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# DouglasBradley

Personal Financial Advisors

## DouglasBradley's MONEYWISE

Financial News and Insight from an Independent Advisor

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### Personal Notes

**Doug** - My work on the BMW suspension is finally completed with the required four-wheel alignment. The car now drives better than new. Lesson learned: I now appreciate why professional mechanics use air tools. It's amazing how much time they save.

Lacrosse is in full swing - I coach my oldest daughter and my youngest son and the differences in play couldn't be more different. While the girls are more reserved on the field and appreciate the benefits of spreading out/getting open for passes the boys sprint all over the field - chasing the ball and slashing each other with their sticks. All that protective equipment really is required - none of them would walk off the field in one piece otherwise...

**Brad** - I've decided to do my share to help stimulate the economy. I bought my house new in 1990 and haven't done anything to update it since. This was the era before hardwood floors, granite counter tops, etc. that seem to have become the standard for many. By way of a timely introduction by a good friend and client, I've been able

### DouglasBradley - The Next Stage

A year ago, we decided we needed to freshen up our website. What started as a simple website redo turned into a real soul search for us. In the midst of the financial melt down, we spent a lot of time thinking about this business of financial advice, the benefits we provide to clients and how the majority of the industry is failing the American public. We gave ourselves permission to break the bonds that the industry places on us.

The result of all this thinking is a new sense of who we are and what we do, which is reflected in the new logo at the top of the page, the action we request that you take at the bottom of the page and all the new content on our website.

We have several changes planned for our clients toward the end of the year that we believe will reinforce our dedication to helping them retire on their terms. But for now, we're excited to share the new web site with you and would love to hear what you think.

[Visit The New Site!](#)

### Beware the Roth Conversion Hype

During the Bush administration, dramatic tax changes were announced that brokerage firms and the financial media have been anxiously anticipating - the 2010 Roth Conversion. While Roth Conversions are nothing new, in years past a taxpayer couldn't convert a traditional IRA to a Roth if the Adjusted Gross Income (AGI) on your federal tax return exceeded \$100,000. This year is the first year the \$100,000 AGI cap is removed. And everyone's jockeying to use the "2010 Roth Conversion" as the financial Holy Grail to attract these wealthy taxpayers who now qualify to convert.

The argument for converting an existing traditional IRA is that a taxpayer should pay income taxes today on the traditional IRA and get the tax-FREE future growth afforded by a Roth IRA. Never paying income tax on the earnings in your new Roth IRA sounds great, doesn't it?

We've spent a considerable amount of time making sure we understand the income tax implications associated with initiating a Roth Conversion. If you have been waiting to do a Roth Conversion or are being advised to do a Conversion, our word of warning is to proceed carefully and thoughtfully. This is not necessarily the slam dunk it has been portrayed as.

to partner with a skilled and knowledgeable general contractor who will guide me through the remodeling process. I'm looking forward to accessing the skilled tradespeople who would have been unattainable in the past due to their workloads. Something I wouldn't have expected, but have quickly come to appreciate, is that the kitchen cabinets (being that they cost a small fortune) will be the determining factor for all other decisions.

**Mahesh** - I'm ready to get back into soccer mode. After taking a four week break from the winter basketball season, I will resume coaching my daughter's soccer team for the 6th season. Her team has been placed into a new conference because of the undefeated season from the Fall of 2009. Coach Mo (aka me) hopes that the level of competition will really challenge the girls! Hopefully, Coach Mo will continue the team's unbeaten streak.

This is far from an exhaustive discussion, but here are some important points to keep in mind:

- The taxable amounts converted from traditional IRAs are added to all your other income on your tax return during the year the conversion takes place. This has the very real potential of pushing a taxpayer into higher tax brackets. (There is a special rule for 2010 conversions: the taxable conversion amount can be split between your 2011 and 2012 tax returns)
- Calculating the taxable amount of the conversion is a very complicated process and takes into account all of a taxpayer's traditional IRAs (including rollovers, SEPs and SIMPLEs). So you can't convert the small IRA you've been making non-deductible contributions to for years and ignore the huge IRA Rollover from your previous employer. You'll get a nasty surprise on your tax return.
- Taxes due on the conversion amount should be paid "out-of-pocket" by the taxpayer; it is ill-advised to pay the taxes from monies in the IRA since you will be undermining the tax benefit and paying penalties.
- The income tax liability is entirely dependent on the taxpayer's situation in the year of the conversion and is based on information that can only be known at the end of the year - presenting a real challenge.
- The argument that tax-free distributions on the future earnings outweigh paying taxes today depends on very important assumptions about the future. These include: the taxpayer's income in the future; future income tax rates; growth of the IRA accounts; length of time the money grows before distribution; and, the continued tax-free status of Roth IRA distributions in the future.

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Our modeling of the various scenarios provides no definitive guidance due to the large number of assumptions and unknowns. We find we can easily generate a recommendation for or against converting using equally realistic assumptions. Our findings have been confirmed by many of our peers who have done the same analyses for their own clients.

In summary, we believe that for the person without extenuating circumstances it will be nearly impossible to arrive at a conclusive answer. Much of the enthusiasm for the Roth Conversion is being driven by those with a vested interest and/or a limited understanding of the income tax subtleties who are content to speak in generalities.

With that said, our modeling also suggests that you cannot make a "wrong" decision either. Therefore, if you fully appreciate the income tax consequences, can pay them out of pocket and have the time to grow the converted amount, we suggest you look at a partial conversion to balance out the possible outcomes.

If you have any questions or would like additional information on Roth Conversions, please contact us and we'll do what we can to help.

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