Should You Convert to a Roth IRA?

Whether an investor benefits from converting assets within a traditional IRA to a Roth account may depend on the amount of time he or she plans to leave the assets invested, estate planning strategies, and his or her willingness to pay the federal income tax bill that a conversion is likely to trigger.

Should you convert all or a portion of your traditional IRA assets to a Roth account? The answer may depend on the amount of time you plan to leave the assets invested, your estate planning strategies, and your willingness to pay the federal income tax bill that a conversion is likely to trigger.

Two Types of IRAs
Each type of IRA has its own specific rules and potential benefits. These differences are summarized in the table below.

	Traditional IRA	Roth IRA
Maximum Annual Contribution	The lesser of 100% of earned income or $5,500 for single taxpayers and $11,000 for couples filing jointly for 2013. An additional $1,000 "catch up" contribution is permitted for each investor aged 50 and older who has already made the maximum annual contribution.	Same as Traditional IRA
Income Thresholds for Annual Contributions	None, as long as the account holder has taxable compensation and is younger than age 70½ by the end of the year.	Single taxpayers with MAGI in excess of $127,000 and married couples filing jointly with MAGI in excess of $188,000 are not eligible in 2013. Income thresholds are indexed annually.
Deductibility of Contribution	Yes, if account holder meets requirements established by IRS.	No. Contributions are made with after-tax dollars.
Contributions After Age 70½	No contributions allowed after age 70½.	Contributions allowed after age 70½ if owner has earned income.
Required Minimum Distributions (RMDs) After Age 70½	Lifetime RMDs are required.	Not required during the original IRA owner's lifetime.
Taxes on Distributions	Distributions are taxed as ordinary income to the extent taxable. Withdrawals before age 59½ may also be subject to a 10% penalty.[1]	Qualified distributions are tax free. Withdrawals from accounts held less than five years and before age 59½ may be subject to taxes and a 10% penalty.[1]

Conversion: Potential Benefits ...
Potential benefits of converting from a traditional IRA to a Roth IRA include:

- A larger sum to bequeath to heirs. Since lifetime RMDs are not required for Roth IRAs, investors who do not need to take withdrawals may leave the money invested as long as they choose which may result in a larger balance for heirs. After an account owner's death, beneficiaries must take required minimum distributions, although different rules apply to spouses and nonspouses.

- Tax-free withdrawals. Even if retirees need withdrawals for living expenses, withdrawals are tax free for those who are age 59½ or older and who have had the money invested for five years or more.

... As Well as a Potential Drawback

- Investors who convert proceeds from a traditional IRA to a Roth IRA are required to pay income taxes at the time of conversion on investment earnings and any contributions that qualified for a tax deduction. If you have a nondeductible traditional IRA (i.e., your contributions did not qualify for a tax deduction because your income was not within the parameters established by the IRS), investment earnings will be taxed but the amount of your contributions will not. The conversion will not trigger the 10% penalty for early withdrawals.

Which Is Right for You?

If you have a traditional IRA and are considering converting to a Roth IRA, here are a few factors to consider:

- A conversion may be more attractive the further you are from retirement. The longer your earnings can remain invested, the more time you have to help compensate for the associated tax bill.
- Your current and future tax brackets will affect which IRA is best for you. If you expect to be in a lower tax bracket during retirement, sticking with a traditional IRA could be the best option because your RMDs during retirement will be taxed at a correspondingly lower rate than amounts converted today. On the other hand, if you anticipate being in a higher tax bracket, the ability to take tax-free distributions from a Roth IRA could be an attractive benefit.

There is no easy answer to the question "Should I convert my traditional IRA assets to a Roth IRA?" As with any major financial consideration, careful consultation with a financial professional is a good idea before you make your choice.

Points to Remember

- Retirement investors at any level of income can now convert assets from a traditional IRA to a Roth IRA.
- Converting assets from a traditional IRA to a Roth IRA may enable an investor to capitalize on qualified withdrawals that are tax free. In addition, because lifetime RMDs are not required from Roth IRAs, account holders potentially may leave the money invested and bequeath a larger sum to heirs.
- Conversion triggers a tax bill. Because IRA contributions are typically made on a before-tax basis, the full amount of the conversion – contributions and earnings – is usually taxable at ordinary rates.
- A conversion may be more attractive the further you are from retirement. The longer your earnings can remain invested, the more time you have to help compensate for the associated tax bill.

1: IRA account holders (both traditional and Roth) may avoid the 10% additional federal tax on withdrawals before age 59½ only if they meet specific criteria established by the IRS. See Publication 590 for more information.

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