

STRATEGIC TAX INSIGHTS

FOR HIGH-NET-WORTH INDIVIDUALS

High-net-worth individuals (HNWIs) often face a complex financial landscape characterized by diverse investments and sophisticated financial concerns. They require comprehensive financial planning to preserve and manage their wealth.

Strategic tax planning is also integral to HNWI's wealth management because it allows them to manage their tax liability as they work toward their financial goals. While every individual's situation is unique, the following are some essential strategic tax insights for HNWIs.

What HNWIs need to know about gifting and taxes

Gift and estate taxes apply to money transfers, property, and other assets. Simply put, these taxes only apply to large gifts made by a person while they are alive or significant amounts left for heirs when they die. There are some nuances that HNWIs must understand when gifting.

ANNUAL GIFT TAX EXCLUSION

The annual gift tax exclusion limit for 2024 is \$18,000. For married couples, the combined limit is \$36,000. HNWIs can donate and deduct up to these limits on their income tax.

Lifetime gift tax exemption

The lifetime gift tax exemption, a critical aspect of estate planning and wealth management, is an IRS tax provision that allows HNWIs to give away a certain amount of their assets during their lifetime without incurring federal gift taxes. This exemption is critical in minimizing tax liability while living and maximizing wealth transfer to heirs at death. Gifts can include cash, real estate, securities, and other property. Most gifts are tax-free for both the donor and the recipient.

An individual's lifetime gift tax exemption is \$13.61 million in 2024 and \$13.99 million for tax year 2025. For a married couple, the exemption doubles. However, any gifts above the yearly exclusions will be subject to the IRS gift tax.

TCJA: EXPIRING IN 2025

The Tax Cuts and Jobs Act (TCJA), signed into law in 2017, overhauled the U.S. tax code with sweeping cuts and changes. However, TCJA expires on December 31st, 2025.

Estate and gift tax provisions- Changes to estate and gift tax provisions doubled under the TCJA but will revert to pre-TCJA levels after 2025. While it is unknown if the tax code will be rewritten for 2026 forward, if not done so, the exemption would revert to around \$3 million per individual.

If the provisions expire, the new tax code will undoubtedly impact gift and estate planning strategies for HNWI's.



1. INCOME SPLITTING

Income splitting is an effective tax strategy often used by HNWI's. This concept is straightforward: It involves shifting income from a higher-income family member to a lower-income one to manage the family tax burden. Various methods allow for objective income splitting. These include utilizing spousal loans for investment purposes, hiring family members in your business, or making retirement savings plan contributions. Because income splitting impacts taxes, consulting a tax professional is vital to understanding this strategy.

2. CHARITABLE GIVING

Charitable giving offers a double benefit for HNWI's. Besides helping causes and organizations they support, charitable giving also provides tax advantages. Contributions made to registered non-profit charities can result in substantial tax credits. Furthermore, donating appreciated securities can also eliminate or reduce capital gain taxes. Since the rules around charitable giving are complex and can change, seeking professional advice is essential.

3. USE OF TRUSTS

Trusts are an estate planning tool that may offer HNWI's considerable tax advantages. Trusts can help split and distribute income, preserve wealth, provide for heirs, or even manage a philanthropic legacy. There are different types of trusts, each with rules and tax implications. Therefore, creating and managing trusts requires professional financial, legal, and tax guidance.

4. TAX-LOSS HARVESTING

Tax loss harvesting involves selling investments that have experienced a loss to offset the capital gains realized on other assets. This strategy can effectively help manage HNWI's tax liability. It can be applied in many situations, including when rebalancing a portfolio and trying to stay in a lower tax bracket.

5. TAX-EFFICIENT INVESTMENTS

Investing in tax-efficient investments may be an appropriate tax strategy for HNWI's. These strategies aim to limit the amount of taxable income distributed to investors. They may invest in stocks that pay little or no dividends, focusing instead on long-term capital appreciation. Furthermore, buying and holding tax-efficient investments may help HNWI's avoid realizing capital gains in years of higher income.

6. BACKDOOR ROTH IRA STRATEGY

The backdoor Roth IRA is a strategy to convert IRA funds into a Roth IRA. However, taxes will be due on the amount transferred to a Roth IRA in the tax year the strategy occurred. Since HNWI's cannot contribute to a Roth IRA due to their high income and IRS rules, this strategy enables them to take tax-free distributions in the future. The backdoor Roth IRA strategy helps HNWI's manage their tax situation as their wealth increases, thereby lowering their overall tax liability later.

Additionally, if the HNWI participates in a 401(k) plan and the plan allows, the 401(k) funds can be transferred to an IRA and later to a Roth IRA to execute this strategy.

The backdoor Roth IRA strategy requires careful planning and understanding of tax rules, but it can offer substantial tax savings for those who can utilize it. Before implementing this strategy, it is vital to meet with financial and tax professionals to understand how it will impact one's tax situation.

While these strategic tax insights can possibly provide a foundation for tax optimization, it's essential to remember that tax planning should be more than a standalone solution. Instead, it should intertwine with wealth management and overall financial planning. Since tax laws frequently change, it's crucial to stay informed of these changes and make modifications as needed.

From understating gifting and taxes to income splitting, charitable giving, trusts, tax-loss harvesting, tax-efficient investing, and the Backdoor Roth IRA strategy, HNWIs can manage their tax situation in numerous ways. However, due to tax laws' complexity and continuously evolving nature, professional guidance is crucial to developing a comprehensive, practical, and compliant tax strategy.



In closing, HNWIs must seek advice from financial and tax professionals specializing in HNWI taxation. These professionals can provide guidance on mitigating tax liabilities and strategies that align with one's wealth planning goals.

With the end of the year approaching, it's time to take action; implementing strategic tax strategies now can help preserve and manage wealth while minimizing overall tax liabilities.

Important Disclosures:

Content in this material is for educational and general information only and not intended to provide specific advice or recommendations for any individual.

Traditional IRA account owners have considerations to make before performing a Roth IRA conversion. These primarily include income tax consequences on the converted amount in the year of conversion, withdrawal limitations from a Roth IRA, and income limitations for future contributions to a Roth IRA. In addition, if you are required to take a required minimum distribution (RMD) in the year you convert, you must do so before converting to a Roth IRA.

This information is not intended to be a substitute for specific individualized tax or legal advice. We suggest that you discuss your specific situation with a qualified tax or legal advisor.

The tax-loss harvesting and other tax strategies discussed should not be interpreted as tax advice and there is no representation that such strategies will result in any particular tax consequence. Clients should consult with their personal tax advisors regarding the tax consequences of investing.

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This article was prepared by Fresh Finance. LPL Tracking #666175

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