IRAs – Opportunities for Now *and* the Future
Part I of II

A recent survey by the Financial Planning Association reported that the most important offering middle-income consumers expect from financial planners is IRAs. That sounds simple enough, but my personal research reveals that consumers often rely on advisors for retirement advice that is woefully lacking in anything other than the basics. It's a brutal market right now, and investment firms are hungry for income. Don't be caught short by an advisor who is more interested in collecting fees than actually helping maximize your retirement and tax benefits!

The financial mess has created some IRA opportunities for people of all ages. Some are "inspired" by Washington, and others are a result of the down market. This month and next, we'll focus on ways to improve retirement options for you ***and*** your family.

Lately, I have been advising more clients than ever to consider a Roth IRA. The responses I have received have convinced me that there is a large comprehension gap as to what a Roth is and who it is for. Let's start with some basic information.

Like a traditional (deductible) IRA, a Roth IRA is used to invest and save for retirement. Although people typically think of mutual funds as the standard IRA investment, you can invest in a wide variety of assets, including real estate, stocks and bonds. The main differences between a Roth and a traditional IRA are –

- A Roth is not deductible when you contribute to it
- Distributions from a Roth are generally not taxed
- You are not required to begin taking funds out of your Roth at age 70-1/2
- The requirements for contributing to a Roth are more relaxed than for a traditional IRA

As you can see, Roth IRAs are not just for "young people". They can also be a great tool for estate planning. However, the fact that contributions are non-deductible has kept many people from funding them. The maximum you can contribute in 2009 to any combination of IRAs is $5,000 ($6,000 if you are 50+).

You can also convert funds from a regular IRA to a Roth IRA, which brings me to this month's planning theme. You may never have a better opportunity to grow wealth for the future than in the current market. Both stock prices and income tax rates are at historic lows. In addition, many people have seen their taxable income take a dip. How can we use this to our advantage and use "lemons" to make lemonade?

For 2009, if your Modified Adjusted Gross Income ("MAGI") is $100,000 or less, you can convert funds from other retirement accounts (including SEP-IRAs, SIMPLEs, 401k's, and traditional IRAs) into a Roth IRA. (In 2010, there is no income restriction.) Since you will have to pay income taxes on any amounts that you put into your Roth IRA, you are probably wondering why on earth I would recommend that you consider doing this. Here's why:

- You will be "paying off the mortgage" on your retirement account using undervalued stocks so that all future growth will be tax-free.
- Your taxable income bracket may be lower than normal, allowing you to pay taxes on the conversion at a lower rate.
- In Kentucky, retirement "income" of up to $41,110 per person is not taxed. You and your spouse could potentially exclude over $80,000 of income from Kentucky taxation!
- You remove the uncertainty of future tax rates from IRA distributions. In other words, you will lock in your IRA at current tax rates.
- Investments kept over a year and sold at a gain are usually taxed at advantageous capital gains tax rates. However, when they are locked inside a traditional IRA, all distributions

are taxed at the taxpayer's highest (incremental) tax rate. By converting (or contributing) to a Roth, you are paying ordinary rates on the contribution only, *not on future growth*. (By the way, this is the reason that I **rarely** suggest that a person in a high tax bracket make a non-deductible IRA contribution.)

- Last, but not least, you will be in control over when – or if – you decide to take distributions out of your IRA. This is especially helpful for our clients who want to leave their IRAs to their heirs. Although the value of the IRA is included in the taxable estate (if any), distributions to heirs are tax-free.

Of course, these strategies assume you **begin** with quality investments that you expect to eventually regain their foothold in the market.

Finally, you may wonder what happens if, after you convert funds to a Roth, your MAGI ends up above the $100,000 threshold. Good news! This is one of the few areas that the IRS allows you a "do-over" (think of it as a tax mulligan) called a "recharacterization". Specific rules apply, so be sure to discuss this with your financial professional.

Can anything good come out of your misfortunes in the stock market? Actually, opportunities abound if you know where to look! Next month, we'll look at more IRA planning tips.