easy answers. Before deciding when to begin claiming benefits, invest in some time with a Certified Financial Planner® or sit down with your SSA rep to run some projections that can help you decide. (See my November 2011 column for more on this topic.)

Myth #4: You should always deduct as many expenses on your tax return as possible.

Buster: This is where a good tax accountant really earns her money. Believe it or not, sometimes your tax liability will be higher when you deduct more expenses. This is especially true when you own a business and could qualify for the Earned-Income Credit. Deductions for fixed asset purchases, for example, can be adjusted for maximum refund. In addition, you need to consider whether you will be in a higher tax bracket in the future and should delay paying deductible expenses or deducting more depreciation at a later time.

Myth #6: Don't sell property if you'll have to pay income taxes.

Buster: Consider that tax rates will probably go up in the future when you may have to sell, costing you even more in taxes. Remember, long-term capital tax rates are at an all-time low and scheduled to go up in 2013. If you're in an especially low tax bracket this year and you can find a better use for the money than keeping it tied up where it is, maybe you should consider selling.

(PS: IRS Code Section 1031 property exchanges are still being done. See an accountant or financial planner who is experienced in handling these before proceeding.)

Myth #7: When you retire, you need to put all of your money in CD's and bonds.

Buster: In its 1/5/12 issue, Financial Planning online stated, "Today, healthy 65-year-olds have at least a 40% chance of living into their 90s." Are low-interest CD's and bonds going to sustain you in 30+ years of an inflationary retirement? No matter what your age, I generally recommend you have *a minimum of* 50% your nest egg in equities (stock mutual funds) to counter the effects of inflation and allow you to maintain your standard of living.

Myth #8: Don't file your income tax return until you can send in the taxes due.

Buster: Actually, this is an easy one. Never file your income tax return late, or you'll be looking at late ***filing*** penalties *in addition to* interest and late ***payment*** penalties. Send in what you can with a timely filed return and let the IRS send you a bill for the balance.

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