A RETIREMENT INSTITUTE GUIDE

Asset Location, Location, *Location*

In real estate it's location, location, location. In retirement, it's which of three tax columns your money calls home.

WELCOME

Knowledge first. Always.

The Retirement Institute exists to help Americans approaching and living in retirement make clear, confident, well-informed financial decisions — without the pressure of a sales pitch.

This is the third guide in our Tax-Free Retirement Series, part of a growing library of educational resources built to put real knowledge — and real control — back in your hands.

In real estate, the value of a property comes down to three things: location, location, location. Your retirement savings work much the same way. *How much* you've saved matters — but *where* it's located, in tax terms, can matter just as much to what you actually get to keep and spend.

Every account you own lives in one of three "tax columns." This guide walks through all three — their real advantages and their real drawbacks — and why the right balance among them is one of the most overlooked decisions in retirement.

BEFORE YOU BEGIN

This guide is for general education only. It is not personalized financial, tax, or legal advice, and no advisor-client relationship is created by reading it. Examples are illustrative and simplified; tax rates and rules change. Please consult a qualified tax or financial professional before acting. (Full disclosures appear at the end.)

INTRODUCTION

Three columns. *One question.*

In the financial world, every dollar you've saved sits in one of exactly three tax "columns." There is no fourth. Knowing which column your money lives in — and how the three work together — is the heart of what planners call **asset location**.

Column 1

Taxable

Bank accounts, CDs, bonds, brokerage, mutual funds. Highly liquid — but taxed along the way.

Column 2

Tax-Deferred

401(k)s, IRAs, 403(b)s, 457s. Taxes are delayed — which we sometimes call *tax procrastination*.

Column 3

Tax-Free

Roth accounts and properly structured cash-value insurance (LIRP). Tax-free access, with no collateral damage.

> Each column has genuine strengths and genuine weaknesses. The goal isn't to crown a winner — it's to understand the trade-offs well enough to build the right **balance** for your life.

Over the next few pages we'll give each column a fair hearing: what it does well, what it costs you, and where it belongs in a retirement built to last.

NUMBER 1 · COLUMN ONE

01

The taxable column

This is the money you can reach at any time: bank and money-market accounts, CDs, bonds, brokerage accounts, and mutual funds. Its great strength is **liquidity**. That makes it the natural home for your emergency fund and short-term goals — a car, a down payment, next year's vacation.

The drawback is in the name: it's *taxable*. Interest, dividends, and capital gains are taxed as you go, and paying tax along the way steadily erodes compounding. Consider an exaggerated illustration: double a single dollar 20 times and you'd have over a million. Now pay tax on each doubling, and watch what's left:

TAX TAKEN ON EACH GAIN	VALUE AFTER 20 DOUBLINGS
None (tax-free growth)	**$1,048,576**
20%	**~$127,500**
25%	**~$72,600**
30%	**~$40,600**

Look hard at that first taxed row. A 20% bite each year doesn't trim a little off the top — it erases more than **$900,000** of the result. **Nearly 90% of the ending balance is gone** — not to a market crash, not to a bad decision, but purely to taxes paid along the way. Raise the rate to 30% and about **96% disappears**. No one doubles their money 20 times — the example is deliberately extreme — but the lesson holds at any scale: paying tax as you go doesn't nick your returns, it guts them. That drag is exactly what the next two columns are designed to defer or avoid.

> *A 20% tax along the way didn't cost 20% of the result. It cost nearly 90% of it.*

NUMBER 2 · COLUMN TWO

02

The tax-deferred (tax-procrastination) column

This is where most Americans hold the bulk of their retirement savings: 401(k)s, 403(b)s, 457s, traditional IRAs, SEP and SIMPLE IRAs — the pre-tax accounts. The appeal is real. Contributions are pre-tax, often with an employer match, and because taxes are deferred, the account can grow larger than it otherwise would. On the surface, it's hard to beat.

Beneath the surface, the deferral comes with real costs — which is why we often call it the tax-*procrastination* column:

- **You're betting taxes will be lower later.** Given the nation's debt and demographic pressures, is it reasonable to assume rates will fall? Deferring a cost to a time when it may be higher — and you have less control — is a meaningful gamble.
- **Your biggest deductions fade in retirement.** The mortgage is paid off, the kids are grown, and you're no longer making pre-tax contributions (you're withdrawing). The three deductions that sheltered you while working largely disappear — right as rates may be climbing.
- **Withdrawals create collateral damage.** Distributions can make your Social Security taxable, trigger IRMAA surcharges on Medicare, and pull capital gains into taxation that wouldn't otherwise exist. The common thread: each of these is largely *caused* by income from qualified, pre-tax accounts — and each is largely *avoidable* with proper planning.

That first point deserves more than a shrug, because the industry repeats the opposite as gospel. The evidence cuts the other way. Today's federal tax rates remain historically low — well below the 70% top rate of the 1970s or the 90%-plus of the 1950s. The Congressional Budget Office projects federal debt climbing to record levels in the decades ahead, and the Social Security and Medicare trustees project funding shortfalls in the 2030s — pressures that point toward higher taxes, not lower. And many diligent savers never reach that promised lower bracket at all: once RMDs begin and Social Security becomes taxable, retirement-era marginal rates can actually *rise* — a documented effect researchers call the "tax torpedo"[1] — with IRMAA surcharges on Medicare stacking on top. Put it together — fewer deductions, sustained upward pressure on tax rates, and the voluntary taxes that pre-tax withdrawals trigger on Social Security and Medicare — and the idea of an overall *lower* tax burden in retirement looks highly unlikely, especially for those who were most diligent during their accumulation years.

> *Procrastinate a problem — in health, in relationships, in taxes — and it often grows. Deferred taxes are no exception.*

03

NUMBER 3 · THE HIDDEN COST

The pre-tax penalty

There's one more cost of the tax-deferred column that almost no one talks about — the other side of the pre-tax equation.

Start with how investment gains are normally taxed. Sell an investment you've held *one year or less* and the profit is a **short-term capital gain**, taxed at your ordinary income rates — the highest there are. Hold it *longer than a year* and it becomes a **long-term capital gain**, taxed at preferential rates that are usually far lower. That long-term break is one of the best deals in the tax code.

Now here's the catch. The investments inside a 401(k) or traditional IRA can be held for years — decades, even. Do those gains qualify for the lower long-term rate when you withdraw them? **No.** Every dollar that comes out of a pre-tax account is taxed as ordinary income — as if it were *all* short-term — no matter how long you held the underlying investment.

That's the deal you accept in exchange for the upfront deduction and tax-deferred growth. It isn't all bad — but it's rarely disclosed, and it's a real cost worth weighing.

> *Decades of patient growth, taxed at the highest rate the moment you withdraw it. That's the pre-tax penalty.*

NUMBER 4 · COLUMN THREE

04

The tax-free column

The third column holds the only two retirement tools whose income is generally tax-free: **Roth accounts** (Roth IRA and Roth 401(k)) and **properly structured cash-value life insurance**, often called a LIRP. There's a trade-off going in — contributions are made with after-tax dollars, so there's no deduction today — but what you gain on the other side is substantial:

- **Tax-free access and distributions.** Qualified withdrawals come out without adding to your taxable income.
- **Potentially greater liquidity and flexibility** than the tax-deferred column, with no required minimum distributions on Roth IRAs.
- **No collateral damage.** Because this income generally doesn't raise your MAGI, it doesn't tax your Social Security, doesn't trigger IRMAA, and doesn't push your capital gains into higher tax — provided your income stays under the relevant thresholds, which holding assets here helps you do.

You pay the tax once, on the way in, and then the account is largely insulated from the future — from rising rates, from RMDs, and from the chain reaction that pre-tax withdrawals can set off.

> *You trade a deduction today for control tomorrow — and control, in retirement, is worth a great deal.*

THE BOTTOM LINE

The right balance keeps the gold.

No single column is the answer. Each one earns its place. The taxable column gives you liquidity for life's near-term needs. The tax-deferred column offers an upfront deduction and an employer match. The tax-free column delivers control, clean income, and freedom from collateral damage.

The real skill isn't picking a winner — it's **balance**. You've surely heard how important it is to diversify among asset classes — stocks, bonds, real estate — and that advice is usually sound. Far less is said about **tax diversification**: spreading your savings deliberately across all three tax columns. Yet it is every bit as important. It hands you something powerful in retirement — the ability to choose *which* dollars to spend each year, and therefore how much tax you pay. The ideal mix is different for everyone, shaped by your income, your goals, and your stage of life.

TWO HONEST QUESTIONS WORTH SITTING WITH

- *Do you know what percentage of your savings sits in each of the three columns today?*
- *Is your tax-free column large enough to give you real control over your income — and your taxes — in retirement?*

There is a right balance for everyone. Finding it is one of the most consequential decisions in retirement planning — often the difference between golden years that keep their shine and ones that turn blue. This guide pairs naturally with its companions, *8 Keys to Roth Conversions* and *How to Get Your Social Security Tax-Free*. Building your balance is a conversation worth having with a qualified professional.

About The Retirement Institute

The Retirement Institute is a non-profit dedicated to financial education for Americans approaching and living in retirement. We publish clear, unbiased guides on the decisions that matter most — taxes, income, healthcare costs, and legacy — so that families can act from knowledge rather than fear. We don't sell products. We teach.

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The "doubling" illustration assumes a dollar doubling 20 times with the stated percentage of each gain withheld for taxes; it is deliberately exaggerated and not representative of any real investment return. Capital-gains treatment, ordinary-income rates, RMD rules, and the taxation of Social Security and Medicare premiums are set by federal law and subject to change. Long-term capital-gain rates apply to assets held more than one year held in taxable accounts; distributions from pre-tax accounts are taxed as ordinary income regardless of holding period.

"LIRP" refers to a properly structured cash-value life insurance policy; tax-advantaged access depends on the policy remaining in force and not becoming a Modified Endowment Contract, involves fees and charges, reduces the death benefit when accessed, and is not suitable for everyone. Roth qualified-distribution rules (including the 5-year rule and age 59½) apply. Consult a qualified tax or financial professional before acting.

[1] The outlook on future tax rates can be checked against public sources, including historical marginal tax-rate data (Tax Policy Center / IRS), long-term federal-debt projections (Congressional Budget Office, *Long-Term Budget Outlook*), the annual reports of the Social Security and Medicare Boards of Trustees, and financial-planning research on the taxation of Social Security benefits — the “tax torpedo.” Projections are updated periodically, reflect assumptions that may change, and are not guarantees of future tax policy.