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## **Roth IRA Conversions--Planning for New Opportunities**

As the events of the past 18 months have unfolded, there has been a great deal of experts who have shown up on the scene telling people what to do with their money. The internet and cable television have been overrun with well intentioned seekers of their “15 minutes” giving sweeping and general advice to the masses about what to do with their hard earned money. The suggestions of buying gold, financial stocks, high yield bonds, etc, etc. garner all of the attention. Unfortunately these “talking heads” are missing the chance to talk about a much less “sexy” topic but one that has the potential benefit to make you and your heirs much richer.

As the federal government continues to go deeper in debt while continuing to spend billions – no-trillions of dollars, a couple of things become pretty evident: 1) income tax rates are probably going up, and 2) that relic of the 70’s, inflation, could be making a return.

The Roth IRA was first offered in 1998 and it swapped the tax deduction of the traditional IRA for the tax free growth. This tradeoff is extremely powerful when you look at the long term. You will have to pay a price today for potential long term benefits that may really mount up. The Government looked at the state of the nation’s retirees and saw that they needed to continue to encourage citizens to save more for retirement instead of relying on Social Security for their only source of income. You were originally allowed to contribute \$2,000 per year into a Roth IRA. But the big attraction in 1998 was that you could convert your existing traditional IRA to a Roth IRA. When you do this conversion you essentially take a withdrawal from your existing IRA and pay taxes on the distribution amount for the opportunity to grow the assets tax-free, instead of tax-deferred. However, in 1998 they allowed you to pay this tax back over 5 years, thus smoothing out the tax cost.

Well that opportunity has come and gone. You can still convert from a Traditional IRA to a Roth, but the taxes are all payable in the year you convert. One way of managing this cost/benefit has been to only convert a small piece of your Traditional IRA each year. The speed bump with this plan over the last few years is that there have been income limits. If you made more than \$100,000 per year as an individual filer or as a joint filer you were excluded from this planning opportunity. Well that is all about to change in 2010.

In 2010 the income limits will be lifted for Roth conversions, allowing those in even the highest tax brackets this opportunity. In addition, they are bringing back the opportunity to spread out the tax payments. In 2010 you can make a conversion from a Traditional IRA to a Roth and pay the taxes over the following two years. This can provide a tremendous opportunity for those taxpayers that are in the top tax brackets.

The assets in a traditional IRA grow tax deferred until you make withdrawals from the IRA. Avoiding paying taxes today on the annual growth in your IRA, allows your annual growth to compound, year after year. Once you reach your retirement years, and you begin to take money out of your traditional IRA, you will need to pay taxes on that growth, and on any previously un-taxed dollars. This deferral



of taxes is recognized by the IRS and therefore, they now require you to make withdrawals from your IRA once you reach age 70 1/2, whether you need the money or not, to force you in to paying taxes.

The dollars in a Roth IRA grow tax free. This allows you to experience the amazing power of compound growth. And, unlike traditional IRAs, there are no required distributions from Roth IRAs. This can be a benefit to your heirs as they would receive the proceeds from the Roth, potentially without paying tax, unlike beneficiaries of a traditional IRA

There are many factors to consider when deciding whether this makes sense for you or not. You should consider how you would pay the tax due upon conversion; your tax bracket now compared to what it will be in your retirement years; how long can you leave the money in the Roth IRA; are you currently receiving social security benefits; will your heirs be subject to estate taxes. These are some of the factors we review with people when entertaining the idea of a Roth IRA conversion. Keep in mind that you can choose to only convert a portion of your traditional IRA assets.

This strategy can be very powerful for you and your family. It makes sense to begin discussing this with your advisor this year so you can make sure the decision that you make in 2010 is the right one. A little planning, research and number crunching can go a long way to helping you prepare for a better retirement.

*The opinions voiced in this article are for general information and not intended to provide specific tax, legal, or investment planning advice. Please discuss your specific situation with your financial, tax, and legal advisor.*

*Restrictions, penalties and taxes may apply unless certain criteria is met; Roth IRA owners must be 59 1/2 or older and have held the IRA for 5 years before tax-free withdrawals are permitted.*

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