

# Revisiting The Roth IRA Conversion

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It is an understatement to say we are living in a difficult economic environment. Headline after headline can make it easy to react by changing the financial television channels and ignoring all things financial. While there may be some wisdom in the first response, it might make sense to reconsider the second. As advisors, our job is to help clients think about ways to further their long-term financial goals. The Roth IRA conversion is one planning technique we believe worth considering.

## Really? Now?

We believe this popular technique could be especially attractive now. The Coronavirus and what will likely become the first “government forced recession” has caused substantial deterioration to the economy and equity markets. As a result, most equities are trading at significantly lower prices as we can see when we look at our account balances.\* Lower values make a Roth conversion more attractive since the tax consequences will also be significantly reduced. Over the longer term, we expect asset prices to come back and continue to grow (hopefully sooner rather than later). We think having that future growth occur in an income tax-free account is ideal.

## Refresher On Roth IRAs

A Roth IRA is an individual retirement account that offers income tax-free growth and income tax-free withdrawals in retirement. Roth IRA rules dictate that as long as you have owned your account for

at least 5 years and you are age 59½ or older, you can withdraw your money when you want to and you will not owe any federal income taxes. You can always withdraw your original contributions without taxes and penalty.

## Benefits Of A Roth IRA Conversion

There are income limitations associated with Roth IRA contributions, but anyone can convert an existing IRA to a Roth IRA regardless of their income. While the conversion itself is taxable, you will not pay income taxes again provided you take a qualified distribution. One key benefit is it will reduce your taxes in the future. Another positive is there are no required minimum distributions (RMDs) from Roth accounts. Converting now will help limit the amount of RMDs you need to take in the future. If you do not need those Roth funds to live on, you and your spouse can leave the assets in the account to grow income tax-free. Ultimately, your final beneficiaries can use this account as a source of tax-free income for up to ten years.

## Still Sound Too Risky?

We appreciate that there is still a lot we do not know about how long the markets will be this volatile. Therefore, it is especially important (to the extent possible) to avoid paying taxes on a conversion, only to have that conversion amount continue to decline in value. For that concern, we are reminded of an investment principle called dollar cost averaging. Instead of converting a lump sum to a Roth IRA all at once, it might be more prudent to spread out the conversion amount. For example, you might consider converting 25% of your total conversion amount



*\* In the current environment, we strongly encourage you to avoid checking your account values too often. Focus on your long-term financial plan instead!*

over each of the next 4 months. While there are no guarantees, this might help mitigate the risk of converting in front of further market declines.

### **Pair This Strategy With Giving**

For those that want to limit their taxable income this year, one way to potentially offset this additional income is to increase your charitable giving. It does not matter if you choose to increase your usual contributions, give to an organization that is helping those affected by the Coronavirus, or add money to a Donor Advised Fund. As long as

you verify that your donations are tax-deductible, you would be helping others and minimizing your income taxes at the same time.

For more information on Donor Advised Funds, check out our website to read an article we wrote 10 years ago, “Donor Advised Funds: Stop Writing Checks to Charities”. Of course, we are also always available to talk.

*Stay healthy!*

### **For more information, please contact:**

Marc Horner, CFP®  
Founder & Wealth Advisor  
mhorner@fairhavenw.com  
630.990.9000

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