IS A ROTH IRA RIGHT FOR YOU?

Should you contribute to a Roth IRA (individual retirement account) or a traditional IRA for the current tax year? There is no definitive answer. However, for many high-income taxpayers, the Roth IRA can produce better results over the long haul.

BASIC PREMISE

Unlike a traditional IRA, contributions to a Roth IRA are never tax deductible. However, qualified distributions from a Roth IRA are 100% tax-free, so you benefit on the back end.

A qualified distribution is made from a Roth IRA in existence for at least five years and paid:

- After reaching age 59½.
- Because of death or disability.
- For first-time homebuyer expenses (up to a lifetime limit of $10,000)

For the 2021 tax year, an eligible individual can contribute to a Roth IRA of up to $6,000 (1,000 more in 2021 if he or she is age 50 or over). This assumes you had at least that amount of annual compensation. The maximum contribution amount is reduced by any contributions to traditional IRAs (but not contributions to a SIMPLE [savings incentive match plan for employees] IRA or a SEP [simplified employee pension] IRA).

However, the allowable contribution to a Roth IRA is phased out for certain high-income taxpayers. For 2021, the phase-out occurs between $196,000 and $206,000 of adjusted gross income (AGI) for joint filers; $124,000 and $139,000 for single filers. As with a traditional IRA, you have until the tax return due date for your return - generally, April 15 of the following year - to contribute for the current tax year.

ROTH IRA CONVERSIONS

In addition to Roth IRA contributions, there's another way to get money into a Roth IRA. It's called a Roth IRA conversion In a Roth IRA conversion, retirement money is withdrawn from an existing retirement account, such as an IRA or 401(k) and is moved into the Roth IRA. The biggest benefit of a Roth IRA conversion is that after the conversion is made, the converted funds and all the future growth may be able to be distributed tax penalty-free.

There are no restrictions on who can make Roth IRA conversions. You can't be too old or too young. You can be working, or you can be retired. There's no minimum amount of income you need or a maximum amount of income you can have. You can file your tax return as a single person, jointly with your spouse or even as a married person with a separate return from your spouse. It simply does not matter.

EXAMPLE

When you make a Roth conversion, you must generally add the amount converted to your income for the year. That income will be taxed at whatever income tax bracket you find yourself in and could potentially result in any of the costly "side effects" described earlier for IRA withdrawals. Roth conversions are irrevocable decisions. If you decide to make one, you'll be stuck with the resulting tax bill. That makes doing your homework *before* making a Roth IRA conversion important. Before converting, you should typically have a rough estimate of the conversion's potential impact on your tax bill, a reasonable expectation that the benefits of "pre-paying" taxes this way make sense in your overall plan, and a strategy for paying the additional taxes.