# Reduce Retirement Tax Burden with Tax Planning

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*The latest tax trap: Paying more taxes in retirement than now.*

There is a trend that is causing a problem for retirees – higher taxes than they dreamed of. Those who have been saving diligently in IRAs, 401(k) plans and other retirement plans have been building up sizable retirement nest eggs. These individuals have been careful to not tap into these funds until they have to at age 70.5. Instead, they have been living modest lifestyles using their savings from their taxable accounts. When they reach age 70.5, they must start drawing down funds per the United States Internal Revenue Service's (IRS) required minimum distribution (RMD). Retirees then feel surprised when they realize how much they have to draw down, and that the funds are all taxable by the state and IRS. To make matters worse, these individuals and couples typically have fewer deductions to help lower their tax rates.

For example, a couple with $3 million in tax-deferred accounts, such as IRAs and retirement plans, that delay taking their RMD until age 70.5 will need to withdraw $113,207 the first year. Add in Social Security income of approximately $40,000, and the couple earn a total of $153,207. Assuming they fall into the 25 percent federal tax bracket and take no deductions, federal and state (Illinois) taxes on this income come to $38,357.

How do can a retiree avoid getting in this trap? It is easier to manage the potential problem before one reaches age 70.5 and has to take the RMD. So, what can you do? Meet with your financial advisor or accountant early on to develop a plan. That plan may include starting withdrawals from retirement accounts as early as 59.5 and managing income from these accounts and other sources each year to retain a modest tax bracket. When the account holder reaches age 70.5, the retirement account may contain less and the RMD will then be less.

Another strategy involves slowing down retirement plan assets' growth by putting high-growth holdings in taxable accounts and more conservative allocations, such as bond and fixed-income investments, in tax-deferred accounts. However, investors have to be careful not to defeat the purpose of this strategy by putting high-turnover investments in taxable accounts, which results in a tax burden as short-term gains will be taxed at one's full rate.

The good news may be that the investor has accumulated a lot in tax-deferred savings. Nevertheless, one can possibly avoid the bad news by aggressively working on making changes before time catches up.

*Disclaimer: The views expressed in this article are the opinions of the author and should not be interpreted as individualized investment advice. Investment objectives, risk tolerances and the financial situation of individual investors may vary. Please consult your financial and tax advisors before investing.*

**Tags: finance, making the most of your money, taxes**

**About Susan Carr-Templeton**

Susan Templeton is the founder of Stafford Wells Advisors, a wealth management firm serving individuals, families and businesses and advising workplace retirement plans. Stafford Wells was founded in 2008 with the mission of delivering independent, complete, unbiased investment and planning advice, free of any conflicts of interest. Susan Templeton has more than 20 years experience in investment management. She received her B.S.B.A. degree in marketing from the University of Denver and her M.B.A. from the University of Chicago. Susan is a trustee for the Advocate Foundation where she chair's the Planned Giving Committee and is a member of the Investment Committee. Susan serves on the investment committee for the Visiting Nurse Association (Chicago) and is a former trustee of the Village of Oak Brook Police Pension Plan.