

Tax Planning and Retirement

When people think about their retirement, the mental picture they summon tends to focus more on beaches and hobbies and less on income taxes. However, the taxes you'll have to pay on your retirement income will have a large impact on how much you'll really need in retirement. While your tax burden will most likely be lower in your retirement than in your highest-earning years, you will still have to deal with income taxes. This means that a part of your retirement planning must include planning for taxes in retirement as well. The good news is that being smart about how you invest and making strategic decisions about where you draw your income from in retirement will better prepare you for a secure future.



How Much of Your Benefit Is Yours to Keep?

One of the biggest surprises that retirees encounter is that Social Security, a cornerstone of retirement income for many, is taxable. However, the portion of your Social Security benefit that is subject to tax depends on your total income for the year. If you rely solely on income from Social Security, you will likely not have to pay taxes on those benefits. But many people use Social Security as a supplement to

what they withdraw from their retirement accounts. For those people, if their adjusted gross income, nontaxable interest received, and half of their annual Social Security benefit adds up to a number between \$32,000 and \$44,000 (and they are married), they may have to pay tax on up to half of their benefit. For single people, that amount would have to be between \$25,000 and \$34,000. If the amount is higher than those figures, up to 85% of the

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Eliminate Tax Refunds

Most people are delighted when they find out they're getting a large tax refund. What they fail to realize is that the government is giving them back their own money, which they loaned to the government interest free.

Don't view tax refunds as a forced savings program, since there are better ways to save than through interest-free loans to the government. If you're concerned that you would just spend the extra money every paycheck, have that amount automatically transferred to an investment account. *(Keep in mind that an automatic investing program, such as dollar-cost averaging, does not assure a profit or protect against a loss in declining markets. Because such a strategy involves periodic investments, consider your financial ability and willingness to continue purchases through periods of low price levels.)*

If too much federal tax is being withheld from your paycheck, fill out a new W-4 to determine how many allowances you should claim. Please call if you need help with these calculations. ○○○

Tax Planning

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benefit could be taxable.

Downtown Living = Downtown Taxes

Another tax-related aspect of retirement many people don't realize has a large impact on their finances is where they plan to live. While it's tempting to move in down the street from the grandkids or downsize to a condo in a walkable city, it's important to make sure you understand the tax situation of the locale before you pack up and resettle. Some U.S. states, like Nevada and Florida, have no personal income tax. That, combined with the warm weather, makes both states popular landing spots for retirees. If you want to live a bit more adventurously, try Alaska, which has no income or sales tax. States like Georgia offer special perks to draw retirees, like not taxing Social Security income or up to \$65,000 of retirement income for people over 65. Other states have higher tax burdens, which can have an outsized effect on your nest egg. You will need to carefully weigh the advantages and disadvantages of any new place to live and budget accordingly.

Mix It Up with Tax-Diversified Investments

It's common for people saving for retirement to place an emphasis on tax-deferred accounts like 401(k) plans. This way, they save on taxes now in their higher-earning years, and then pay tax when they draw on the funds in retirement and in a potentially lower tax bracket. While there is nothing wrong with this strategy, it's also a good idea to have some accounts to draw on that will not incur any taxes, like a Roth IRA. This gives retirees more of a choice about what they will draw on and if they will have to pay taxes on those funds. You can also keep some of your investments in regular tax-

Stock Selection Tips

Consider the following tips when selecting stocks for your investment portfolio:

- ✓ Purchase stocks that fit your investment goals and criteria.
- ✓ Don't worry about the overall stock market and whether it is at a high or low level. Instead, concentrate on purchasing stocks for the long term at a fair price.
- ✓ Don't invest based solely on a stock tip. The tip may be valid, but you need to carefully research the company.
- ✓ Invest in stocks whose businesses you understand.
- ✓ Carefully research a company before investing in its stock. Read the company's annual report, Form 10-K, and analyst reports.
- ✓ Don't rush into purchasing a stock. Good stocks can rise in value for years.
- ✓ While diversification is an important portfolio strategy,

only purchase as many stocks as you can reasonably monitor.

- ✓ Monitor your stocks after purchase. Read quarterly and annual reports.
- ✓ Maintain realistic expectations. High expectations often result in frequent trading.
- ✓ Set target selling prices — both high and low — when you purchase a stock. You don't have to sell when the stock reaches those prices, but you should at least reconsider the investment.
- ✓ Analyze and learn from your mistakes. Understand why you lost money on a particular stock so you can try to prevent the same thing from happening.
- ✓ Review all your stocks at least annually. Look at them as a whole to make sure they are still compatible with your overall investment objectives. ○○○

able accounts, which provide income that is taxed at a lower capital gains rate.

If you are not currently contributing to a Roth IRA, you may want to consider a rollover from a tax-deferred account into a tax-free account. Of course, you will have to pay any taxes owed when the rollover occurs, but you will also have more options for income to draw on in retirement. Because this is not a good choice for everyone, you should speak with a financial advisor to make sure it is appropriate for you.

Don't Forget about Required Minimum Distributions (RMDs)

Many people are not in the enviable position of being well-off enough to leave funds untouched through their 60s. But for those who are in that situation, they must keep

in mind that by the time they turn age 70½, they are required to start making withdrawals from their 401(k), Roth 401(k), IRA, or other similar account. Whether they need the money or not, they have to start taking the RMDs...and that added income could bump them into a higher tax bracket. The best course of action is entirely dependent on your specific situation, but one strategy is to begin making withdrawals before 70½ as long as you remain in a lower tax bracket, and reinvesting the unneeded amount elsewhere. There is also the option to rollover the funds into a Roth IRA, which is the only type of retirement account not subject to RMDs. Speaking with a financial advisor can give you a clear picture of what strategies work best for you — the most important step is to have a plan. ○○○

Having the Talk

Take a moment and pretend your older sister and her husband pass away unexpectedly, leaving their three young children behind. You are called into their lawyer's office immediately. You learn that you and your husband were named guardians of your three nieces and the family dog. You've also been designated as full beneficiaries of your sister's estate. While you love your nieces, your life just changed in the blink of an eye. You went from being a professional, childless, young couple in a condo to a five-person family with a dog and a two-story home. Situations like this don't just happen in movies — they happen to people in real life, and not as infrequently as you might think.

Now imagine you are the parents of those three children. What if your younger sister and her husband weren't able (or willing) to care for your children? What if they decided to pass guardianship on to the next person; or worse, what if the children had to go live in foster care? Or what if your sister and her husband accept guardianship of your children, but move them into that condo in the city? Is that what you would have wanted? These conversations are absolutely critical if you have dependents, no matter how young and healthy you are.

Say you don't have dependents. Does that mean you don't need an

estate plan, or don't need to talk about your plans with your family? It doesn't. Take another example: Bill and Connie have two adult children who both have families of their own. When Bill and Connie sat down to create their estate plan, they realized that their two largest assets were their home and their life insurance policy. They weren't sure how they should allocate between their two children, so they all sat down to talk about it. Their daughter was very connected to their home and it was important to her to keep it in the family. On the other hand, their son already had a home with his family and would have preferred to receive the cash benefit from the life insurance policy. So Bill and Connie left their home to their daughter and the life insurance policy to their son.

In many families, finances and estate talk are taboo. Other families laugh and make jokes about inheritances. No matter what kinds of family dynamics exist in your life, talking about what will happen after a person dies can be painful and scary, but necessary. It's important to talk with your loved ones about what you want, what they want, and what is laid out in your will.

✓ **Keep it light** — Having this discussion can bring up a lot of emotions for your loved ones; thinking about losing someone you love so dearly is painful. So keeping the conversation light but to the point can help keep it on track and productive. There may also be tensions that arise through the process — maybe multiple people want the same thing, or someone gets offended by how you've decided to split your money. You might consider having conversations with people individually to avoid upset.

✓ **Talk openly and honestly** — A decision you have made may

hurt someone's feelings, or there may be things you don't want to tell people about, but it is crucial to be open and honest with your beneficiaries. For example, if you have an adult child who does not handle money well or has exhibited reckless behavior, you may feel it is appropriate to have a trust in place for that child. Both the beneficiary and the trustee should be aware of the situation. If you have children from more than one marriage, being open and honest with all of them is especially crucial.

✓ **Discuss values, not just valuables** — When you die, how do you want people to remember you? What parts of you do you want to live on? This may include traditions, values, family names, rituals, religious beliefs, and so on. This is an important matter to bring up during discussion with your family. Think back on times that meant a great deal to your family or traditions that have brought joy. Maybe it's important to you to have your grandmother's name passed on from generation to generation. Talk about these things with your family to share how you feel and see how they feel.

✓ **Have a professional present** — Having your estate planner present can be helpful, and in some cases, necessary. In many cases, a professional has a better understanding of how estate planning works and can assist by answering any questions your loved ones may have. You might have a family-only conversation first and then a second conversation with your family and the estate planning professional.

Like any important discussion, this talk may be difficult. Every family is different and every talk will be different, but make sure you have it. Please call if you'd like to discuss this in more detail. ○○○



Expenses Cutting into Savings?

For those who are getting close to their retirement years, there are ongoing expenses that put a major dent in retirement savings. There are ways to increase retirement sources without increasing income, and they have to do with monthly ongoing expenses that can be reduced.

Refinance — Your mortgage is most likely your largest debt, so if you can refinance at a lower interest rate, you could save a significant amount of money. Experts say if you can reduce your rate by a least 1%, then refinancing probably makes sense.

Credit Cards — Ask your credit card company for a rate reduction or transfer balances to a lower-rate card. You can also look for a card that offers a 0% interest rate for 12 to 18 months.

Energy Costs — If you make home modifications, such as weather-stripping, caulking, using a programmable thermostat, switching to energy-efficient lightbulbs, insulating your hot water heater, and reducing your water heater setting to 130 degrees, you could save up to 20% on your utility bills.

Food — According to experts, you can cut your annual grocery bill in half. Strategies include mak-

ing a grocery list and sticking to it, buying advertised specials, using both paper and electronic coupons, buying items in bulk, and stockpiling items when they are on sale. Also, if you take your lunch to work and stop buying that morning coffee, you could save approximately \$1,900 per year.

Transportation — First, shop around for less expensive car insurance and look at raising your deductible. Also, if you are in an area with good public transit, the American Public Transportation Association says you could save up to \$9,600 per year (Source: Investopedia.com, September 15, 2017).

Entertainment — The Bureau of Labor Statistics reports that the average American spends \$2,800 per year on entertainment (Source: Investopedia.com, September 15, 2017). Take a serious look at what entertainment expenses you can cut or reduce. Think about things you may not be using, such as subscriptions to newspapers or magazines, club memberships, a different cable package, or cell phone plans.

By employing some of these strategies, you could be putting thousands more toward your retirement. Please call if you'd like to discuss this topic in more detail. ○○○

Calculating Your After-Tax Rate of Return

Conceptually, an investment's total return equals the change in market value plus any dividends, interest, or capital gains, divided by the beginning market value. Practically speaking, however, total return can be difficult to calculate, especially if you invested additional money or took distributions during the year. You may need the help of a computer to calculate your total return precisely.

Once you know your total return, calculate your after-tax return. From your dividend, interest, and short-term capital gain income, deduct the amount paid in taxes at your marginal tax rate. From your long-term capital gains, deduct capital gains taxes paid. You can then calculate your after-tax return.

If there's a significant difference between your total return and after-tax return, reevaluate your investment strategy to make it more tax efficient. Emphasizing investments that generate capital gains or placing income-generating investments in a tax-deferred account are just two strategies you may want to consider. If you'd like help evaluating the tax efficiency of your portfolio, please call. ○○○

Financial Thoughts

For the 2018–2019 school year, the average cost of tuition and fees (does not include room and board) is \$35,676 at private colleges, \$21,629 at a state university for out-of-state students, and \$9,716 for state residents at public universities (Source: *U.S. News & World Report*, 2019).

Of parents with 10th grade students, approximately 40% have not discussed how much their

children will be expected to contribute to their college savings and 50% have not discussed how the financial aid process works (Source: Fidelity, 2018).

In a recent survey, when asked what they would do with a sudden windfall, 53% of the respondents said they would share their wealth with family, friends, and charity; 51% said they would pay off debt; 49% said

they would invest the wealth; and 18% said they would splurge and spend freely. About 43% believed their goals would stay the same as before the windfall occurred (Source: BMO Wealth Management, December 2018).

The average amount borrowed by a college graduate in 2017 was \$29,884 (Source: SavingForCollege.com, 2018). ○○○