

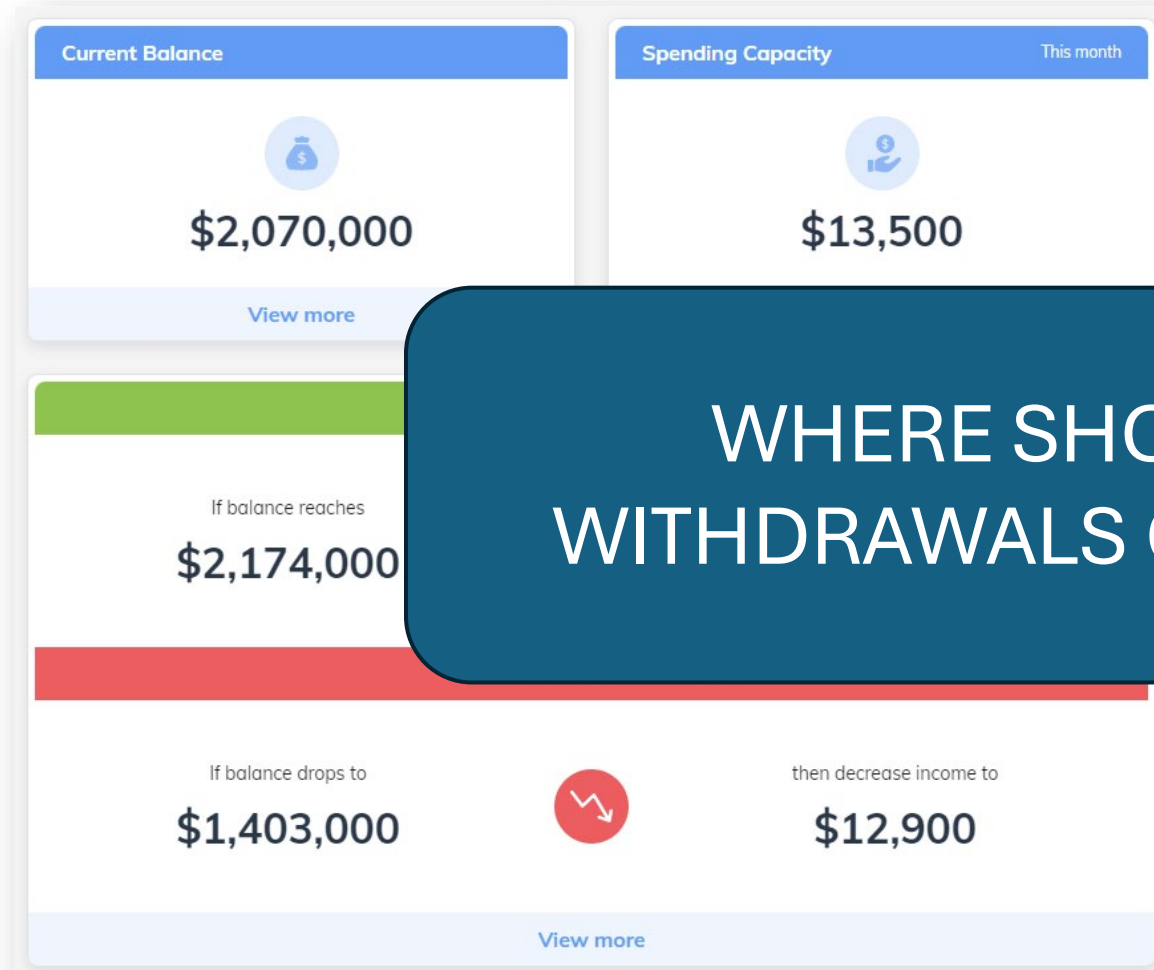
WHERE THE MONEY COMES FROM

Building a tax-smart withdrawal order

| WHAT IS THE PURPOSE OF FINANCIAL PLANNING?

- To help people live the best life they can
 - ... with the resources they have
 - ... in the time they have
 - ... and the world they happen to live through

SPENDING AND ADJUSTMENT GUIDANCE



How much can I spend?

WHERE SHOULD THE
WITHDRAWALS COME FROM?

Do I need an adjustment?
(or a change?)

How much would I adjust?

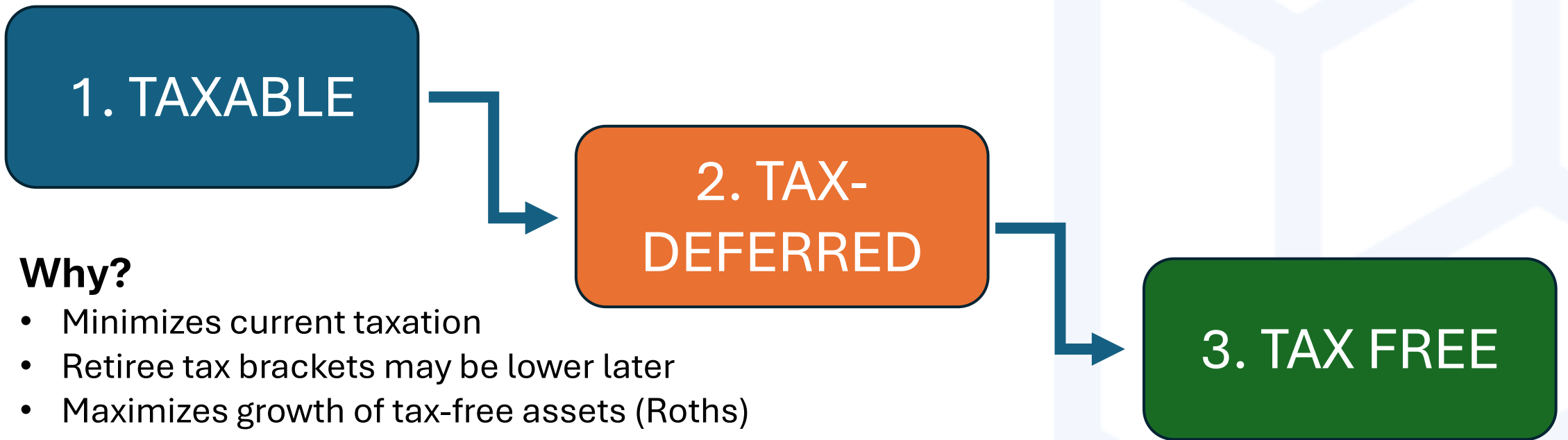
| TODAY'S AGENDA: TAX-SMART DISTRIBUTION PLANNING

- Strategic:
How to plan long-term withdrawal phasing and systematic withdrawals to set clients up for more net-of-tax income
- Tactical:
How to optimize outside-of-plan distributions



STRATEGIC TAX-SMART DISTRIBUTION PLANNING

A COMMON RULE OF THUMB: THE “TAX-TYPE WATERFALL”



Why?

- Minimizes current taxation
- Retiree tax brackets may be lower later
- Maximizes growth of tax-free assets (Roths)
- Roths are great to inherit
- Easy to implement

| TAXATION & INHERITANCE

	Taxation	AGI	NII	RMDs	QCDs	Beneficiaries
Taxable	LTCG, ongoing	Yes	Yes	No	No	Stepped-up basis
Tax-Deferred	Ordinary, wd only	Yes	No	Yes	Yes (IRAs)	Taxable
Tax-Free (Roth)	None	No	No	No	No	Not taxable

| PROBLEMS WITH THIS RULE OF THUMB

- Ignores actual tax rates and phases of retirement
- Can lead to high or very high RMDs in later years, when spending needs are lower
- What if future tax rates are higher than today's?
 - Because of RMDs or other income sources
 - Because of tax policy changes

| THE ALTERNATIVE: TAX ARBITRAGE

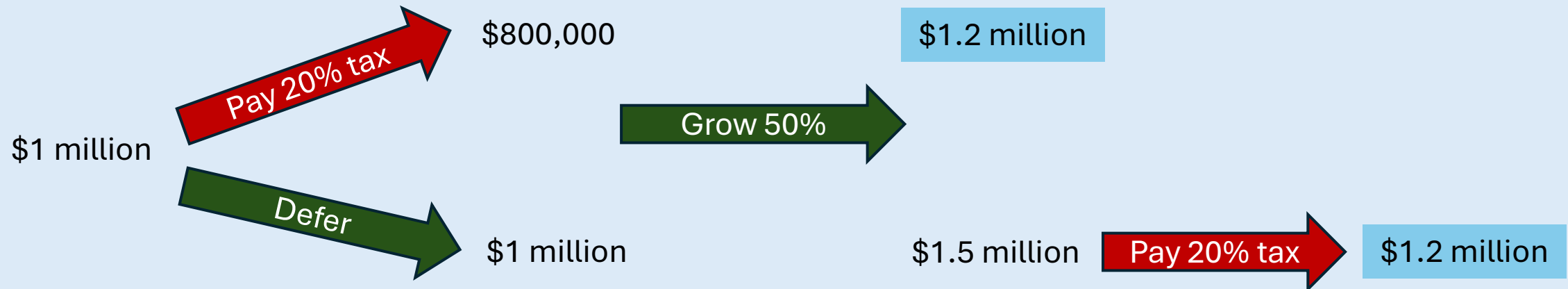
- The value of a withdrawal strategy comes from moving taxable income across time, not merely minimizing it this year.
- Use Roth conversions to pay tax on tax-deferred dollars when rates are low to avoid paying higher rates in the future when rates are high due to:
 - RMDs
 - Other income
 - The “Widow’s Penalty”
 - Higher beneficiary tax rates, or
 - Policy changes

TAX ARBITRAGE: THE BASIC IDEA

If, in the future, you expect a...

Lower Rate	Same Rate	Higher Rate
Don't convert	Indifferent	Convert

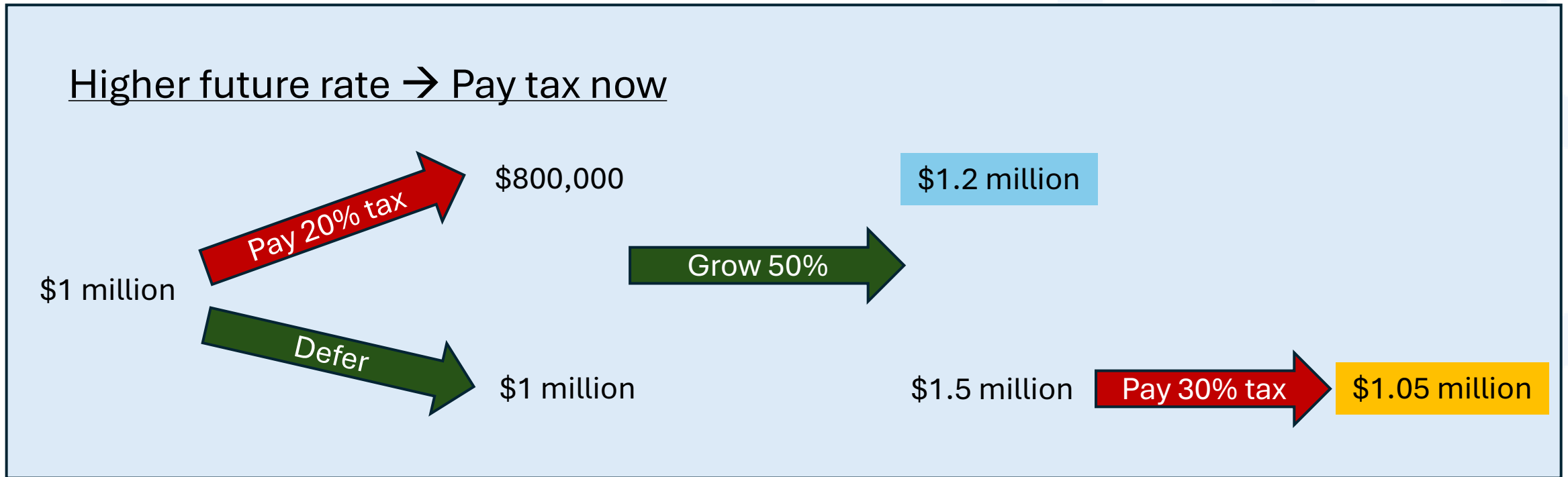
Same rate → Same result



TAX ARBITRAGE: THE BASIC IDEA

If, in the future, you expect a...

Lower Rate	Same Rate	Higher Rate
Don't convert	Indifferent	Convert

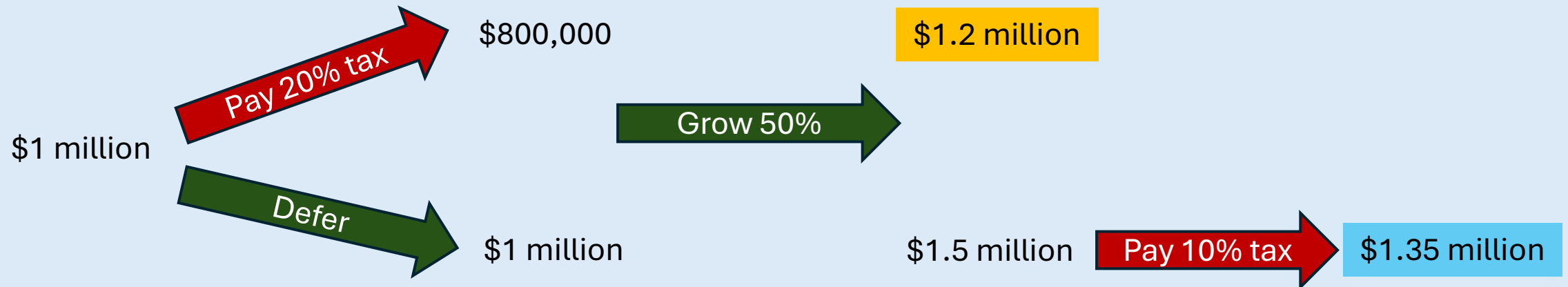


TAX ARBITRAGE: THE BASIC IDEA

If, in the future, you expect a...

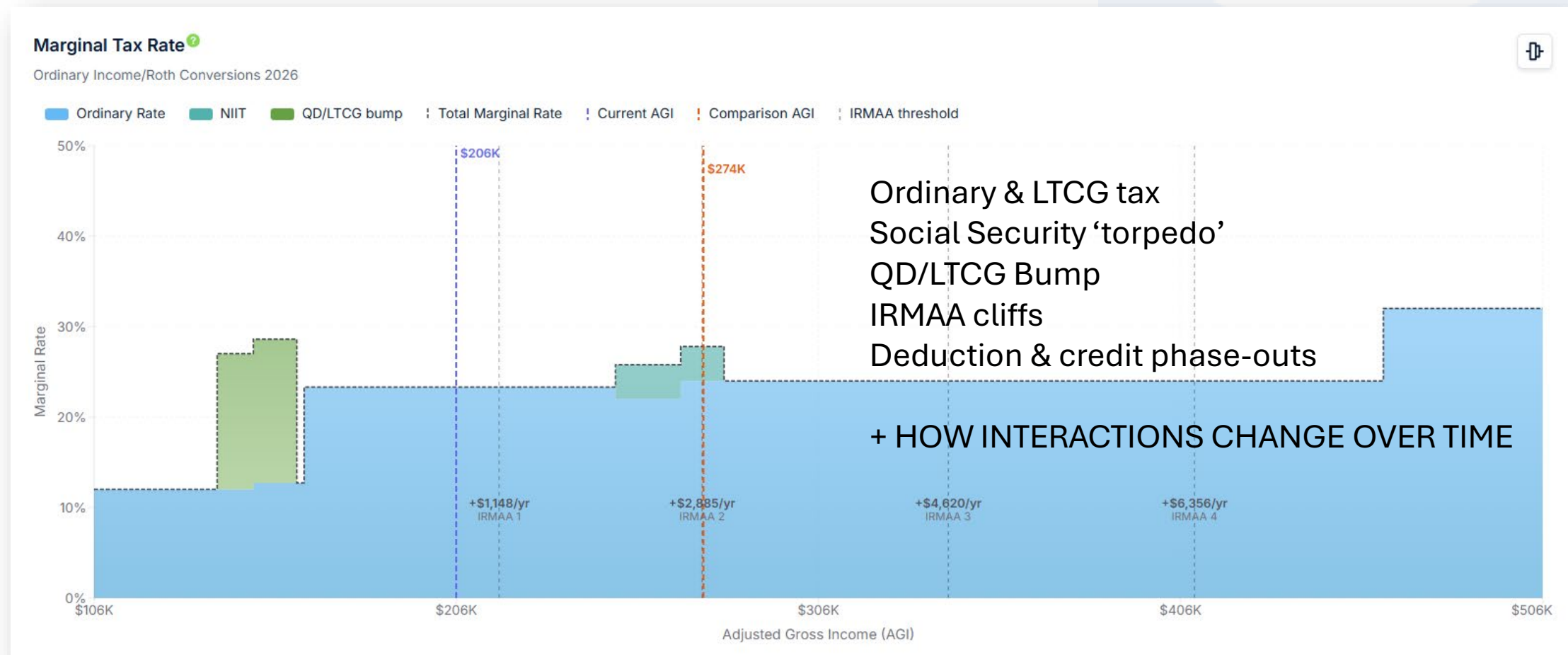
Lower Rate	Same Rate	Higher Rate
Don't convert	Indifferent	Convert

Lower future rate → Defer taxes

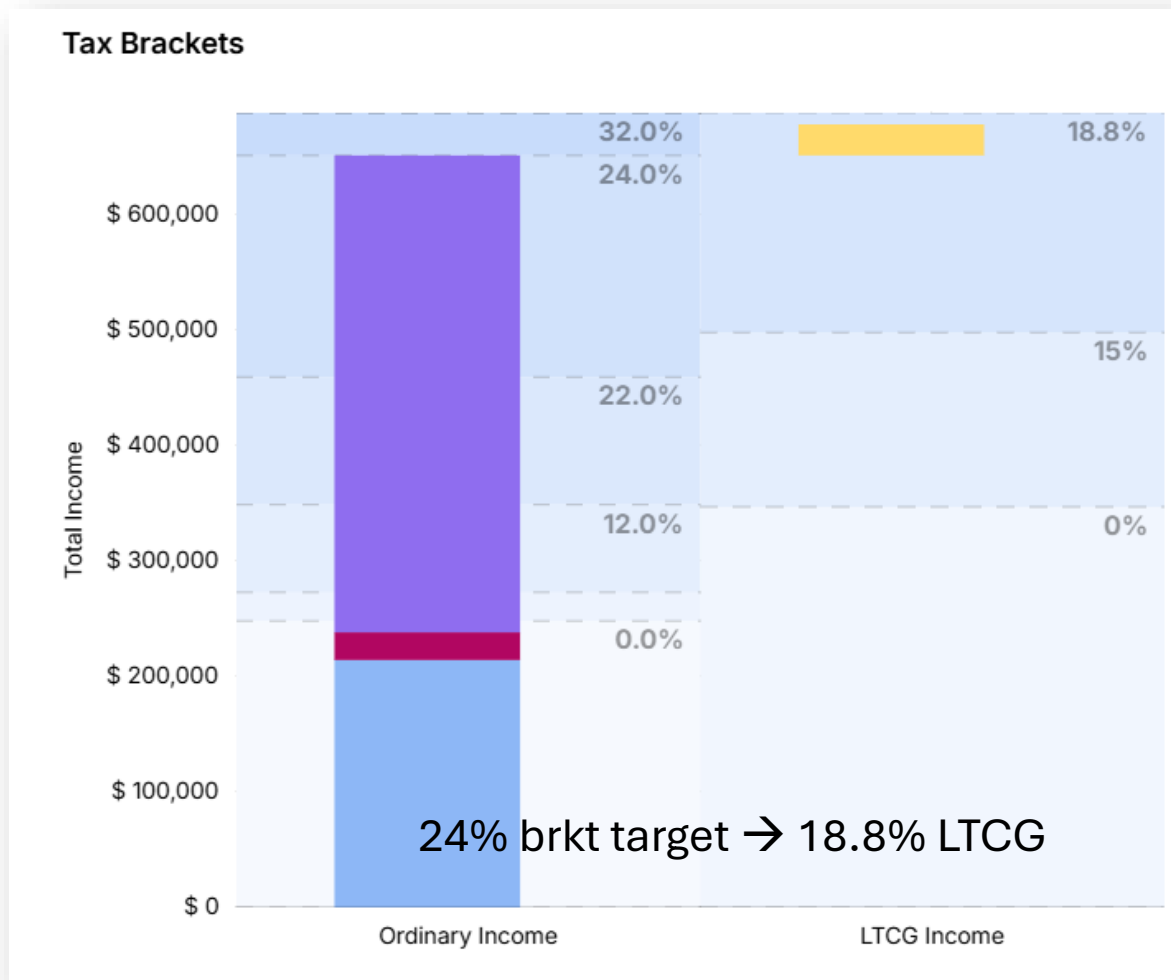


PROBLEM 1: COMPLEXITY

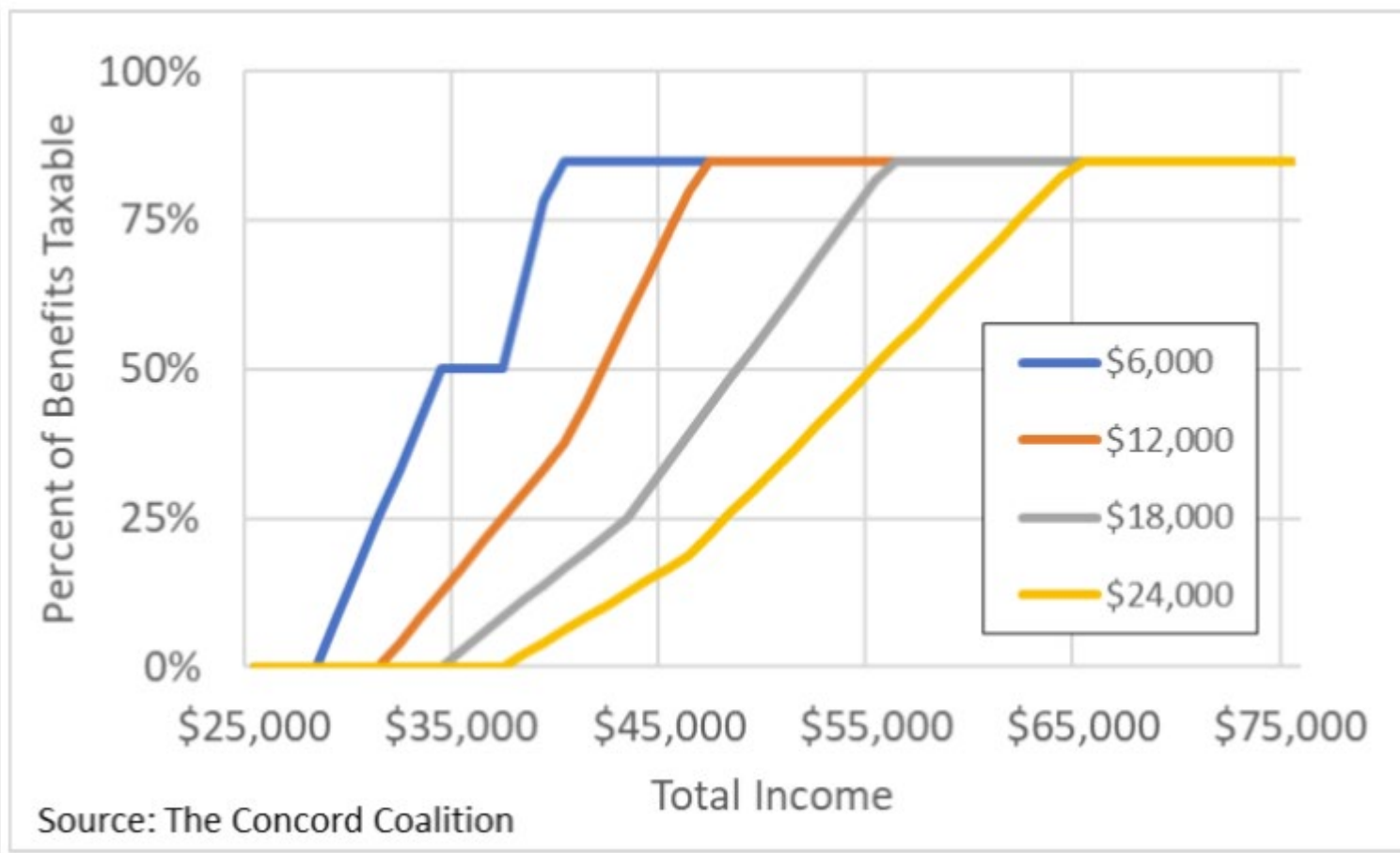
Taxes paid are not a simple matter of knowing a tax rate



PARTS OF THE TAX CODE: ORDINARY & LTCG



PARTS OF THE TAX CODE: SOCIAL SECURITY



- The Social Security tax torpedo depends on “combined income”, not AGI
- So range of phase-in depends on total Social Security benefits.

| SOCIAL SECURITY TAX TORPEDO

$12\% * 150\% = 18\%$

$12\% * 185\% = 22.2\%$

	Lower Income	Medium Income	Higher Income	Maxed Out
Other taxable income	\$10,000	\$40,000	\$50,000	\$70,000
Social Security Benefits	\$60,000	\$60,000	\$60,000	\$60,000
Total	\$70,000	\$100,000	\$110,000	\$130,000
“Combined” Income	\$40,000	\$70,000	\$80,000	\$100,000
Taxable SS	\$4,000	\$28,100	\$36,600	\$51,000
Taxability %	6.7%	46.8%	61%	85%
Tax on SS @ 12%	\$480	\$3,372	\$4,392	\$6,120
Marginal Rate on \$1	18%	22.2%	22.2%	12%
Marginal SS Taxability	50%	85%	85%	0%

| PARTS OF THE TAX CODE: SOCIAL SECURITY

Year	Non-Taxable Social Security Income	Taxable Social Security Income	Roth Conversions
2026	\$0	\$0	\$413,000
2027	\$0	\$0	\$413,000
2028	\$2,250	\$12,800	\$400,000
2029	\$5,400	\$30,600	\$384,000
2030	\$5,400	\$30,600	\$45,500
2031	\$13,900	\$40,100	\$0
2032	\$20,800	\$39,200	\$0
2033	\$42,000	\$18,000	\$0
2034	\$41,400	\$18,600	\$0
2035	\$40,800	\$19,200	\$0

The Pre-Social Security phase is especially well-suited for Roth conversions.

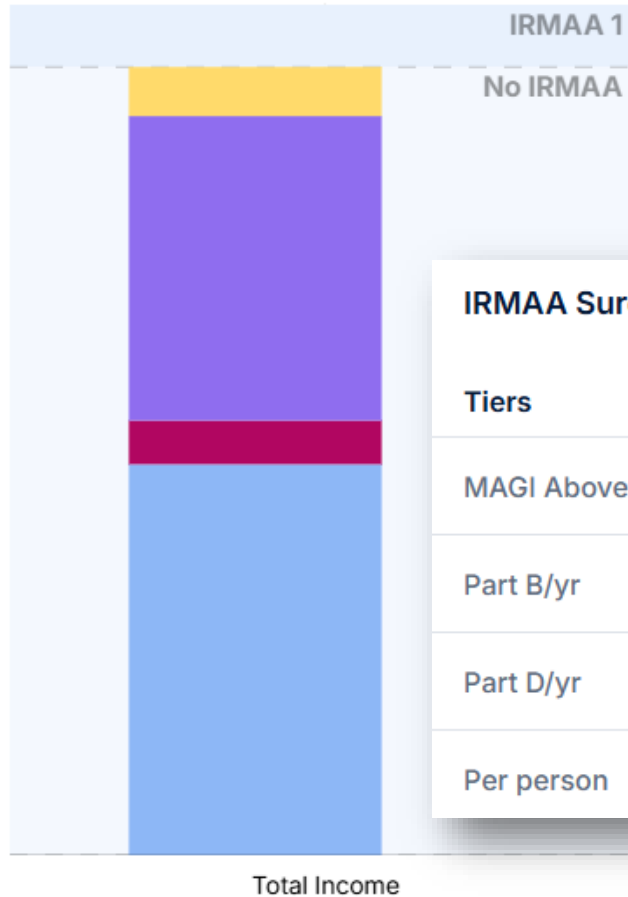
| PARTS OF THE TAX CODE: CHANGE OVER TIME

THRESHOLD OR AMOUNT	VALUE
Social Security taxability thresholds	\$25k/\$32k (50%) & \$34k/\$44k (85%)
3.8% NIIT	\$200k/\$250k
0.9% Additional Medicare Tax	\$200k/\$250k
OBBBA thresholds	\$75k/\$150k Senior Bonus
Top IRMAA bracket	\$500k/\$750k; begins indexing in 2028
Child tax credit thresholds	\$200k/\$400k
Home sale gain exclusion amount	\$250k/\$500k

With 3% inflation, by 2048 the 3.8% NIIT will hit below the 15% LTCG bracket.

PARTS OF THE TAX CODE: (M)AGI & IRMAA

IRMAA Brackets



What is IRMAA?

- Additional Medicare premiums based on MAGI
- Based on MAGI from 2 years previous
- A 'cliff' tax: \$2,296 for \$1 over first threshold

IRMAA Surcharge Breakdown

Tiers	IRMAA 1	IRMAA 2	IRMAA 3	IRMAA 4	IRMAA 5
MAGI Above	\$218K	\$274K	\$342K	\$410K	\$750K
Part B/yr	\$974	\$2,435	\$3,895	\$5,356	\$5,844
Part D/yr	\$174	\$450	\$725	\$1,000	\$1,092
Per person	\$1,148	\$2,885	\$4,620	\$6,356	\$6,936

PARTS OF THE TAX CODE: (M)AGI & IRMAA

Deductions, Credits & Thresholds (2026)

⚠ 2 Impacted

Metric	Before	After	Change
Standard Deduction Fixed — not income-dependent	\$33,850	\$33,850	--
QBI Deduction (\$199A) No qualifying business income	\$0	\$0	--
⚠ Senior Bonus (OBBBA) Phaseout triggered	\$2,632	\$0	(\$2,632)
Child Tax Credit No qualifying children	\$0	\$0	--
Other Dependents Credit No qualifying dependents	\$0	\$0	--
ACA Premium Tax Credit Not enrolled / no benchmark entered	\$0	\$0	--
⚠ NIIT (3.8%) Threshold crossed — NIIT triggered	\$0	\$927	+ \$927
Additional Medicare Tax (0.9%) Applies to wages only — not conversions	\$0	\$0	--
SS Benefits Taxable Already at 85% max taxable	\$7,352	\$7,352	--

Additional AGI/MAGI can lead to phase-out or loss of deductions and credits.

SOLUTION:
Don't isolate a single tax element. Run all tax calculations. And look at overall life impact.

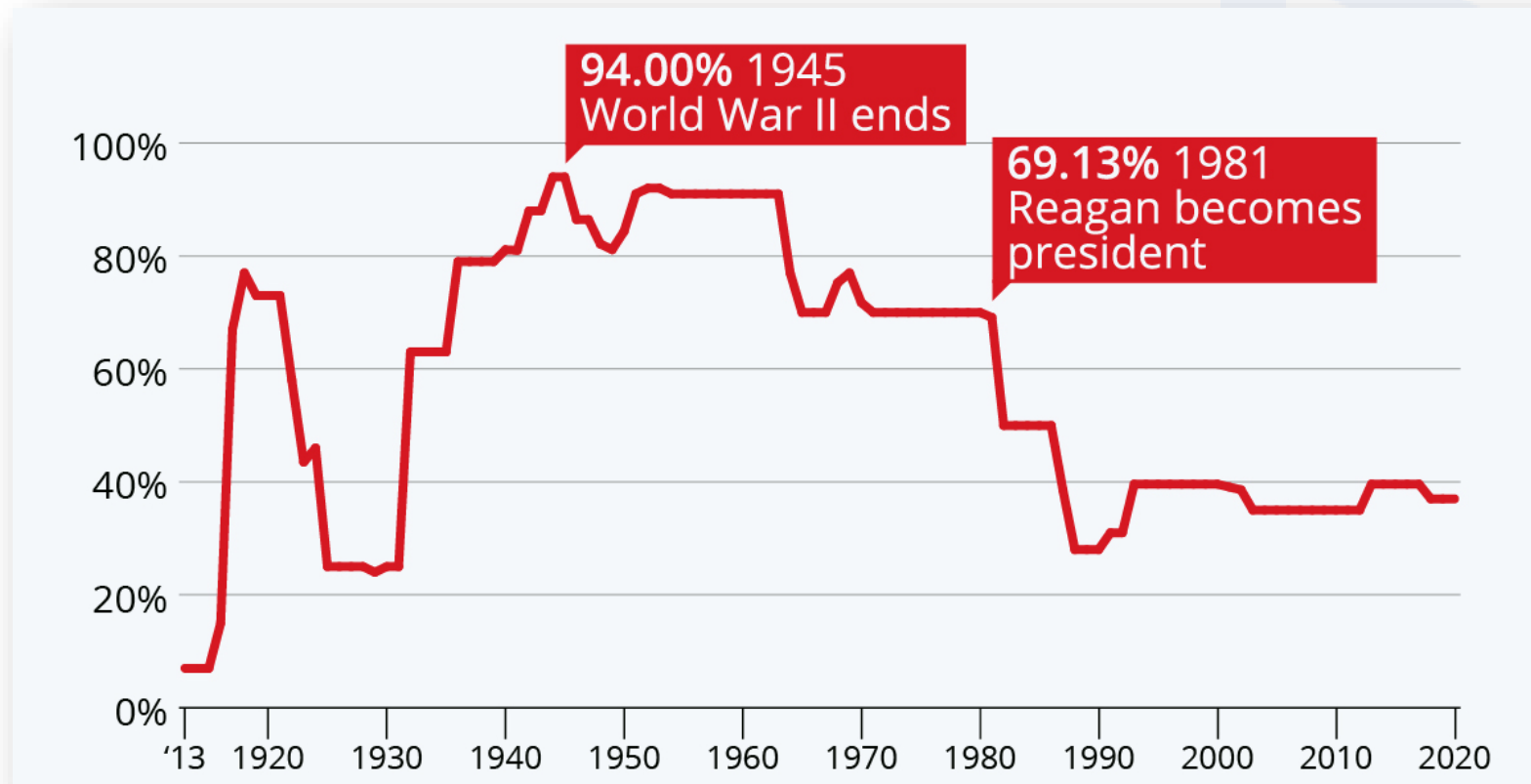
Select a Tax Strategy

Values shown in today's dollars

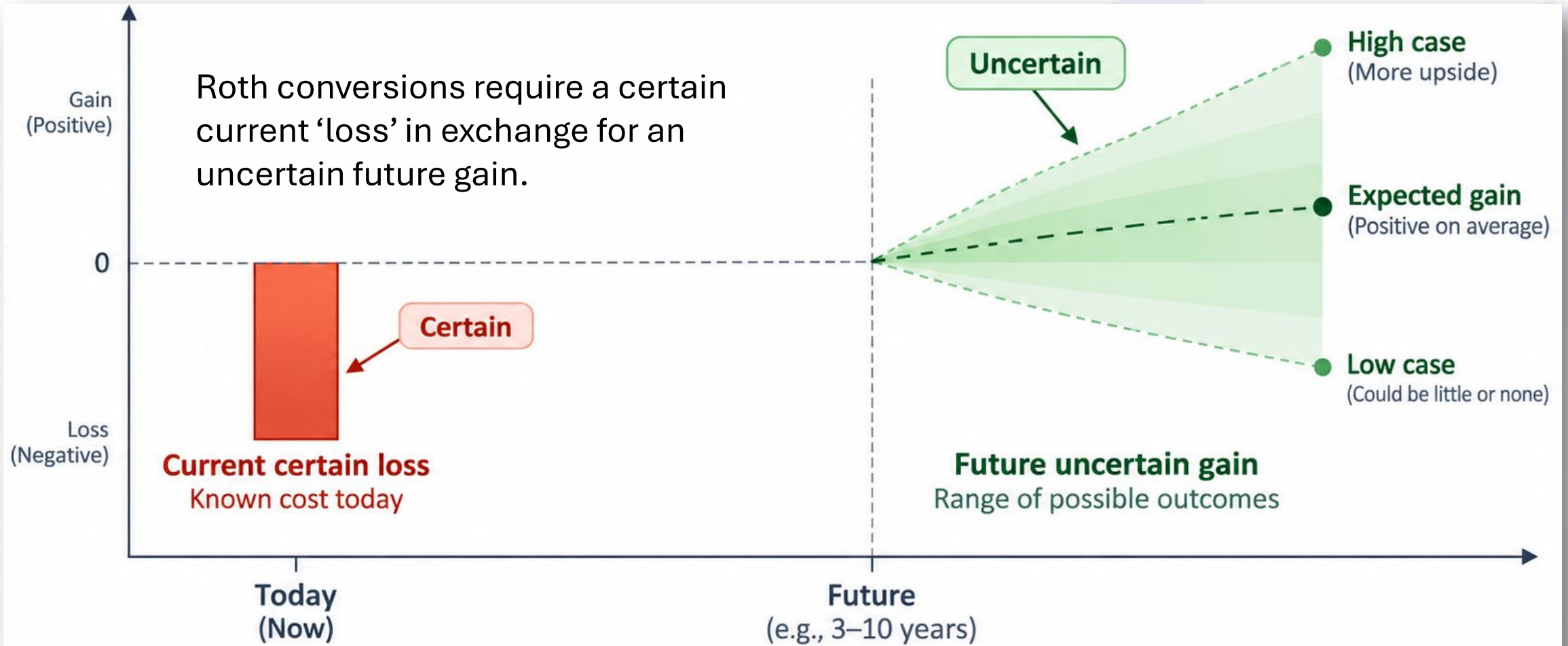
☐	Tax-Free, Tax-Deferred, Taxable	13.55%	\$1,255,000	\$4,663,000	\$8,942,000
☐	Tax-Free, Taxable, Tax-Deferred	14.43%	\$1,574,000	\$4,344,000	\$7,861,000
☐	Roth Conversions to fill 0% Brkt	13.17%	\$1,230,000	\$4,688,000	\$8,161,000
☐	Roth Conversions to fill 10% Brkt	12.56%	\$1,133,000	\$4,784,000	\$8,215,000
☐	Roth Conversions to fill 12% Brkt	9.36%	\$699,000	\$5,218,000	\$8,509,000
☒	Roth Conversions below IRMAA Brkt 1 Viewing Now	7.03%	\$515,000	\$5,403,000	\$8,641,000
☐	Roth Conversions to fill 22% Brkt	6.23%	\$469,000	\$5,449,000	\$8,510,000
☐	Roth Conversions below IRMAA Brkt 2	6.27%	\$474,000	\$5,443,000	\$8,504,000
☐	Roth Conversions below IRMAA Brkt 3	6.03%	\$468,000	\$5,449,000	\$8,404,000
☐	Roth Conversions below IRMAA Brkt 4	5.96%	\$458,000	\$5,459,000	\$8,423,000
☐	Roth Conversions to fill 24% Brkt ☆	5.96%	\$455,000	\$5,462,000	\$8,442,000
☐	Roth Conversions to fill 32% Brkt	6.1%	\$463,000	\$5,454,000	\$8,480,000
☐	Roth Conversions below IRMAA Brkt 5	6.37%	\$482,000	\$5,436,000	\$8,542,000
☐	Roth Conversions to fill 35% Brkt	6.65%	\$502,000	\$5,415,000	\$8,569,000

PROBLEM 2: UNCERTAINTY

We do not know the tax system 20 years from now.



PROBLEM 3: PRESENT TAX PAIN & PSYCHOLOGY



PROBLEM 3: PRESENT TAX PAIN & PSYCHOLOGY



Roth Conversions to fill 24% Brkt

— vs —

Taxable, Tax-Deferred, Tax-Free



Average Tax Rate

Saves
7.5%

Roth Conversions to fill
24% Brkt

6%

vs

Taxable, Tax-Deferred,
Tax-Free

13.5%

Total Taxes

Saves
\$819,000

Roth Conversions to fill
24% Brkt

\$455,000

vs

Taxable, Tax-Deferred,
Tax-Free

\$1,274,000

Total Net Income

Goes up
\$819,000

Roth Conversions to fill
24% Brkt

\$5,462,000

vs

Taxable, Tax-Deferred,
Tax-Free

\$4,644,000

Net Legacy

Goes up
\$305,000

Roth Conversions to fill
24% Brkt

\$8,442,000

vs

Taxable, Tax-Deferred,
Tax-Free

\$8,137,000

PROBLEM 3: PRESENT TAX PAIN & PSYCHOLOGY

 Taxable, Tax-Deferred, Tax-Free — vs — Roth Conversions to fill 24% Brkt 

Average Tax Rate

Costs
7.5%

Taxable, Tax-Deferred,
Tax-Free

13.5%

vs

Roth Conversions to fill
24% Brkt

6%

Total Taxes

Costs
\$819,000

Taxable, Tax-Deferred,
Tax-Free

\$1,274,000

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Roth Conversions to fill
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\$455,000

Total Net Income

Goes down
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\$8,137,000

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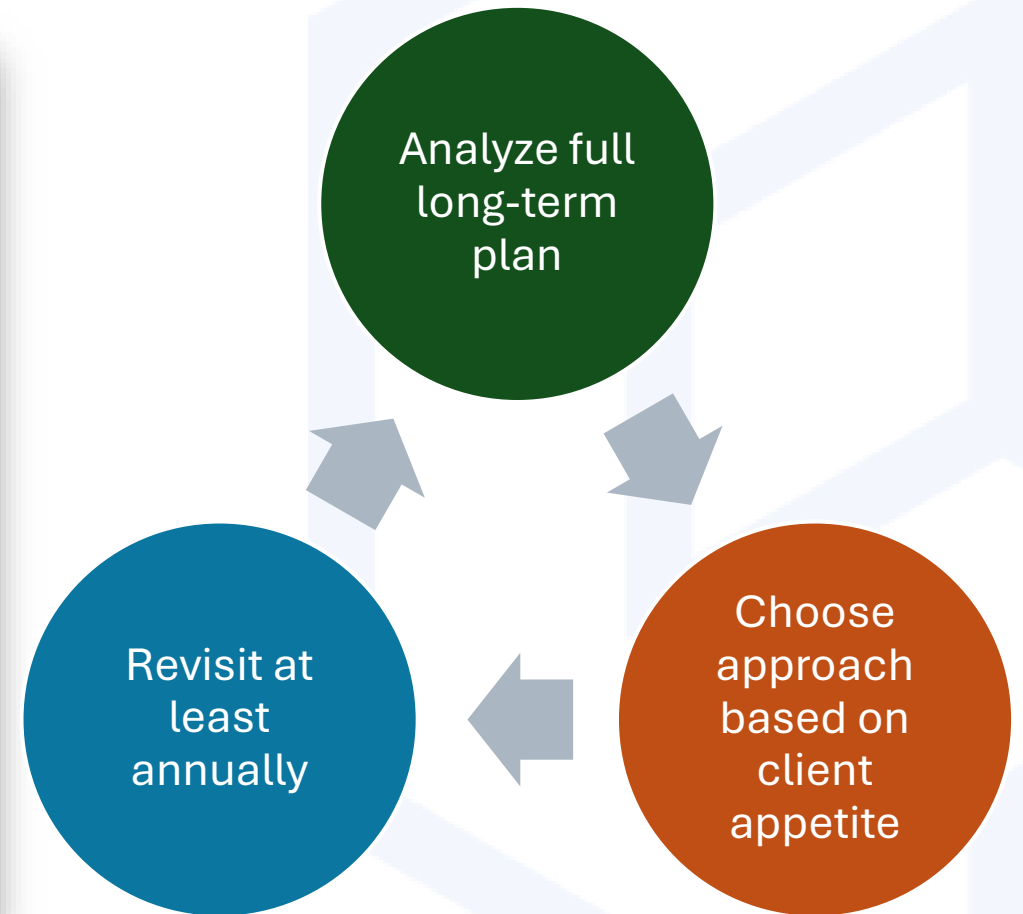
\$8,442,000

| NOT AN ANSWER... A PROCESS

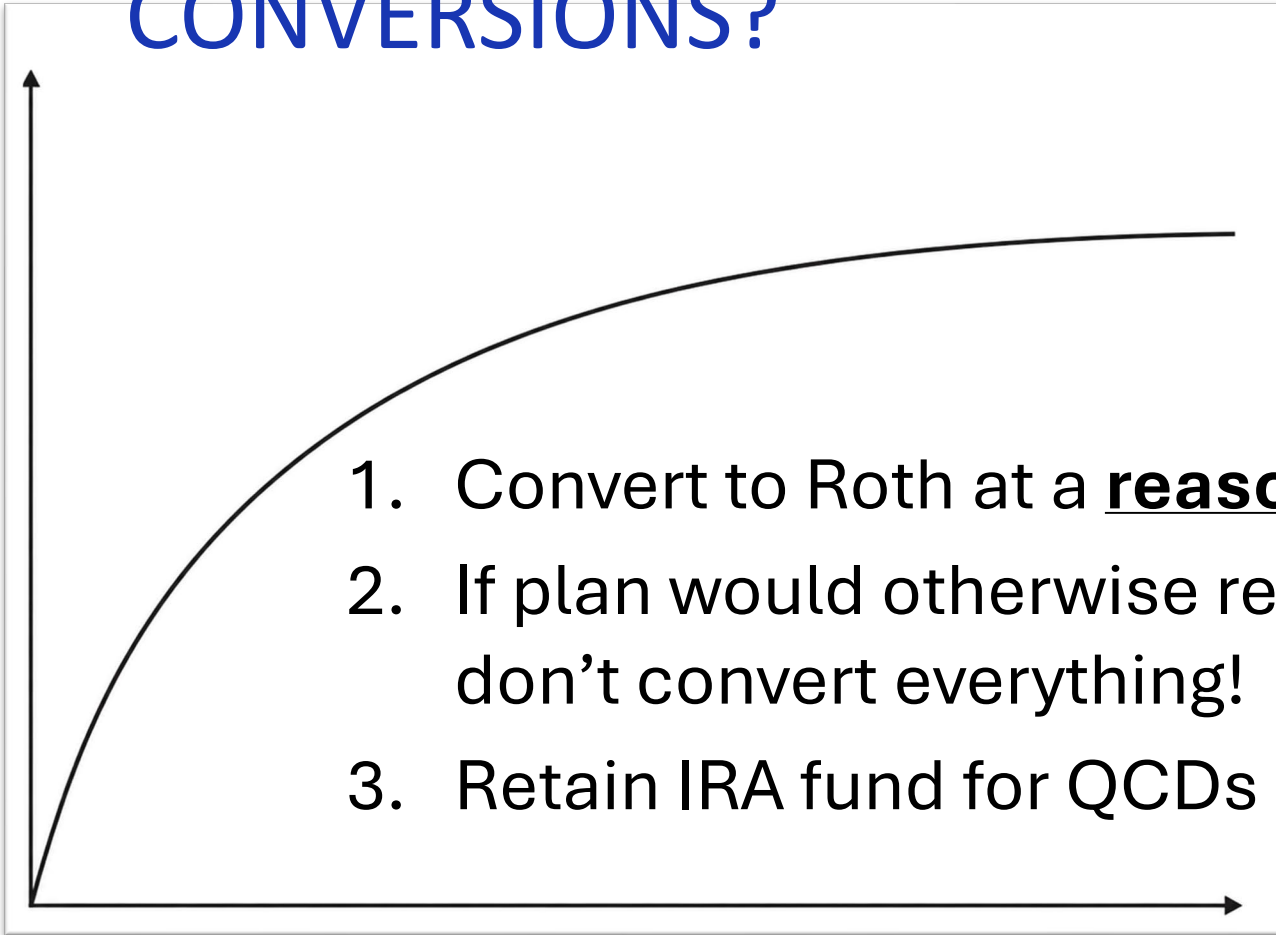
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Don't fixate on precision and a single answer. Look for patterns and trends and reasonable ways forward.



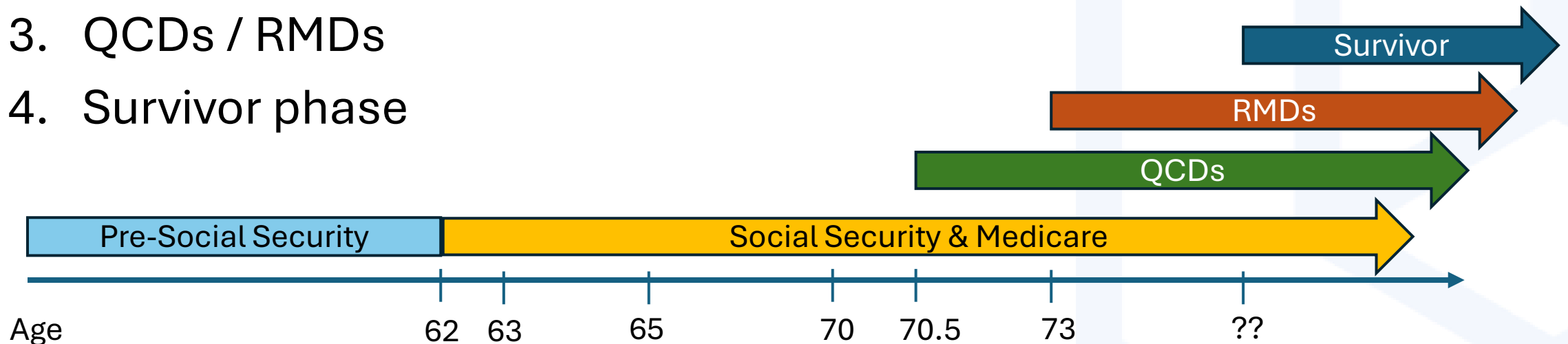
WHERE IS THE TAX VALUE WITH ROTH CONVERSIONS?



1. Convert to Roth at a **reasonable rate**, given the plan
2. If plan would otherwise result in 0% tax in later years, don't convert everything!
3. Retain IRA fund for QCDs at age 70.5+

KNOW THE TAX LIFE-PHASES

1. Pre-Social Security
2. Medicare / Social Security
3. QCDs / RMDs
4. Survivor phase





TACTICAL TAX-SMART DISTRIBUTION PLANNING

| THE CLIENT REQUEST

“I need \$50,000. Can you sell some things and send me a check?”

| THE ADVISOR TASK

- They asked for \$50k, but do I need to gross this up for taxes?
- Which accounts should they tap / not tap?
- Which holdings should they sell / not sell?
- Should they sell high-basis stock in taxable accounts?
- Should they harvest losses to offset gains?
- Should they harvest gains to book 0% capital gains and reset basis?

| THE ADVISOR TASK

- What are the tax consequences of this action?
- Could this lose them some deductions or credits?
- Should they withdraw from Roth accounts to control AGI, MAGI, or taxable income and avoid entering new Medicare IRMAA brackets, income tax bracket, or to avoid losing tax or ACA credit advantages?
- Should they take from tax-deferred accounts?
- If so, what withholding levels should they set?
- Should they use standing withholding orders or change them?
- Are there RMDs still to be taken this year that should be handled now as part of this withdrawal?

| THE ADVISOR TASK

- Is there an opportunity to do charitable giving to offset some of the tax impacts of this withdrawal?
- Are there federal or state estimated tax payments to be made?
- Will they meet safe harbor provisions or could this cause tax penalties and interest?

| WHAT ADVISORS THINK

“HOW DO I GET THIS RIGHT?!?”

| WITHDRAWAL PLAN SHOULD BE...

INVESTMENT-
SMART

TAX-SMART

PLAN-SMART

| INVESTMENT-SMART

- Follow the investment policy statement (IPS), if there is one
- Exclude from the withdrawal any shares or holdings that should be held (not sold)
- Exclude from withdrawal any accounts that are not to be tapped (e.g., “Take the money from John’s accounts, not Mary’s”)
- Good advice can lead to better net-of-tax returns

“ ‘Gross-of-tax returns’ is a vanity metric ”

| TAX-SMART

Design a withdrawal plan that is aware of:

- Tax thresholds / Deduction and credit phase-outs
- Interaction of different parts of the tax system (e.g., ordinary and LTCG income)
- Medicare IRMAA (2 years in future)
- ACA Credits
- Social Security taxability
- Tax loss harvesting
- Tax gain harvesting (in 0% bracket)
- Safe harbor rules
- Withholdings and estimated tax payments

| IMPACTS OF TAX-SMART INVESTING

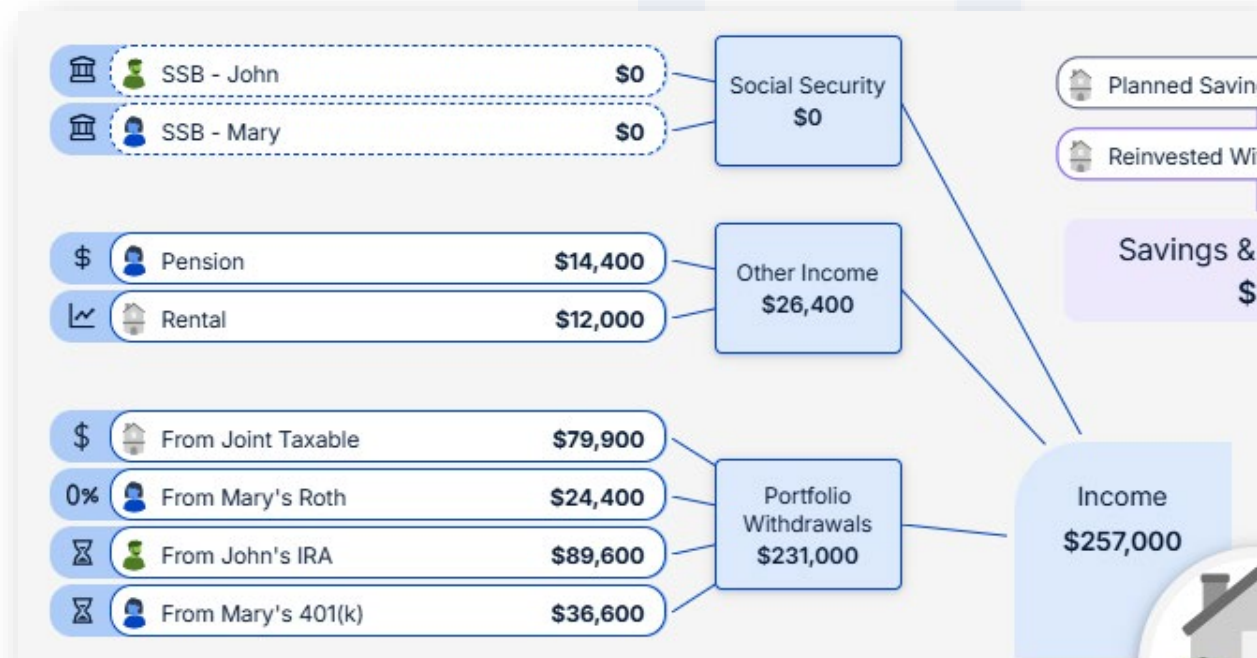
	Potential Impact*	Reference
Asset Location	Up to 0.30%	Vanguard
Tax loss harvesting	0.4% to 0.8%	Fin. Analysts Journal [FAJ 2]
Direct indexing TLH	1%+ in some cases	J. of Beta Inv. Strategies/AQR
Withdrawal Sequencing	Up to ~1.2%	Vanguard, Kitces.com

** Not necessarily additive.*

PLAN-SMART

Design a withdrawal plan that is aware of:

- Other non-portfolio income expected this year (and their tax consequences)
- Other withdrawals planned this year, including from where (tax consequences)
- RMDs
- Medicare timing
- Social Security timing
- Prior year AGI (for safe harbor)



WITHDRAWAL OPTIMIZATION

Recipe

[Expand All](#)

Account	Withdrawal	Federal Withholding	NJ Withholding	Net of Withholding
Joint Taxable Taxable	\$50,000	—	—	\$50,000
John's Inherited IRA Inherited traditional	\$75,472	\$15,094 (20.0%)	—	\$60,378
Total	\$125,472	\$15,094	\$0	\$110,378
Estimated tax payments				(\$10,378)
Net Total				\$100,000

Making and documenting a smart withdrawal plan can save clients and advisors a lot of pain.

Pro Tip: Leave some margin for error



Tax Actions

- A total of \$15,094 will be withheld from these withdrawals.
- Make a \$2,506 federal estimated tax payment (Form 1040-ES) by Jan 15, 2027.
- Make a \$7,872 NJ estimated tax payment (Form NJ-1040-ES) by Jan 15, 2027.

HOLDING	TOTAL HOLDINGS		THIS SALE		
	BALANCE	BASIS	PROCEEDS	REALIZED GAIN	GAIN %
AAPL · Apple Inc.	\$948,660	\$900,000	\$10,000	\$513	5%
C · Citigroup Inc. · loss	\$279,140	\$300,000	\$40,000	(\$2,989)	-7%
Total	\$1,227,800	\$1,200,000	\$50,000	(\$2,476)	

| WHO DOES WITHDRAWAL OPTIMIZATION HELP?

Clients who...

- Have investments in multiple account types (IRA, Roth, taxable, etc.), or...
- Have embedded/unrealized capital gains, or...
- Have unrealized capital losses, or...
- Have RMDs, or...
- Are within the progressive marginal rate zone, or...
- Have ACA credits or Medicare (or will have Medicare in 2 years or less), or...
- Are taking Social Security, or...
- Are charitably inclined

| WHO DOES WITHDRAWAL OPTIMIZATION NOT HELP?

Clients who...

- Have investments in only IRAs/401(k)s or only in Roths, or...
- Do not pay taxes because income is so low (even with the extra withdrawal)



CONCLUSIONS

| TAKE-AWAYS FOR STRATEGIC PLANNING

- The ‘taxable, tax-deferred, tax-free’ rule of thumb is often a bad idea
- A current low tax bill might be a sign of a missed planning opportunity
- Pay attention to which ‘tax life-phase’ a client is in
- Don’t focus on one tax rate alone. Consider the whole picture
- Forward projections cannot hope to be exactly correct, so don’t sweat the precision in a decades-long plan.
- Client preferences and ability to pay taxes matter

| TAKE-AWAYS FOR TACTICAL PLANNING PLANNING

- *Ad hoc* withdrawals are a key place where after-tax returns are locked in
- Out-of-plan withdrawals are common, but few have a good process for making sure they are done with investments, taxes, and the overall plan in mind.
- Withdrawal optimization requires a detailed plan of the current year's income
- This is a place where more precision is possible, but leave some margin for error!



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