

CHEAT SHEET

Roth Conversions

Are you looking for tax-free income in retirement? A Roth conversion can be an effective strategy that allows you to pay taxes today on your retirement savings in an effort to reduce taxes in retirement when your income may be lower or your taxes may be higher.

Traditional IRA vs. Roth IRA

There are a few key differences between traditional and Roth IRAs. The most significant is how they are taxed.

Traditional IRAs allow many people to take a tax deduction during the year in which contributions are made. Those contributions grow tax deferred within the account and are taxed as ordinary income when they are withdrawn.

Roth IRAs, on the other hand, are funded with after-tax contributions, which means there is no tax benefit during the year in which contributions are made. However, withdrawals from Roth accounts are tax-free, assuming the taxpayer has reached age 59 ½ and has held the account for at least five years.

	TRADITIONAL IRA	ROTH IRA
<i>Deductible contributions?</i>	Yes, depending on income	No
<i>Tax treatment of distributions</i>	Taxed as ordinary income	Tax-free after age 59 ½ and five years
<i>Required minimum distributions?</i>	Yes, beginning at age 73	No
<i>Tax treatment of death benefit</i>	Beneficiary payouts taxed as income	Tax-free beneficiary payouts

IRA Contributions

Both traditional and Roth IRAs have the same annual contribution limits.¹In contrast to traditional IRA contributions, Roth IRA contributions are gradually phased out based on the taxpayer's income.

How does a Roth conversion work?

Following is a step-by-step guide to Roth conversions.

1. *Fund a traditional IRA.*

In order to complete a Roth conversion, you must hold assets in a traditional IRA. The traditional IRA can either be comprised of assets you have been contributing over time, or it can be a rollover of a previous balance held in an employer-sponsored retirement account.

2. *Open a Roth IRA.*

Before completing the conversion, you must have an account that can accept the direct transfer of assets.

3. *Pay taxes on the converted assets.*

Keep in mind that all assets withdrawn from a traditional IRA are taxed as ordinary income, not capital gains. This includes distributions made for a Roth conversion.

4. *Transfer the traditional IRA assets to the Roth IRA.*

Be sure to work with a qualified financial professional to complete this step and ensure the assets are directly transferred to your Roth account.

5. *Wait at least five years to qualify for tax-free distributions.*

For Roth IRA distributions to be tax free, you must be at least age 59 ½ and have held the Roth account for five years. If you make the mistake of withdrawing from the account early, you'll miss out on the benefit of tax-free distributions.

Tip – If possible, pay the conversion tax with assets outside of the IRA. If you use IRA funds to pay taxes, you reduce the amount available to fund the new Roth IRA, which also reduces the benefits of tax-deferred growth and tax-free distributions. By using other assets to pay the taxes, you can maximize the amount directed to your Roth IRA.

Converting an employer plan account to a Roth IRA is a taxable event. Increased taxable income from the Roth IRA conversion may have several consequences including (but not limited to) a need for additional tax withholding or estimated tax payments, the loss of certain tax deductions and credits, and higher taxes on Social Security benefits and higher Medicare premiums. Be sure to consult with a qualified tax advisor before making any decisions regarding your IRA

Interested in learning more about whether a Roth conversion is right for you?

Consult with a qualified financial professional to determine how a Roth conversion may impact your overall financial picture.



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