FOUNDATIONS FOR TAX PLANNING OF RETIREMENT ASSETS:
Are Your Employees Heading in the Right Direction?

February 2, 2017

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1 TAKE ADVANTAGE OF TAX BENEFITS

- Lower your current year tax bill – pre-tax and tax-deductible contributions
- Then delay taxes until you take withdrawals
- Or make Roth contributions for TAX-FREE withdrawals
2 DIVERSIFY YOUR TAX SITUATION

- Roth contributions are better if your tax rate is higher when you take withdrawals and vice-versa for Pre-Tax contributions.

- But the future and what Congress does is uncertain.

Diversify – aim to retire with a mix of pre-tax, Roth, and even taxable account assets.
3 SEE IF YOU CAN MAX YOUR CONTRIBUTIONS

2016 LIMITS

- $36,000
- $24,000
- $18,000

457 Plan

- You may be able to contribute accrued sick & vacation leave

IRA

- $6,500
- $5,500

+$18,000 during each of the three years prior to your normal retirement age*

+$6,000 if age 50 or over as of year-end

+$1,000 if age 50 or over as of year-end

* “Normal retirement age,” as defined in the plan and based on extent to which maximum contributions not made in previous years. The two catch-up provisions cannot be combined in the same year.
4 MANAGE YOUR TAX BRACKETS

Your income is taxed at different rates

<table>
<thead>
<tr>
<th>2016 Tax Rates</th>
<th>Individual Taxpayers</th>
<th>Married Taxpayers Filing Jointly</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax Rate of...</td>
<td>...applies to each $ of taxable income that is between/over...</td>
<td></td>
</tr>
<tr>
<td>10%</td>
<td>$0 to $9,275</td>
<td>$0 to $18,550</td>
</tr>
<tr>
<td>15%</td>
<td>$9,275 to $37,650</td>
<td>$18,550 to $75,300</td>
</tr>
<tr>
<td>25%</td>
<td>$37,650 to $91,150</td>
<td>$75,300 to $151,900</td>
</tr>
<tr>
<td>28%</td>
<td>$91,150 to $190,150</td>
<td>$151,900 to $231,450</td>
</tr>
<tr>
<td>33%</td>
<td>$190,150 to $413,350</td>
<td>$231,450 to $413,350</td>
</tr>
<tr>
<td>35%</td>
<td>$413,350 to $415,050</td>
<td>$413,350 to $466,950</td>
</tr>
<tr>
<td>39.6%</td>
<td>$415,050+</td>
<td>$466,950+</td>
</tr>
</tbody>
</table>

When making financial decisions, consider consequences of being bumped into higher brackets
5 AVOID PENALTY TAXES

May apply before age 59½

- 457 plan exception\(^1\) – but not if transfer to non-457 plan
- Age 55 exception – 401 plans\(^2\)
- Other exceptions, too – visit www.irs.gov – search for Instructions for Form 5329

Early withdrawals should be last resort – tax impact AND increased risk of outliving asset

\(^1\) 10% penalty tax never applies to withdrawals of original 457 plan contributions and associated earnings. But penalty may apply to non-457 plan assets rolled into a 457 plan and subsequently withdrawn prior to age 59½.

\(^2\) Does not apply to other previous employer-sponsored retirement plans
Weigh the impact of taxable events on Social Security benefits

\[
\frac{1}{2} \text{Social Security Benefits} + \text{Other income} = \$\quad
\]

<table>
<thead>
<tr>
<th>SOCIAL SECURITY BENEFITS</th>
<th>SINGLE FILER</th>
<th>MARRIED JOINT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to 50% taxable</td>
<td>$25,000-$34,000</td>
<td>$32,000-$44,000</td>
</tr>
<tr>
<td>Up to 85% taxable</td>
<td>$34,000+</td>
<td>$44,000+</td>
</tr>
</tbody>
</table>

www.ssa.gov/planners/taxes.html
7 KNOW THE IMPACT ON MEDICARE

Weigh impact of taxable events on Medicare premiums

- Part B & D premium surcharges if just $1 over income limits*
  $85,000+ (single) or $170,000+ (married)

- Based on 2 years prior tax return
  2016 premiums > look at 2014 tax year

www.ssa.gov/pubs – search for “Medicare Premiums”

* Modified Adjusted Gross Income, which refers to total adjusted gross income and tax-exempt interest income.
8 PLAN AROUND TAX WITHHOLDING

- If you need $10,000, 20% is generally withheld up front, per IRS rules

- So must request $12,500 to get $10,000 after taxes

20% is not the exact amount you OWE – you may end up owing more or less

For illustrative purposes only. Not applicable to qualified distributions of Roth assets.
9 EVALUATE ROTH CONVERSIONS

Pay taxes now for tax-free withdrawals later?

TRADITIONAL IRA or EMPLOYER PLANS

CONVERT TO
(A Taxable Event*)

ROTH ASSETS
(Roth IRA or within 457 plan**)

Tax-free income LATER that won’t impact

- Medicare premiums
- Social Security benefits
- AGI phase outs that reduce tax deductions

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* Subject to taxes on the converted amount. If subsequently withdraw Roth assets within a 5-year period and you are under age 59½, also subject to a 10% penalty tax. Note: each conversion carries its own 5-year limit.

** Also available to 401(k) and 403(b) plans, if adopted by plan sponsor.
ROTH CONVERSION STRATEGIES

- **PARTIAL** conversions of existing assets – to avoid bump to a higher tax rate
- Avoid paying taxes **OUT OF** the converted assets
- Consider impact of the **CONVERSION TAX BILL** on Social Security benefits, Medicare premiums
- Weigh Roth IRA vs. in-plan 457 conversions – including IRS RMD and recharacterization rules
10 PLAN AROUND RMDS

Yearly, taxable withdrawals beginning in the year you turn 70½

- 457/401 plans, traditional IRAs
- Not applicable for
  - Roth IRAs
  - If still working (current employer’s plans only)
- If fail to take, subject to 50% penalty
- Consider IRA charitable rollover rules

Plan for – MAY make sense to take withdrawals before RMD age to smooth out tax bills
11 HAVE A WITHDRAWAL STRATEGY

You could aim to defer taxes as long as possible

1. Withdraw just from taxable accounts + any RMDs

2. Withdraw from tax-deferred accounts only if need added funds

3. Delay Roth account withdrawals as long as possible
WITHDRAWAL STRATEGIES

But different strategies may make more sense...

WITHDRAW SOONER FROM...

- Roth assets to avoid HIGHER tax brackets
- Tax-deferred assets in LOW tax-bracket years

WITHDRAW LATER FROM...

- Taxable account assets with LARGE gains so heirs get stepped-up basis

May make sense to withdraw A MIX each year of pre-tax, Roth, and taxable assets based on your specific situation
CONSIDER STATE TAXES, TOO

Where you live in retirement impacts your tax bill, too!

- Some states have preferential rules for pension income or retirement accounts
- Some have no income tax but higher other taxes
- Consider all taxes that may apply and the cost of living
CHECKLIST

- Look for ways to manage current AND FUTURE taxes
- Consider federal and state and local taxes
- Don’t make a decision just to save taxes – it should make sense for your investment portfolio, too
- Review tax rules periodically
  - Top tax rate has changed 37 times since 1913*
- Seek help as needed – a qualified tax professional

* Source: Tax Policy Center. Refers to federal income taxes.
LEARN MORE

- www.irs.gov
- www.icmarc.org/tax
- www.icmarc.org/taxplanning
- Qualified tax professional

For more tips and tools on these and related topics visit www.icmarc.org/realize
QUESTIONS