MANAGING YOUR FINANCES

Age Isn't a Big Factor For Roth Conversions

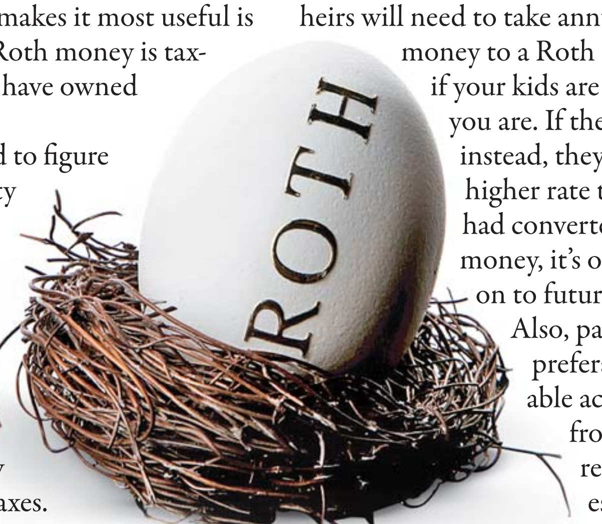
OLDER INVESTORS are often reluctant to convert traditional IRA money to a Roth IRA. They must pay the tax tab upfront and worry they won't benefit from many years of the Roth account's tax-free growth.

But a Roth conversion, of at least part of your traditional IRA, can make sense, depending on your tax bracket, the size of your IRA and legacy goals. One great benefit: The Roth has no required minimum distributions when you turn 70½, as a traditional IRA does.

James Lange, a certified public accountant in Pittsburgh and author of *The Roth Revolution* (Morgan James, $20), says older investors have nothing to lose from a conversion as long as the additional income from the conversion doesn't increase their tax bracket. No matter when you withdraw from a traditional IRA, you'll need to pay income taxes, he notes. Say the investor is in the 25% tax bracket and has $100,000 in an IRA and $25,000 in a taxable account. He'll only have $100,000 to spend—whether he converts to a Roth or simply withdraws the money from the IRA. He'll need to pay $25,000 in taxes in either case. "Measured in purchasing power, you break even on day one," says Lange.

The tax-free income stream from a Roth can help lower taxes on other benefits, especially for higher-income retirees. "If you do take income out of the Roth, it's not counted in adjusted gross income as long as the holding period is met," says Lynn Mayabb, a senior managing adviser in the Kansas City, Mo., office of BKD Wealth Advisors. "What makes it most useful is managing the tax bracket." All Roth money is tax-free if you are 59½ or older and have owned a Roth for at least five years.

Adjusted gross income is used to figure the income tax on Social Security benefits, premium surcharges for Medicare Parts B and D for high-income seniors, and the "Medicare surtax" on certain investment income that goes into effect in 2013. By taking money from a Roth as income, you might keep your AGI below the thresholds for any of those taxes.



The best time to convert is when your tax bracket is low and you expect a jump in future years. Lange says the years just after retirement and before 70½ are a great time to convert. Your tax bracket may have dropped because you no longer have income from a job. Plus, you may not have started Social Security benefits, and you don't have RMDs yet.

Once you hit 70½, "you can get put in a higher bracket when forced to take RMDs," says Jean Dorrell, founder of Senior Financial Security, in Summerfield, Fla. That's especially true if you have a very large IRA. By converting part of your retirement account, you will reduce the size of your taxable RMDs, producing income-tax savings for years. If you convert any of your IRA after 70½, you must take that year's RMD first.

Rein in the Tax Bill

One way to reduce your tax bill when you convert is to do a series of smaller conversions for several years. "If your annual income is stable, you should convert just enough each year to remain in your usual tax bracket," says Paul Jacobs, a certified financial planner in the Atlanta office of Palisades Hudson Financial Group. For example, married taxpayers filing jointly with $50,000 of income in the 15% bracket could convert up to $20,700 to take them to the top of that bracket.

You are in a prime spot for a conversion if you have negative taxable income, which is common among retirees, says David Hill, a certified financial planner for Brinton Eaton, in Madison, N.J. A taxpayer with, say, an AGI of $40,000 but itemized deductions worth $70,000 could convert just enough to use those deductions and pay zero taxes, he says.

Your heirs can also benefit. When you die, your heirs get a pot of tax-free money, although nonspouse heirs will need to take annual RMDs. Converting money to a Roth could be particularly smart if your kids are in a higher tax bracket than you are. If they inherit a traditional IRA instead, they will pay income tax at a higher rate than you would have if you had converted. "If you don't need the money, it's one of the best things to pass on to future generations," Hill says.

Also, paying tax on the conversion, preferably using money from a taxable account, can remove money from your estate, perhaps reducing or eliminating an estate tax. K —RACHEL L. SHEEDY