



THE FINANCIAL SIDE OF RETIREMENT PLANNING

Converting your Traditional IRA to a Roth IRA?

Three considerations when converting to a Roth IRA

Both traditional IRAs and Roth IRAs are powerful savings tools, and it is important to determine with your advisors whether your current IRAs best fit your retirement plan. If you have a traditional IRA and are thinking about converting it to a Roth IRA, three considerations may help you determine if it is the best option for you.

1) Traditional IRAs vs. Roth IRAs

It is important to understand the basic income tax differences between a traditional IRA and a Roth IRA. Traditional IRAs offer a tax-deferred method of saving for retirement, but the pre-tax contributions and earnings will be taxed at ordinary income tax rates as distributions are made. Roth IRAs, on the other hand, allow the assets within the account to grow free of income tax, but only after contributions have been subject to income tax.

2) Factors to weigh

Roth IRAs can generally be created by contributing after-tax dollars to a Roth account or to an employer-sponsored Roth plan or by converting a traditional IRA to a Roth IRA. Converting a traditional IRA to a Roth IRA involves consideration of a number of factors, including the following:

- **Income taxes** – With a Roth conversion, you pay income taxes on the total amount converted in that tax year. The resulting tax liability – and how it will be paid – can be a significant factor in determining how much of a Roth conversion is appropriate.
- **Income tax rates** – Since a Roth conversion triggers ordinary income, another important factor can be the income tax rate that applies to your taxable income today and the rate that may apply in the future (for you or your beneficiary). If your current tax rate is relatively high, then it may not be as beneficial to trigger a significant amount of ordinary income today.
- **Distributions** – A key feature of Roth IRAs is that there are no required minimum distributions, which means the full value of your Roth IRA is positioned for future potential growth and eventual tax-free distributions. However, if you may need to access the assets within five years or while you are under 59 ½, then you may want to reconsider the amount being converted.
- **Estate planning** – Converting to a Roth IRA now may allow you to provide your designated beneficiaries with income tax-free access to a substantial sum of money. However, if you intend to use your IRA to benefit charity during life or upon death, a Roth conversion may be less valuable.

3) Order of distribution

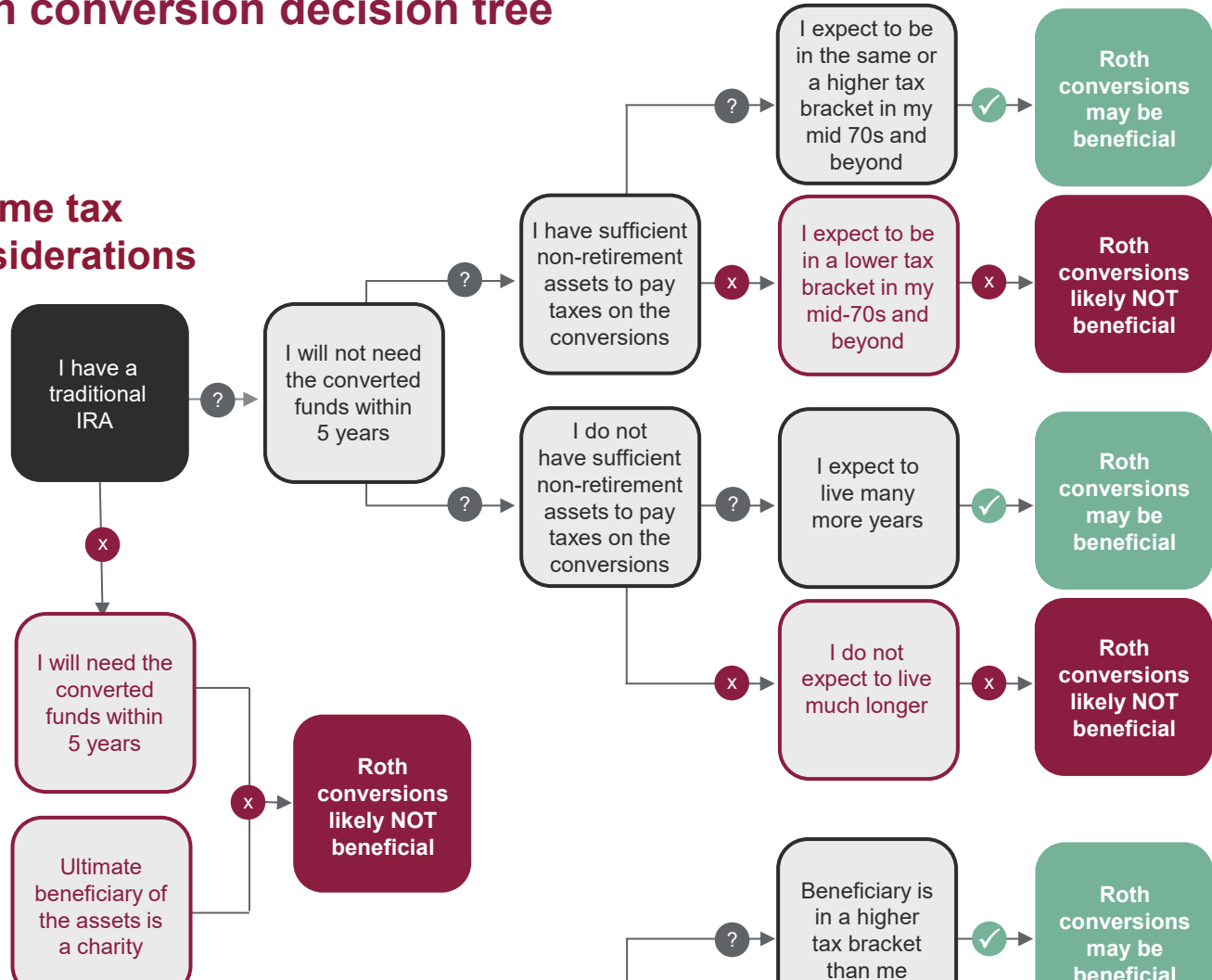
Once a conversion to a Roth IRA has been made, there is a five-year period during which some part of a distribution may still be subject to tax. The rules for determining whether a distribution is a tax-free distribution (often referred to as a “qualified distribution”) include the following:

- **Regular contributions** – Because regular contributions are contributed after tax, distributions of those regular contributions are free of federal income tax.
- **Conversion contributions** – Taxes have already been paid on converted contributions. However, withdrawals made before the five-year period ends may be subject to a 10% premature distribution penalty tax.
- **Earnings** – Qualified distributions of earnings are not subject to federal income tax or penalties. However, nonqualified distributions made before the five-year period ends are taxable to the extent earnings are withdrawn. Also, if earnings are withdrawn before the age of 59 ½ then they may be subject to tax and penalties if an exception does not apply.

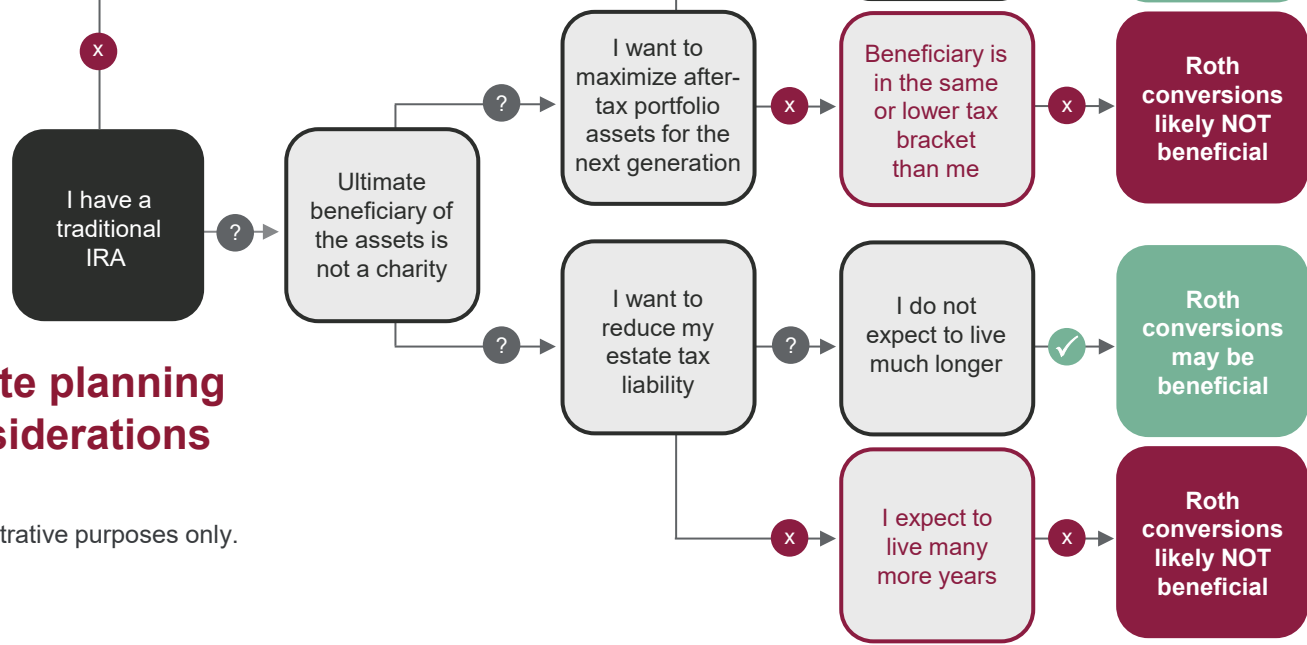
The determination of whether converting a traditional IRA to a Roth IRA is right for you involves a number of considerations that depend on your personal circumstances. The following decision tree with an income tax branch and an estate planning branch may help you decide; if you get a different result when working through each branch, you may need to decide which set of considerations is more important to you. **For more information on IRAs, talk to your CIBC Private Wealth advisor or visit our *The Financial Side of Retirement Planning* resource page.**

Roth conversion decision tree

Income tax considerations



Estate planning considerations



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