# Future retirees focus on taxes

Clients expect advice on tax-efficient withdrawal strategies

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In the past, retirees relied on their accountants for tax advice. But future retirees increasingly are looking to their financial advisers for guidance on how to maximize their spendable retirement income by minimizing their taxes, according to a new survey released Thursday by the Nationwide Retirement Institute.

Over half of future retirees surveyed said they wished they better understood how their income in retirement will be taxed, according to an online study of U.S. adults age 50 or older. One-third of the respondents were characterized as affluent future retirees who have investible assets of $150,000 or more and who plan on retiring in the next 10 years.

"Building tax flexibility into a retirement income plan is crucial," said Eric Henderson, president of Nationwide's life insurance business. "Doing so allows you to use different types of investments and retirement accounts — taxable, tax-deferred and tax-free — to avoid higher tax brackets."

The failure to plan for taxes may have an adverse impact on current and future retirees. Nearly half of the recent retirees in the survey say they wish they had been better prepared for paying taxes in retirement, and 24% say they have paid several thousands of dollars more in taxes than they had expected to pay in retirement.

While current retirees in the survey depend mostly on Social Security and pensions, future retirees said they expect to use a **variety of sources** for retirement income, including Social Security (91%), savings accounts (70%), a 401k (68%), stocks (57%), an IRA (56%), a pension (51%), mutual funds (48%), a Roth IRA (38%), employment (35%) and annuities (30%).

Depending on the source of those funds, that income may be fully taxable, partially taxable or tax-free. A retiree's income also dictates how much he or she pays for **Medicare premiums** each year.

"When planning for taxes in retirement, the goal is to reduce **the unintended impact of taxes** on combined income sources like Social Security, Medicare or capital gains," Mr. Henderson said. "Smart strategies for sequencing withdrawals can extend a client's income in retirement up to an additional six years."

Mr. Henderson was referring to research published in a 2015 issue of the **CFA Institute Financial Analysts Journal** that disputed the traditional wisdom about withdrawing from taxable accounts until they are exhausted, then from tax-deferred accounts until they're exhausted and finally tapping tax-exempt accounts such as a Roth IRA. The authors presented evidence that more tax-efficient withdrawal strategies, in which each type of account was tapped each year in various proportions based on an individual's tax bracket, could extend the life of a portfolio.

Most older consumers who use a financial adviser expect guidance on tax-efficient withdrawal strategies, according to the Nationwide survey. More than 80% of future and recent retirees and 68% of those who have been retired more than 10 years say they expect their financial adviser to help them plan for taxes in retirement. And 38% of future retirees say they would switch advisers to get one who could help them plan for taxes in retirement.

The new tax law that took effect this year may further complicate tax planning for many retirees depending on where they live, their sources of income and their health, noted William John Marco of Marco Wealth Strategy. In addition to lowering tax brackets and raising the standard deduction, the Tax Cut and Jobs Act also capped or eliminated certain key deductions.

Retirees who previously itemized their deductions will need to determine whether the near doubling of the standard deduction, to $12,000 for individuals and $24,000 for joint filers, makes up for lost deductions, Mr. Marco said.

For example, since the state and local tax deduction is now capped at $10,000, retirees living in states with high property taxes may not be able to deduct the full amount of the property taxes they paid. And those taxpayers who do not itemize can't deduct their charitable contributions.

But taxpayers age 70½ and older who must take required minimum distributions can request that up to $100,000 of their RMDs be transferred directly to a charity each year. Although the donation does not qualify for a deduction, that money is not included in the taxpayer's adjusted gross income, which could reduce income taxes and future Medicare premiums.

"It is important to develop a plan for how taxes will impact retirement income based on a person's situation and goals," Mr. Henderson said. "Financial advisers can help people plan for and live in retirement by providing a fact-based estimate of taxes in retirement and a unique plan to address those costs."