



Managing Taxes Pre- and Post- Retirement:

A Guide for Higher Education Professionals

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This white paper explores tax planning strategies for **higher education professionals approaching retirement**. It offers insights into optimizing tax outcomes by leveraging various retirement accounts to accomplish ideal tax optimization, managing income in the years leading to and in retirement, and understanding the nuances of timing retirement.

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Introduction

Retirement brings significant changes, especially financial changes. For higher education professionals, the complexity is further increased with the professionals' ability to manage income via deferrals prior to retirement in various account types. As high-earning professionals, tax planning becomes increasingly more important, especially as retirement is on the horizon. This white paper aims to educate on various tax management strategies that may help to ensure a financially secure retirement.

Problem Statement

Higher education professionals face unique challenges in tax planning pre- and post-retirement. Without proper planning, these complexities can lead to missed opportunities and unnecessary financial stress due to unforeseen future tax liabilities.

Background/Context

Personal financial planning encompasses many diverse facets of financial life. Tax planning as a subset of personal financial planning is an area where expertise, attention to detail, and strategy can materially improve financial quality of life for individuals. Understanding the various accounts and benefits available to university professionals is crucial in the pursuit of comprehensive personal financial planning. Common account types include 403b accounts, TDAs, 457b deferred compensation plans, in addition to the widely used IRAs and Roth IRAs. Proper utilization of these accounts, along with tax planning coordination acumen, can significantly impact your tax situation.

Definitions

Defined Contribution Plan: A retirement plan where employees and/or employers contribute a fixed amount or percentage of paychecks into individual accounts for the benefit of the employee.

403b: A retirement plan for employees of public schools, tax-exempt organizations, and certain ministers, like a 401(k).

TDA/TSA/SRA: Tax-Deferred Annuity/Tax-Sheltered Annuity/Supplemental Retirement Annuity; retirement savings plans that allow pre-tax contributions and tax-deferred growth, often used in conjunction with 403(b) plans.

457: A deferred compensation retirement plan available to government and some non-profit employees.

IRA: Individual Retirement Account; a retirement savings account with tax advantages for individuals, offering tax-deferred or tax-free growth.

Roth: A type of IRA or 401(k) where contributions are made with post-tax dollars, but withdrawals in retirement are tax-free.

Pre-Tax: Contributions made to retirement accounts before income taxes are deducted, reducing taxable income for the year of the contribution.

Post-Tax: Contributions made to retirement accounts after income taxes have been deducted; does not reduce taxable income for the year of the contribution.

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Discussion

TAX PLANNING CONSIDERATIONS PRE-RETIREMENT

Maximize Deferrals in Three Categories

Most universities allow for salary deferral of up to \$65,000 in total across plans, plus employer contributions (i.e. pension or self-managed) plus age 60-63 extra catch-up if eligible. In some cases, within 3 years of retirement, the allowed amount can grow to \$81,500 of possible deferrals plus the additional mentioned above. Utilizing catch-up contributions to deferred compensation accounts like 457s can significantly enhance retirement savings and optimize tax brackets now and in retirement. Further discussion on 457s is included later in the paper.

Where you save is crucial as you develop your portfolio. An optimal approach is to save into three tax “buckets”:



This savings strategy gives you maximum flexibility as you look to transition. Typically, Roth savings would accumulate while your tax bracket is low, and/or you are young. Pre-tax savings would accumulate later when your tax bracket is higher, and you are closer to retirement. Taxable assets are the icing on this proverbial savings cake.

Roth Contributions – Increasing Taxes Now to Decrease Later

For many that come through our doors, the Roth “bucket” is often the smallest, or not in the equation at all. For some, this is due to the lack of knowledge around the salary deferral types offered by the employer—Pre-Tax is often the default, with post-tax, aka Roth, contributions being an ‘opt-in’ decision. Even if you have not accumulated into Roth yet, there are ways to ‘fill the bucket’. The simplest would be to begin Roth deferrals now into accounts already available to you like your supplemental 403b and 457 accounts.

If you have accumulated a substantial amount of assets in the pre-tax “bucket”, you may have a larger tax liability looming once required minimum distributions come into play at age 73 or 75. Couple those required distributions with Social Security income and the tax liability grows. Anecdotally, we have witnessed

individuals jump two tax brackets from their W-2 wages to their retirement income, simply due to the amount they had accumulated in pre-tax accounts and what was required to be distributed under Federal law at age 73. While increasing contributions to Roth now may increase your liability today, it may, in fact, decrease your tax liability over the long-term.

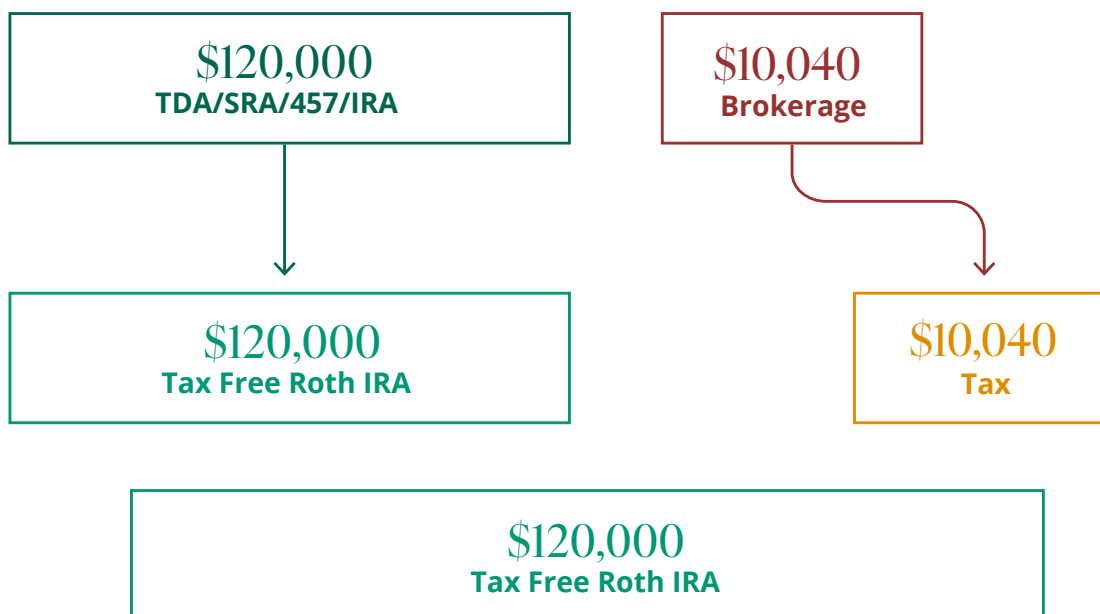
Another method to fill the bucket is the Roth Conversion strategy described below.

Roth Conversion – Maximizing Tax-Free Growth

Simply put, a Roth conversion is an action whereby assets previously categorized as pre-tax are now categorized as post-tax (aka Roth assets). With that change, taxes are due on the amount that is converted. While the taxes are paid immediately on the conversion, rather than on the withdrawal of pre-tax assets, the future growth and distribution of assets are tax-free. This may be advantageous for many reasons, namely the time to compound growth of tax-free assets, the ability to maximize tax brackets and smooth future tax liabilities, the opportunity to pass tax-free assets to beneficiaries as part of an estate plan, plus much more.

A minimal example of a Roth conversion is demonstrated visually on the following page.

In the example, let's assume you plan to retire before beginning Social Security. You have \$120,000 in pre-tax assets within a retirement account. The assets could be held in a TDA/TSA/SRA, 457, or IRA. You also have taxable assets outside of retirement and are generating no W-2 wages. You would have the ability to convert that \$120,000 in pre-tax assets to Roth assets via a Roth IRA conversion for a little more than \$10,000 in taxes. This allows for that \$120,000 to grow tax-free until you distribute or pass the assets on via your estate. This assumes lowest tax rates are applied and standard deduction is taken.



Timing Your Taxes: Your Retirement Date Does Matter

There are many nuances, and pitfalls, to consider when determining when to retire. Focusing specifically on tax implications, retiring at different ages can have different implications. Below are a few target ranges and what opportunities may be associated.

Retiring Before Age 65

Monitor your income closely around your retirement date to manage tax implications. For example, the Medicare Part B monthly surcharge is calculated utilizing the income from two years prior to the year the surcharge is assessed. This means that if you retire in 2026, your Medicare Part B surcharge is based on your 2024 income. As such, be aware of income levels in the year you turn 63 to avoid Medicare surcharge penalties if you retire before age 65.

Retiring After Age 65 but Before Age 73 (Or 75 if born after 1960)

Paying \$0 in taxes is a suboptimal outcome for most individuals, especially those with large pre-tax account balances. Retiring before RMD Age (73 or 75) gives you a window of opportunity to accelerate income and move funds into a Roth IRA from your Pre-Tax retirement accounts. This strategy can be enhanced by delaying Social Security to Age 70. While the Social Security benefits grow by 8% per year when delayed beyond full retirement age, you can accelerate income in the lowest tax brackets, optimizing your tax situation and maximizing optionality.

As already discussed, pay attention to income two years before retirement to avoid Medicare Part B surcharge penalties. When you do retire, a Medicare Challenge is an option to reduce or eliminate surcharges for previous years of high wage income, especially if you expect your taxable income to be lower going forward.

Retiring After Age 73 (Or 75 if born after 1960)

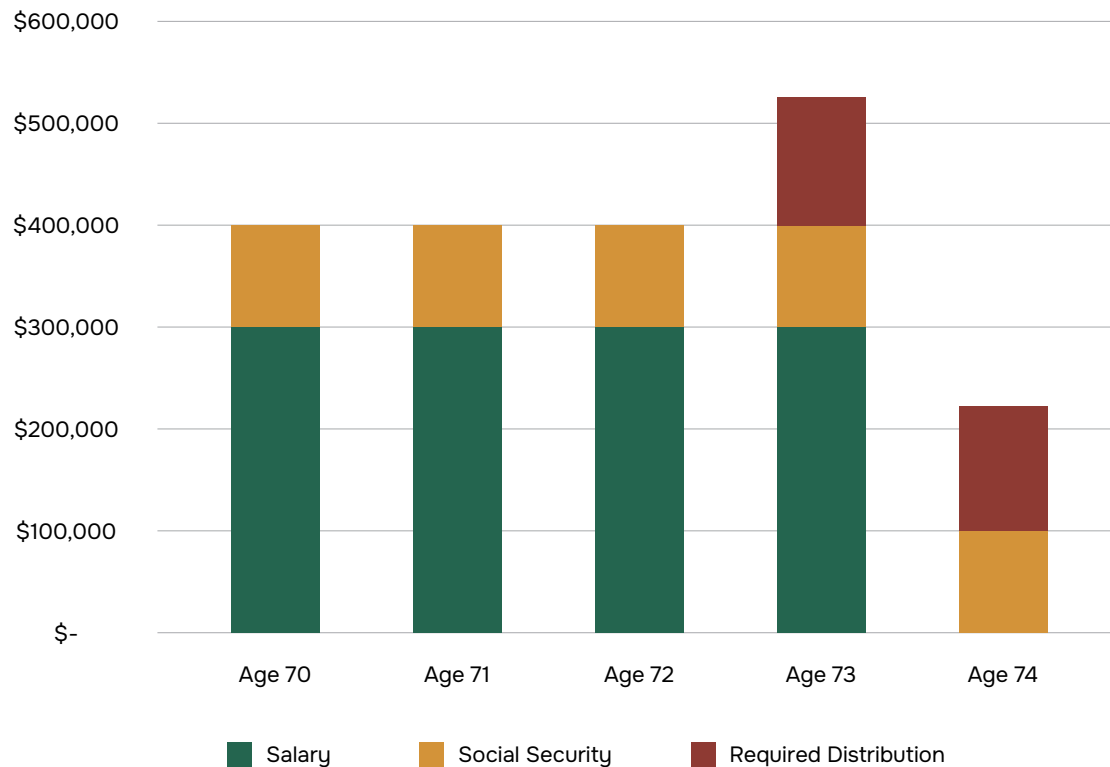
While ending your career on the last day of the year sounds like a sensible move, it may be one of the costliest mistakes you make. Retiring on January 1st rather than December 31st can help avoid immediate Required Minimum Distributions due to tax law surrounding the year you retire.

With employer sponsored retirement accounts, a minimum distribution is not required until after age 73 if the participant born in 1959 or earlier (or after age 75 if born in 1960 or later) is still working. However, current tax law requires anyone over the RMD age to take a distribution in the year of retirement from their employer sponsored retirement accounts even if the date is December 31st. Just delaying that retirement date by one day could save you thousands in tax liability.

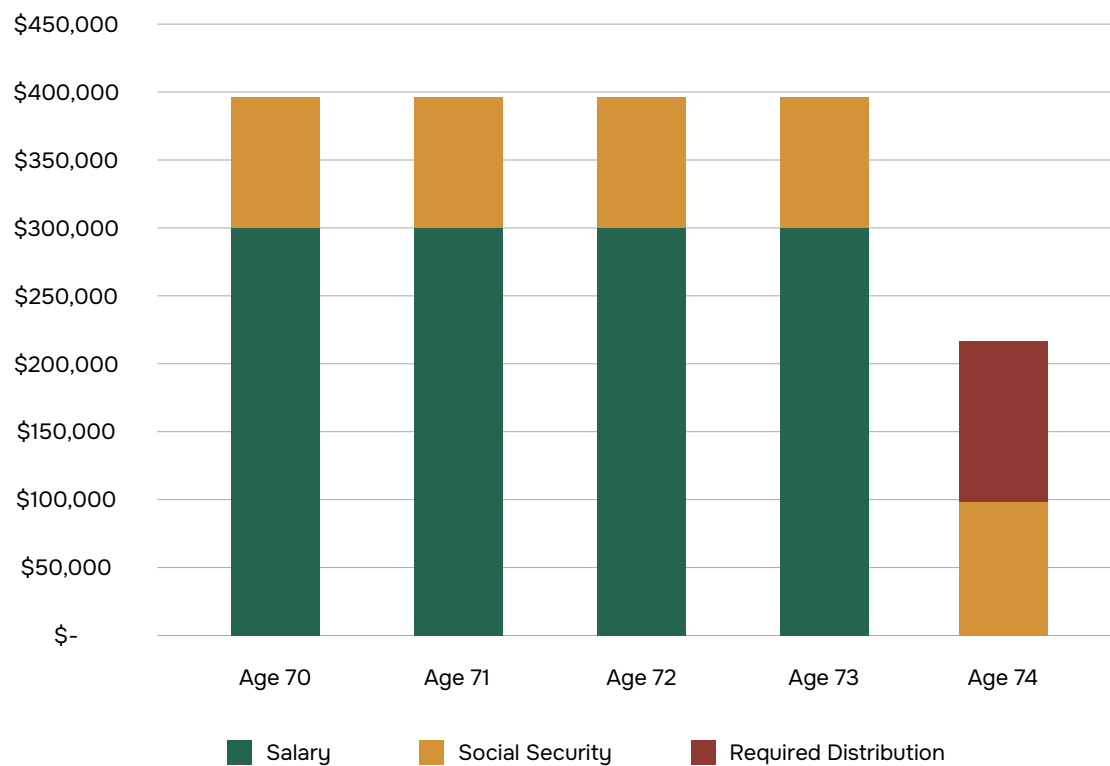
Below is a minimal example of this delay in retirement date:

In the example, Bob and Suzy have a combined income of \$300,000, in addition to Social Security of \$4,000 per month each. They are debating retirement and are considering two dates, December 31st of 2026 and January 1st of 2027. Bob and Suzy currently possess pre-tax retirement accounts totaling \$3,000,000 with a first year Required Minimum Distribution of approximately \$120,000. In the below graphs you will observe that by delaying retirement by one day, Bob and Suzy eliminate the tax liability on the additional \$120,000 that would have been required to be distributed. In their tax bracket, this is more than \$40,000 in tax savings.

If Bob and Suzy Retire December 31st of Year Age 73:



If Bob and Suzy Retire January 1st of Year Age 74:



Other Considerations - Small Decisions with Big Impact

Charitable Intent?

If you give to charity, consider moving funds to an IRA before December 31st of the year prior to your required distribution age so that you can give directly to charity and avoid paying taxes on pre-tax assets donated. If the charity is a 501c3, the IRS recognizes up to \$111,000 in donations that are paid directly from your IRA as a tax-free distribution that counts towards satisfying the required minimum distribution amount if 73 or over. If under RMD age, the distribution is still tax-free.

Optimizing Social Security Timing

Delaying Social Security to age 70 can allow for tax optimization by filling lower tax brackets through strategies like Roth conversions during years without wages. It can also enhance your income by up to 32% as the benefit grows by 8% per year that is delayed beyond your full retirement age.

457 Catch-up Contributions – A Way to Supercharge Retirement Savings

Deferred compensation plans like 457s are a great way to enhance savings beyond the ORP and TDA accounts. Something unique about 457 plans is that they often have a provision for a 'super-catch up' contribution prior to retirement. This provision allows a participant to contribute more than the maximum allowable contribution for three years prior to a retirement date. This additional contribution amount can supercharge savings, but also lower tax liability if the contribution is pre-tax. This often-missed opportunity is one of the best levers to pull when close to retirement to help lower taxes.

Conclusion

Effective tax planning is vital for a financially secure retirement. By understanding the unique challenges and opportunities available, higher education professionals can make informed decisions that significantly impact their financial future. Everyone's situation is unique, and while this white paper provides general information and education, consulting with a professional is not just recommended, it is essential. Our team at Briaud Financial Advisors is experienced in navigating these complexities and can provide tailored advice to optimize your tax planning strategy.

We invite you to [schedule a 30-minute consultation](#) with Briaud Financial Advisors to discuss your unique retirement planning needs. [Contact us](#) today to learn how we can help you achieve a tax-efficient retirement.

ABOUT

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