

What the Experts Are Doing With Their Own Roth IRAs

The Wall Street Journal

August 14, 2010

By Laura Sanders

Is it finally time to convert a traditional individual retirement account to a Roth? And if so, how should you do it?

We asked four IRA experts those questions and got four slightly different, but smart, answers worth considering.

This is the first year all taxpayers have been eligible to switch into Roth IRAs, which promise tax-free withdrawals in the future. With higher taxes on the horizon, many are gritting their teeth and taking the tax hit now. Fidelity Investments says that as of June 30 it had handled 100,000 conversions, four times the number for the same period last year.

But the decision to convert can be tricky, involving assumptions about future investment returns and tax laws. So we asked CPAs Ed Slott and Robert Keebler, and attorneys Seymour Goldberg and Natalie Choate what they are doing with their own accounts.

The gist: Three say they have either made Roth conversions or plan to do so soon, and the fourth says he will do so if the market tanks. Thus, all believe their own tax rates will be the same or higher in the future, and they aren't worried that Congress will curtail Roth benefits enough to make them rue the move. In addition, all say they will use non-IRA funds to pay any conversion taxes.

Beyond these general similarities, however, each has taken a different tack.

Here are their strategies:

Ed Slott: An IRA adviser and vocal Roth advocate, Mr. Slott, 56 years old, says he converted nearly all his six-figure IRA in January. With his adviser's help, he separated the funds into a half-dozen Roth accounts, each for a different asset class or sector such as energy, health care or real estate.

Mr. Slott says he plans to monitor his Roths and then reverse the conversions (called "recharacterization") of accounts that have dropped in value or lagged behind. The tax law allows this move as late as Oct. 15 of the year after the conversion date. So he has a 21-month window to decide which accounts to undo, and how much tax to pay. Yet his taxes will be figured as of his conversion date last January.

"It's the way to get the biggest bang for my tax buck," says the Long Island, N.Y., accountant. But he left a few hundred dollars in his regular IRA so that it could receive any money from reversed conversions, which cuts paperwork.

An open question: whether Mr. Slott will pay his conversion taxes at this year's top rate of 35% or elect a one-time deferral into tax years 2011 and 2012. On one hand, tax rates likely will rise after this year. On the other, the deferral combined with the six-month extension available to all taxpayers would push the payments for his 2010 conversion into 2012 and 2013. Once elected, this deferral can't be reversed, but he doesn't have to decide until October 2011, when his 2010 tax return will be due.

Robert Keebler: Mr. Keebler, a CPA in Green Bay, Wis., says he plans to make a Roth conversion of about 20% of his retirement assets before 2011. He will leave the rest in a company pension plan that offers better asset protection than Wisconsin gives to Roth holders. "I've never been sued," he says, "but this I think this makes sense." (State law varies on asset protection; Mr. Slott says New York's protection is ample for him.)

Working with his broker, Mr. Keebler, 49, hopes to convert during the market's next tumble, but he will carefully time his state tax payments so that they fall in the same tax year as his federal tax, to avoid triggering the alternative

minimum tax the following year.

Seymour Goldberg: Mr. Goldberg, an attorney in his 70s also from Long Island, says he will make a partial conversion of assets if the market craters. That is because, as a retired college professor, he is getting nearly a 5% yield from a vintage TIAA-CREF retirement account. Converting to a Roth would mean removing assets from this thriving account, so he has to assess carefully.

Natalie Choate: An attorney with Nutter McLennen & Fish in Boston, Ms. Choate, 64, switched a low-six-figure amount to just one Roth account in early July. The move fulfills her frequent advice to convert as soon as possible in order to "start the five-year clock running." To take tax-free withdrawals of earnings from a Roth, the owner must usually be at least 59½ and have held the account five years.

By converting during a market dip, Ms. Choate says she hopes she won't have to reverse the switch. So far her Roth account is up more than 5%, she says, but she dreads paying the conversion taxes, which she won't defer into 2011 and 2012. The thought of writing a five-figure check to Uncle Sam has kept her up at night.

Because she advises clients to write such checks, her dread has been "instructive," she says: "Next, I have to decide whether to convert more assets or remodel my kitchen. Right now, the kitchen is winning."