VANTAGE FINANCIAL PARTNERS LIMITED

IRA CONVERSIONS

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Much has been written lately about the new Roth IRA conversion rules beginning in 2010, to allow high-income taxpayers to convert part or all of their traditional IRAs to Roth IRAs. The IRS is even encouraging conversions by allowing taxpayers to pay the tax for a 2010 conversion in two installments in 2011 and 2012. But the question facing many is this: Does it makes sense to convert and pay the tax up front or keep the current tax deferral until it needs to be withdrawn?

Currently, through 2009, Roth conversions are only allowed if your adjusted gross income does not exceed $100,000 (either single or married). Starting in 2010, there is no income limit for conversion so high income earners have the opportunity to convert to a Roth for the first time.

TRADITIONAL VS. ROTH

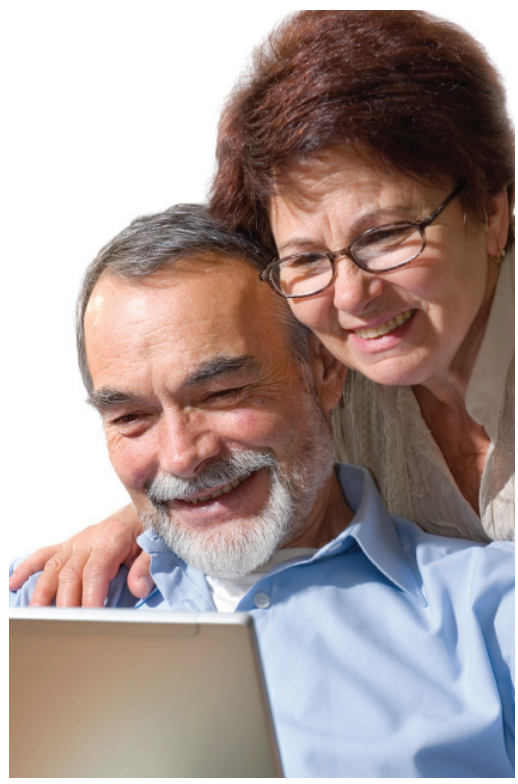
A traditional IRA allows the taxpayer to deduct both contribution and earnings until the time of distribution when the entire amount is taxed. The typical taxpayer still in the workforce is theoretically in a higher tax bracket when the contribution is made, and in a lower tax bracket when it is distributed in retirement. In this situation, the traditional IRA makes sense. The Roth IRA, on the other hand, is not tax deductible when contributed. However withdrawals, including earnings, are tax free when distributed in retirement. The Roth IRA essentially shifts the risk of rising tax rates back to the government. If you think tax rates will climb or your income will grow over time, then a Roth could be a good hedge against rising tax rates.

There are other rules for each of these IRAs that complicate the process of deciding which is better for a given taxpayer. Both types of IRAs generally require you to be 59½ before any distribution or suffer a 10% penalty (subject to a common exception). However, a traditional IRA forces you to take a required minimum distribution at 70½, whereas a Roth has no such requirement. A Roth, on the other hand, must be in existence at least 5 years before any tax-free distributions can be made.

Your heirs will prefer a Roth to a traditional IRA. Those who inherit a traditional IRA will have to pay income tax on any distribution, whereas inheriting a Roth entails no income tax liability to the heirs.

SHOULD I CONVERT?

The decision to convert some or all of a traditional IRA to a Roth is often a difficult one. The future of tax rates is a key consideration. We know tax rates are likely to go up once the Bush tax cuts expire in 2011 and the Clinton-era top brackets are restored at 39.6%. If the rates go even higher due to the growing deficits, it may be worthwhile to convert a portion to a Roth in 2010 while the rates are low. On the other hand, if your income is likely to be much lower in retirement, it may be wise to preserve the status quo even if rates go up since your actual tax rate may be lower.



While the IRS allows the tax cost of a 2010 conversion to be split in two and delayed until the 2011 and 2012 tax years by election, those later years will likely have higher rates than in the year of conversion. For high bracket taxpayers it may be beneficial to pay the entire tax in 2010 at the lower rate than to delay the tax but pay a higher rate.

It may make more sense for younger taxpayers to convert to a Roth as the conversion is likely to be smaller and the tax rates lower than later in their lives. In general, the younger the person the better a Roth looks when compared to a traditional IRA.

If you find yourself unemployed, or otherwise anticipate that for the year your income will be unusually low, you might want to consider converting some of your IRA while temporarily in a lower tax bracket.

Finally, with any conversion the maximum benefit is realized only if you pay the tax out of other funds and transfer the entire IRA amount to the Roth. In addition, if you pay the tax out of the converted amount and are under 59 ½, you will be subject to the 10% penalty. So if you do not have other funds available then you may want to wait or convert gradually over time.

WHAT TO DO?

Your relationship manager will be happy to discuss the pros and cons of a Roth conversion in your particular situation.

VANTAGE NEWS

We hope everyone enjoyed a wonderful Thanksgiving with family and friends as we did. Thanksgiving is a time to appreciate all that we have to be thankful for but can also be a time to help others. Many Vantage team members and their families were privileged to serve alongside the volunteers and founders of PATH – Palatine Assisting Through Hope in preparation for their 4th Annual Day of Giving. PATH is a not-for-profit organization primarily focused on serving the needs of families within the local community of Palatine, Illinois. This year's annual Day of Giving provided donated clothing to almost 400 needy families! Thank you PATH for helping so many families and for providing us an opportunity to serve.

REMINDER – Beginning next month, this newsletter will only be available to email subscribers. If you are not currently receiving this via email, please contact us to insure we have your current email address on file.