

The Components of the Retirement Income Engine

Your Money Matter | The Components of the Retirement Income Engine

In retirement, income is not derived from a single source. It is generated from multiple accounts, each with different characteristics and tax treatment.

At a high level, most retirement income is drawn from three types of accounts:

- Taxable accounts
- Tax-deferred accounts
- Tax-free accounts

These form the core components of what we describe as the **retirement income engine**

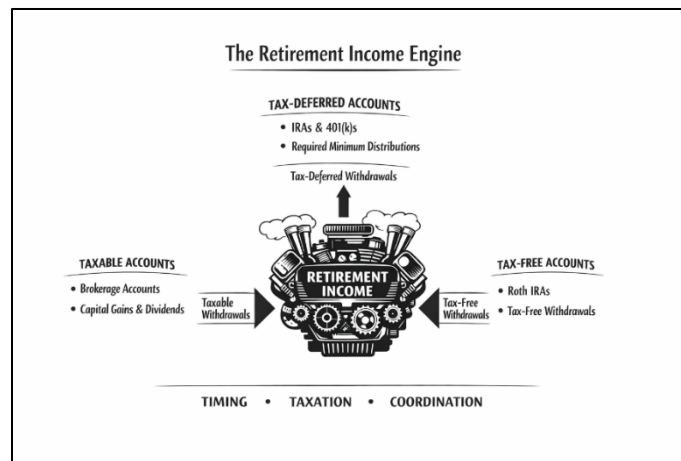


Figure 1 – The Retirement Income Engine

How different account types work together to generate retirement income

Taxable Accounts

Role

Flexible source of retirement income

How it is taxed

- Return of principal: not taxed
- Dividends and interest: taxable in the year received
- Capital gains: taxed when realized, often at preferential rates

Key characteristic

Provides control over the timing and amount of income

Considerations

- Subject to ongoing taxation
- Sensitive to market conditions and investment decisions

Tax-Deferred Accounts (IRAs and 401(k)s)

Role

Primary source of income for many retirees

How it is taxed

- Contributions typically made on a pre-tax basis
- Growth is tax-deferred
- Withdrawals are generally taxed as ordinary income

Key characteristic

Allows for long-term compounding, but creates future taxable income

Considerations

- Subject to Required Minimum Distributions (RMDs)
- RMDs increase over time as a percentage of the account balance
- May become a significant driver of taxable income in later years

Tax-Free Accounts (Roth Accounts)

Role

Strategic source of tax-free income

How it is taxed

- Contributions made with after-tax dollars
- Qualified withdrawals are generally tax-free

Key characteristic

Provides flexibility in managing taxable income

Considerations

- Not subject to RMDs during the owner's lifetime
- Can be used to manage tax brackets in later years
- Often valuable in legacy and estate planning

Key Insight

Retirement income is not determined by any single account.

It is shaped by how taxable, tax-deferred, and tax-free sources are coordinated over time.

How the Components Work Together

Individually, each account type has its own advantages and limitations.

However, retirement income is not generated in isolation.

It is the **interaction between these components** that ultimately shapes:

- how income is distributed over time
- how that income is taxed

- and how much flexibility remains in later years

In many cases, households hold all three types of accounts, yet withdrawals are not always coordinated across them.

Income may be drawn from a single source out of habit, convenience, or default rules, rather than as part of a broader structure.

Over time, this can lead to:

- higher taxable income in certain years
- reduced ability to manage tax brackets
- and less flexibility as income sources begin to layer

From Accounts to Structure

The purpose of understanding these components is not to determine a fixed order of withdrawal.

There is no single sequence that applies universally.

Instead, each account represents a different **lever** — one that can be used, adjusted, and coordinated as retirement unfolds.

The objective is not to follow a rule. It is to design a structure.

And it is this structure — rather than any individual account — that ultimately determines how retirement income behaves over time.

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