Decreasing Your Taxes as a Physician

INVESTING MORE.

Written by Stephan McKee

Physicians have a unique set of circumstances. They start work later in life, typically have large amounts of debt, and worst of all are taxed a considerable amount. The question is how can you mitigate those taxes to keep more of your hard-earned money in your pocket?

Deducations Based on Itemization

If you are a self-employed physician, you have the option to itemize your business expenses and use those to create tax deductions. You can claim many of the following items: office equipment, medical equipment, the cost of renting a clinic, licensing and renewal fees, CME, staff wages, employee benefits, malpractice insurance premiums, and several more.

An accounting firm can help you list and claim these deductions.

Deducations Based on Contributions

Contribution to various accounts provide deductions against your taxable income. This allows you to reduce your total tax burden. Depending on the amount of deductions, your adjusted gross income (AGI) may be minimized enough to lower your marginal tax bracket.

These contributions include the following:

1. Interest paid on home mortgage debt
   - up to $750,000 married filing jointly
2. Interest paid on home equity line of credit (HELOC)
   - $750,000 married filing joint, if used to “buy, build or substantially improve the taxpayer’s home”
3. Interest on student loan payments
   - up to $2,500 per year
4. 529 college savings plan contributions
   - limit of $17,000 if single, $34,000 married filing joint, per recipient, per year
5. Health insurance premiums
   - paid for yourself, spouse, or dependents
6. Self-employment tax
   - up to 50%
7. Charitable donations
   - up to 60% of a physician’s adjusted gross income
8. Contributions to pre-tax retirement savings plans
   - 401(k)s, 403(b)s, 457 plans, IRA

Deductions Based on Income Received

Qualified Business Income Deduction (QBID): If a self-employed physician owns an LLC, partnership, S-Corps, or sole proprietorship (“pass-through” business) —it is possible to utilize a qualified business income deduction of up to 20% of business income and a deduction for qualified rental property. These are complex and require a CPA or tax attorney to utilize.

Deductions Based on Investments

Alternative Investments
Private equity investments not correlated with the stock market. They can range from real estate, natural gas, oil, wildlife, and numerous other options. Using various IRS codes, such as accelerated depreciation, intangible drilling costs, depletions, and other options, they can provide above and below the line deductions against W2, 1099, or passive income.

Qualified Opportunity Zones
After the sale of an asset, a physician can invest their realized capital gains into a QOZ. These offer permanent exclusion of taxable income on new gains, the realized capital gains are deferred until December 31st, 2026, and upon the sale of the QOZ, the investor’s realized gains are tax free.

Delaware Statutory Trusts (DSTs)
Allows investors to defer taxes on realized gains from the sale of an investment property by 1031 exchanges. Taxes will be deferred until the investor’s ownership in a DST is sold. The investor can utilize another 1031 exchange to continue deferring taxes, allowing their money to continue growing.

Tax-loss harvesting
This is an investment strategy that can lower the capital gains taxes by creating a capital loss. An investor would sell investments at a loss and then buy a similar investment back to maintain a diversified portfolio. Capital losses created by this strategy are limited to $3,000 per year but can be carried forward each year until fully used.

Investment property depreciation
An investor could segregate the cost of an investment property with an accelerated depreciation schedule. This depreciation loss can be subtracted from your taxable income every year which can lower your taxes and possibly place you in a lower tax bracket.

Backdoor Roth IRA

Roth IRA contributions do not decrease the amount you pay in taxes. In fact, you will pay taxes on the money contributed up front, but once that money is inside it can grow tax free, shielding you from any tax on the growth and any distributions taken in retirement. The goal is to tax the seed rather than the harvest. To increase the value of your Roth IRA, it may be beneficial to convert pre-tax accounts like an IRA, 401k, 403b, etc. This will create a single time tax impact, but that money will now grow tax-free. Conversions may be beneficial prior to the Tax Cuts and Jobs Act of 2017 expiring Dec 31st, 2025. Pending any new legislation, the marginal tax bracket percentages will increase 1-3% (37% to 39.6%) and cost physicians much more in taxes.

Deductions Based on Families

Hire Your Children: Self-employed physicians can hire their children under 18. This must be well documented, and the income paid should reflect their age and skills. By hiring them, a physician can shift up to $13,850 (2023 standard deduction) tax-free to the child’s returns and therefore decrease the parent’s taxable income.

Child Tax Credit: If a physician’s modified adjusted gross income is below $200,000 for single parents, or below $400,000 for married filing jointly couples, they can deduct $2,000 per dependent child.

Want to Learn More About Tax-Saving Strategies? Visit 25Financial.com

25 Financial is a team of financial advisors who only work with Physicians and High Net Worth Individuals to provide unique tax mitigation strategies as well as comprehensive financial planning services. To learn more about avoiding costly tax mistakes, reducing your tax burden, and developing your financial future and goals, contact one of our trusted advisors today.

This content is intended to be used and must be used for informational purposes only. It is important to do your own analysis before making any investment or tax strategy based on your own personal circumstances. 25 are not tax professionals. You should consult with your tax professional before taking actions which affect your tax situation.