Financial Concepts and Strategies to Consider

1. Asset Location

Overview: Tax efficiency depends on where you hold your investments. Tax-efficient assets like ETFs and index funds belong in taxable accounts due to their low taxable distributions. Tax-inefficient assets like REITs and bonds are better suited for tax-advantaged accounts, such as IRAs or 401(k)s.

Example: Holding a REIT fund in a taxable account means dividends are taxed as ordinary income (up to 37%). Instead, place the REIT in an IRA to defer taxes until withdrawal while keeping an S&P 500 index ETF in your taxable account to benefit from lower qualified dividend tax rates (e.g., 15%).

2. Tax-Efficient Withdrawal Strategies

Overview: A smart withdrawal plan reduces taxes and extends portfolio longevity in retirement. Begin by drawing from taxable accounts, then tax-deferred accounts like traditional IRAs or 401(k)s, and finally Roth accounts. This approach avoids high tax brackets later in life while maximizing tax-free growth in Roth accounts.

Example: A retiree with $1M in taxable accounts, $1M in a traditional IRA, and $500K in a Roth IRA withdraws from taxable accounts first while converting some IRA funds to Roth accounts during low-tax years. This lowers future required minimum distributions (RMDs) and keeps the Roth account compounding tax-free.

3. Charitable Contributions with Appreciated Stock

Overview: Donating appreciated securities, rather than cash, avoids capital gains taxes while providing a full tax deduction for the market value of the donation. This strategy is especially useful when rebalancing or supporting charities.

Example: Donating $15,000 of a tech stock purchased for $5,000 avoids $10,000 in capital gains (saving $1,500 in taxes at a 15% rate). You also receive a $15,000 tax deduction, optimizing your tax situation while supporting a cause.

4. Backdoor Roth IRA Contributions

Overview: For high-income earners who exceed Roth IRA income limits, the backdoor Roth strategy offers a workaround. Contribute to a traditional IRA, then convert it to a Roth IRA. If the contribution was non-deductible and you have no other traditional IRA balances, the conversion is nearly tax-free.

Example: You earn $200,000 (above the Roth income limit), contribute $6,500 to a traditional IRA, and immediately convert it to a Roth IRA. The $6,500 grows tax-free for decades, even though you weren't eligible for direct Roth contributions.

5. Health Savings Accounts (HSAs) as Retirement Tools

Overview: HSAs offer triple tax advantages: contributions are pre-tax, investments grow tax-free, and withdrawals for medical expenses are tax-free. After age 65, withdrawals for non-medical expenses are taxed like a traditional IRA. By investing rather than spending early, HSAs can become a powerful retirement tool.

Example: Maxing out an HSA ($8,300 family limit in 2024) and investing it for 20 years at a 7% annual return grows the account to $346,000. You can withdraw tax-free for medical expenses or pay ordinary income tax for other needs after 65.

6. 529 Plan to Roth IRA Conversion

Overview: Leftover 529 funds can now be rolled into a Roth IRA for the beneficiary (effective 2024), subject to a lifetime cap of $35,000 and annual Roth contribution limits. The 529 must have been open for at least 15 years, and recent contributions are excluded from rollovers. This flexibility makes 529 plans an attractive option, even if not fully used for education.

Example: A 529 plan grows to $75,000 after funding a child's education, leaving $40,000 unused. You roll $35,000 into their Roth IRA over several years, converting educational savings into tax-free retirement funds.