

2010 Roth IRA Conversion:

Great Opportunity or a Shell Game?

(Camp Hill, PA – January 4, 2009) Local financial services expert, Matthew Dobbie, Managing Partner of Financial, offers his professional perspective on the upcoming 2010 Roth IRA changes:

“The financial world is buzzing with the upcoming tax law changes surrounding Roth IRAs in 2010. Everywhere you look there are articles touting this tremendous chance to move your money from a taxable to a tax-free account.

Does this sound too good to be true? Should you jump on this timely opportunity right away, or is it more like a shell game, where all the odds are stacked in someone else’s favor?

Let’s start with what we do know. Unlike traditional IRAs, there are no federal income tax deductions for contributions to a Roth IRA. However, a Roth IRA does provide benefits that aren’t found in any other retirement plan, a tax-free withdrawal of all earnings and principal. So far, everything sounds great.

Starting in 2010, taxpayers, regardless of their income, will be allowed to convert a traditional IRA or 401(k) to a Roth IRA. This conversion will involve paying the federal taxes on this money since they have not been taxed till this point. One nice wrinkle is that the income taxes due on the 2010 conversion can be spread over two years. So the 2010 conversion amount may be included as taxable income in 2011 and 2012 - helping to spread out the tax bite. This sounds even better.

So the question becomes, why wouldn’t everyone start making their conversions in 2010? Here is where, as they say, the rubber hits the road.

Again, we can start with what we know. There are some straight forward calculators any financial advisor can use to determine when the benefits of converting work in your favor. Specifically, how long will it take until the cost of paying the taxes due now, is offset by the fact that your money will now be eligible for use on a tax-free basis?

However, a couple of problems start to arise when doing these calculations. First, what rate of return are you going to get on your money? Is it going to grow at 5%, 8%, or 10% per year? What happens if the stock market stays flat for the next 5 or more years? Also, what is your

future tax rate going to be? Higher, lower, or the same? All of these factors can make a significant impact on whether this conversion is right for you.

Now, let's consider for a moment what we don't know. All of the above scenarios assume the rules governing the tax treatment of Roth IRAs will not change. Meaning, we are assuming the government will never change their mind and decide to tax Roth IRAs in the future if they need more revenue. Could you conceive of a time when more tax dollars are needed to support government programs? If this happened, is it possible you could be taxed twice on the same money?

My dad always warned me never to bet on a shell game in Central Park. When the person running the game can stack all the rules in their favor, it is best to stay away.

So, are Roth conversions a modern day shell game? Probably not. However, you may want to consider all of your options before making any significant changes to your investments. You may want to hire a qualified financial planner and a tax advisor to review all of your options.

Your investment time horizon and tax circumstances can make all the difference in the world when deciding when whether a conversion is right for you."

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About uFinancial

uFinancial offers a full range of financial products and services for individuals and businesses. The Camp Hill, PA based company also has offices in State College and Chester County. It is a general agency of Massachusetts Mutual Life Insurance Company, which has been serving the Central PA region since 1890. The firm is experienced in retirement planning, education funding strategies, estate planning, life, disability and long-term care insurance, employee benefits, and succession planning. Matthew Dobbie, general agent, and the rest of the uFinancial team can be reached at 717-763-7365 or mdobbie@finsvcs.com. uFinancial is on the Internet at www.uFinancialGroup.com.

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