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Optimize and Maximize: Tax Planning for Major Life Events

By: Holly Swan | March 6, 2024

Life is full of significant moments that bring joy, change, and new responsibilities. You can bring value to your clients during these times by helping them navigate the income tax planning opportunities that accompany them.

Here are four major life events where you can help clients optimize financial outcomes with some advanced planning:

Marriage

When two individuals tie the knot, their tax situation often changes. Here are some key considerations:

- **Filing status:** Married couples have the option to file jointly or married filing separately. Filing jointly can often result in lower tax rates and increased deductions, but it's essential to evaluate both options to determine the most advantageous approach.
- **Spousal deductions:** Encourage clients to take advantage of the deductions that are available to married couples, such as combining medical expenses or maximizing mortgage interest deductions.
- **Tax credits:** Review available tax credits, such as the earned income tax credit (EITC) or the child and dependent care credit, to see if they qualify for increased benefits as a married couple. Note that the EITC is for low to moderate income levels and varies depending on the number of children and investment assets.

Birth of a Child

It's one of the more joyous life events. The birth of a child also brings significant change and new tax planning opportunities:

- **Child tax credit:** This credit can provide a significant tax benefit for eligible parents.
- **Dependent exemptions:** Clients should claim their children as dependents to benefit from exemptions and deductions related to dependent care.
- **Education savings:** Explore options like 529 plans or Coverdell Education Savings Accounts (ESAs) to help clients save for their child's future education costs while enjoying certain tax advantages.

Retirement

Advanced planning for clients nearing retirement is critical for optimizing tax outcomes. Here are three strategies for clients to consider:

- **Tax-efficient withdrawals:** Strategize retirement account withdrawals to minimize tax liabilities. Consider factors such as tax brackets, required minimum distributions (RMDs) and social security benefits.
- **Health savings accounts (HSAs):** If your clients aren't enrolled in Medicare, they may be able to contribute to an HSA. It offers triple tax advantages: tax-free contributions, growth, and withdrawals for qualified medical expenses.
- **Roth conversions:** Evaluate the benefits of converting traditional retirement accounts to Roth IRAs to potentially reduce future tax burdens. This may be a good option for clients who are in a lower tax bracket and don't need to access the funds for an extended period.

Divorce

Divorce brings significant change to your clients' personal and financial lives. Here are the tax implications to consider during and after

divorce:

- **Filing status:** If clients are legally separated or divorced on the last day of the year they are required to file as single unless they qualify for head of household status.
- **Property division:** Carefully consider the tax implications of dividing assets during divorce. Seek professional advice to ensure a fair and tax-efficient distribution.

Bottom Line: Major life events are key moments where advisors can help clients make better planning decisions that optimize their tax situations and enhance their financial well-being.

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