

private client services update

November 17, 2009

THREE ROTH CONVERSION PLANNING OPPORTUNITIES

Shad C. Fagerland, Esq.
David Kamer, Esq.

Beginning in 2010, the current income limit on conversions from a traditional IRA to a Roth will be lifted, allowing high-income taxpayers to take advantage of this powerful tax-planning vehicle for the first time. While a Roth conversion may not appeal to all taxpayers, here are three situations where conversion might be particularly attractive.

1. Charitable Giving. Individuals who are planning charitable gifts in coming years might consider accelerating those gifts into the 2010 taxable year in order to offset taxes triggered by a Roth conversion. Normally, a Roth conversion triggers income tax at combined state and Federal rates of approximately 40% of the value of the converted IRA. If the taxpayer makes charitable donations equal to the value of the converted IRA in the same year, this could reduce the income tax hit to 20% of the converted IRA value. For the charitably inclined, it might be an opportune time to add a Roth conversion to the mix.

For Roth conversions done in 2010, a one-time rule allows the taxable income to be spread over two years, so charitable gifts in this instance could be made half in 2010 and half in 2011 to offset the Roth conversion taxes.

2. The Roth Mulligan. In a time of market uncertainty, some individuals may be concerned that they will pay taxes on a Roth conversion only to have the underlying investments lose value, in which case they would have been better off leaving the assets in a traditional IRA. Fortunately for taxpayers, the Roth conversion rules include a liberal "recharacterization" option that allows taxpayers to "undo" Roth conversions by October 15th of the following year. This recharacterization opportunity applies separately to each Roth IRA established by an individual.

These rules allow taxpayers to effectively take a "mulligan" on any Roth investments that perform poorly out of the gate. For instance, consider a taxpayer who converts a traditional IRA to a Roth IRA in 2010 and invests the proceeds in three different mutual funds. If the individual establishes three different Roth IRAs, one for each of the three mutual funds, he will then have until October 15, 2011 (assuming that the taxpayer duly extends his tax return filing date) to decide which of the Roths to keep and which to scrap. Any funds that have gained in value since the conversion date can remain in the Roth account. Any funds that have lost value can be recharacterized as a traditional IRA, with the result that the taxpayer no longer owes taxes in connection with the Roth conversion and is further entitled to a refund of any taxes previously paid on the conversion. Better yet, any IRAs recharacterized in this manner can again be converted to Roths in future taxable years, with yet another chance to recharacterize if the underlying investments perform poorly by the recharacterization deadline.

3. The Roth Business Ownership Plan. In a previous client alert, we outlined the Roth Business Ownership Plan or "Roth BOP," a strategy that allows an individual to use assets held in a Roth account to purchase a closely held business. A recent decision by the Tax Court (*Taproot Administrative Services, Inc.*, 133 T.C. 9) confirmed the viability of this approach, ruling that a Roth IRA may be a majority shareholder of a corporation controlled by an individual provided that the corporation is a "C" corporation and not an "S" corporation. This ruling, while not surprising, reaffirms the usefulness of the Roth BOP for an individual who wishes to purchase a business using funds held in a Roth account.

KAUFMAN & CANOLES

attorneys at law

P.O. Box 3037
Norfolk, VA 23514

PRSR STD
U.S. POSTAGE
PAID
Newport News, VA
Permit #110

IN THIS ISSUE

- THREE ROTH CONVERSION PLANNING OPPORTUNITIES

ABOUT THE AUTHORS



Shad C. Fagerland is a partner in the firm's Williamsburg office, where his practice focuses on qualified and nonqualified retirement plans. Shad can be reached at (757) 259.3828 or scfagerland@kaufcan.com.



David Kamer is a partner in the firm's Norfolk office, where he maintains a trusts & estates practice with particular focus on professionals and executives and non-profit organizations. David can be reached at (757) 624.3175 or dkamer@kaufcan.com.

PRIVATE CLIENT SERVICES

Visit our new website at www.kaufCAN.com.

who we are

Vonda W. Chappell	vwchappell@kaufcan.com	(757) 546.4150
Lawrence G. Cumming	lgcumming@kaufcan.com	(757) 224.2910
Jason R. Davis*	jrdavis@kaufcan.com	(757) 624.3119
Gregory R. Davis	grdavis@kaufcan.com	(757) 259.3820
Robert C. Goodman Jr.	rcgoodman@kaufcan.com	(757) 624.3238
Philip L. Hatchett	plhatchett@kaufcan.com	(757) 873.6316
R. Braxton Hill III	rbhill@kaufcan.com	(757) 624.3106
William L. Holt	wlholt@kaufcan.com	(757) 259.3885
David Kamer	dkamer@kaufcan.com	(757) 624.3175
Kirkland M. Kelley	kmkelley@kaufcan.com	(757) 624.3283
Alison V. Lennarz	avlennarz@kaufcan.com	(757) 259.3830
Sarah E. Messersmith	semessersmith@kaufcan.com	(757) 224.2950
E. Duffy Myrtetus*	edmyrtetus@kaufcan.com	(804) 771.5750
W. Hunter Old*	whold@kaufcan.com	(757) 259.3870
Alexander W. Powell Jr.	awpowell@kaufcan.com	(757) 259.3877
Robert H. Powell III	rhpowell@kaufcan.com	(757) 624.3245
Winthrop A. Short Jr.*	washort@kaufcan.com	(757) 873.6301
James G. Steiger	jgsteiger@kaufcan.com	(757) 624.3234
Edward R. Stolle	erstolle@kaufcan.com	(757) 491.4033
Lewis W. Webb III	lwwebb@kaufcan.com	(757) 624.3247

* Attorneys whose practice is limited to litigation matters

If you would like to be added to the Kaufman & Canoles mailing list or if your name, title, company, or address needs to be revised, please notify Kerry Martinolich, Kaufman & Canoles, P.O. Box 3037, Norfolk VA 23514 T (757) 624.3158 F (757) 624.3169 kamartinolich@kaufcan.com

Copyright © 2009. Kaufman & Canoles. All Rights Reserved. The contents of this publication are intended for general information only and should not be construed as legal advice or a legal opinion on specific facts and circumstances.