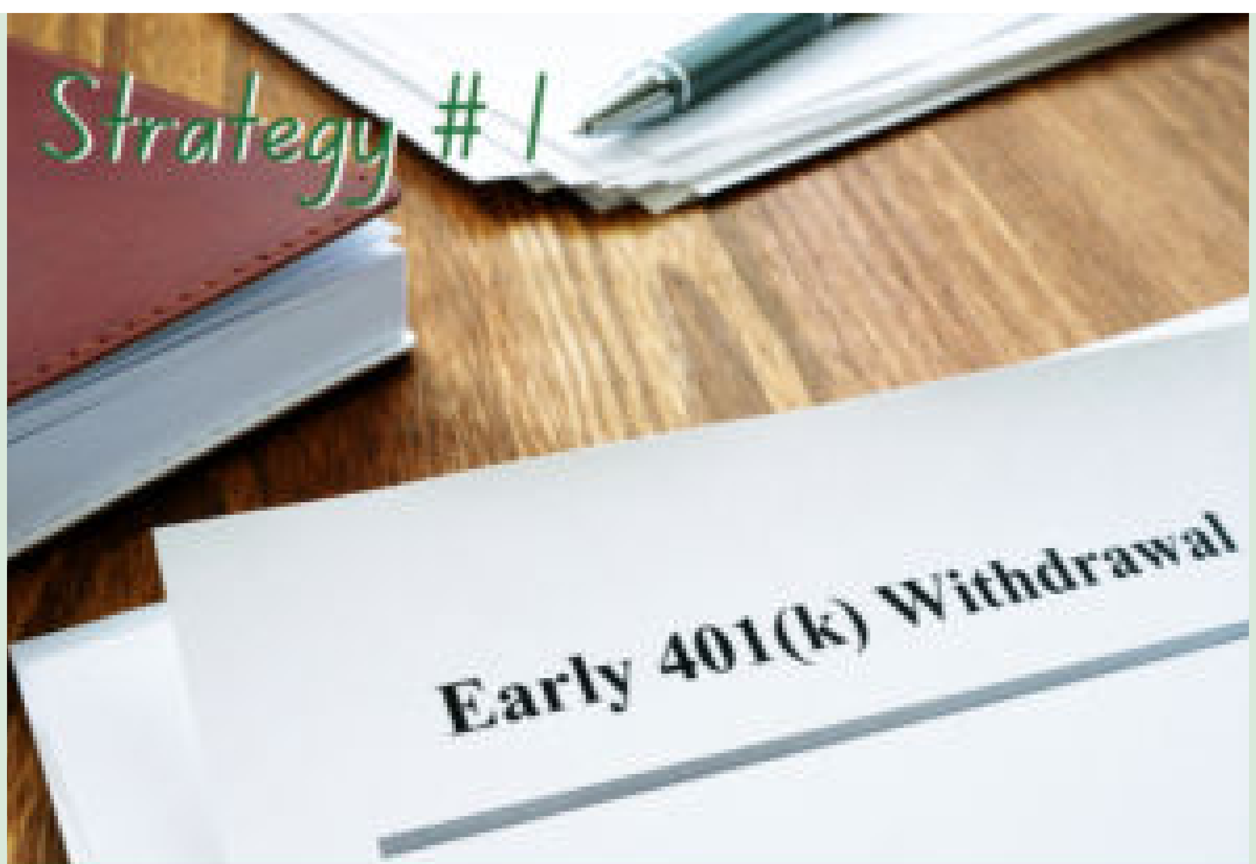
Retirement Savings Strategies

Preparing and Planning to Minimize Taxes in Retirement

While taxes are a fact of life, the amount you pay is NOT. Having a fixed income doesn't mean your taxes will be fixed at the same bracket or amount annually. How do you know if you're paying more than you should?

There are proven ways to minimize your tax liability in retirement, so make sure you're not paying more than you need to.



Make Withdrawals Strategically

In retirement, you often have income coming from many different accounts. Some of those accounts will be tax-deferred accounts, and it may be in your best interest to delay withdrawals from those accounts as long as possible limiting your taxable income each year. So, if you have a non-taxable withdrawal account such as a ROTH IRA and a taxable withdrawal account such as a 401K, you may want to defer making withdrawals from the 401k for as long as possible depending on how taxable withdrawals will affect your tax bracket. You want to avoid moving to a higher tax bracket and having a higher tax bill.

MAX Out Your Tax Bracket

If, at the end of the year, you find you haven't maxed out your current tax bracket consider withdrawing income from tax-deferred accounts to reduce your future taxable income. For example, if you have a large IRA and still have some wiggle room before you max out your current tax bracket, consider withdrawing funds from that IRA in the current year. Yes, you will be taxed on the money you withdraw, but only at your current tax rate. Each year you can reduce the amount of your IRA, the less money you have to pay in taxes in the future.

Strategy #3:

Reduce Expenses

Sometimes paying less in taxes in retirement simply means reducing your current expenses. The less money you have to put out each month is less money you have to withdraw from your retirement accounts. Talk with your accountant to see what type of tax hit you might take if you paid off major expenses such as your car note, a mortgage – if you still have one – and other bills that aren't part of monthly living expenses. You may find taking one big tax hit to eliminate those bills, means a much lower tax liability in the future as you will need far less money to live on month-to-month.

Retirement Savings Strategies, *cont.*

Deduction Bunching

Try pulling some deductions into the current tax year to help minimize your overall tax liability. An example would be bunching two years' worth of charitable giving into a single year to get over the itemized deduction threshold. Granted, this technique might put an undue strain on cash flow and savings but is an option for those that can afford it. With those extra charitable deductions, you can maximize your deductions for the current tax year.

Minimize Social Security

Your Social Security benefits are taxed based on your combined income. If you file jointly and your income is below the current annual income threshold, you won't have to pay taxes on your Social Security benefits. If you're single your threshold is lower before you will owe taxes on your Social Security benefits. As your taxable income increases, however, you may have to pay taxes on your Social Security benefits. Make sure you discuss these thresholds with you financial professional.

Consider moving to a Roth IRA

While this isn't a strategy that will work for everyone, if you have a large IRA consider moving some of it to a Roth IRA to help reduce future tax liability. The move can also help minimize your future minimum IRA distributions. To see if this strategy will work for you, mock up a tax return in the fourth quarter and see how much money you can remove before pushing yourself into a higher tax bracket.

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