

Tax rate on retirement account withdrawals can be higher than you expect

Article by Scott Burns | Published: 08 April 2015 | Dallas Morning News

Can you explain this tax situation? We are in the 15 percent tax bracket. Our taxable income is less than \$73,800, and we are filing a joint return for the 2014 tax year. We take required minimum distributions from our IRAs because we are both over 70½ years old.

If we take another \$100 distribution from an IRA, line 15b on our 1040 goes up by \$100. Then the Social Security worksheet line 11 increases by \$100 (Note: Our line 7 is more than \$44,000) and Social Security worksheet line 15 increases by \$85 (also lines 16 and 18).

Then our form 1040 taxable income, line 43, goes up by \$185 and our tax bill goes up about \$30. So I'm now taxed 30 percent on the \$100 of additional income.

Is this correct? What is wrong with this?

It's correct. Your actual tax will be about \$185 times your 15 percent tax bracket. This means you will pay \$27.75 in additional income taxes for an additional IRA withdrawal of \$100. What economists call your marginal tax rate — the rate you pay on a dollar of additional income — is 27.75 percent, not 30 percent.

But you and I know that the difference is quibbling. The real issue is what you've just been hit in the face with — you're paying a lot more in income taxes as a retiree than you expected to pay. For many, the added tax of Social Security benefits literally means their income tax bill doubles.

Equally important, the burden of that tax falls entirely on the money you have saved in your qualified retirement plans. In effect, you are paying a penalty for being a saver when our friends in Congress, regardless of party, continue to talk about encouraging people to save more.

There have been efforts to repeal the tax. So far, they have gone nowhere. And don't expect any help from AARP. At the end of January, however, the president of the Association of Mature American Citizens reiterated its support of the Senior Citizens Tax Elimination Act (HR 589). The AMAC is a conservative counterpart to AARP. You can learn more about the bill on the AMAC website, amac.us.

Will AMAC make progress toward eliminating the tax? Sorry, the bill doesn't have nearly enough sponsors. According to the website govtrack.us, which tracks legislation, the bill has only a 1 percent chance of getting past committee and no chance of being enacted.

My suggestion? If you are a retired middle-income taxpayer, calculate the federal income tax you have to pay. Then calculate the tax you would pay if Social Security benefits were not taxed. Figure out the difference. Then tell your representative in Congress about it and that you want the tax repealed.

If H&R Block does your taxes, as it does for millions of people each year, tell your adviser that doing the calculation is part of its advertising promise to help "get your billions back."

And, yes, we are talking billions. According to estimates by the Social Security trustees, the taxation of benefits will bring in \$33 billion this year.

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