



## Individual Tax Planning, 2023

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Tax planning is a vital tool for managing your financial landscape. It's not just about reducing your tax liability for the current year but also about planning for future years. Understanding the nuances, such as the timing of income and deductions, can lead to significant tax savings.

### **What is Tax Planning?**

Tax planning is the process of reviewing various options for conducting business and personal transactions with the aim of reducing tax liability. It involves making decisions on the timing and method of completing transactions as well as the reporting of income, deductions, and credits.

The primary goal is to minimize income taxes as much as legally possible. Tax planning is considered an integral part of financial planning, and it often requires the advice of professionals like attorneys or [certified accountants](#).

### **What is it and why should I care?**

Tax planning is essential because it can result in substantial tax savings. The opportunity for tax planning generally ends on December 31 for those who compute federal income tax on a calendar-year basis. Effective tax planning involves timing income and deductible expenses to be taxed at lower rates or claimed in years when you are in a higher tax bracket.

### **How Can Taxes Affect Me?**

Taxes can affect you primarily through the timing of your income and deductions. The goal is to time these so that income is taxed at a lower rate and deductions are claimed when you're in a higher tax bracket. Effective tax planning can result in substantial tax savings.

### **What is the 3.8% surtax and who has to pay it?**

The 3.8% surtax applies to net investment income for individuals with modified AGI exceeding \$250,000 for joint filers, \$200,000 for single filers, and \$125,000 for married taxpayers filing separately.

### **What is the Alternative Minimum Tax (AMT)?**

The Alternative Minimum Tax (AMT) is a separate method of determining tax liability designed to ensure that high-income taxpayers do not completely avoid federal income tax through deductions, exemptions, and credits. All individuals, estates, and trusts subject to regular income tax are also subject to the AMT.

### **Tax Brackets**

Tax brackets play a crucial role in determining how much you owe in taxes each year. Understanding how they work can offer valuable insights for effective tax planning, allowing you to make informed decisions about your income and deductions.

### **How do tax brackets work?**

Tax brackets are ranges of income that are taxed at different rates. There are seven tax brackets for individuals: 10%, 12%, 22%, 24%, 32%, 35%, and 37%. The income level at which these rates apply depends on your filing status (Page 2).

### **How can timing affect my taxes?**

Timing is crucial when getting [tax services San Bernardino](#). The basic strategy is to time income so that it will be taxed at a lower rate and to time deductible expenses so they may be claimed in years when you are in a higher tax bracket.

### **Married or Single: Does it Matter?**

Your marital status affects the income levels at which tax brackets apply. Generally, it is more beneficial for married individuals to file jointly, as tax rates are sometimes higher when income is separately taxed. However, in some instances, filing separately may reduce overall tax liability.

### **What happens if my income changes significantly?**

If your income changes significantly, various tax planning opportunities may arise. For example, if you anticipate being in a higher tax bracket next year due to events like marriage, divorce, or changes in employment, you may want to accelerate income into the current year. This can help you spread your income more evenly across multiple years, potentially reducing your overall tax burden.

### **What Counts as Income?**

Income can come from a variety of sources and is generally subject to taxation. According to the PDF, types of income include but are not limited to:

- Income or profits from a business

- Gains from dealings in property like real estate and securities
- Interest income from bank accounts, CDs, and loans
- Rents collected from real or personal property
- Dividends and royalties
- Annuities, pensions, distributions from retirement plans, and Social Security benefits
- Income from the discharge of a debt
- Income from an interest in an estate or trust
- Prizes and awards

It's important to note that some types of income are specifically excluded from gross income, such as gain from the sale of a principal residence or interest on certain state and municipal bonds.

### **How Can I Plan My Taxes?**

Planning your taxes involves several key strategies that focus on the timing and method of reporting income, deductions, and credits. The primary goal is to minimize your income taxes as much as legally possible. Here are some detailed points on how you can plan your taxes:

#### **Timing is Everything**

The basic strategy for tax planning is to time your income so that it will be taxed at a lower rate and to time deductible expenses so that they can be claimed in years when you are in a higher tax bracket.

If you expect to be in a lower tax bracket next year, you should defer receiving income to the next year and accelerate deductions into the current year. Conversely, if you expect to be in a higher tax bracket next year, you should accelerate income into the current year and defer deductions until the next year.

#### **Cash vs. Accrual Method**

Most individuals use the cash method of accounting, where income is reported when actually or constructively received, and expenses are claimed when paid.

This method offers flexibility in timing income and expenses. For example, if you're self-employed, you can accelerate income by ensuring all billing is done so you can collect the income before the end of the year.

#### **Maximizing Deductions**

It's crucial to make sure you meet the requirements to claim deductions for certain expenses paid during the year. Planning your expenses can help determine whether some of

them can be shifted from one year to another to maximize their effect in calculating tax liability.

### **Investment Income**

If you have investment income, you'll also need to plan for the possibility of being subject to the 3.8% net investment income tax. This could include spreading out investment income over several years.

### **Retirement Contributions**

Making maximum allowable contributions to retirement plans can also help in deferring income and reducing current tax liability.

By understanding these strategies and applying them judiciously, you can optimize your tax situation and potentially save a significant amount of money.

### **Conclusion**

Effective tax planning is not just a one-time activity but a continuous process that can yield significant financial benefits. The strategy revolves around the timing of income and deductions, the choice of accounting method, and maximizing allowable deductions.

Being proactive in your tax planning can open the door to various opportunities, such as retirement contributions and investment strategies, that can further reduce your tax liability. It's a complex but rewarding endeavor, often requiring the advice of professionals like attorneys or [CPA accounting firm](#) for optimal results.

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