

ADVANCED ROTH CONVERSION STRATEGIES

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MICHAEL E. KITCES

MSFS, MTAX, CFP®, CLU, ChFC, RHU, REBC, CASL

Partner, Director of Research, Pinnacle Advisory Group

Publisher, The Kitces Report, www.kitces.com

Blogger, Nerd's Eye View, www.kitces.com/blog

Twitterer, @MichaelKitces, www.twitter.com/MichaelKitces



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TO ROTH OR NOT TO ROTH

	Traditional IRA	Roth IRA
Contributions	Deductible (Potentially)	Non-Deductible
Growth	Tax-Deferred	Tax-Deferred
Withdrawals	Taxable	Tax-Free (Potentially)
Income Limits	Only for deductibility	Yes
Lifetime RMDs	Yes	No
RMDs After Death	Yes	Yes
Early Withdrawal Penalty	Yes	Yes
Contribution Limit	\$5,500 (+\$1,000 catch-up)	\$5,500 (+\$1,000 catch-up)

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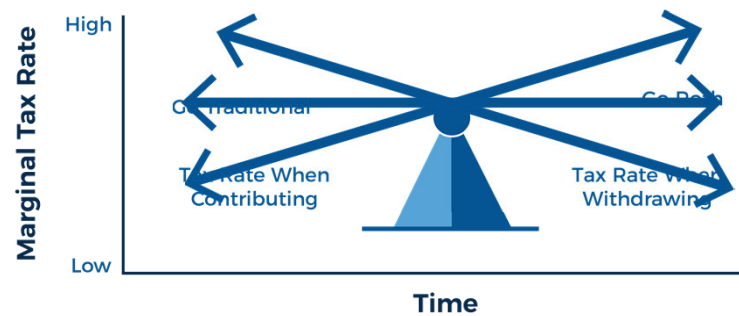
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TO ROTH OR NOT TO ROTH

- Roth vs. traditional IRAs



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TO ROTH OR NOT TO ROTH

- Current vs. Future tax rates
 - ***Tax equivalency principle***

A certain amount of pre-tax income results in the same amount of after-tax wealth in the end, regardless of which account type it goes to, whenever tax rates remain the same

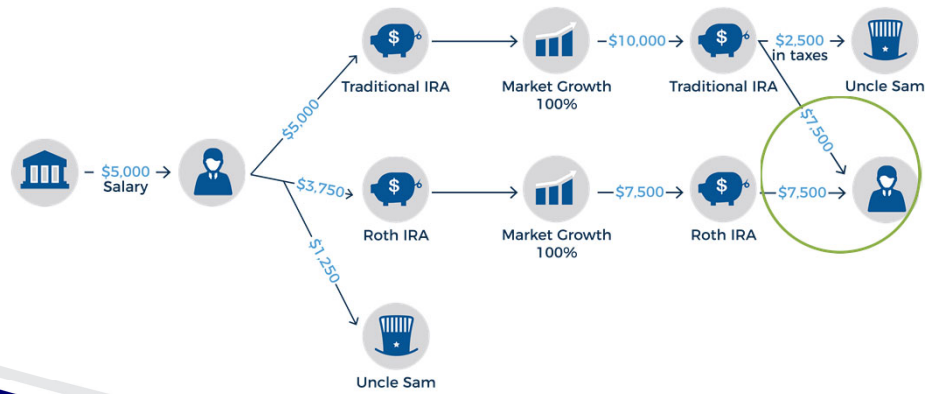
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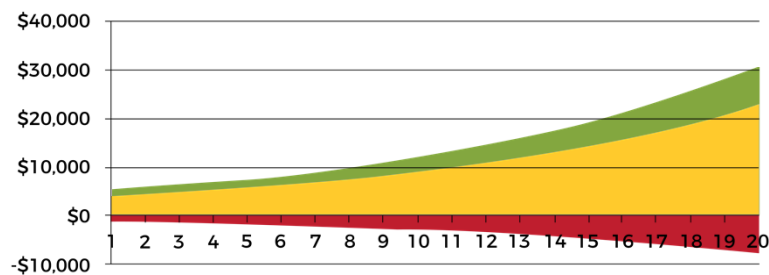
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TO ROTH OR NOT TO ROTH

- Tax Equivalency Principle



- Equivalency principle – then what happens when tax rates do change?

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TO ROTH OR NOT TO ROTH

- Contribution under current 25% tax rates:
 - \$5,000 to Traditional IRA
 - \$3,750 to Roth IRA (less 25% in taxes)

Future Tax Rate	15%	25%	35%
Tradition 401(k)	\$8,500	\$7,500	\$6,500
Roth 401(k)	\$7,500	\$7,500	\$7,500

- Pay your taxes whenever the tax rate will be lower!

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TO ROTH OR NOT TO ROTH

- Current vs. Future tax rates
 - Pay your taxes when the tax rate will be lowest!
 - If tax rates are lower now, pay today (Roth IRA)
 - If tax rates are higher now, pay later (Trad. IRA)
- Lesser To-Roth-Or-Not factors
 - Extending tax-deferred growth during life (RMDs)
 - Paying taxes w/ outside money
 - (State) estate taxes

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TO ROTH OR NOT TO ROTH

- Strategies To Maximize Roth Conversions:
 - Backdoor Roth Contributions
 - Mega Backdoor Roth for 401(k) Plans
 - Conversion-Cost-Averaging & Barbelling
 - Systematic Partial Roth Conversions
 - Starting The 5-Year Clock

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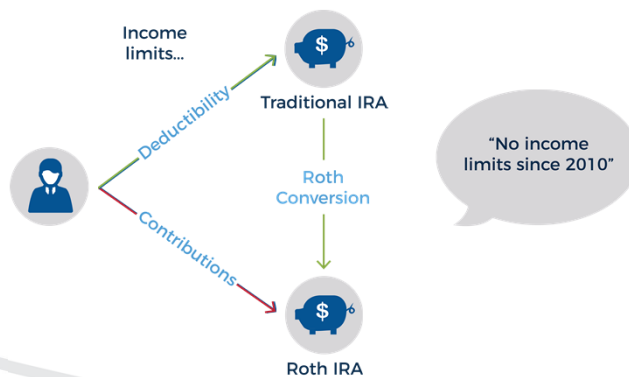
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“BACKDOOR” ROTH IRA

- “Backdoor” Roth Contribution Rules



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"BACKDOOR" ROTH IRA

• Tax Consequences Of Backdoor Roth Contributions

Non-Deductible IRA Contribution on Form 1041

7	Wages, salaries, tips, etc. Attach Form(s) W-2	7	
8a	Taxable interest. Attach Schedule B if required	8a	
b	Tax-exempt interest. Do not include on line 8a	8b	
9a	Ordinary dividends. Attach Schedule B if required	9a	
b	Qualified dividends	9b	
10	Taxable refunds, credits, or offsets of state and local income taxes	10	
11	Alimony received	11	
12	Business income or (loss). Attach Schedule C or C-EZ	12	
13	Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/>	13	
14	Other gains or (losses). Attach Form 4797	14	
15a	IRA distributions	15a	\$5,500
b	Taxable amount	15b	\$5,500
16a	Pensions and annuities	16a	
b	Taxable amount	16b	
17	Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E	17	
18	Farm income or (loss). Attach Schedule F	18	
19	Unemployment compensation	19	
20a	Social security benefits	20a	
b	Taxable amount	20b	
21	Other income. List type and amount	21	
22	Combine the amounts in the far right column for lines 7 through 21. This is your total income	22	
23	Educator expenses	23	
24	Certain business expenses of reservists, performing artists, and fee-basis government officials. Attach Form 2106 or 2106-EZ	24	
25	Health savings account deduction. Attach Form 8889	25	
26	Moving expenses. Attach Form 3903	26	
27	Deductible part of self-employment tax. Attach Schedule SE	27	
28	Self-employed SEP, SIMPLE, and qualified plans	28	
29	Self-employed health insurance deduction	29	
30	Penalty on early withdrawal of savings	30	
31a	Alimony paid - b. Recipient's SSN	31a	
32	IRA deduction	32	\$5,500
33	Student loan interest deduction	33	
34	Tuition and fees. Attach Form 8917	34	
35	Domestic production activities deduction. Attach Form 8903	35	
36	Add lines 23 through 35	36	\$5,500
37	Subtract line 36 from line 22. This is your adjusted gross income	37	\$0

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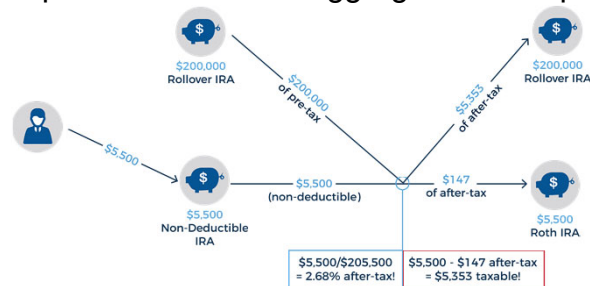
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"BACKDOOR" ROTH IRA

- The IRA Aggregation Rule: IRC 408(d)(2)
 - Requires that all IRAs aggregate for tax purposes



- NOT included: Spouse's IRAs, inherited IRAs, Roth IRAs, or any employer retirement plan

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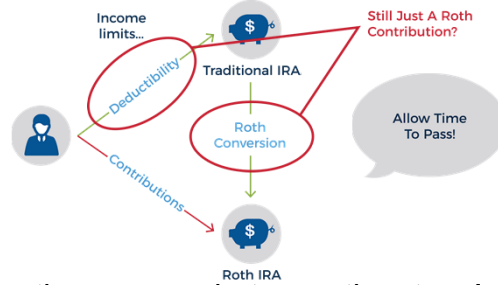
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“BACKDOOR” ROTH IRA

- The Step Transaction Doctrine

- If separate steps are part of a “single” transaction, the IRS can tax it like a single transaction!



- Unless time passes between the steps!

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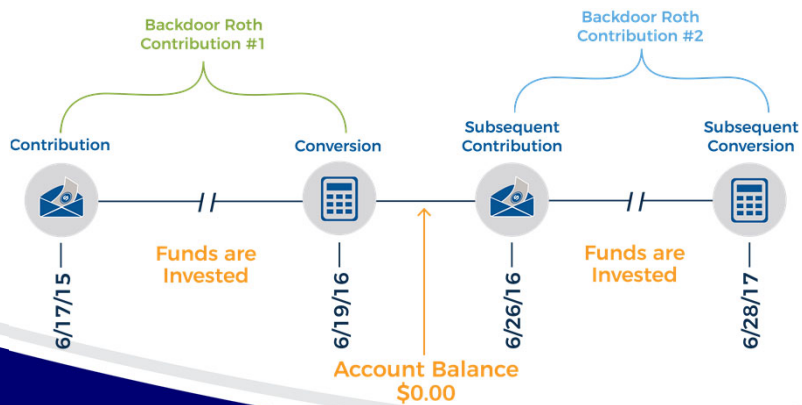
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“BACKDOOR” ROTH IRA

- Avoiding The Step Transaction Doctrine

- Allow Time To Pass Between The Steps!



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“BACKDOOR” ROTH IRA

- Best Practices In Backdoor Roth Contributions
 1. Avoid the IRA aggregation rule. Roll *in* to a 401(k) plan if necessary (even if you have to create it!).
 2. Avoid the step transaction doctrine by allowing time to pass between contribution & conversion
 3. Don't keep notes in the client file about “backdoor Roth contributions” –can be used against your client!

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MEGA “BACKDOOR” ROTH IRA!

- From Backdoor Roth to MEGA Backdoor Roth!
 - Converting after-tax dollars not exclusive to IRAs
 - 401(k) plans can have after-tax dollars too!
 - IRS Notice 2014-54 allows after-tax dollars to be split
 - Send the pre-tax to a rollover IRA
 - Send the after-tax to a Roth IRA (conversion)

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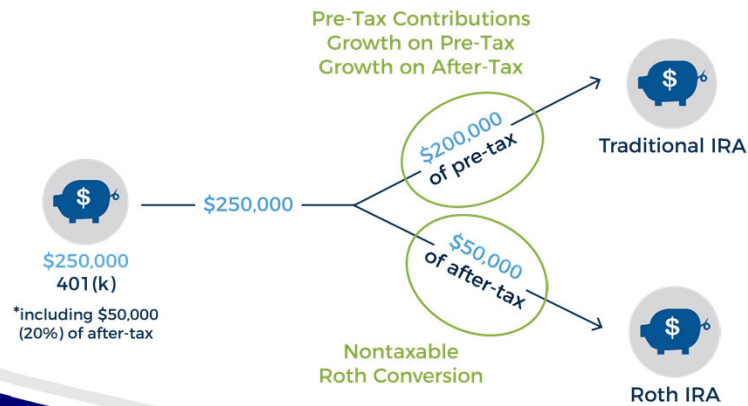
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MEGA "BACKDOOR" ROTH IRA!

- Splitting After-Tax Dollars From A 401(k)



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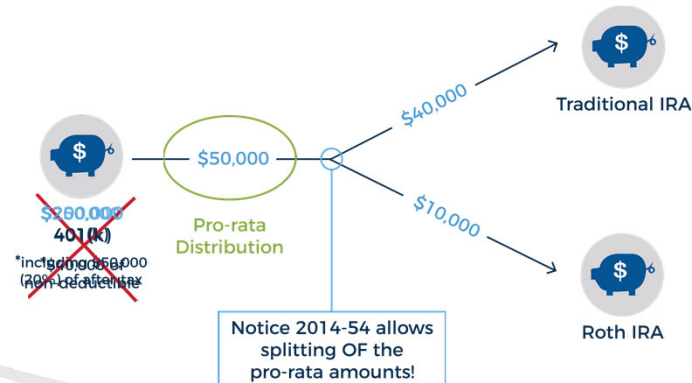
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MEGA "BACKDOOR" ROTH IRA!

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MEGA “BACKDOOR” ROTH IRA!

- Maximizing The Mega-Backdoor Roth 401(k)
 - Contribute after-tax dollar amounts (up to 415 limits)
 - Only relevant *after* maxxing out salary deferrals!
 - Must actually have (more) salary to contribute!
 - Plan must allow after-tax contributions
 - Can be added, but watch out for ACP testing
 - Beware that IRS could shut the door!
 - Can do Roth conversions now, if plan allows in-service distributions?

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MEGA “BACKDOOR” ROTH IRA!

- Maximizing The Mega-Backdoor Roth 401(k)
 - Hierarchy of Tax-Efficient Retirement Savings
 1. Obtain 401(k) match
 2. Max out 401(k) salary deferral (pre-tax or Roth)
 3. Deferred Roth contributions (after-tax 401(k))
 4. Non-qualified annuities for tax deferral

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PARTIAL ROTH CONVERSIONS

- Partial Roth Conversions
 - No requirement to be “all or none”
 - Can do *any* dollar amount *up to* 100%!
 - No longer can “recharacterize” a conversion!
 - Eliminated under 2017 Tax Cuts & Jobs Act (TCJA)
 - 2017 conversions still able to be recharacterized by Oct 15th 2018
 - Future recharacterizations no longer possible!

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TIMING ROTH CONVERSIONS

- Optimal Timing for Roth Conversions
 - In the past, “convert early and re-evaluate later”
 - Keep if markets went up, undo if markets went down
 - Recharacterizations provided a 21-month window!
 - Going forward...
 - Converting early “loses” if markets decline
 - Converting late “loses” if markets rise
 - So... average in over time?

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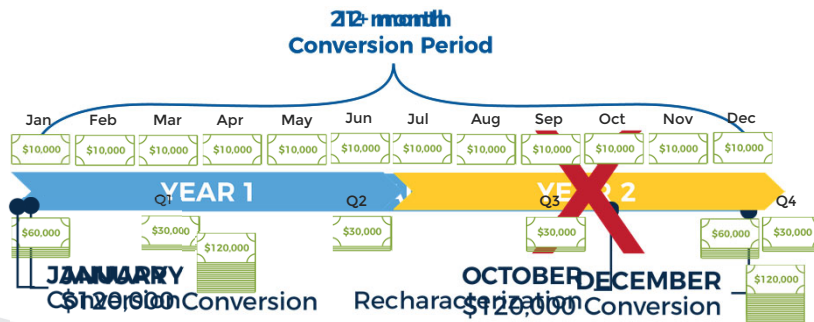
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TIMING ROTH CONVERSIONS

- Conversion-Cost-Averaging
 - Investor wants to convert \$120,000...



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TIMING ROTH CONVERSIONS

- Conversion Barbell
 - Investor wants to convert \$100,000... "ish"?
 - Exact conversion amount depends on...
 - Final total of deductions?
 - Cumulative income with uncertain bonuses?
 - End-of-year fund distributions?
 - Instead of converting all, or none, or evenly...
 - Convert what you "know" and add the rest later!?

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TIMING ROTH CONVERSIONS

- Conversion Barbellling
 - Investor wants to convert \$100,000... “ish”?
 - Convert what you know early, and true-up at the end?



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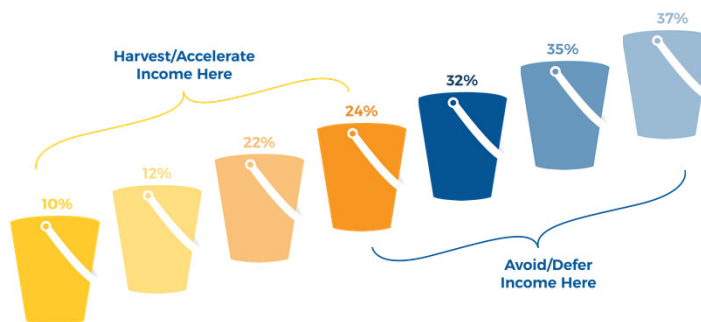
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PARTIAL ROTH CONVERSIONS

- Filling The Lower Tax Bracket Buckets



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PARTIAL ROTH CONVERSIONS

- Partial Roth Conversion Barbell
 - Donald & Donna are retired
 - ~\$50,000 of current income
 - ~\$15,000 of deductions
 - Want to fill the 12% bracket (\$77,400)
 - Uncertain about year-end mutual fund distributions
 - Donald & Donna do a \$30,000 Roth conversion now...

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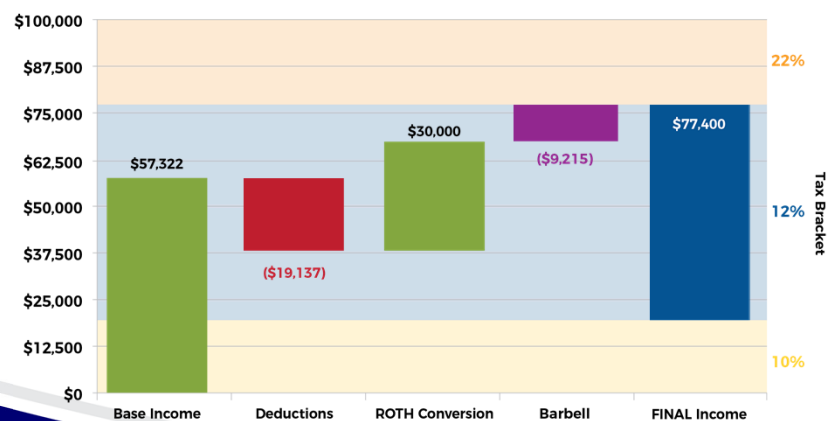
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PARTIAL ROTH CONVERSIONS

- Partial Roth Conversion Barbell



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PARTIAL ROTH CONVERSIONS

- Systematic Partial Roth Conversions
 - Betsy is a 60-year-old widow
 - Receives \$20,000 of Social Security survivor
 - Receives \$40,000 survivorship pension
 - Has \$200,000 brokerage account
 - Has \$700,000 IRA
 - Faces \$50k+ RMDs in 10 years given growth
 - Betsy begins to do \$40,000 partial Roth conversions...

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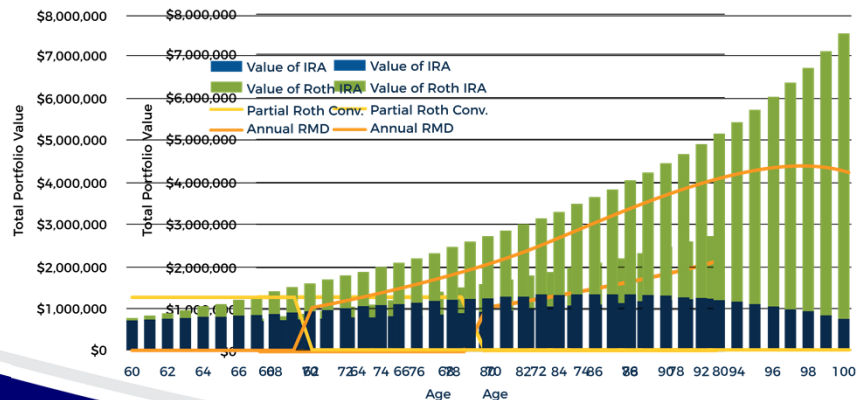
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PARTIAL ROTH CONVERSIONS

- Systematic Partial Roth Conversions



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PARTIAL ROTH CONVERSIONS

- Spotting Partial Roth Conversion Opportunities
 - Low-income years
 - Between jobs/after layoff?
 - Big loss year for a business?
 - The valley after employment and before RMDs
 - Can repeat systematically over time?
 - May even be relevant after RMDs begin!?
 - Roth conversions while spending from taxable accts?
 - Which tax bracket do you want to fill up to?

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5-YEAR RULE FOR TAX-FREE ROTH

- Satisfying The 5-Year Rule For Tax-Free
 - Roth accounts must meet “5-year rule” to be tax-free
 - In *addition* to being after 59 ½, dead, disabled, or for first-time homebuyer exception
 - Separate from the 5-year rule for Roth *conversions* to be *penalty* free
 - Measured from the beginning of the first year you *ever* created a Roth IRA
 - Roth 401(k)s separate, no carryover to Roth IRAs

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5-YEAR RULE FOR TAX-FREE ROTH

- Starting The Clock On The 5-Year Rule
 - Make a contribution in *any* year below income limits
 - \$135,000 for individuals, \$199,000 for MFJ in 2018
 - Do a (partial) Roth conversion
 - Even if just for \$100 (or \$1,000?)
 - Beware account fees/minimums

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ROTH CONVERSION OPPORTUNITIES

- Backdoor Roth contributions
 - Siphon off pre-tax dollars to a 401(k)?
 - Waiting period between contribution & conversion
- Mega Backdoor Roth contribution
 - Maximize salary deferral limits first!
 - Add to the 401(k) plan if not already allowed?

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ROTH CONVERSION OPPORTUNITIES

- Partial Roth Conversions
 - Who is having a low income year to fill up?
 - Systematic conversions for early retirees?
 - Conversion cost averaging in over time?
- Roth Recharacterizations
 - Remember they're gone!
 - Even "mistakes" can't be fixed now!
- A small conversion for all – start the 5-year clock!

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