



Even Tiger has

- Trading Books/Videos
- Daily Set-Ups
- Training CD-ROMs
- Stocks
- Options

TM University

Market Analysis

Indicators

News & C

Daily

- Haggerty's Views
- Trader's Edge
- Trading E-minis & SPYs
- Before The Show
- Swing Trading With Dave Landry
- Nightly Daytraders Report
- Intermediate-Term Traders Report
- Live From TradersWire
- Stocks Wall Street Is Watching
- Traderswire AM Audio Alerts
- Mid-Day Opportunities
- Edward Allen's Dominant Themes

Semi-Weekly

- Kaltbaum's Momentum Trading
- TM Charts Ready to Explode
- Tim's Aggressive Growth Edge
- Derrick Hobbs' Swing Trading With Fibonacci
- Rob Hanna's Putting It All Together

Weekly

- Boucher On The Big Picture
- Connors' Weekly Battle Plan
- The Market Next Week
- Navarro's Art Of The Macroplay
- Ruggieri's Medical Technology Insight

Periodic

Ruggieri's FDA Decision Alert

Members Commentary

SEARCH

[Home / Stocks - Market Analysis / The Big Saturday Interview](#)

[HELP](#) | [PRINT](#) | [E-MAIL](#)

The Big Saturday Interview



Keep More Of Your Hard-Earned Money! Robert A. Green, CPA Tells You How
By Brice Wightman

TradingMarkets.com
April 11, 2003 11:00 PM ET

Robert A. Green CPA is a leading authority on trader tax. His virtual tax firm, GreenTraderTax.com has clients across the country. He is a monthly contributor to Active Trader Magazine, and has been featured in Barron's, Fortune, and SmartMoney.com, and has appeared on CNBC and Bloomberg Television. GreenTraderTax.com builds and operates tax centers for leading direct-access brokers and trading schools.

The following conversation took place between Robert Green, CEO of GreenTraderTax.com, and TM's Editor-in-Chief Brice Wightman on Wednesday, April 9, 2003.

Brice Wightman: Let me first say that I'm glad there are people like you doing this because it's a pretty deep topic and there are a lot of complex rules involved. Let's start with your firm. How did you begin specializing in taxes for traders?

Robert Green: I've been handling traders since 1983, before as Green & Company CPAs on Wall Street; I was New York City based. I was very interested to see what traders went through using the Internet resources, as many of my clients were traders. At that point, I got familiar with the community. And in 1997, Congress changed the tax laws to bring in the new **mark-to-market accounting** which turns capital losses into ordinary losses. That's a real panacea for traders, and I was there on the Internet when that happened and I quickly saw that the trading community did not know about it. So I immediately took on the job of educating traders about mark-to-market (MTM)

[Dollar Crash - Can You Profit From A Falling Dollar?](#)

FREE TRIAL!

Sign Up For Your Free TradingMarkets Trial And Receive \$150 For Trading Books & More!
[Click Here](#)

FIDELITY ACTIVE TRADER PRO™

Nasdaq Level II: AAPL

AAPL

Nasdaq Level II

AAPL APPLE COM	
Last 16.3000 ↑	
Bid	
Size	ID
02	ADFN
08	ARCHIPELA
25	AMEX
04	TRAK
03	BLOOMBER
14	BRASS UT
10	CINN STOC
01	UNTERBERG
01	J.P. MORG
01	SMITH BA
01	COWEN SE
01	SUSQUEHA
01	MAYER SCH
09	TIMBER HI
01	PIPER JAF
01	GOLDMAN
01	SOUNDVIE
01	DAIN BOSW

Streaming Nasdaq® Level II quotes

Confine to this section 

accounting (IRC 475).

Wightman: Well, let's talk about that. What is MTM, and what's the advantage of electing mark-to-market?

Green: The advantage is that your losses are ordinary, so you're not stuck with the capital loss limitations of \$3,000 per year. For securities traders, the gains are taxed the same way at the ordinary tax rate. For commodity traders, we *don't* recommend mark-to-market because they have the benefit of the 60/40 split (60% long-term capital gains) so they would have to, in effect, give that benefit up to get ordinary loss treatment. So we recommend it for securities traders. In order to *elect* it, you must qualify as being in the business of trading, which means that you trade basically every day, all day, either full time or part time -- and if you're part time, you're even *more* scrutinized by the IRS, so you really need to prove that you're running a business. If you *qualify* for trader tax status business treatment, then you must elect mark-to-market accounting by April 15. So, it's April 15, 2003 for the *year* 2003. So if you're planning to qualify or you already have qualified this year, 2003, for a full or part year, you should consider mark-to-market accounting. It's pretty much right for *all* securities traders except the following conditions:

When a securities trader has what we call tax "baggage." They have large capital loss carryovers from the prior year. In that case, you have a predicament when it comes to electing mark-to-market accounting. It's sort of a gamble. You need to commit by April 15. If you elect MTM and end the year with large trading gains, those gains will be "ordinary" gains and you will not be able to offset them with your capital loss carryovers from 2002. And you'll be sorry you elected mark-to-market accounting.

Now *conversely*, if you end the year with large losses, you'll be very happy you elected MTM accounting because your losses will be *ordinary* and you can offset those ordinary losses in full, without *any* limitations against *all* your other income, including your spouse's income and if you have *negative* income, you may have a "net operating loss" which you can carry *back* two years for immediate tax refund. So, mark-to-market accounting is right for all securities traders but if you have a capital loss carryover, you need to think twice about it. If you're a profitable commodities

"The advantage (of MTM accounting) is that your losses are 'ordinary,' so you're not stuck with capital loss limitations."

ARCHIVES

April 11, 2003
[Keep More Of Your Hard-Earned Money! Robert A. Green. CPA Tells You How](#)
 Brice Wightman

March 29, 2003
[Nearly Every Wall Street Desk Reads This Man! An Interview With Dennis Gartman](#)
 Larry Connors

March 01, 2003
[An Interview With Tony Saliba's Head Trader, Joe Corona](#)
 Larry Connors

February 08, 2003
[Nelson Freeburg On Developing The Perfect Trading System, Part II](#)
 Larry Connors

February 01, 2003
[Nelson Freeburg On Developing The Perfect Trading System](#)
 Larry Connors

January 18, 2003
[I've Been Known To Fire People Who Like Stocks!](#)
 Larry Connors

January 03, 2003
[In Memory Of Leon Levy, 1925-2003](#)
 Larry Connors

December 21, 2002
['Not Dead, Can't Quit' -- No Limit Thinking With Navy SEAL Veteran Richard Machowicz](#)
 Larry Connors

trader, I would skip it. And you *can* elect for securities only, and not commodities, or both, or vice versa.

Wightman: What about traders who trade both stocks *and* futures?

Green: We suggest that you elect MTM for securities only and that's IRC 475. There's a statement -- it's not a form, it's a statement --and we have it in our Trader Tax Status And Mark-To-Market Accounting Guide that we sell for \$40 and you can download it immediately off our website. It also consults you on all the nuances and strategies regarding mark to market. So it's important to select which one you are electing for. Now, if you want more flexibility, consider having an *entity*. You can form your own entity now, which is a "**new taxpayer.**" A new taxpayer elects internally within 75 days of inception -- they don't file the election to the IRS -- so then you can make the election internally. You can't change your mind but it's an internal election, so only you really know what you did.

Another type of entity you can use is a "**Husband/wife general partnership,**" a "trading business" partnership. You can use that for 2003 and even for 2002, a *de facto* trading partnership. If you have a joint trading account and your spouse is listed on your statement and your spouse has contributed some of the money to the account or your joint money, and your spouse participates in the business, although the spouse doesn't actually have to trade -- just kind of looks over your shoulder -- it just may be that in 2002 that you *have* a husband/wife "trading" partnership. The IRS rules state that a sole proprietor trader who is in business with their spouse cannot file a joint Schedule C (which is a profit or loss business form for an individual). Instead, the rules require that they file a partnership return. And you don't have to *register* that partnership with any state and there are no fees associated with it.

So, if you *missed* the mark-to-market election by April 15, 2002 *for* 2002 and you have a large trading loss for 2002 that's subject to the capital loss limitations, you will be very interested to read about the "**Husband/wife 'trading' partnership**" which is featured on [our website](#) on the home page and if you *qualify* for it, you can file a late partnership return for 2002 *after* April 15, but if you read the article this weekend, you should file a partnership extension by April 15 so the return is *not* late.

If it's late, it's subject to \$100 penalty but that's not high, and this partnership fix, in effect, will give you mark-to-market accounting for 2002. There are also

nuances and requirements and things you have to do verbally with your spouse. It's not that easy. It's very complex. You need to consult with us about it. So that's the lay of the land about mark to marketing. It's something you want to have -- it's that partnership fix for 2002 and even 2001 -- and for 2003, you want to elect it by April 15.

Just to sum it up: (It's like) your trading business is your house. And if your house burns down, you want insurance. Mark-to-market accounting is that insurance. And the insurance is free. So, all it requires is knowing about it and making the election by April 15.

Wightman: What is the biggest mistake traders make in their filing status?

Green: Well, the first thing, the word "status" refers to trader tax status vs. *investor* tax status. Trader tax status means that you are a business person or a business partnership in the *business* of

"Traders who are... very serious in their trading...will qualify, in the eyes of the IRS, as being in the *business* of trading."

trading. Those active traders who utilize the Internet, the online and direct access firms and websites like TradingMarkets.com, they're very serious in their trading, day in and day out. Many are daytraders. Some are swing traders. Most of them -- certainly daytraders and many swing traders -- will qualify, in the eyes of the IRS, as being in the *business* of trading. There are no set exact numbers or rules that you can look to. What you *can* look to is IRS Publication 550, Chapter 4, "Special Rules For Traders," where it lays *out* the rules. The key point is this: If you *qualify* as being in the business of trading, then all of your *expenses* related to that business are *business* deductions, and they offset any income "above the line" on your tax return. If you *don't* rise to the level of business treatment, known as **"Trader Tax Status,"** then you are treated as an investor, the default method.

Now, investors are penalized under the tax code in many ways: First of all, there are very few types of expenses investors can deduct. Second of all, those expenses are taken on Schedule A as itemized deductions and they are subject to many *haircuts*. For example, investment expenses are Miscellaneous Itemized Deductions which are only deductible in excess of 2% of your adjusted gross income. Investment expenses are *not* deductible for Alternative Minimum Tax (AMT), that dreaded tax which applies to wealthy people -- and now middle-class people. So you cannot deduct a home office if you are an investor, you cannot deduct seminars if

you are an investor.

Really, reaching the level of business treatment will save the average trader about \$5,000. Margin interest is deducted on a business trader's Schedule C, in full, but investment interest expense for an investor is *limited* to investment income, otherwise carried over to the next year.

So the first order of business to unlock all trader tax benefits is your status. You want to see if you have Trader Tax Status for all or part of the year, and you need to do this each and *every* year as the factors change. If you *have* Trader Tax Status as a prerequisite, then you may utilize mark-to-market accounting, provided you elected it on time, and you elect it once and it carries over to the next year.

Wightman: What are some of the benefits that you would get with Trader Tax Status. You mentioned a home office deduction. How much do you think the average trader can save using the home office deduction?

Green: Between \$5,000 and \$10,000. Most traders *have* a home office and the rule is it must be exclusively used for your business. It cannot be a den, it cannot be a children's playroom, it cannot be a guest room. It's exclusively used for your business. Most traders *have* that because they don't want guests or children playing with their equipment, which is expensive anyway. The way the deduction works is: If you have a three-bedroom apartment and one room is used solely for trading, a little less than one third of the apartment is the home office. Therefore, close to one third of the rent, one third of the utilities, one third of every general expense of that apartment is deducted on Form 8829. You then *transfer* these deductions to Schedule C where the business trader reports their sole proprietor business expenses.

The one *requirement* of a home office deduction is that you have sufficient income to drive the deduction. If you lose money trading, you can *report* the deduction but then you must carry it over into the next year -- which is very useful, but not useful to you in the current year. Now keep in mind you need some special filing strategies when you file as a trader. Your trading gains are on Schedule D if you're using the cash method and they're on Form 4797 if you're using the mark-to-market method. Your expenses are on Schedule C, so if you don't make any of the moves that we suggest you make, you'll have a loss on Schedule C from the expenses which will disallow the home office deduction. So what we do is -- and we explain this in our Individual Tax Return Examples Guide (also available on our website) -- we show you how to transfer some of the gains from Schedule D or Form 4797 to Schedule C,

to "zero out" Schedule C.

So if you have \$22,000 of expenses on Schedule C, including margin expenses, and you have \$8,000 of Code Section 179 depreciation, which is 100% depreciation on computers equipment and furniture - - we can discuss that next -- and you have a \$10,000 home office deduction, your total expenses are \$40,000. If you don't do the transfer, your tax software will only pick up the loss of \$22,000 on Schedule C, and carry over the home office and 179 depreciation deductions to 2003. But if you transfer \$40,000 from Schedule D or Form 4797 to Schedule C, then you'll "zero out" Schedule C, and you'll have a \$40,000 reduction on your Schedule D or Form 4797. And if you're in a 40% tax bracket, that will put \$16,000 in your pocket.

Wightman: Let's talk about the 100% deductibility of the computers and equipment that you just mentioned. You're saying that's not amortized?

Green: When you purchase computers and equipment -- capital assets or fixed assets (equipment assets that will give you future benefit besides the current year) -- you're supposed to *capitalize* it and then *depreciate* it. The depreciation rules for computers, if you're aggressive, is over three years. Usually, everything else is over five years. But there is 100% depreciation, which is Section 179 depreciation, and it goes up every year. For tax years beginning in 2003 and later, the dollar limit is \$25,000. For tax years beginning in 2001 and 2002, the limit was \$24,000.

What happens is that if you purchase \$25,000 of computers, equipment, furniture, desks, rugs and the like (and most traders *do* spend less than that) and if you have trading *gains*, you'll get a 100% deduction. If you *don't* have trading gains, rather than carry over the 100% deduction until the next year, fall back and instead use the regular depreciation for computers over three years and equipment and furniture over five years. Plus there's bonus depreciation from recent tax law changes which gives you an extra kick of even more depreciation than just being over three years. And the regular rates are accelerated to begin with anyway, so you're really getting a lot more than one third the first year anyway.

Wightman: Earlier, you mentioned seminars. To what extent are seminars and other educational materials like books, etc., deductible?

Green: Well, there's a key point about seminars and education. Before you start your trading business, if you go and train at, let's say, one of the trading schools... if you haven't started your trading

business yet, that's considered a *start-up* expense and then you need to capitalize it -- like we were talking about -- and instead of depreciating it, you need to *amortize* it over five years. So it's better to say that you entered the business, then you took your training, so you can get 100% deduction right away. Now if you're an investor, you cannot deduct education. So you need to be in the business of trading and then have the education afterwards, after you started the business. Because if it's before you started the business you can deduct it but over five years. Now the other items like books, subscriptions and online services, they're all fully deductible for both investors and traders but for business traders, you can get a business deduction. For investors you get that haircut deduction on Schedule A that's subject to all the limitations.

Wightman: What do you see are the advantages and disadvantages of, let's say a single member LLC vs. a sole proprietorship? Are those the two large tax status entities?

Green: Yes, the third one being the husband/wife general partnership. If you're single, you can't have a husband/wife general partnership. A **single member LLC** can have just that -- one member -- and the nice thing about it is that you don't even have a separate tax return to worry about. You report everything on your individual return. But to answer your question about the different entities and the differences to traders, the answer is: A trader does not need an entity to deduct business expenses and to elect MTM accounting. Those comprise 90% of the benefits that a trader would want on their tax return. So a sole proprietor can accomplish just about everything necessary to improve their tax situation. What a sole proprietor can't do is deduct health insurance premiums from adjusted gross income and can't deduct a retirement plan contribution.

The reason is that **sole proprietor** traders or traders in any entity are not generating "earned income," and they don't owe self employment (SE) taxes like FICA and

"...if you're a part-time trader, the IRS will really scrutinize your Trader Tax Status."

Medicare. So there's good and bad news. The trader doesn't generate earned income which means that he saves SE taxes, and that's 15.3% x the first \$84,900 and 2.9% thereafter -- that's a significant benefit. On the other hand, without earned income, you cannot deduct your health insurance premiums from adjusted gross income and you can't deduct or contribute to retirement plans -- and we can talk about mini 401k plans

which are extremely exciting and provide the best retirement benefits for traders. So if you *want* to deduct your health insurance premiums and you want to provide for your retirement with tax deductibility which puts money in your pocket, then you need to have an entity and you need to trade as an entity, and then the entity pays you a fee or a salary which creates earned income and other opportunities for the retirement plan contribution. So figure that a sole proprietor will save \$10,000 or \$12,000 vs. an investor. A single member LLC might save another \$7,000 or \$8,000 over that. And a single member LLC is very inexpensive to set up, \$300 or \$400 in most states. Now if you are a *part-time* trader (meaning that you have a W-2) and you don't have *that* many trades -- and a lot of traders are like that -- the IRS will really scrutinize your Trader Tax Status.

You might be interested to file a partnership return with your spouse, which is a separate tax return and that will deflect some IRS scrutiny of your status because the partnership return will be separate from your individual return and they won't see that the two go together. But if you're single, you can't file a partnership return so then you could consider an S Corporation. If you're considered a single member LLC, then you don't file a separate tax return. But an S Corporation does file a separate tax return. Take note there are various potential minimum taxes in each state and you need to consult with experts like us to see what those potential taxes are. Even if there is a potential minimum tax, it is usually a few hundred dollars at most.

Wightman: Tell me briefly about the mini 401k plan you mentioned.

Green: The mini 401k plan combines a 401k elective deferral (and many people are familiar with this from work). It's \$11,000 per year for 2002 -- it's up to \$12,000 for 2003. So you can contribute that. Plus, you can do a profit-sharing plan, which is 25% before tax or 20% after tax.

For example, for 2002, had you set up a mini 401k plan with your entity, you could pay yourself a "fee" of \$17,500 and you could get deductions of \$17,284 and that will save \$6,914 in income tax. You'll pay self employment taxes of \$2,473, so you're putting \$4,441 in your pocket. So you're basically contributing \$13,632 to the mini 401k (which is the \$11,000 elective deferral plus 20% of the adjusted "fee"). Then you are able to deduct your health insurance premiums, and you deduct half the SE tax. So whether you want to go on the low side and contribute close to \$14,000 or if you want to contribute the maximum, \$40,000, it's the best plan of choice, because if you contribute \$40,000, the "fee" that's required is \$152,320.

Now if you were to have a regular SEP IRA or KEOGH plan, the "fee" would have to be \$200,000, so you're saving the Medicare tax of 2.9% on that difference of close to \$48,000 and you're saving close to \$1,400 SE tax. Plus you're providing for your retirement and having tax-deferred growth of your assets.

Wightman: OK... Every taxpayer's nightmare: What happens if you get audited?

Green: By the way, the IRS is auditing traders with more frequency now, and the IRS is auditing all taxpayers with a new vengeance. The environment has changed quite a bit with the budget deficit. The IRS has a renewed lease on life to examine a lot of taxpayers. There are new IRS audit programs recently passed by Congress.

If you're a part-time trader and a money losing trader, and you have mark-to-market accounting and you're getting *huge* refund checks from the IRS, they're going to be prejudiced to disallow your Trader Tax Status. And, as pointed out before, there are no specific rules, so your "trader tax status" is really defined by case law and they're going to look to a whole series of cases. We've analyzed all those cases in our Trader Tax Status and Mark-to-Market Accounting Guide, a whole new case law section brand new for this year and we show you how to fight and beat the IRS at their own game.

"Five out of ten times, the IRS agent (at first) just didn't even know the law..."

So what the IRS will want to do is attack your Trader Tax Status, because if they can disallow *that*, then you won't get business loss treatment and you can't use mark to market accounting. So that's where the exam will be focused. And if you have less than 1,000 round turn trades, you may want to consult with an expert. We stand by all our clients to the very end. We represent them before the IRS and we handle all these matters for them. Five out of ten times, the IRS just didn't even know the law when the exam started. By the way, if you file a tax return correctly, and use the strategies that we advocate, and use the footnotes that we provide you with in our guide, you really reduce the chance of examination because you've *answered* many of the questions. You nip the bud before it grows into a problem. So that's what happens with the IRS.

Wightman: I guess we should point out that taxes are right around the corner, just next week and that it's not too late if you have questions or you want to change something, you can always file an

extension. If I've got my number right, that's Form 4868, correct?

Green: Yes. We have an entire extension section on our website. You can reach it on the home page -- automatic extension Form 4868 and we also have the state resources and a list of all states that accept the Federal form. The key at this point is that all our clients at this point are filing extensions. We advocate that most clients file extensions *every* year, because the IRS picks out the returns to audit just *before* the 15th. If you file during the summer months, we think you have a much lower chance of being audited. The key point is that an extension is only valid if you pay 90% of your taxes with the extension. You need to do a good estimate of what you owe and to pay at least 90% of it. Pay 100%, pay 110% to be safe. If you're making money this year, instead of paying Q1 2003 estimated tax, you can apply the overpayment from your 2002 return to 2003. So overpay with the extension to be safe. Then you won't be subject to interest or penalties, but don't forget to attach the MTM election.

"If you file during the summer months, we think you have a much lower chance of being audited...."

Now, if you don't know what you owe and you have no idea and can't even pay what you owe, file an extension anyway and attach that MTM election. The extension won't be valid, but the MTM will be valid. And also you can appeal to the IRS that you used good faith and paid as much as you could and probably get the penalties abated.

Wightman: Let's just go over some contact information in case some of our members want to reach you. Your website is <http://www.greencompany.com>, correct?

Green: Yes, that, or <http://www.greentradertax.com> which most people know it as. Our phone number is (203) 938-4716 and we offer consultations. If you'd like to discuss any of these things, you need to sign up for a 15- or a 30-minute consultation and that will be with me personally. We are scheduling appointments through April 15.

Wightman: Terrific. Mr. Green, I really appreciate your time; this has been a really informative talk.

Green: Thank you very much.

All analyst commentary provided on TradingMarkets.com is provided

for educational purposes only. The analysts and employees or affiliates of TradingMarkets.com may hold positions in the stocks or industries discussed here. This information is NOT a recommendation or solicitation to buy or sell any securities. Your use of this and all information contained on TradingMarkets.com is governed by the [Terms and Conditions of Use](#). Please click the link to view those terms. Follow this link to read our [Editorial Policy](#).

PREMIER SPONSORED LINKS

- [Trade the most liquid market in the world -- Click here for Risk Free Trial!](#)
- [Why Do Good Stock Traders Make Great Currency Traders? Find Out.](#)
- [JP Futures/ Astor Managed Account](#)

© 2003 TradingMarkets.com Inc.