LOFTUS WEALTH STRATEGIES

Monthly Newsletter

Loftus Wealth Strategies
Michael Loftus
Managing Director
35785 Atlantic Ave.
Millville, DE 19967
302-251-8901 x102
PA - 484-331-6296
michael@loftuswealthstrategies.com
www.loftuswealthstrategies.com

December 2013

Should You Pay Off Your Mortgage During Retirement?

For many homeowners, paying off a mortgage is a financial milestone. This is especially true when you are retired. Not having the burden of a monthly mortgage payment during retirement can free up money to help you live the retirement lifestyle you've always wanted.

To pay off, or not to pay off: that is the question

Some retirees are lucky enough to have paid off their mortgage before they reach retirement. For others, however, that monthly obligation continues. If you are retired, you may be wondering whether you should pay off your mortgage. Unfortunately, there's no one answer that's right for everyone. Instead, the answer will depend upon a variety of factors and how they relate to your individual situation.

Return on retirement investments vs. mortgage interest rate

One way many retirees pay off their mortgage is by using funds from their retirement investments. To determine whether this is a good option for you, you'll need to consider the current and anticipated rate of return on your retirement investments versus your current mortgage interest rate. In other words, do you expect to earn a higher after-tax rate of return on your current retirement investments than the after-tax interest rate you currently pay on your mortgage (i.e., the interest rate that you're paying, factoring in any mortgage interest deduction you're entitled to)?

For example, assume you pay an after-tax mortgage interest rate of 4%. You are considering withdrawing funds from your retirement investments to pay off your mortgage balance. In general, you would need to earn an after-tax return of greater than 4% on your retirement investments to make keeping your money invested for retirement the smarter choice.

On the other hand, if your retirement funds are primarily held in investments that typically offer a lower rate of return than the interest rate you pay on your mortgage, you may be better off withdrawing your retirement funds to pay off your mortgage.

Additional considerations

As you weigh your options, you'll also want to consider these additional points:

- **Effect on retirement nest egg--** If you rely on your retirement savings for most of your income during retirement, you should generally avoid paying off your mortgage if it will end up depleting a significant portion of your retirement savings. Ideally, you should pay off your mortgage only if you have a small mortgage balance in comparison to your overall retirement nest egg.
- **Tax consequences--** Keep in mind that if you are going to withdraw funds from a retirement account to pay off your mortgage, there are some potential tax consequences you should be aware of. First, if you withdraw pretax funds from a retirement account, the amount you withdraw is generally taxable. As a result, you'll want to be sure to account for the taxes you'll have to pay on the amount you withdraw from pretax funds. Depending on your tax bracket, that could be a significant amount. In addition, if you take a large enough distribution from your retirement account, you could end up pushing yourself into a higher income tax bracket. Finally, unless you are 59½ or older, you may pay a penalty for early withdrawal.
- **Comfort with mortgage debt--** For many retirees, a monthly mortgage obligation can be a heavy burden. If no longer having a mortgage would give you greater peace of mind, give the emotional benefits of paying off your mortgage some extra consideration.