



To Convert OR Not To Convert?

CONVERTING A **TRADITIONAL IRA**
TO A **ROTH IRA** MIGHT BENEFIT
CERTAIN TAXPAYERS

Williams-Keepers LLC

■ CERTIFIED PUBLIC ACCOUNTANTS & CONSULTANTS

■ WINTER 2010

Starting in 2010, taxpayers of all income levels have the opportunity to convert amounts in a traditional IRA and certain other investment accounts to a Roth IRA. Prior to 2010, only taxpayers with modified adjusted gross income of \$100,000 or less had this opportunity. Also unique to 2010, any income recognized as a result of the Roth conversion can be deferred and recognized ratably in 2011 and 2012. These opportunities are prompting many of our clients to ask an important question – “Is a Roth conversion right for me?” There is no uniform answer, and a Williams-Keepers LLC advisor can help evaluate whether you might benefit from a Roth conversion.

The benefits of a Roth IRA

Like many other retirement plans, including 401(k) plans and traditional IRAs, the earnings within the account are tax-sheltered, meaning they are not subject to income tax while invested within the account. However, income tax is levied on withdrawals from these other plans, while withdrawals from a Roth IRA are generally not taxed.

One of the most important benefits is the flexibility that a Roth IRA provides. The owner of a traditional IRA must begin to make lifetime required minimum distributions (RMDs) after attaining 70½ years of age. Owners of Roth IRAs are not subject to this RMD requirement. Accordingly, the IRA owner has flexibility in determining when he or she takes withdrawals from the account. The ability to defer distributions enables investors to benefit from the tax-sheltered growth of the account.

The cost of conversion

The catch—and it’s a big one—is that the rollover to a Roth IRA will be fully taxed, assuming the rollover is being made with money that was deductible when contributed

to an IRA. For example, if you are in the 28 percent federal tax bracket and roll over \$100,000 to a Roth IRA from a regular IRA funded entirely with deductible dollars, you will owe \$28,000 in federal income tax. As a result, you will be paying tax now for the future privilege of tax-free withdrawals and freedom from the RMD rules.

Should I convert?

There is no uniform answer that can be given to this question. One cannot answer it without an intimate knowledge of you, your occupation, your family, and your future hopes and dreams. Your WK advisor can help you analyze whether you could benefit from a Roth conversion. In general, if any of the following circumstances apply to you, we recommend you strongly consider a Roth conversion.

- You have liquid assets outside your retirement funds with which to pay the income tax due on the rollover. Keep in mind that if you use retirement plan funds to pay the tax on the rollover, you will have less money available to accumulate in a tax-sheltered manner within the account.
- The tax rate you face in the future might go up. Many observers believe that tax rates for upper middle income and high income individuals will trend higher in future years. This likelihood makes the current income tax due on a Roth conversion more palatable.
- You can allow the IRA to grow for a long period of time without taking payouts. This will give you a chance to recoup via tax-deferred earnings the current income taxes you must pay on the rollover.
- You are willing to pay a tax price now for the opportunity to grow the account free of income tax and to pass the account to your children and grandchildren as a source of tax-free income.

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2010 conversions only: Deferred income recognition

Unique to 2010 conversions, the income on conversion can be deferred to 2011 and 2012. However, many taxpayers who chose to convert might benefit from paying the tax on conversion with their 2010 income tax return. Why? Keep in mind that, absent Congressional action, after 2010 the tax brackets above the 15 percent bracket will revert to their higher pre-2001 levels. That means the top four brackets will adjust as follows:

2010	2011	Increase
25.0%	28.0%	3.0%
28.0%	31.0%	3.0%
33.0%	36.0%	3.0%
35.0%	39.6%	4.6%

If you believe that there is a strong chance your tax rates will go up after 2010, you might consider paying the tax on the Roth rollover in 2010 instead of deferring it to 2011 and 2012.

How a WK advisor can help

It is important to consider your family's entire financial situation before you plan for a large rollover to a Roth IRA. A thorough understanding of your situation is essential to fairly evaluate the merits of a Roth conversion. There also are many details to consider, such as whether the amounts you are thinking of switching to a Roth IRA are eligible for the rollover, whether you can make rollovers from your employer-sponsored plan, and the tax impact of rolling over amounts that represent nondeductible as well as deductible contributions.

Our firm's broad service offerings in the areas of tax, estate, and small business succession planning places us in a unique position to help you to consider how a Roth conversion might fit within your overall financial plan and to navigate the mechanics of the conversion process.

Contact your WK advisor at (573) 442-6171 or (573) 635-6196 to discuss the pros and cons of conversion to a Roth IRA.



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