



## Taming the tax tangle if you're retiring soon

Retirement is often viewed as an opportunity to travel, spend time with family or simply enjoy the fruits of a long career. Yet the transition may bring a tangle of tax considerations. Planning carefully can help you minimize tax bills. Below are four steps to take if you're approaching retirement, along with the tax implications.

### 1. Consider your post-career lifestyle

Begin by assessing what retirement might look like for you. For example, will you relocate to a different state or downsize by selling your home? Will you continue to work part-time?

**Tax implications:** Moving to a state with lower income or property taxes may stretch your retirement savings. If you sell your home and the capital gain exceeds \$250,000 (\$500,000 for married couples filing jointly), you'll need to pay tax on the amount over the exclusion limit. And if you work part-time, your earnings could reduce your Social Security benefits (depending on your age) or push you into a higher tax bracket.

### 2. Assess your income sources

*Social Security* is a major income component for many retirees, and deciding when to start collecting benefits is crucial. The government will permanently reduce your monthly benefit if you begin collecting before your full retirement age. Conversely, if

you delay benefits past your full retirement age (up to age 70), you'll receive larger monthly payments.

**Tax implications:** Depending on your total income (including wages, retirement distributions and taxable investment income), up to 85% of your Social Security benefits could be taxable. Proper planning can help you manage taxable income and potentially reduce or avoid higher taxes on benefits.

If you're fortunate enough to have a *pension*, find out your payout options. Some pensions offer lump-sum distributions, while others offer monthly annuity payments.

**Tax implications:** Most pension income is taxable at ordinary income tax rates.

In addition to retirement accounts, you may have *savings and investments* in brokerage accounts that can supplement your income.

**Tax implications:** Capital gains and dividends may be taxed differently than ordinary income, potentially at lower rates. Strategic withdrawals from taxable accounts and retirement accounts can help you manage your overall tax liability.

### **3. Develop a retirement account withdrawal strategy**

Once you turn 73, you must take required minimum distributions (RMDs) from most tax-deferred retirement accounts such as traditional IRAs and 401(k)s. Failing to do so can result in hefty penalties.

**Tax implications:** RMDs are treated as ordinary income for tax purposes. If you don't need them for living expenses, you might consider a qualified charitable distribution (QCD) to lower your taxable income. With a QCD, funds go directly from your retirement account to a qualified charity. They can count toward your RMD but aren't included in your taxable income.

Distributions from Roth IRAs and Roth 401(k)s are generally tax-free (if holding-period requirements are met), making them valuable tools for reducing taxes in retirement. If you have traditional and Roth accounts, you might choose to take withdrawals from Roth accounts in years when you want to manage your tax bracket more carefully.

**Tax implications:** Roth accounts don't require RMDs during the original owner's lifetime.

### **4. Plan for health care expenses**

Medical costs can significantly impact retirees. Medicare premiums, hospital visits, prescriptions and potential long-term care are just some of the expenses that can eat into your retirement savings without careful planning.

**Tax implications:** Health Savings Accounts (HSAs) allow for tax-deductible contributions, tax-free growth and tax-free withdrawals for qualified medical expenses. If you're retiring soon and have a high-deductible health plan, maximizing HSA contributions can be a smart move. In addition, qualified medical expenses can sometimes be deducted if they exceed a certain percentage of your adjusted gross income (AGI).

### **Final thoughts**

Retirement can span decades, and tax laws frequently change. By combining various withdrawal strategies and staying proactive about tax changes, you can tame the tax tangle. These are only some of the tax issues and implications. Contact us. We can help forecast tax outcomes under different scenarios and advise on strategies that complement your retirement goals.

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