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What They're Not Telling Us About Our Retirement Savings

By Steven Crawford

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Americans are facing a crisis in retirement. According to a survey by GoBankingRates, 42% of Americans have less than $10,000 saved for retirement.[1] For those who are more fortunate and have accumulated six figures or more in retirement savings, there is another issue that is often not discussed with their current advisors: It is not how much your statement says, it's how much of that money is actually yours and how long it will last.

See, there are many enemies to our future plans, and one of them is good ole Uncle Sam. Yes, everyone's favorite uncle is not always the most generous. In fact, our Uncle Sam is quite the contrary. Quite frankly, he's not very patriotic when it comes to our retirement income.

Anyone remember the Boston Tea Party and the American Revolutionary War? I can recall in school learning about that famous line uttered by Paul Revere and William Dawes, "The British are coming!" regarding the British soldiers planning their attack on the colonies for fighting against one of the things we are fighting today: unfair taxation! So, who is warning us about the impact taxes play on our retirement income now? Is it your broker? How about Uncle Sam?

What about all of our friends on Wall Street who love to protect our interest and post about the *average returns* for the S&P over the last ten or twenty years? By the way, the *average returns* may have absolutely nothing to do with your *actual returns*. Let's say you have a $1000 investment over two years with a first year market loss of -50% and a gain in the second year of 50%. The average return would equal 0%; however, the actual return on your $1000 investment is -25%, because the initial $1000 suffered the 50% loss, leaving you with $500. The remaining $500 then gained that 50%, meaning you end up with $750 – or a -25% loss on your initial $1000 investment.

But let's focus on this warning: *"Taxes are coming!"*

Taxes, like death, are inevitable, but how we plan for this threat to our "golden years" is vital to our peace of mind and lifestyle we want to ultimately live. Americans hold well over $19 trillion in tax deferred accounts (401(k)s, traditional IRAs), and while that sounds great to have those taxes deferred, the problem is as we retire, we tend to gather more assets; family responsibilities grow (helping to pay for grandkids in college, health issues, and more) and we tend to not want to sacrifice our overall lifestyle as much as we get closer to retiring, which is why many retirees continue to work.

Another fallacy we tend to believe is that our tax brackets will go down in retirement, but that is simply not factual. Under our current administration, the actual tax brackets were lowered with the 2017 Tax Cuts and Jobs Act. We now have the following tax brackets: 10%, 12%, 22%, 24%, 32%, 35% and 37%, and for those of us who own businesses, the corporate tax rate was 35% (currently 20%). Keep in mind all of these rates are scheduled to sunset in 2025.[2]

Why is 2025 an important year? For those of us planning to retire between now and then, it may be a good time to

consider a Roth conversion because our current tax brackets are the lowest they have been in years, and a significant increase in taxes could greatly impact our future retirement income. Tax rates were as high as 94% during World War II, and with our current deficit over a record-breaking $19 trillion, the President has discussed, you guessed it: taxing our qualified accounts today to help reduce the deficit![3]

Those accounts look great when the market is doing well, but what they're not telling us about our retirement is that the account balance is not accurate. What do I mean by that? Well, remember that account has not been taxed yet, nor does it take into account the management fees, required minimum distributions (RMDs), and other fees that are still to come over the years. What a nice friend we have in Wall Street and our government (please note the sarcasm).

Oh, what I did not yet mention is what happens to the income in those tax-deferred accounts when you reach Full Retirement Age (FRA) and its impact on your Social Security. Uncle Sam says, "I need more tax money!"

Here is what I mean: If you and your spouse make more than $44,000 as a married couple filing jointly, up to 85% of your Social Security benefit may be taxable![4] This is something called "provisional income." To calculate this, Uncle Sam looks at all income, including the following:

- Half of your Social Security income
- Wages, if still employed
- Distributions from, you guessed it, 401(k)s and traditional IRAs
- Capital gains from brokerage accounts
- Pension payments
- Inheritance
- Interest and dividend income
- Tax-free Municipal Bond Interest

Now, I am not saying to avoid paying taxes. The goal is to educate Americans about the negative impact taxes can have on their income without proper planning. Many brokers are not savvy in "retirement distribution planning," but focus on just the "accumulation phase," which is why it's important to work with firms who understand the distribution stage just as fully. We highly suggest that your planning makes use of both tax-deferred and tax-free retirement accounts because of the uncertainties in our "progressive tax" laws and the volatility associated with the markets.

A good retirement plan doesn't leave your retirement to speculation or completely in the hands of external forces. My belief is that a balanced approach, one that has guaranteed future income with protection against downside market risk and utilizes tax-free strategies like Roth conversions or cash value life insurance policies, because those are not included when Uncle Sam calculates our Social Security and while the tax brackets are its lowest in years, is best.

[1-4] For sourcing and more information, please visit https://www.forbes.com/sites/impactpartners/2019/08/19/what-theyre-not-telling-us-about-our-retirement-savings/#72c0cedd71c4.

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