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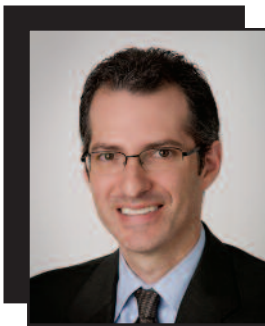
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By Steven M. Sheldon, CFA

About SMS Capital Management

SMS provides investment management services to individual investors desiring to preserve and build long-term wealth. As a fee-based firm, SMS has an independent, objective and sound approach to portfolio management. The firm is a Registered Investment Adviser.



About the Author

Steven Sheldon has more than thirteen years of professional experience analyzing and managing investments. Prior to founding SMS, Mr. Sheldon worked as a senior member of a corporate principal investments group. Mr. Sheldon has an MBA from Tulane University and a BBA from The University of Texas. In addition, he is a CFA charterholder and a member of both the CFA Institute and the Houston Society of Financial Analysts (HSFA).

Should You Convert? - The 2010 Roth Conversion Option

In 2010, the income restriction on converting an IRA into a Roth IRA will be lifted, potentially giving some investors a good opportunity to utilize the Roth IRA retirement savings vehicle.

In the past, only households with Modified Adjusted Gross Income below \$100,000 were eligible to convert. However, starting in 2010 there will be no income limit on conversions (annual contribution limits will still apply for Roth IRAs) and any resulting taxable income can be deferred equally to 2011 and 2012. All types of pre-tax IRA accounts qualify for conversion including traditional, rollover, and SEP.

Who Will Benefit from Conversion?

The key difference between a traditional IRA and a Roth are that Roth IRA funds are “after tax”; the money grows tax-free and withdrawals in retirement are also tax-free. Furthermore, Roth IRA funds are not subject to Minimum Required Distributions (MRD’s) during retirement.

By converting a traditional IRA to a Roth IRA an investor can pay tax today on existing IRA funds (at current tax rates) rather than in retirement at some unknown future tax rate. So, investors that anticipate being in a lower tax bracket in 2010 and a higher one in retirement certainly are prime candidates for converting to a Roth. Also, those with adequate funds outside of their IRA accounts to pay the taxes would benefit the most since utilizing retirement funds to pay the tax bill is generally not advisable.

In determining if it’s advantageous to convert or not, investors need to be aware that funds being converted to a Roth count as ordinary income in the year of conversion. Depending on the amount being converted, it is possible that the additional income may move the taxpayer into a higher tax bracket; thereby making the conversion less beneficial.

Even if a taxpayer is in a high tax bracket, a full or partial conversion still might make sense. Another benefit of Roth IRA’s is that they are not subject to the Minimum Required Distribution (mandates required distributions beginning at age 70 ½) during retirement so investors can keep more funds invested in a tax advantaged vehicle during retirement. Also, for those with retirement accounts comprised of all “pre-tax” savings vehicles, the Roth offers an opportunity to hedge against higher future tax rates.



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Working the Math and Taking Action

For those that are considering the conversion, it is important to work through the numbers under various assumptions to see if there is an economic benefit. Important variables include expectations for future tax rates, expected return on investments, and age of withdrawals. SMS Capital Management can work with you to consider whether or not a conversion (either full or partial) to a Roth makes sense.

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