

Tax Planning: It's Not Just for the Super Wealthy

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It's no secret that some of the wealthiest people in the United States pay the least income tax. According to some reports, billionaires can even get their income tax down to zero, and it's entirely legal.

In some instances, they build their wealth through ownership of shares in one or more companies and then borrow against that wealth to cover their expenses. And because they don't realize any gains from selling shares, they're not earning income subject to tax. In fact, they can even claim the interest they pay on their loans as a deduction against any income they earn!



Here at SWC, that's what we call savvy tax planning. Don't you wish you could do that?

Well, you may not be wealthy enough or low-income enough to pay zero income tax, but if you're somewhere in between, strategies are available for reducing your tax bill and building your wealth at an accelerated rate. Tax-saving strategies include maximizing tax deductions and credits and contributing to tax-deferred retirement accounts. And you don't have to be super-rich to take advantage of them. You just need to engage in tax planning.

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What Is Tax Planning?

Tax planning is the process of analyzing your financial situation to minimize tax liabilities. It involves careful consideration of income, expenses, investments, deductions, credits, and future opportunities to take advantage of all available tax laws and regulations.

Suffice it to say, tax planning plays a crucial role in building wealth. By investing some or all of the money you save on taxes, you can provide yourself with additional tax-savings options while your investments grow in value.

Understanding Tax Planning: Tax planning is the exercise of reviewing the amount of tax you pay in an effort to maximize your after-tax income. To do this properly, it is important to understand myriad federal and state rules and regulations related to deductions, credits, income deferral, and tax minimization strategies where possible.

When you engage with a tax planning firm like SWC, the process is designed to help you or your business pay the least amount of tax legally possible, based on current tax law and regulations as they relate to your current and future financial goals and objectives. Legal tax strategies encompass leveraging retirement planning, estate planning, investment income, investment vehicles, and the optimization of your business operations if you own a business or work in an entrepreneurial capacity.



Here are some of the ways tax planning can help you build wealth:

- **Identify deductions and credits for which you qualify.** Deductions and credits enable you to reduce your taxable income, so you keep more of the money you earn.
- **Build wealth faster with tax-deferred investments.** Using tax-deferred accounts such as individual retirement accounts (IRAs) and 401(k)s, your investments grow tax-free until you withdraw them.
- **Allocate assets thoughtfully.** Tax planning can help you decide which investments are better to hold in a taxable account as opposed to a tax-deferred account. For example, holding bonds in tax-advantaged accounts while keeping stocks in taxable accounts can help to reduce your taxes.
- **Take advantage of tax-loss harvesting.** This strategy involves selling investments at a loss to offset gains, reducing your overall tax liability while preserving capital for reinvestment.
- **Minimize estate taxes.** Effective tax planning can help to ensure that a greater portion of your wealth is passed on to your heirs instead of the government. ([Learn about our *estate and tax trust planning services for all stages of life.*](#))

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- **Make your retirement savings last longer.** Planning contributions to and withdrawals from retirement accounts can help you take advantage of lower tax brackets.
- **Adapt to changes in tax laws.** Experts in tax planning closely monitor tax laws to help their clients adjust their plans to minimize their tax obligations. Tax planning is usually an ongoing process, not a one-time event.

Why Tax Planning Matters Regardless of How Wealthy You Are

You don't need to be wealthy to benefit financially from tax planning. In fact, if you aren't what you would consider wealthy, you should be even more committed to learning about and participating in tax planning. That's because you cannot afford to be handing more of your hard-earned money over to state and federal governments than you're obligated to pay.

Besides, all that money you stand to save on taxes can be put toward more precious things, such as your financial security and peace of mind, your children's and grandchildren's education, your retirement, your home, helping loved ones in need, contributing to your favorite causes, and building wealth to pass down to your heirs – not to mention enjoying your own rich and fulfilling life.

Using Deductions and Credits Reduce Your Income Tax

Baked into the Internal Revenue Code of 1986 (IRC) are two means for reducing the amount of income tax you pay – deductions and credits:

- *Deductions* lower your adjusted gross income (AGI), which is the amount of your income that is subject to tax. Reducing your AGI can help you save taxes in two ways:
 - It can place you in a lower income tax bracket, so you pay a smaller percentage of tax on your income.
 - It reduces the amount of income subject to tax.
- A *tax credit* is a dollar-for-dollar reduction of the tax you owe based on your AGI. After calculating the tax liability on your AGI, any credits you qualify for are subtracted directly from the tax you owe.



Tax planning involves using both deductions and credits to lower your tax bill.

With deductions, you have two options – claiming the standard deduction or itemizing. Most people take the standard deduction, which in 2024 is \$27,700 for married couples filing jointly, \$20,800 if you file as Head of Household, and \$13,850 if you file as Single or Married Filing Separately. However, you may qualify for a larger deduction by itemizing, assuming your total itemized deductions exceed your standard deduction. If you itemize, you can deduct expenses such as the following:

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- Mortgage interest you pay on up to two homes
- Student loan interest
- Your state and local income or sales taxes
- Property taxes
- Medical and dental expenses that exceed 7.5 percent of your AGI
- Charitable donations

Regardless of whether you itemize or claim the standard deduction, you can also reduce your AGI by contributing to tax-deferred retirement accounts, such as an individual retirement account (IRA) or a 401(k). “Tax deferred” means the money isn’t taxed now but later when you withdraw it from the account.

Contributing to a health savings account (HSA) can also reduce your AGI, but you can contribute to an HSA only if you have a high-deductible health insurance policy. The money you place in your HSA isn’t subject to tax, assuming you spend it on qualifying medical expenses.

Tax credits are like government subsidies to help cover certain expenses. One of the most substantial tax credits is the child tax credit, which is up to \$2,000 per qualifying child. Other tax credits include the Earned Income Tax Credit, tax credits for education expenses (such as the American Opportunity Credit and Lifetime Learning Credit), the Electric Vehicle Tax Credit, and the Energy Efficient Home Improvement Credit.

Tax Planning Strategies for Different Financial Situations

Tax planning is not a one-size-fits-all solution. Every taxpayer’s situation is unique. However, we can offer some general guidance based on overall income bracket to illustrate some general strategies:

- **Low- to Middle-Income Households**
 - Consider claiming the standard deduction. Most low- to middle-income households don’t pay enough in mortgage interest, property taxes, medical expenses, and other categories to benefit from itemizing.
 - Claim all qualifying child tax credits.
 - Claim the Earned Income Tax Credit (if you qualify).
 - Contribute as much as possible to tax-deferred retirement accounts.
- **Middle- to Upper-Middle Income Earners**
 - Itemize deductions (only if your qualifying expenses exceed the standard deduction).
 - Claim all qualifying child tax credits, education credits, and other qualifying credits.
 - Employ tax-loss harvesting and optimize capital gains.



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- Contribute as much as possible to tax-deferred retirement accounts.
- Contribute to 529 college savings plans.
- **Business Owners and Freelancers**
 - Deduct all business expenses, so you're paying taxes only on your net business income (your business's net profit).
 - Claim the home office deduction, assuming your business qualifies for it.
 - Claim the qualified business income (QBI) deduction.
 - Explore strategies to reduce your self-employment tax, such as forming a corporation. You can then receive compensation from the corporation as a combination of salary, which is subject to self-employment tax, and distributions, which are not.

Adjusting Your Tax Plan in Response to Major Life Events

Major life events such as getting married or divorced, having children or enrolling them in college, buying or selling a home, and starting or selling a business, can all have a big impact on your financial situation and your taxes. Whenever you experience a major life event, schedule a meeting with your financial planner or advisor to adjust your tax plan.

Be sure to schedule your meeting as soon as possible after the life event or even in anticipation of it – the sooner the better. Failing to adjust your tax plan accordingly could result in paying more tax than necessary – money that's rightfully yours.

Pro Tip: If you're facing divorce, read [Divorce and Social Security: What You Need to Know](#), on the SWC Blog.



Getting Started with Tax Planning

Regardless of your situation, tax planning is a key component of minimizing your tax bill and building wealth. How you get started is up to you. You can do it yourself, use tax software, or consult a certified public accountant (CPA) or other qualified financial professional, or – as we recommend – engage with a [tax planning firm](#) like SWC, where our mission is to increase our clients' net worth.

We strongly suggest – even for die-hard do-it-yourselfers – that you hire a professional for your first tax-planning session. This approach ensures that you have a competent and comprehensive tax plan in place for your current situation that you can then modify as your situation changes. In the process, you get a glimpse of what a good financial advisor brings to the table. You can then decide whether you want to establish a long-term relationship or proceed on your own.

Your choice depends mostly on your situation, how financially savvy you are, and the amount of time and effort you want to invest in learning and keeping current with the ever-evolving tax code. If your finances are fairly simple – you have only W-2 income, few deductions, and no complex investments – you may be fine managing

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your tax plan yourself or with the help of tax software. However, if your life and finances are more complicated, working with a professional may be the wiser and most cost-efficient approach.

Tax Planning as an Ongoing Process

Start with simple strategies, such as maximizing your contributions to tax-deferred retirement accounts and then build out your plan by adding more sophisticated strategies. Review whenever you experience a major life change (or in anticipation of such a change) and revise your plan, if necessary.

Remember: Tax planning is for everyone; it is not exclusively for the ultra-rich. Start thinking about your tax situation now and start looking for ways to reduce your tax bill. Use the money you save on taxes to build wealth and create additional tax-saving opportunities. Do it right, be persistent, and you may end up joining the ranks of the ultra-rich!

If you live, work, or do business in California, we can help. SWC is Southern California's independently owned tax planning and financial strategies advisory firm for entrepreneurs and small business owners, real estate investors, and high-net-worth individuals. Helping our clients minimize their taxes and build and leverage their wealth to enhance their personal and financial freedom is what we do.

[Contact us](#) to schedule a consultation.



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