

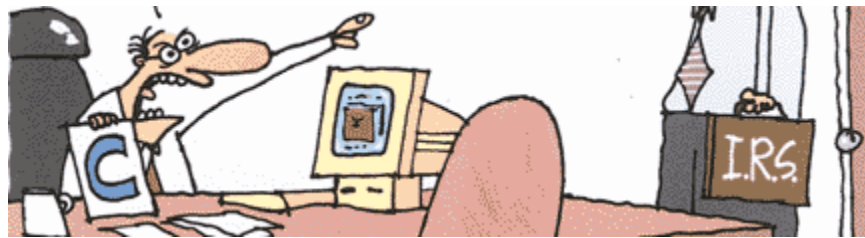
TAXES

It's What You Keep That Counts

by Ted Tesser, CPA

Trader status, which has always been one of the hottest but least understood topics whenever taxes are discussed, has always left market participants confused. Here's a certified public accountant who also trades to explain it all to you.

Trader status has always been one of the most hotly discussed topics whenever taxes are discussed amid those in the industry. Until recently, the Internal Revenue Service (IRS) code left us in the dark, and all we had to go on were the divergent opinions of certified public accountants (CPAs), tax lawyers, and other tax professionals. With the passage of the Taxpayer Relief Act of 1997 and subsequent Congressional interpretations of the law, trader status has finally been addressed, and in fact, taken on greater significance because of certain benefits extended to traders.



ART BY JERRY KING

THE BENEFITS OF TRADER STATUS

This distinction actually first became quite important with the passage of the Tax Simplification Act of 1986. President Ronald Reagan simplified the code just by eliminating many perks that investors had always enjoyed. It put an end to the deductibility of investment seminars, established the 2% to 3% floor on itemized investment expenses, phased out all itemized deductions after \$109,000 of adjusted gross income, imposed a stiff alternative minimum tax on investors, phased out investment interest expense beyond investment income, and limited investment income to dividends and interest. (Capital gains could no longer be considered investment income unless the long-term capital gain tax rate preference was waived.)

The trader, on the other hand, could continue to enjoy these benefits as well as others. Traders get to write off 100% of trading expenses rather than as itemized deductions. Since 1997, traders have had the option of deducting all their losses in the years in which they take place by making a timely Section 475 election, rather than being limited to a net \$3,000 loss in any one year.

In addition, traders can elect to take the depreciation of any new business asset all in one year up to \$18,500, instead of over three, five, or seven years, and can be entitled to the home office deduction. Investors do not have these options. Further, Congress has specifically stated that although gains and losses are now ordinary, most traders will still not be subject to self-employment tax/Social Security tax on their earnings.

Ted Tesser is president of Waterside Financial Services in Boca Raton, FL. Tesser has developed a questionnaire to evaluate trader status; for a free copy, E-mail him at info@taxtrader.com, or call 800 556-9829.

Excerpted from an article originally published in the January 2000 issue of Technical Analysis of STOCKS & COMMODITIES magazine. All rights reserved. © Copyright 1999, Technical Analysis, Inc.