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## How to Convert "Just Enough" to a Roth IRA

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Oct. 14, 2015



**(This is part of our series of “sweet 16” year-end tax planning ideas.)**

This could be the year you finally pull the trigger on a Roth conversion. Optimally, you might arrange a series of conversions over several years instead of facing a hefty tax by converting all your traditional IRA funds. But how much should you convert in 2015 if you take this route? The tax law allows you to benefit from a nifty maneuver.

But before we cover that, let’s quickly review the basics. Generally, contributions to a traditional IRA may be wholly or partially tax-deductible, especially in the earlier part of your career, but distributions are taxed at ordinary income rates reaching up to 39.6 percent. In addition, you must begin taking required minimum distributions (RMDs) from your IRAs in the year after the year you turn age 70½.

Conversely, contributions to a Roth are never tax-deductible, but post-age 59 1/2 distributions made after five years are completely tax-free. Earlier payouts may be wholly or partially tax-free under rules treating the amounts as coming first from nondeductible contributions. What's more, Roths are exempt from the RMD rules during your lifetime, so you can preserve more of your nest egg if you want.

Prior to 2010, you could not convert to a Roth if your adjusted gross income (AGI) for the year exceeded \$100,000. But the bar has been permanently lifted. Currently, a Roth conversion is available to everyone regardless of their AGI, increasing the popularity of this technique.

Yet there's no such thing as a free lunch. When you convert from a regular IRA to a Roth, you must pay the tax price. The switch is treated as a taxable event in the year of the conversion. This often gives taxpayers a reason to pause.

So when should you convert to a Roth? Unfortunately, there's no definitive answer. It depends on a number of variables, including the size of the account and amount that will be converted, your current tax bracket, your expected tax bracket in retirement, whether you have independent funds to pay the current tax, if you need to take RMDs in retirement and any other extenuating circumstances.

It's a no-brainer if you anticipate inheriting a windfall in retirement that will put you in a significantly higher tax bracket than you are now. Obviously, you should go ahead and convert in that case. Otherwise, you have to crunch all the numbers.

Assuming you decide to convert in 2015, you can minimize the conversion tax by keeping your overall taxable income just below the threshold for the next highest tax bracket. For instance, if someone is a joint filer normally in the 25% bracket and he or she expects to have \$125,000 of taxable income this year, the taxpayer can convert up to \$26,200 to a Roth before crossing the \$151,200 threshold for the 28% bracket.

Typically, you won't know exactly how much income you'll have in 2015, but here's where the smart tax maneuver comes to the rescue. You can convert plenty more than you need and go back later to recharacterize the excess back into a traditional IRA. The deadline for recharacterizing a Roth conversion is the tax return due date for the year of the conversion plus any extension – in other words, October 15, 2016 for a 2015 conversion.

Let's go back to our example of a joint filer in the 25% bracket. If the taxpayer converts \$26,200 a Roth at year-end and subsequently finds out his or her taxable

income is \$135,000, all the taxpayer has to do is recharacterize \$10,000 of the conversion. This allows you to minimize the tax damage from a conversion in the current year.

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