



**Regardless of your filing status or how much you earn, you'll be able to convert a traditional IRA to a Roth IRA starting in 2010.**

## Roth IRA Conversions in 2010: Goodbye, Income Limits!

With the lure of tax-free distributions, Roth IRAs have become popular retirement savings vehicles since their introduction in 1998. But if you're a high-income taxpayer, chances are you haven't been able to participate in the Roth revolution. Well, that's about to change.

### What are the current rules?

For 2009, if your modified adjusted gross income (MAGI) is greater than \$100,000, you can't convert a traditional IRA to a Roth IRA. This \$100,000 limit applies whether you're single or married filing jointly. And if you file your taxes as married filing separately, you can't make a conversion at all--regardless of your income level.

In addition, your ability to make annual contributions to a Roth IRA depends on your MAGI:

If your federal filing status is:	Your Roth IRA contribution is reduced for 2009 if your MAGI is:	You can't contribute to a Roth IRA in 2009 if your MAGI is:
Single or head of household	\$105,000 but less than \$120,000	\$120,000 or more
Married filing jointly or qualifying widow(er)	\$166,000 but less than \$176,000	\$176,000 or more
Married filing separately	More than \$0 but less than \$10,000	\$10,000 or more

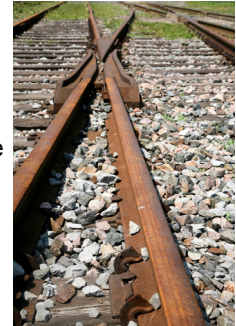
### What is--and isn't--changing

In 2006, the Tax Increase Prevention and Reconciliation Act (TIPRA) became law. TIPRA repeals the \$100,000 income limit for conversions, and allows conversions by taxpayers who are married filing separately, beginning in 2010. This means that regardless of your filing status or how much you earn, you'll be able to convert a traditional IRA to a Roth IRA starting in 2010.

Unfortunately, TIPRA does not repeal the income limits for annual Roth contributions. However, depending on your circumstances, beginning in 2010 you may be able to make your annual IRA contribution to a traditional IRA, and then convert that IRA to a Roth. Your financial professional can help you determine if this works for you.

### Convert now, pay later

Normally, when you convert a traditional IRA to a Roth IRA, you're required to include the amount converted--minus any nondeductible contributions you've made--in your gross income in the year you make the conversion.



However, to ease the pain of a potentially large tax hit in 2010, TIPRA includes a special rule for 2010 conversions only: if you convert your traditional IRA to a Roth IRA in 2010, you can report half the income from the conversion in 2011, and the other half in 2012.

For example, assume that in 2010 your sole traditional IRA is worth \$200,000, and you've made \$50,000 of nondeductible contributions. If you convert the entire IRA to a Roth in 2010, \$150,000 will be subject to federal income taxes. If you use the special rule, you can report half of the taxable amount (\$75,000) as income in 2011, and the other half as income in 2012. Alternatively, you can report the entire \$150,000 as income in 2010. (Note: state tax rules may differ.)

(Note that a SEP IRA can also be converted to a Roth IRA, and a SIMPLE IRA can be converted two years after you begin participating in your employer's SIMPLE IRA plan.)

### Is a Roth conversion right for you?

The answer is complicated, and depends on many factors, including your income tax rate, the length of time you can invest the funds without withdrawals, your state's tax laws, and how you'll pay the income taxes due on the conversion.

Even if you decide to convert, whether it makes sense to use the special 2010 deferral rule depends on your individual situation. It may also depend on where you think income tax rates are headed. If you expect rates to be lower in 2010 than in 2011 and/or 2012, deferring the tax hit may not be a good idea. Your financial professional can help you run projections to determine if the special rule is appropriate in your particular case.

## Estate Planning Opportunities in a Down Market

A down market can mean tough times, but it can also present unique opportunities to minimize property transfer (gift and estate) taxes. While owning assets that are losing value might seem like a bad thing, it may actually be a great time to reduce your taxable estate by gifting those assets to beneficiaries. That's because current low asset values and interest rates enable you to make gifts at a lower gift tax cost. And, if and when the market rebounds, those assets will be growing in your beneficiary's estate and not in yours. Here are a few gift-giving techniques that take advantage of today's economic climate.

**Note:** *This article discusses federal tax rules only. Individual states impose their own property transfer taxes using rules that may be different from the federal rules.*

### Basic gifting

Each year, you can make gifts of up to \$13,000 to anyone you want, to as many people as you want, tax free under the annual gift tax exclusion. You can give away twice that amount if both you and your spouse make the gifts together (this is called gift splitting). And, you can give away an unlimited amount if you pay tuition or medical bills on behalf of another person (just be sure to make these payments directly to the school or health-care provider).

### Family loans

You can lend money to your children at the current IRS minimum interest rate (known as the AFR, which changes monthly), and then potentially forgive an amount equal to the gift tax exclusion each year. (The gift tax exclusion amount is adjusted for inflation; \$13,000 is the figure for 2009.)

### Grantor retained annuity trust (GRAT)

A GRAT is an irrevocable trust with a specified term (e.g., 10 years) into which you gift assets that you expect will greatly increase in value in the future. You receive annuity payments during the trust term, and at the end, your beneficiaries receive any remaining property.

The transfer of assets to the GRAT is a taxable gift to the trust beneficiaries. The value of the gift for tax purposes is determined based on the current IRS rate (known as the 7520 rate, which also changes monthly).

Tax savings are achieved because the

annuity payments are calculated to result in a gift tax value of zero. It's anticipated, however, that the actual interest earned will be higher than the 7520 rate, leaving a substantial value in the GRAT at the end of the term. This remaining value is passed on to your beneficiaries tax free.

### Intentionally defective grantor trust (IDGT)

An IDGT is an irrevocable trust that has a purposeful flaw (i.e., you retain some control over the trust) so that you, and not the trust entity, pays the income taxes on trust income (thus, an IDGT is ideal when you want to transfer income-producing assets). Even though you retain some control over the trust, IDGT assets will generally not be included in your taxable estate at your death.

You sell assets to the IDGT in return for an installment note, with interest calculated based on the current AFR. There is no gift tax because it is a "sale" (except for an initial gift that "seeds" the trust). However, because you and the trust entity are considered the same taxpayer, no gain is recognized on the sale, and interest you receive under the note is not considered taxable income.

Tax savings are achieved because, hopefully, the value leaving your estate via the sale will exceed the value returned to your estate via the note. You also reduce your estate by paying the income taxes on IDGT income.

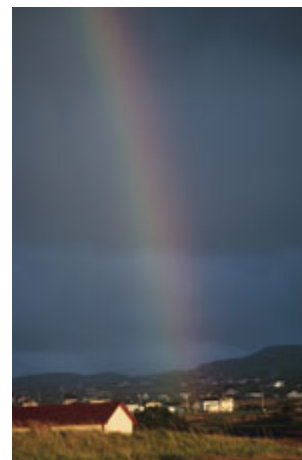
### Charitable lead trust (CLT)

A CLT is an irrevocable trust with both charitable and noncharitable beneficiaries. It's called a lead trust because it is the charity that is entitled to the first or lead interest from the trust property. After the specified term, the remaining trust property passes to you or another named noncharitable beneficiary.

At the time assets are placed into the CLT, you receive a current gift tax deduction equal to the present value of the income stream that will be going to the charity. The interest rate used is based on the current 7520 rate. The lower the interest rate, the higher the deduction. As with a GRAT or IDGT, it is hoped that the CLT assets will appreciate beyond the 7520 rate, allowing the excess to pass tax free.

### Conclusion

These gifting strategies, and others, can turn this economic downturn into a mixed blessing.



**A down market can mean tough times, but it can also present unique opportunities to minimize property transfer (gift and estate) taxes. While owning assets that are losing value might seem like a bad thing, it may actually be a great time to reduce your taxable estate by gifting those assets to beneficiaries.**

**Estate planning tools that are generally less attractive when interest rates are low:**

- *Qualified personal residence trust (QPRT)*
- *Charitable remainder annuity trust (CRAT)*