

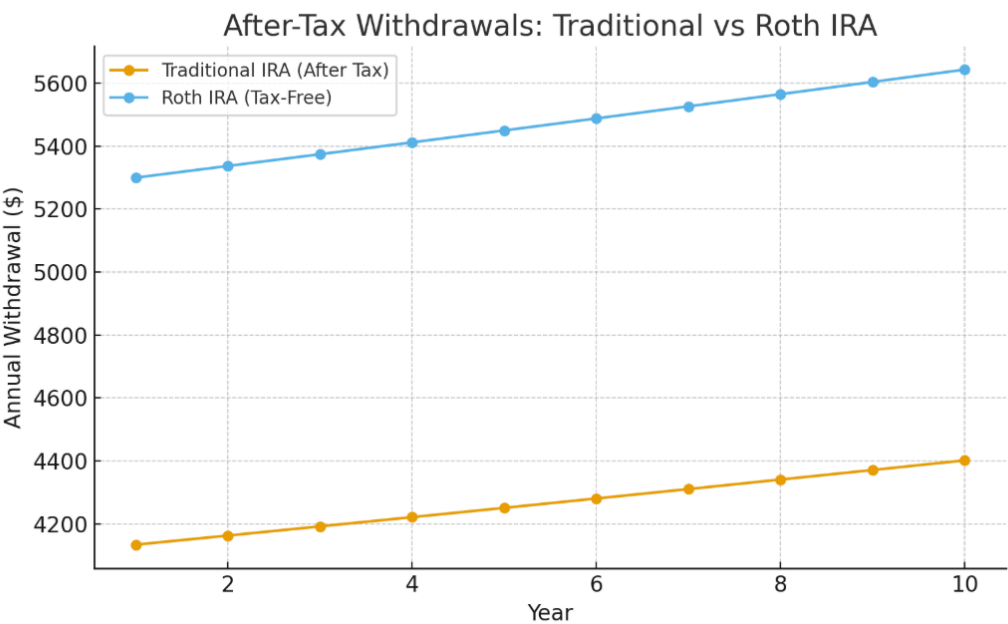
Understanding Roth Conversions: A Client Guide



Understanding Roth Conversions

A Roth conversion is when you move money from a traditional retirement account (like a Traditional IRA or 401(k)) into a Roth IRA. It is a powerful way to pay taxes now, allowing you to enjoy tax-free growth and withdrawals later during retirement.

- + **Taxes now, tax-free later** – Traditional retirement accounts are funded with pre-tax money, so you pay taxes when you withdraw in retirement. With a Roth IRA, you pay taxes on the money when you convert it, but future withdrawals are tax-free.
- + **Why it matters** – Converting can be a smart move if you expect to be in a higher tax bracket later, want to reduce future required minimum distributions (RMDs), or want to leave tax-free money to heirs.
- + **Timing matters** – Because you owe taxes on the conversion, doing it strategically in years when your income is lower can save you money.



Key tax implications include:

- + **Ordinary income taxes apply** – The amount you convert is treated as taxable income in the year of conversion.
- + **No early withdrawal penalty** – Even if you’re under 59½, you won’t pay the 10% penalty, but you still owe income taxes.
- + **Potential higher tax bracket** – A large conversion could push you into a higher tax bracket for that year.
- + **Impact on other taxes/benefits** – The extra income could affect Medicare premiums, Social Security taxation, or eligibility for tax credits.
- + **Future tax-free withdrawals** – Once converted, future qualified withdrawals from the Roth IRA are tax-free.
- + **Five-year rule** – Converted funds must generally stay in the Roth for 5 years (or until age 59½, whichever is later) to avoid penalties on withdrawals of the converted principal



Important pros and cons to consider

Pros

- + Pay taxes now, lock in today’s tax rate (helpful if you expect higher rates later).
- + Future qualified withdrawals are 100% tax-free.
- + Reduces future RMDs since Roth IRAs don’t require them.
- + Can help with estate planning since heirs would inherit tax-free Roth money.
- + Diversifies tax treatment of retirement income (gives flexibility in managing taxable income later).

Cons

- + Conversion amount is taxable income immediately, which can create a large tax bill.
- + May push you into a higher tax bracket the year of conversion.
- + Could increase Medicare premiums (IRMAA) or make more of your Social Security taxable.
- + Five-year holding rule applies before you can withdraw converted funds penalty-free.
- + Paying taxes from the retirement account itself (instead of outside funds) can shrink long-term growth.



5 questions to ask your advisor before making a decision

1. How will this affect my taxes this year?

Will the added income from a conversion push me into a higher tax bracket or change my tax situation in other ways?

2. Should I convert all at once or over time?

Would it be more tax-efficient to convert in smaller amounts over several years rather than a lump sum?

3. Do I have the cash to pay the taxes?

Can I cover the tax bill from non-retirement funds, so more of my converted money stays invested and growing?

4. How could this impact my Medicare premiums or Social Security taxes?

Could the higher income from a conversion increase my healthcare costs or taxes on Social Security benefits?

5. Does this fit my long-term goals?

Will converting now help me reduce RMDs later, create more flexibility in retirement income, or support estate planning by leaving tax-free assets to heirs?

Bottom line: Roth conversions are powerful but should usually be done strategically, often in lower-income years or in partial amounts to avoid spiking your tax bill.



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SRC-S-IMA-AV-100225

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