

Retirement Blueprint

Episode 7

Hidden Tax Traps in Retirement

Transcript

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When most people think about Social Security, they think about income. They think about a check showing up in the mail—or these days, in their bank account—every month.

It feels simple, predictable, and safe.

But here's what most people don't realize:

Up to 85% of your Social Security benefits could be taxed—not because you did anything wrong, but because of how your other income interacts with it.

And the real kicker?

The thresholds that determine those taxes haven't changed since 1983.

Four decades later, we're living in a completely different economy—yet we're still playing by the old numbers.

So today, we're going to talk about what I call hidden tax traps—how Social Security interacts with the rest of your retirement income, how taxes quietly eat into your benefits, and what you can do to keep more of what's rightfully yours.

Because financial freedom isn't just about earning more—it's about keeping more.

Let's start with the basics.

Social Security taxes are based on something called provisional income.

Now, this isn't a term you'll see on your tax return.

It's a behind-the-scenes calculation the IRS uses to decide how much of your benefits are taxable.

Here's the formula:

Provisional income = your adjusted gross income + any tax-free municipal bond interest + half of your Social Security benefits.

So if you're drawing income from IRAs, selling investments, or earning interest from bonds, all of that adds up.

Once that total crosses \$25,000 for an individual or \$32,000 for a couple, up to 50% of your Social Security becomes taxable.

Cross the next threshold—\$34,000 for individuals or \$44,000 for couples—and up to 85% of your benefits can be taxed at ordinary income rates.

Think about that.

These thresholds were set when a gallon of gas cost less than a dollar and the average income was half of what it is today.

Yet they've never been indexed for inflation.

That means more retirees are being pulled into taxation every single year simply because their cost of living or portfolio income has grown.

Now, to be clear—this doesn't mean you're paying 85% of your benefit in taxes. It means up to 85% of it can be included in your taxable income.

But the effect is the same:

Less money in your pocket, and more going to the IRS.

And it can be especially painful when you've spent your whole life saving diligently—only to realize that every withdrawal you take could make your Social Security less tax-efficient.

The solution starts with understanding that your income sources are connected. How and when you take money from different accounts directly affects how much tax you pay on your benefits.

Let me tell you about John and Lisa.

They were both retired executives in their mid-60s, enjoying the fruits of decades of hard work.

They had solid investment portfolios, healthy savings, and both started Social Security at 66.

As John said, "We've earned it, so we might as well get it started."

When they came to me, they weren't looking for a Social Security plan—they were looking for a tax plan.

John had noticed their tax bill kept creeping up, even though their spending hadn't changed.

When we dug into their return, the cause became clear:

85% of their Social Security was being taxed.

Here's why:

They were taking about \$150,000 a year in IRA withdrawals to cover expenses and travel.

Because IRA distributions count as ordinary income, those withdrawals pushed their provisional income well above the top threshold.

So not only were they paying income tax on their IRA withdrawals—but that income also made their Social Security more taxable.

It's a double tax hit—what I call tax stacking.

We built a new plan.

The next year, they reduced their IRA withdrawals and instead drew from their after-tax brokerage accounts—money that had already been taxed years before.

We also completed partial Roth conversions in earlier retirement years when their marginal tax rate was lower.

Within two years, we cut their taxable Social Security from 85% to roughly 40%.

Their total tax bill dropped by \$12,000 per year.

And because their adjusted gross income fell, they also avoided the Medicare premium surcharge known as IRMAA.

Lisa joked, "We didn't make a penny more, but somehow we feel richer."

Exactly—because it's not what you make, it's what you keep.

That one conversation changed how they viewed retirement forever.

Here are the three biggest mistakes that cause retirees to fall into the Social Security tax trap—and the good news is, they're all preventable:

Mistake #1: Claiming too early while taking IRA withdrawals

When you claim at 62 or 63, you're often still drawing from pre-tax accounts.

Those withdrawals inflate your provisional income and make your benefits taxable.

It's often better to live off savings or bridge income first and delay Social Security until it aligns with your tax strategy.

Mistake #2: Ignoring Roth conversion opportunities

The years between retirement and starting Social Security—often your early 60s—can be a golden window for tax planning.

Your income may be lower, meaning your tax bracket is lower too.

Converting part of your IRA to a Roth IRA during that time can reduce future required minimum distributions, lower your taxable income later, and help more of your Social Security remain tax-free.

Mistake #3: Forgetting about Medicare premiums

Your income doesn't just affect your tax bill—it also affects how much you pay for Medicare Part B and Part D.

Go even \$1 over certain thresholds, and you could pay hundreds more per month in premiums.

That's what we call a stealth tax—it doesn't show up clearly on your return, but it impacts your cash flow just the same.

Each of these mistakes happens because people treat retirement decisions in isolation—one at a time—instead of as an integrated system.

You don't need a finance degree to avoid them.

You just need a plan that looks at the full picture.

Let's talk about sequencing—the order in which you draw from different accounts in retirement.

Most retirees withdraw from whatever is easiest or most familiar.

But the sequence matters more than you think.

If you pull from your IRA and Social Security at the same time, your provisional income spikes.

If instead you use after-tax savings for the first few years and delay claiming, you can reduce taxable income and increase your future benefit.

Think of it like juggling three buckets of money:

Taxable

Tax-deferred

Tax-free

The art of retirement is deciding which bucket to tap—and when—to keep your tax burden low and your income steady.

For example, a retiree who spends from their Roth IRA or brokerage account early may be able to keep their provisional income under key thresholds for years—keeping their Social Security benefits nearly tax-free.

I once had a client say, “Glenn, this feels like cheating.”

And I laughed—because it's not cheating.

It's simply using the rules the way they were written.

Taxes aren't about being clever—they're about being coordinated.

The wealthiest retirees I know have one thing in common:

They don't make decisions in isolation.

They make decisions in sequence.

We spend so much of our lives focused on earning—earning promotions, earning returns, earning more income.

But once you step into retirement, the game changes completely.

The winners in retirement aren't the ones who earn the most—they're the ones who keep the most.

Social Security is designed to provide stability.

But taxes can quietly erode that stability if you're not paying attention to the fine print.

Understanding provisional income, coordinating your withdrawals, and timing your conversions aren't just financial tactics—they're freedom tactics.

Clients who retire most confidently are the ones who know exactly where their income is coming from, how it's taxed, and how long it will last.

They're not reacting to surprises in April—they're managing their income all year long.

So the next time you think about maximizing Social Security, don't just think about how to get the biggest check.

Think about how to keep most of it.

Because retirement isn't a game of chance—it's a game of coordination.

And when you master that game, you give yourself something more valuable than money:

Peace of mind.

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