Tax-Free Wealth: How to Build Massive Wealth by Permanently Lowering Your Taxes

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The key to remember is that very few people had the chance to influence this leigslation. Everyone has the same chance to take advantage of the windfalls given to the winners. Employees can choose to be independent contractors and receive the 20% small business deduction. Service professionals who were left out of the 20% deduction can now become C corporations and reduce their tax rate to 21%. Investors who received tax benefits from the costs of investing in the stock market can either begin investing in real estate, with its massive tax benefits, or invest through their Roth IRA or Roth 401(k) and avoid tax altogether on the income and gains from their investments.

Part 1: How the Tax Law Can Be Your Best Friend

Chapter 1: Taxes are Stealing Your Money, Your Time, and Your Future

Not so fast. The 10% return from the stock market will get you $10,000 before taxes. You will pay capital gains tax of about 20%, counting both federal and state taxes, leaving you with an after-tax return of $8,000. The 7% return on the real estate investment will get you a before-tax return of $7,000. Due to the magic of depreciation (chapter 7), you won't pay any tax on your $7,000. Still, $7,000 is less than your after tax return of $8,000 in the stock market, so it seems you are still better off in the stock market.

Only, your real estate investment doesn't just give you tax-free cash flow. It actually reduces your taxes on your salary and/or business income, because while there is positive cash flow of $7,000, the depreciation deduction of about $27,000 gives you a tax deduction against your other income of $20,000 ($27,000 less $7,000 to offset real estate income). That $20,000 additional deduction against your other income is worth $6,000 of reduced taxes on your other income in a typical 30% ordinary income tax bracket.

So your real return from your real estate is $7,000 plus an additional $6,000 of tax refund on taxes you normally would have paid on your salary and business income for a total return of $13,000, or %5,000 more than your after-tax return from the stock investment.

Chapter 2: Taxes are Fun, Easy, and Understandable

Tax Strategy #2 - Invest Where you Travel

Any travel can be deductible by making it a business or investment expense. As long as your travel has its primary purpose as business, then all of the travel expenses, including hotel, airfare, and meals, will be deductible. In order for travel's primary purpose to be business, the IRS says that you have to spend more time doing business than you do in recreation.

Chapter 4: Put Money Back In Your Pocket - Nowa

Tax returns can be a royal pain. And most people just want to get them done and over with as quickly as possible. But what if you could get a 20 to 30 percent discount on all of your purchases any time of the year? That's exactly what happens when you change your expenses from a personal expense to a business deduction. The government essentially pays for 20 to 30 percent of your purchase in the form of a tax deduction.

Chapter 5: Entrepreneurs and Investors Get All the Breaks

Tax Strategy #5 - Put Your Family to Work in Y our Business and Investing

Kids can also earn income from working in the family business or from investments. The nice thing about having your children work for you is that you get a tax deduction at your higher tax bracket for the payroll and they report the income at their lower tax bracket.

My long-time friend and client did this with his 9-year-old daughter. He put her to work doing the bookkeeping for his real estate investments. She is a very intelligent 0-year old and has no problem understanding the bookkeeping. Her mother, who is in charge of their real estate, supervises her. She gets a reasonable wage for her work as compared to other bookkeepers. In a year, she might earn $4,000. That $4,000 will be a deduction to her parents. She doesn't earn any other income and the standard deduction is more than $4,000. So, she doesn't pay any tax. In my client's 40 percent tax bracket, that $4,000 in pay to their daughter means a tax savings of $1,600.

Chapter 6: You Can Deduct Almost Anything

Become an Entrepreneur

Then, be careful with your money. Don't spend money on stupid stuff. Spend it on things that will likely grow your business. Spend it on things that other people in your business might buy. This is called making expenditures that are ordinary in your line of business. Make your expenses count. Make them work for you. When you do that, your expenses become necessary. And when your expenses are necessary, voila, they're deductible.

Become an Active Investor

A great book to read on this topic is the book Robert Kiyosaki and I wrote together, *Why the Rich are Getting Richer*. (Plata Publishing, 2017)

The Passive Investor

In many countries, only certain individuals are allowed to be passive investors. In the United States, these individuals are called "accredited investors." Accredited investors meet certain minimum wealth and earning guidelines set up by the government.

Chapter 7: Depreciation: The King of All Deductions

Chez Pierre

How much Pierre gets to deduct depends on how fast the government will let Pierre depreciate the building. In the United States, for instance, commercial buildings are currently depreciated over 39 years. That means that Pierre would get a deduction each year of $20,000 for 39 years ($780,000 / 39).

Sure, you may have interest expense for the loan or certain out-of-pocket expenses associated with maintenance, but those expenses are also deductible. The actual building cost is a non-cash expense (an expense that doesn't reduce your cash flow) that gives you a deduction. Even better, you not only get a deduction for the money you put into the building but you also get a deduction for the money the bank puts into the building. That's right, you get a depreciation deduction for the entire cost of the building, even if you borrowed all the cash to pay for it from someone else. Now that's what I call magic.

Real Estate Investing and Depreciation

His cash flow from the apartments totas $12,000 a year after paying the bank and all other expenses.

The land is worth $200,000. So the building and its contents are worth $600,000. Let's suppose that $100,000 of the $600,000 is for the contents and $500,000 is for the building. Depreciation in the United States on residential property is about 3.6 percent per year. That means Pierre will get a depreciation deduction for the building of about $18,000 and another $20,000 of depreciation on the contents (20 percent, remember!) each year. That's a total of $38,000.

Since his cash flow from the apartment is only $12,000, when he subtracts the depreciation expense, Pierre ends up with a loss for tax purposes of $26,000. So Pierr's $12,000 of cash flow is entirely tax-free. In addition, Pierre has $26,000 of loss to use against other income. If Pierre is in a 40 percent tax bracket, this $26,000 of loss will create a tax refund for him of over $10,000. Again, Pierre can use that money to reinvest in his business or in real estate.

Usually, I just see land, building, and whatever equipment the client purchased after he or she bought the building. This means that the taxpayer's tax preparer was too lazy or uneducated to break out the component parts of the purchase. (Breaking out the component parts of a building is called a cost segregation or chattel appraisal.) How dumb is this? The client's tax-return preparer has postponed the deduction to a much later year and penalized the client because of laziness. Instead of getting his money back from the government now, the client has to wait for several years. Remember, it's your money. Don't let the government have it any longer than needed.

Chapter 9: Take Advantage of Your Tax Brackets

Tax Strategy #9 - Make Your Parents Your Business Partners and Reap the Tax Benefits

We've discussed several tax strategies for your children. But what if you don't have children, or your children are grown successful, and in a high tax bracket? You can use C corporations like we discussed earlier in this chapter, but another way to make the most of the tax brackets is to involve your parents. Many people have elderly parents who are in a very low tax bracket. Did you know that you can give a part of your business or real estate to your parents and reap major income tax savings? Here's how it works. You give a portion of your limited partnership, S corporation, or LLC to your parents. Any income from their share of the business then flows through to their income tax return and is taxed at their rates.

Chapter 10: Credits: The Cream of the Tax-Saving Crop

Charity Credits

And speaking of credits for giving back, that's what we're discussing next - *charity credits*. Many countries and states or provinces give tax credits to incentivize people to give to schools, to the poor, and to other charities. Often, these credits are in addition to the deduction allowed for charitable donations. There may even be times when you end up with more money in your pocket by giving through the combination of a tax credit and a tax deduction than if you hadn't donated the money in the first place. Now that's an incentive to give.

Tax Strategy #10 - Saving for Your Child's Education with Maximum Tax Benefits

The challenge I have with government-sponsored educational savings plans is that the government is in control of your money, how you use it, when you use it, and how it's taxed. For example, in a 529 plan (also called a Coverdell IRA), the earnings of the plan are tax free when you use it for your child's education. Sounds almost too good to be true, doesn't it? LWhat sort of limitations do you think the government places on these funds in order to control your money? First, they control how much you can contribute. Then, they control what you can do with the money in the plan, even controlling how you invest the money. Next, they control what expenses you can pay for with the fund. Only certain educational expenses qualify. Finally, if you don't use the funds for education, you only have two choices. One choice is to transfer the money to a relative who can use it for their education. The other is to distribute it your yourself and pay taxes and penalties. So, if you make too much money from your investments in the plan, you pay a penalty for not using all of the money for education. What if you could have all of the tax benefits of a 529 plan without giving the government any control over your money? Wouldn't that be a lot better? In tax strategy #5 we talked about paying your children to work in your business. When I teach this principle in my Tax and Asset Protection class, the question always comes up about what to do with the money you pay them. This is the perfect opportunity to have your children pay for their own education without having to rely on Section 529 plans or other tax-deferred, government controlled educational savings plans. Your children can contribute their money to an LLC, limited partnership, or S corporation that owns a business or investments. Like a 529 plan, you get a deduction when you pay your child a salary. Like a 529 plan, there is no tax to the child when received. Like the 529 plan, with good planning, especially in real estate, there is no tax on the cash flow from the investment. But unlike a 529 plan, you have full control over the investment. Unlike a 529 plan, you can take it out and use it for any expense for your child (except for support, like food and clothing),, and you can take it out any time you like. Unlike a 529, there are no penalties for distributing the money or accumulating a huge amount over a lifetime. Now isn't that a much better plan that a government-controlled savings plan? Stop using government plans and make your own plan. You will have much more control and get better tax benefits than the government plans.

Chapter 13: Estate Planning is Good Tax Planning

I'm also talking about having the title of your assets taken care of before you die so that your family doesn't have to go through probate.

Probate is the process of changing an asset's title (i.e., who owns it) from the person who died to that person's heirs. Heirs are simply the people or organizations that get your assets when you die, such as your family or your favorite charity.

Part 2: Your Tax Strategy for Tax-Free Wealth

Chapter 15: Plan to Take Control of Your Taxes: Entities

Tax Tip: Have a business partner? Form your own entity taxed as an S Corporation and have that entity be the partner in your business rather than you personally. This structure will reduce your self-employment taxes and provide maximum flexibility to you and your partner.

Chapter 21: Commodities Can Be Your Tax Friend

This income is subject to a 15% depletion allowance, so only 85% of the income is taxed.

The other two types of investments in oil and gas are both investments in the actual drilling operation - and they provide great tax benefits. You can either invest in exploratory operations, also called "Wildcat" drilling, or you can invest in development operations. Exploratory operations can be very risky, as there is no assurance that there is oil in the ground where you are drilling. Of course, with better and better technology, this risk is always decreasing with the better operators.

Development wells are drilled in established oil fields where the reserves of oil are proven. The developer may need more money to drill additional wells to get more oil out of the ground. This tends to be less risky than the exploratory drilling, though you can still lose your money. I once investment in a development well where the developer had huge absolute proof of huge reserves. The only problem was that we couldn't get to the oil. So, we lost our investment.

These expenses normally would be a cost of the well and would be depreciated or amortized over the life of the well. However, Congress decided to allow people to deduct both their IDC and their equipment costs in the year they spend the money, which is usually the first year of investment in the drilling operation. If you invest $100,000, you get a deduction for $100,000 the first year. At a 40 percent tax rate, that's equivalent of the government immediately giving you $40,000 ($100,000 x 40%) for investing in the oil and gas operation.

This isn't the only tax benefit for investing in oil and gas. You also get to deduct 15 percent of the well's gross income each year. This is called depletion. It's like depreciation, only you get it every year, even after you have deducted all of the IDC and the equipment costs. Basically, it's a gift from the government. Gross income for depletion purposes includes all of the sales proceeds from the oil and gas, and isn't reduced by any expenses. So, you could have $1,000 of gross income, and expenses of $400, for net income of $600. You would then get a depletion deduction of $150 ($1,000 x 15%) and only pay tax on $450 of income ($600 less $150 depletion).

In order to qualify for IDC, equipment and depletion deductions, you have to own a direct interest in the drilling operations. Owning stock in the drilling company or owning a royalty interest in the oil and gas doesn't qualify. Be sure to meet with your tax advisor about this before you invest in oil and gas. And one other thing, in order to get all of the IDC and equipment deductions to which you are entitled, you have to own your investment through a general partnership or sole proprietorship. You can't own it through a corporation, LLC, or limited partnership. If you live outside the United States, be sure to check on your country's tax laws to find out what tax benefits they allow.

Chapter 23: Choose the Right Tax Advisor and Preparer

Yes, he charged less than my Tax-Free Wealth Network(™) firm. We charged about $20,000 to do the tax planning for Jill. But that $20,000 was the best investment Jill has ever made. Her return on investment (ROI) amounts to 350 percent per year.