

## SUSAN TOMPOR

POSTED: NOV. 19, 2009



### Roth IRA conversion isn't for everyone

BY SUSAN TOMPOR  
FREE PRESS COLUMNIST

The topic may make your head spin, but the Roth IRA conversion is definitely building buzz.

Beginning next year, many business owners, two-career households and higher-net-worth individuals who earn \$100,000 or more in a year will be eligible to convert their traditional IRA to a Roth IRA.

Right now, the only people who could convert to a Roth IRA are those who have incomes less than \$100,000. And a married person filing separately cannot convert a regular IRA into a Roth IRA. Both of those rules go away in 2010.

What's the big deal? If you meet certain requirements, you are able to withdraw earnings in retirement from a Roth tax-free. You pay income taxes on withdrawals from a regular IRA. You're also not required to take minimum distributions each year from a Roth after age 70 1/2, as you are with a regular IRA.

Some well-off savers do not want to withdraw the money and would like to be able to pass it along to their children or grandchildren income tax-free via the Roth. Traditional IRAs pass to heirs with tax consequences.

So everybody should convert, right?

If someone tells you that, you know they're a fast talker. This is not a great idea for everyone.

"It goes back to: What's your tax bracket? Do you have the funds outside the IRA to pay the tax? And what's your time frame for needing those assets?" said Jill Garvey, vice president and regional manager for the wealth planning group at Comerica Bank.

#### **A costly conversion**

Top reason for skip it and forget it?

Money. The Roth conversion isn't a freebie.

"A Roth conversion is expensive. There's a big up-front cost to doing this," said Tim Steffen, financial and estate planning manager for Robert W. Baird & Co. in Milwaukee.

Even if you'd only convert \$10,000 in the process, some taxpayers could owe \$2,500 to \$3,500 in taxes for the 2010 return, depending on their income tax bracket. You could convert all the money in your IRAs or part of it, depending on your tax situation.

"In today's economy, the average person doesn't have a lot of cash laying around to pay these taxes," said Kim Saunders, senior tax analyst at the tax and accounting business of Thomson Reuters.

A wealthy person who converts \$100,000 from a regular IRA to a Roth IRA could owe \$35,000 in taxes based on the highest tax bracket for 2010. Plus, if that person is younger than age 59 1/2, they're likely looking at a 10% penalty on the amount that's taken out of a regular IRA specifically to pay the tax. If you took \$35,000 out to pay the tax, for example, the penalty would be \$3,500.

For conversions made in 2010 only, it is possible to choose to take advantage of a 2-year spread.

You could take the \$100,000 that's converted in 2010 to a Roth IRA and elect to report \$50,000 on a 2011 return and \$50,000 on the 2012 return. But then you'd pay taxes based on the rates and your income for 2011 and 2012. For some people, it's possible that delaying that 2010 tax bill could result in higher taxes.

Garvey points out that the current federal income tax rates expire at the end of 2010 if Congress takes no action. If that happens, for example, she noted the highest tax rate would jump to 39.6%, up from 35%.

"It's a little more art than science," said John Carl, president and founder of the Retirement Learning Center in Brainerd, Minn. "How much taxes are you willing to fund now for a lifetime of tax-free income?"

### **To aid your decision**

What if you don't have money in a savings account to pay these extra taxes?

Well, no one should take even more money out of the IRA to cover the taxes.

If you do that, you're cutting into your retirement savings and destroying the long-term potential for tax breaks.

"Congress didn't change this rule out of the goodness of the heart," said Rande Spiegelman, vice president of financial planning for the Schwab Center for Financial Research.

The conversions would bring tax revenue to the federal government sooner, rather than later.

To figure out whether it's good or bad for you, you should talk to a tax adviser and run some numbers.

Who can this work well for?

Saunders suggested you might consider a conversion if you do not need that Roth money for the next 15 to 20 years to really get the benefits of a tax-free withdrawal in retirement.

Garvey noted that it also could work if you know you'll have a high income in retirement, too.

However, if you know that your income would be far less in retirement than you're making in 2010, you might reconsider this idea.

Contact *SUSAN TOMPOR*: 313-222-8876 or [stomp@freepress.com](mailto:stomp@freepress.com).

A version of this story appears on page 5B of the Thursday, Nov. 19, 2009, print edition of the Detroit Free Press.