

New Rules for Roth IRAs Is a Roth Conversion Right For You?

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A little background: Money that you have in a traditional IRA can be converted to a Roth IRA. This is accomplished by paying the income taxes on the converted amount now. Paying the taxes now might seem contrary to conventional wisdom, however, there are many advantages to a Roth IRA. For example, the money grows tax-free, meaning you won't be taxed on any future qualified distributions from the account regardless of how much it has grown. Also, since you've already paid taxes on the amount you contributed or converted, the government won't benefit when you take distributions, therefore it doesn't require you to take distributions at age 70 ½ or thereafter.

Tax laws regarding Roth IRA conversions have changed. Currently, Roth IRA conversions are not allowed if your adjusted gross income exceeds \$100,000. Beginning in 2010, Roth conversions will be available to everyone regardless of income level. A Roth conversion, as mentioned above, is a taxable event. However, if the conversion is made in 2010 and completed by December 31st, you have the option of reporting the converted amount on your 2010 tax return, OR reporting half of the amount on your 2011 tax return and the remainder on your 2012 tax return. This ability to spread the taxes over **the subsequent** two years applies only to Roth conversions completed in 2010.

For higher wage earners, this may be a prime opportunity to convert money into a Roth IRA to enjoy tax-free growth. Remember, once you've paid taxes on the amount converted, you'll owe no taxes on future earnings as they are withdrawn. Also, while your heirs will be required to take distributions over their life expectancies when they inherit your Roth IRA, these distributions will be tax-free for them as well. A Certified Financial Planner™ can help you determine how a conversion might best be handled. In some cases, it might even be appropriate to involve your estate planning attorney to ensure that the strategy is consistent with your estate planning.

The rules require your Roth IRA to "age" for 5 years to be tax-free. This means that you must avoid taking a withdrawal from the Roth IRA for 5 years after conversion. The clock starts to tick on January 1st of the year in which you converted your Roth IRA. If you do take a withdrawal from your Roth IRA prior to meeting the 5 year rule, then you will owe taxes on any earnings that are withdrawn and, depending on your circumstances, a 10% penalty may be

assessed, too. Some exceptions to the 5 year rule include: disability, higher education expenses and first time homebuyer expenses.

Furthermore, given the bear market and its resulting depressed account values, the timing for a Roth conversion may be terrific. You'll be taxed on the value of the account at the time of the conversion, regardless of what it may have been worth in past years. So, if your IRA account value is close to its 5-6 year low, consider converting soon rather than waiting for the market to recover.

The media may lead you to believe the "to Roth or not" decision is an easy choice. In reality, there are a number of issues to consider before converting and your individual circumstances will influence whether a Roth Conversion is a good idea for you.

If you are interested in discussing whether a Roth conversion is an appropriate strategy seek the assistance of your Certified Financial Planner™, accountant and/or estate planning attorney.

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