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Manage Income Taxes on Your Investments in Retirement

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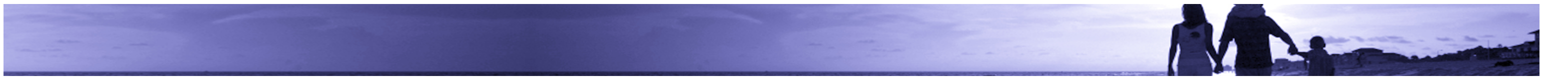

Manage Income Taxes on Your Investments in Retirement

Increasing your after-tax retirement income

During your retirement years, it's important to pay close attention to the income tax consequences of your investment decisions. If you receive a great deal of investment income when retired, for instance, the taxation of your Social Security benefits may be impacted adversely. Furthermore, if you have accumulated substantial investment income in a tax-deferred retirement plan and fail to manage distributions properly during your retirement years, you may find yourself pushed into a higher tax bracket when you are forced to take required minimum distributions after age 70½. There are several steps you can take to manage the income taxes on your investments.

Caution: *As of 2013, a 3.8 percent Medicare tax is imposed on interest, dividends, capital gains and other investment income for individuals making more than $200,000 a year ($250,000, if married filing jointly).*

How can investment income affect Social Security benefits?

To determine whether your Social Security retirement benefits are taxable, you must perform a calculation. Your benefits are taxable if one-half of your Social Security benefits plus all of your other income exceeds a certain base amount for your filing status. (All of your other income includes taxable pensions, wages, interest, dividends, and all other taxable income. It also includes tax-exempt interest income plus normally excludable income such as interest from Series EE savings bonds and foreign earned income.) If you determine that your Social Security benefits are taxable, either up to 50 percent or up to 85 percent of your benefits will be taxable, depending on your filing status and the amount by which you exceed the base figure.

Reducing investment income

Since investment income (e.g., taxable interest income and dividend income) must be included in gross income, reducing the amount of income you earn from your investments will help decrease your adjusted gross income. This, in turn, can help minimize taxation of your Social Security retirement benefits . To reduce investment income, you might consider investing in growth stocks or in mutual funds that appreciate rather than pay dividends. To shift income and tax, you might also consider gifting income-producing investment assets (such as stock) to your relatives.

How might you get pushed into a higher tax bracket during your retirement years?

Most people expect to be in a lower tax bracket after retirement due to diminished earned income. But this is not always the case. For instance, if you accumulated substantial income in a tax-deferred retirement plan over the years and are now over age 70½, you might find yourself pushed into a higher tax bracket. After age 70½, you must start withdrawing minimum amounts of your money annually from certain qualified retirement plans; this rule is known as the required minimum distribution rule. Basically, your annual minimum distribution is calculated by dividing the value of your retirement plan by your life expectancy. Therefore, the higher the value of your retirement plan, the more taxable income you'll have to withdraw.

If your retirement assets are such that you could be pushed into a higher tax bracket after age 70½, you might wish to consider withdrawing a portion of your retirement plan money annually upon retirement (or at any time after age 59½), instead of waiting until age 70½. By controlling and managing your retirement distributions during your early retirement years, you may be able to prevent a tax bracket problem (i.e., higher income taxes) later on. Of course, the challenge will be to figure out precisely how much money you should withdraw each year. Such a calculation is fairly involved; for more information, consult your financial professional.

If you have substantial investment portfolio income, you might consider making gifts of unneeded income-producing assets to lower-tax-bracket individuals such as family members. This strategy will remove a certain amount of taxable interest, dividends, and capital gains from your financial picture.

Important Disclosures

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