CORIENT

Roth Conversions

A Roth Conversion is a tax planning strategy used to transfer assets from a traditional IRA or other tax-deferred retirement account into a Roth IRA, potentially providing tax benefits over time.

DESCRIPTION OF STRATEGY

In a Roth conversion, the account holder moves funds from a tax-deferred account (traditional IRA, pre-tax 401(k) etc.) to a post-tax account (Roth IRA). Because of this, the conversion is subject to taxes in the year of the conversion as the transferred funds are considered taxable income. Once in the Roth IRA however, the assets grow tax-free and qualified withdrawals are also tax-free.

KEY BENEFITS

Tax-Free Growth

Assets in a Roth IRA grow tax-free, allowing for potentially greater accumulation of wealth over time.

Tax Diversification

By converting some traditional IRA funds into a Roth IRA, individuals can create a tax-free income source in retirement.

No RMDs

Unlike traditional IRAs, Roth IRAs do not have required minimum distributions during the account holder's lifetime, allowing for greater control over retirement income planning.

Legacy Planning

Roth IRAs can be passed onto heirs tax-free, providing potential estate planning benefits and the opportunity for beneficiaries to receive distributions tax-free.

RISKS/DRAWBACKS

Immediate Tax Liability

Converting to a Roth IRA requires paying taxes on the converted amount in the year of the conversion, which can create significant upfront costs.

Medicare Premiums

For incomes above a certain threshold, an additional fee is applied on top of regular Medicare Part B and Part D premiums. This is known as the Medicare Income-Related Monthly Adjustment Amount (IRMAA). Converting assets may push the taxpayer into a higher bracket which can trigger this surcharge.

OPPORTUNITIES TO UTILIZE

Lower Income Tax Bracket	Taxpayers in a lower income bracket today than in the future can take advantage of their situation by converting in a low tax environment with the intention of using tax-free funds later in a potentially higher tax environment.
Higher Income Tax Bracket	Taxpayers who will likely always be in a high tax bracket should still consider Roth conversions to hedge against future tax law changes.
Large Taxable Estate	The amount subject to estate taxes can be reduced by spending down current assets to pay taxes on the conversion.