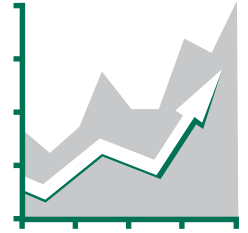


# Financial Adviser



## Roth IRA Conversions: Income Limit to be Removed January 1

Under current regulations, taxpayers can convert traditional IRAs and qualified retirement accounts to a Roth IRA, so long as their modified adjusted gross income is \$100,000 or less and their filing status is not married filing separate. Beginning January 1, 2010, under the Tax Increase Prevention and Reconciliation Act of 2005, there will no longer be an income limitation, or any restrictions on filing status. In short, all taxpayers will have the ability to convert retirement assets into Roth IRAs.

These changes in conversion requirements present a unique opportunity for taxpayers. The income limits with regard to deductible contributions to traditional IRAs or contributions to Roth IRAs have prevented many taxpayers from the tax benefits of a traditional or Roth IRA. Higher income taxpayers could always make nondeductible contributions to traditional IRAs, but there are several drawbacks that limited the benefit of doing so. Under the new regulations with no income limits, these same taxpayers can make nondeductible contributions to traditional IRAs and then convert into a Roth IRA in 2010. Essentially, the elimination of the income limit for converting to a Roth IRA eliminates the income limit for contributing to a Roth IRA. For conversions made in 2010, a taxpayer can recognize the conversion amount ratably in 2011 and 2012, or they can elect to recognize the income in 2010.

### What's the Difference?

Traditional and Roth IRAs both allow income held in the account to grow tax free, but there are many differences separating the two. Contributions to a traditional IRA can be deductible, but contributions to a Roth IRA are never deductible.

Further, distributions from traditional IRAs are taxable (unless no deduction was taken for the contributions that comprise the account); qualified distributions from a Roth IRA are not taxable. Traditional IRAs have required minimum distribution (RMD) rules, but Roth IRAs do not. These rules were put in place to make sure that the traditional IRA account is distributed and taxed during the taxpayer's life rather than saved for the next generation. Another difference is that individuals cannot contribute to a traditional IRA after age 70. Roth IRAs, on the other hand, can be contributed to as long as the taxpayer has earned income.

### Factors to Consider

Careful planning should be performed to determine if a taxpayer should take advantage of this new development. The first thing to consider is whether the individual has the resources to pay the tax on the conversion. If the taxpayer has to use a distribution from the converted IRA to pay the tax, that amount also will be taxed. Additionally, if the distribution is an early withdrawal, it will be subject to an additional 10-percent penalty.

Another principal concern is whether the taxpayer believes he or she will be in a lower or higher tax bracket after retirement. If an individual believes they are going to fall into a lower tax bracket during retirement, it may be more beneficial to take advantage of the tax deferral quality of a traditional IRA. Similarly, it is important for the taxpayer to consider whether they believe that income tax rates will increase or decrease in the future. When looking at historical statistics, our current income tax rates are considerably low. However, with recent economic decline and budget

deficits, many feel that a tax increase is on its way sooner than later. If this scenario plays out, it may be beneficial to pay the tax on the Roth conversion now while rates are low.

These are just a couple of the factors that should be taken into consideration when planning whether to convert retirement assets into a Roth IRA. The elimination of the \$100,000 income limitation was designed by the government to be a revenue-producing tax measure. However, for many high-income taxpayers, this may be an opportunity for significant tax savings. ☆

*Converting retirement assets into a Roth IRA should only be done after careful consideration of circumstances and tax planning. For assistance in determining if a Roth conversion is right for you, contact Michael Neubauer at McGill, Power, Bell & Associates, LLP at 814/453-6594 or [mneubauer@mpbcpa.com](mailto:mneubauer@mpbcpa.com).*

*Michael S. Neubauer, CPA, CVA, MBA, is a supervisor in the Erie office of the certified public accounting firm of McGill, Power, Bell & Associates, LLP. His area of specialization is the manufacturing niche. Neubauer serves as president-elect for the Erie Chapter of the Pennsylvania Institute of Certified Public Accountants (PICPA), the treasurer of the Presque Isle Partnership, and was recently named one of the PICPA's 40 under 40 members to watch.*

