

5 Reasons Why You Should NOT Get A Big Tax Refund

By Wayne M. Davies

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Wayne M. Davies
Wayne@YouSaveOnTaxes.com

YouSaveOnTaxes.com <http://www.YouSaveOnTaxes.com/toolkit.html>

I will never forget the day one of my tax clients came to pick up his personal income tax return.

"How's it look?" he asked.

"Well," I said, "You're getting a refund."

"Great! How much?"

"Oh, it's a big one," I said. "Over \$5,000 dollars."

Mr. Taxpayer couldn't have been happier. He face lit up like a light bulb. He was ecstatic -- he sincerely believed that he had "beat the tax man" by getting such a large refund.

I was not so happy. I couldn't understand his thinking. So I asked him if he really meant to get such a big refund. Mr. Taxpayer was a W-2 employee and so I wondered if his payroll department made a mistake -- were they doing his withholdings wrong? Did he really want to have so much tax taken out of his paycheck each week?

Mr. Taxpayer went on to tell me that he has a tremendous fear of having a balance due on his return. For some reason, he just assumed that if he ended up owing money to the government at the end of the year, somehow he would get in trouble with the IRS. So he went to the opposite extreme.

In addition, he thought that getting a big refund was a great way to save money during the year, so that at the end of the year he got a nice little "bonus" from the government. You know, a forced savings plan.

I can think of at least 5 reasons why Mr. Taxpayer's

thinking is flawed.

REASON #1: When you get a big refund, you are loaning your money to the government.

My biggest objection to getting a large refund is the simple fact that you have given the IRS an interest-free loan of your hard-earned money.

Mr. Taxpayer's \$5,000 could have been earning interest over the course of the year. So by letting the government keep his money, he was actually losing money!

Sure, with rates so low, maybe we're not talking about a lot of interest income here, but why give the government your money any sooner than necessary?

REASON #2: Getting a big refund does not mean you are paying less tax.

I know how complicated are tax system is. It's crazy, convoluted, chaotic and inconsistent. I deal with our tax laws every day, and there's stuff in there that will drive any sane person over the edge.

But on this point, there really is a lot of misunderstanding on the part of innocent (but misinformed) taxpayers:

Getting a large refund does not mean that you somehow paid less tax than if you got no refund.

I'm serious here -- there are taxpayers out there who think that getting a refund means that you somehow "beat the system." This is nonsense. Think about it -- all you did was get your own money back! It was your money all along, all you did was postpone getting it.

REASON #3: Having a balance due does not increase the chance of audit.

If you have a balance due, you do NOT end up on some IRS "hit list." But for some reason there are many taxpayers who have this unfounded fear of owing money to the government. This fear causes people to unnecessarily go to the opposite extreme -- "I've got to make sure I never owe, so I'll just have way too much withheld to be safe."

Safe from what? This fear of an audit is pure hogwash.

REASON #4: Getting a large refund is usually a sign of poor (or non-existent) tax planning.

Many folks do not realize how easy it is to get out of the "big refund rut".

You have control over how much you pay in to the IRS during the year. If you or your spouse are W-2 employees, you can change your withholdings very easily. Just file a new Form W-4 with your employer and you won't have to wait so long to get your money back.

If you are self-employed and making quarterly estimated tax payments, the same principle applies. With a little number-crunching you can determine the minimum amount of estimated tax payments you are required to make.

Whether you are self-employed or work for someone else, if you're not sure how to do these calculations, get help from your local tax professional.

REASON #5: Getting a large refund is usually a sign of poor (or non-existent) financial planning.

My client insisted that he needed a large refund so he could have a nice nest egg to look forward to every Spring. He was using the government as his short-term savings plan.

I told Mr. Taxpayer this:

"If you want to save \$5,000 dollars over the course of the year, just authorize your employer to deposit \$100 per week into your savings account. Then at the end of the year, your \$5,000 will be sitting in your own bank account instead of at the U.S. Treasury.

And you won't be in such a frantic frenzy to get your tax return filed."

So I urge you to reconsider such an approach to money-management. Why let the government have your money? Don't wait until the end of the year to get your money back. With a little planning and self-discipline, you can take control of this part of your life.

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