the Legacy Group

Top 10 Tax Planning Strategies

To Keep More of Your Savings in Retirement



If you’re considering retirement in the next 5 to 10 years, it’s essential to be aware of the potential financial challenges you face.

One of the biggest mistakes is not having a solid plan to minimize taxes. While many focus on their savings and investments, understanding the tax implications of your retirement income can significantly impact your overall financial health. Without proper planning, you might find yourself paying more than expected, potentially diminishing the longevity of your retirement resources and leaving less for your heirs or your other legacy objectives.

In this guide, we discuss 10 tax strategies for you to consider. While not every strategy will be appropriate for you, it’s essential to assess them to create a comprehensive tax strategy based on your own unique financial situation and retirement goals. If you need help creating your customized tax-efficient retirement income plan, we’d be happy to help.

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Maximize Retirement Accounts

Why We Recommend This Strategy

Retirement accounts, such as traditional IRAs, Roth IRAs, and 401(k)s, are specialized savings designed with tax advantages to support retirement preparation. These accounts can either offer immediate tax deductions when you contribute to them, tax-free growth, or even tax-free distributions, all depending on the type. The amount you can contribute to an IRA or 401(k) changes every year; check IRS.gov for current contribution limits. Maximizing these contributions allows you to accumulate and build tax-advantaged retirement resources for the future. For many in higher tax brackets, maximizing 401(k) annual contributions is one of the last large annual income tax deductions available.

How it Can Help You

- Offers potential tax deductions on your contributions
- Provides tax-deferred growth for your investments
- Allows for more tax-efficient wealth accumulation over time

What You Need to Do

- **Maximize contributions:** If you have enough income and room in your budget, consider increasing your contributions to the maximum annual limit. Be sure to take advantage of "catch-up" contributions if you are age 50 or over. Starting in 2025, don't overlook the special additional catch-up limits for those age 60-63.
- **Diversify your portfolio:** Ensure you're not overly concentrated in a single asset class or a few individual stocks. A well diversified portfolio can potentially reduce risk and enhance returns over the long term.
- **Review your risk tolerance:** Especially as you near retirement, it's crucial to understand your tolerance for volatility and inevitable market declines at this stage of life. Realign your asset allocation as appropriate or talk to us about how to best navigate your portfolio during retirement.

2

Optimize Tax Efficiency With Investment Holdings

Why We Recommend This Strategy

Where you hold and allocate your investments can play a significant role in minimizing tax liability. It's distinct from asset allocation, which focuses on the mixture of investments you hold. The primary goal of this technique is to strategically place assets in taxable, tax-deferred, or tax-free accounts based on their tax efficiency, with the ultimate goal of improving after-tax returns.

For example, some investment holdings will be appropriate for taxable accounts, while other investments are better for tax-deferred accounts, with others best suited for tax-free accounts.

When appropriate, another tax-efficient strategy we often recommend is "direct indexing." As opposed to owning "index funds" that seek to mimic a particular index, direct indexing involves actually owning proportionate shares of an index's components in one's portfolio. Long-held index fund positions may accumulate substantial capital gains exposure over time, whereas direct indexing allows for year-round tax-loss harvesting, which may offer greater tax benefits than owning index funds.

How it Can Help You

- Potentially reduces unnecessary tax liabilities by holding investments in the most tax-appropriate account type
- With lower tax liabilities, potentially boosts after-tax investment returns over time
- Aligns investments with your overall financial goals

What You Need to Do

- **Categorize assets:** List out all investments and whether they are tax-efficient or tax-inefficient. Consider criteria such as whether investments will generate short-term or long-term capital gains, annual dividends or interest and if the investments themselves offer tax-advantages, (e.g., municipal bonds are tax-exempt already).
- **Reallocate:** Determine the best location for each of the investments you would like to own. Consider holding tax-inefficient investments in a tax-advantaged account.
- **Assess regularly:** Tax laws often change, especially after election years. It's important to periodically review your investment holdings to confirm they are held in the most tax-appropriate account.

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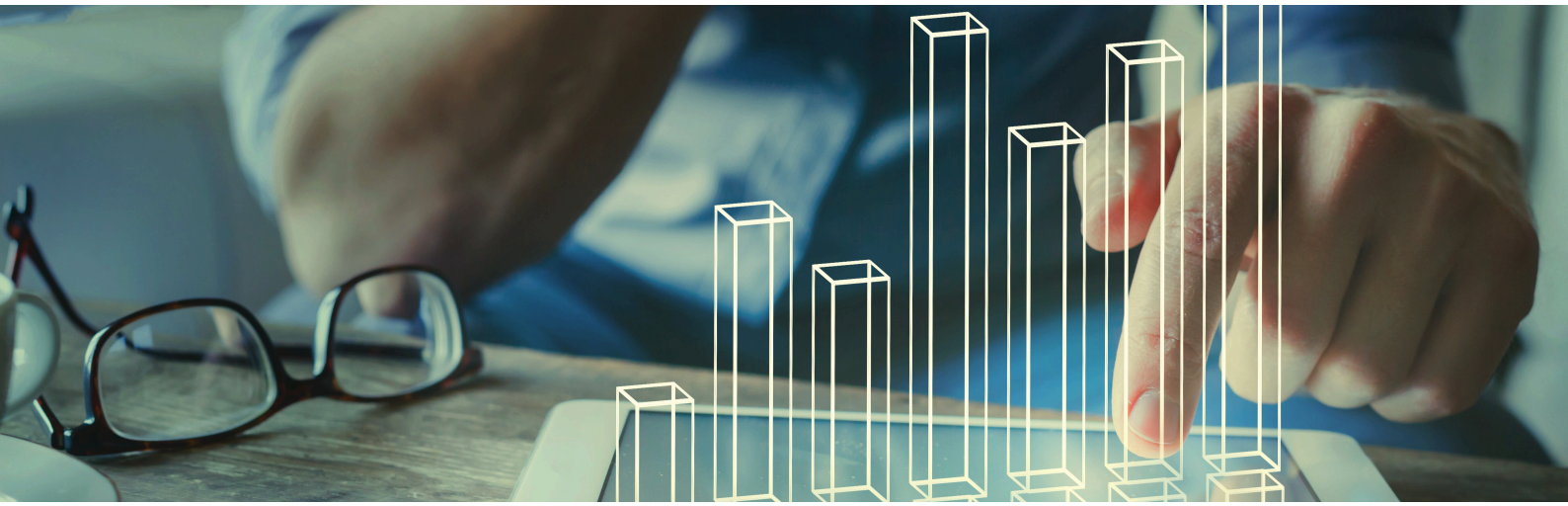
Choose Tax-Efficient Investments



Why We Recommend This Strategy

Tax-efficient investments are those designed to produce the least taxable income, helping you keep more of your gains. These can include certain mutual funds, ETFs, and municipal or government bonds. By including these investments within your taxable investment accounts, investors can manage and potentially reduce the tax drag on their portfolio, enhancing after-tax returns. Other investments you may want to own (like dividend-producing stocks or bonds) might be better suited in a tax-advantaged account, as discussed in the last section. In certain circumstances, building wealth within a life insurance policy may be an appropriate tax strategy, since a policy's cash value can grow tax-deferred and total death benefits are tax-free to beneficiaries.

How it Can Help You

- Reduces the tax drag on your investment returns
- Potentially enhances overall after-tax portfolio performance

What You Need to Do

- **Research:** Make informed selections of funds that have low turnover rates like index funds or ETFs.
- **Allocate investments in tax-appropriate accounts:** Confirm you have the right investments in the right types of accounts.
- **Avoid frequent trading:** Minimize buying and selling to reduce taxable events and higher-taxed short-term gains.

4

Consider a Roth Conversion

Why We Recommend This Strategy

A Roth conversion is achieved by converting all or a portion of a pre-tax traditional or Rollover IRA into an after-tax Roth IRA. Doing so will trigger taxable income in the year of conversion, so it's essential to consult with your tax or financial advisor before implementing this technique. The premise of this strategy is to pay taxes now on the converted amount and allow the funds to grow tax-free for the future. In addition to building a tax-free retirement resource, Roth IRAs are not subject to the same required minimum distribution (RMD) rules as traditional/rollover IRAs or qualified retirement accounts, such as in a 401(k). We work with our clients to evaluate the long-term benefits and whether this strategy is appropriate for their own situation.

How it Can Help You

- When properly structured, provides tax-free withdrawals in retirement from Roth accounts
- Properly timed, converting tax-deferred IRAs and other qualified accounts into Roth savings in low-income years may potentially lower future Medicare-added surcharges/premiums; i.e., Income Related Monthly Adjustment Amount (IRMAA).
- Offers future potential to remain in lower tax brackets when taking retirement account distributions
- Potentially lessens the impact of higher marginal tax rates in the future
- By converting sooner, the amount of pre-tax retirement assets subject to RMDs could decrease, thereby reducing taxable RMD income.

What You Need to Do

- **Evaluate tax brackets and current/near-term income:** Assess if paying taxes now could benefit you later.
- **Plan conversion:** Possibly spread conversions over multiple years to manage the tax hit.
- **Calculate conversion amount:** Determine the best amount to convert without pushing you into too high of a tax bracket. Always consult with your tax professional as to the effect of implementing this strategy on your own tax situation.

5

Optimize When to Claim Your Social Security Income

Why We Recommend This Strategy

Social Security is a key source of income for retirees, even for those with significant assets and income, and it's important to think through this decision. Most people can claim their Social Security benefits between the age of 62 and 70. If you delay until age 70, you will receive the largest benefit amount possible, while claiming it at age 62 means your benefit amount will be smaller but you'll receive those benefits much earlier in your life.

Strategically taking Social Security benefits means assessing the best age and circumstance to start your claim. This requires balancing other income sources, pensions, continued career income, or withdrawals from retirement accounts, to optimize Social Security benefits while minimizing the long-term effects of ascending to higher tax brackets as well as minimizing Medicare-related expenses, such as IRMAA surcharges on Medicare premiums.

How it Can Help You

- Potentially maximizes lifetime Social Security benefits for you and your spouse
- Brings more awareness and planning for taxes on Social Security and other income
- Enhances the overall efficiency of retirement income streams

What You Need to Do

- **Analyze income streams:** Review your various income sources and their respective tax implications.
- **Consider your timing:** Determine the best age for you (and your spouse) to claim your benefits. Make this decision in conjunction with your other income sources.
- **Understand tax implications:** Recognize the tax impact on your other income by claiming your Social Security income benefits now or defer until later.
- **Be aware of earnings limits:** If you earn too much income while receiving Social Security benefits, your benefits may be reduced. Weigh the pros and cons of taking Social Security while you have earned income especially if you claim your benefits prior to your full retirement age (FRA).

6

Implement a Tax-Efficient Strategy

Why We Recommend This Strategy

Creating a tax-efficient distribution strategy is vital for retirees as it dictates how they'll pull money from various accounts throughout retirement. This isn't just about how much to withdraw but also from which account and in what order. A well-thought-out strategy balances enjoying life today with the goal of minimizing overall long-term tax liability as well as maximizing the longevity of tax-advantaged accounts throughout one's retirement. Depending upon your tax situation, you might consider spending down qualified accounts (such as 401(k) or IRA accounts) first and leave non-qualified assets to heirs to achieve favorable tax treatment for the family as a whole.

How it Can Help You

- Coordinates distributions from retirement accounts in a tax-efficient manner
- Potentially reduces tax liabilities over your retirement
- Potentially extends the life and compounding growth capabilities of tax-advantaged retirement accounts

What You Need to Do

- **Calculate annual needs:** Determine the amount you need each year to live comfortably, and how much you can reasonably withdraw from your investments.
- **Determine the proper order of distributions:** Do you want to pull from taxable, tax-deferred, or tax-free accounts first? After that, what's next?
- **Adjust for market conditions:** When times are good in the stock market, how much will you withdraw? When times are more volatile, how much will you withdraw? Come up with a strategy where you know if (and when) you will need to make changes on your withdrawals.
- **Don't overlook required minimum distributions in a given year:** If RMDs are required, adjust other distributions accordingly for that year.
- **Plan for inherited IRA tax implications:** Consider whether your distribution plan might result in large traditional IRA inheritances to non-spousal beneficiaries and the tax implications for them. Non-spousal IRA beneficiaries are required to fully withdraw inherited IRA balances within a 10-year time frame, and distributions are fully taxable at ordinary income rates. Such requirements may cause tax headaches for beneficiaries in the future.
- **Leverage permanent life insurance for legacy planning:** Owning permanent life insurance (whether directly or within a special trust outside your estate) may enable you the freedom to fully spend your other assets during retirement while still realizing your legacy objective via a tax-free inheritance to your loved ones and heirs.

7

Consider State Taxes if Moving Your Retirement Residence

Why We Recommend This Strategy

Every state in the U.S. has different tax rules and structures, and these can vary significantly when it comes to retirees. Some states offer more favorable conditions by not taxing certain types of retirement income, including Social Security benefits and pensions. Others might have no income tax at all.

How it Can Help You

- Offers a more accurate assessment of your tax liabilities
- Keeps your overall financial strategy optimized
- State income taxes can be 5-7% or more of your annual retirement income—a critical consideration if you are considering moving to another state in retirement.

What You Need to Do

- **Research your state:** Identify if your state offers any tax breaks to retirees.
- **Plan relocation:** If you would like to leave your current state, research the tax laws in any new state you consider.
- **Understand sales and property taxes:** Lower income taxes might be offset by higher other taxes. Factor in the total tax burden.



8

Consider Charitable Gifting

Why We Recommend This Strategy

Charitable gifting in retirement planning involves donating assets or funds to charitable organizations, both as a philanthropic gesture and as a strategic move for tax benefits. This can be done through direct donations, donor advised funds, or qualified charitable distributions. By incorporating charitable giving in your financial plan, you can align your charitable goals with tax-saving strategies.

How it Can Help You

- Achieves personal philanthropic goals while receiving current and future tax benefits
- Potentially bypasses capital gains tax by gifting appreciated assets
- Potentially increases your deductions and lowers your taxable income with cash donations
- Lowers your taxable RMD amount by donating via qualified charitable distributions

What You Need to Do

- Evaluate which charities and organizations you'd like to support.
- Determine which charitable gifting strategy is best for you and your family. Given the numerous choices, don't simply default to one without examining the others.
- Three popular choices:

    - **Qualified charitable distributions:** Send RMDs straight to charities through QCDs.
    - **Gift appreciated assets:** Donate assets that have gained value to reduce capital gains taxes.
    - **Establish a donor-advised fund:** Set up a fund for ongoing charitable contributions, offering a tax break up front.

9

Stay Updated With Changing Tax Law



Why We Recommend This Strategy

Tax laws and regulations are frequently evolving, reflecting changes in economic conditions, political climates, and broader societal needs. For retirees, these changes can significantly impact financial planning. Staying informed about these updates helps you maximize opportunities and reduce potential pitfalls associated with changing tax laws.

How it Can Help You

- Avoids unintended tax penalties or liabilities
- Seizes new opportunities for tax savings
- Keeps your overall financial strategy optimized and aligned with your objectives and current tax law

What You Need to Do

- **Partner with a professional:** Consult with an experienced, tax-savvy wealth advisor and tax professional team who will help you develop a comprehensive financial plan that accounts for your tax situation.
- **Educate yourself:** Stay informed about any changing laws and how they might affect you.
- **Focus on what you can control:** While you may like or dislike certain tax laws, focus less on them and more on what you can do to make the best financial choice.

10

Maximize and Leverage HSAs

What HSAs Are and Why We Recommend Them

Health savings accounts (HSAs) are tax-advantaged accounts designed to cover out-of-pocket medical expenses. When following all the rules, they allow for tax-deductible contributions, tax-free growth, and tax-free withdrawals for qualified medical expenses. While you can't contribute to an HSA once enrolled in Medicare, funds from an existing HSA can be utilized to cover Medicare expenses. However, you do need to be enrolled in a high-deductible health insurance plan to be HSA eligible, and there are annual contribution limits.

How HSAs Can Help You

- **Tax deductions:** Contributions to HSAs reduce taxable income.
- **Tax-free growth:** Investments inside HSAs grow without incurring taxes.
- **Tax-free distributions:** Withdrawals from HSAs for qualified medical expenses are not taxed.

What You Need to Do

- **Consider an HSA:** If you have the option to enroll in an HSA, carefully consider if you are comfortable with a high-deductible health insurance plan. If so, max out the HSA contribution if you have room in your budget.
- **Invest wisely within your HSA:** After you contribute to your HSA, you then need to invest those funds. Consider the allocation of assets within the HSA to match your risk tolerance and time horizon.
- **Stay updated on qualified expenses:** Regularly review the list of HSA-qualified medical expenses to maximize the tax-free distribution benefits for current and future healthcare needs.

BONUS STRATEGY

Have Your Advisory Team Work Together



Beyond consulting with a tax professional, you'll want to be sure your entire financial team is working together to provide cohesive oversight and guidance. This should include professionals like CPAs, wealth advisors, and estate attorneys. Your finances don't exist in a bubble, and neither will your tax minimization strategies. When your advisory team works together, strategies are easier to identify and execute, and proactive tax solutions become much easier to implement, reducing your tax bill.

At The Legacy Group, our mission is to help you live a life of greater confidence, choice, and financial freedom through strategic planning and unparalleled advice.

Driven by our values, we strive to build meaningful, long-term relationships with clients through a "Service First" philosophy. Whether your focus is building or preserving wealth, our commitment to a cross-disciplinary planning process allows us to design your financial blueprint through a collaboration of financial, legal, and accounting perspectives. Our three-dimensional planning approach identifies coordination gaps in your current plans and new planning opportunities that can have a significant impact on your legacy and future generations.

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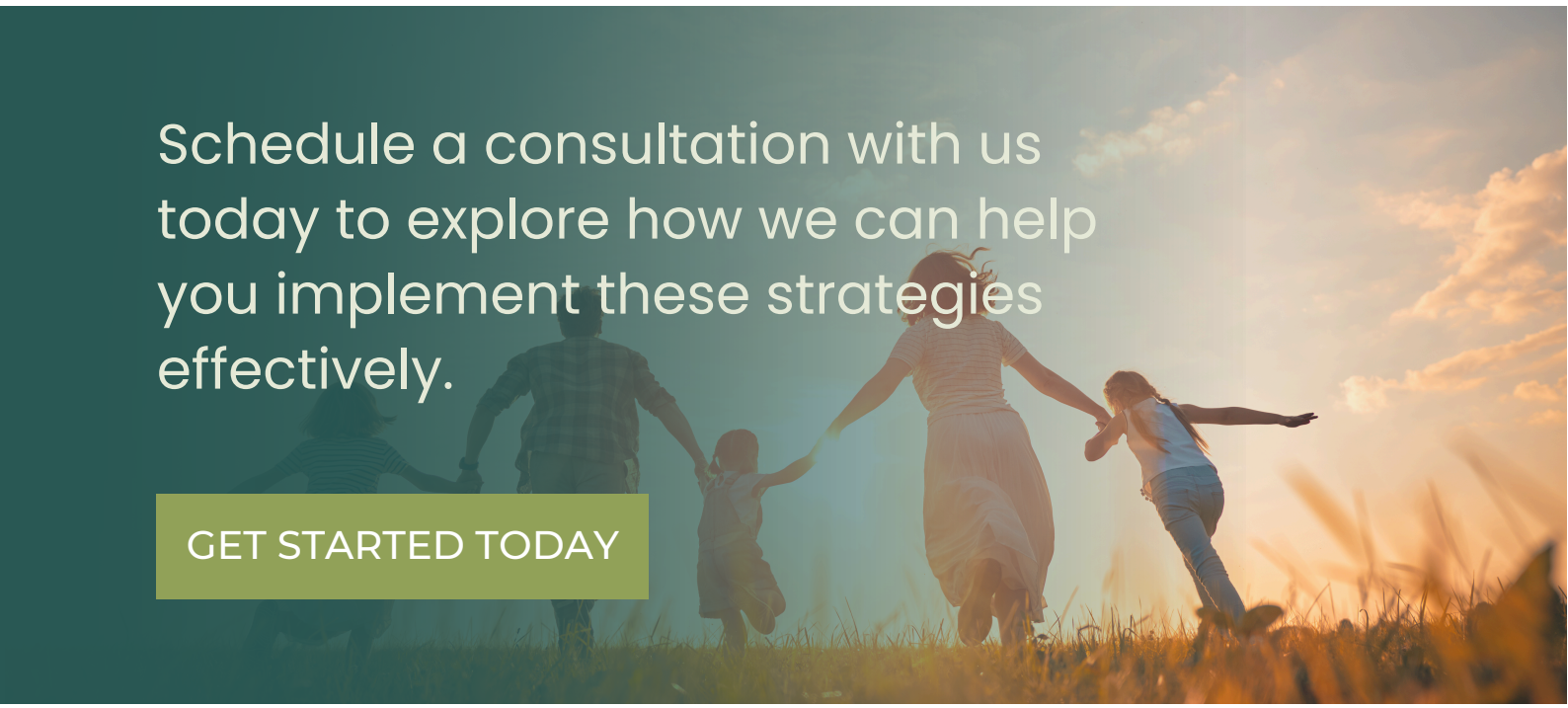

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