



DIVIDEND ASSETS CAPITAL, LLC

INVESTMENT ADVISORS

## Should I Convert to a Roth IRA?

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We've been asked this question many times over the years and one would think it would be a pretty straight forward response---Yes or No.

Like all great questions, before it can be sufficiently answered, you will need to begin by asking the right questions. Answering these questions, will help determine if converting a Traditional IRA to a Roth IRA would make sense. Each scenario is different and what works in one case may be completely inappropriate for another.

Let's look at these questions and a couple of scenarios below:

- Will I need the income distributions from my retirement account?
- Who are my beneficiaries?
- Will I, or my beneficiaries, be subject to higher or lower income taxes in the future?
- Do I have cash or investable assets outside my IRA to pay the taxes due upon conversion?
- Do I have charitable inclinations?
- Do I have a 5+ year investment time horizon on my IRA monies?

### **Scenario One:**

Mr. and Mrs. Smith have determined they will not need income distributions from his Traditional IRA. His beneficiary is his spouse and she will be in a lower bracket when he passes. They have cash and investments in their joint name, outside his IRA, to cover taxes due and have no charitable inclinations. Mr. Smith is in poor health and will most likely pass before Mrs. Smith. He is several years away from required distributions.

Under this scenario Mr. Smith should not convert his Traditional IRA to a Roth IRA.

### **Why?**

Mrs. Smith will be in a lower tax bracket when Mr. Smith passes, negating the potential tax advantages of converting.

### **What if Mrs. Smith remained in the same or higher tax bracket upon Mr. Smith's passing?**

Then converting to a Roth IRA could make sense. Why? Mrs. Smith does not need the income distributions and will benefit from tax-free growth while she's alive; they have enough liquidity to cover the taxes due and they have no charitable inclinations.

Additionally, the IRA withdrawal rules will allow for contributions and converted amounts to be withdrawn tax free should Mrs. Smith need funds from the Roth IRA. Although there is one wrinkle to be aware of, a Roth IRA must be held for a minimum of 5 years before earnings withdrawals are tax free.

## **Scenario Two:**

Mr. and Mrs. John Doe will need income distributions from their IRAs. Mrs. Doe's IRA has a significantly higher balance than Mr. Doe's. They do have charitable inclinations; but would like their children to inherit the bulk of their assets upon both their passing. Additionally, they have cash on hand and other investments in joint name. They foresee their income brackets staying the same upon the passing of either spouse. They are several years away from required distributions. Most of their income needs could be met from Mrs. Doe's Traditional IRA distributions, before and after her required distributions begin.

Under this scenario it may make sense to convert part of their Traditional IRAs to a Roth IRA(s).

### **Why?**

Mr. Doe has a significantly lower balance in his Traditional IRA than Mrs. Doe. He could consider converting part or all his Traditional IRA to Roth IRA. Their income tax bracket is expected to stay the same throughout retirement and they have enough cash on hand to pay the taxes due. They can meet their income needs on Mrs. Doe's IRA distributions.

### **What about leaving assets to their children?**

He should also consider naming their children as his Roth IRA beneficiaries. This would ensure their children inherit his Roth IRA income tax free and allows for many years of tax deferred growth.

### **What about their charitable inclinations?**

Mrs. Doe could consider using some of her Traditional IRA for Qualified Charitable Deductions (QCDs) to meet some of their charitable gifting inclinations. She can do this after age 70 1/2 and the portion she gifts would not be subject to ordinary income tax. From age 72 onward, these QCDs would help her meet her required distributions, while lowering her taxable income.

Each scenario above resulted in a different choice that worked best for their individual goals and objectives; but began by answering those simple questions. One additional note, this process should also include multiple conversations with a tax professional to help determine the exact dollar amount to convert based on the unique income tax picture.

If you would like to discuss whether converting your Traditional IRA to a Roth IRA is the best option for your scenario, please do not hesitate to call your Portfolio Manager. We are happy to walk you through this process and work with your tax professional to determine your best path forward.

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