

Direct rollovers to Roth IRAs

When you retire or change employers, arranging for a rollover directly from your company retirement plan to an IRA allows you to continue to defer tax on your money until you reach age 70½. Then you'll have to begin making annual taxable withdrawals.

Starting in 2008, you may be able to arrange for a direct rollover from a 401(k) or other tax-qualified plans to a Roth IRA. Combined with the upcoming elimination of a restriction that will make Roth IRAs available regardless of income, this new choice is likely to become more popular.

Here's why you should consider a Roth IRA rollover

With a Roth IRA, withdrawals may be completely tax free. (Earnings will be taxable, and penalties may be imposed, on withdrawals if you have not owned the Roth IRA for at least five years or if you make them before reaching age 59½. You can keep the funds in your Roth IRA for as long as you live and never have to worry about following a schedule of required withdrawals. And you can leave your Roth IRA to your heirs free of income tax.

Of course, there's usually a "but" somewhere, and here there are two:

First, you have to pay tax on the amount that you roll over, at regular tax rates of up to 35%. (State and local taxes may apply as well.) If the sum is sizeable, you may need significant resources to cover the tax bill. There's a small silver lining in that cloud: At least you will have removed what you paid from the threat of being taxed as part of your estate.

Second, in 2008 you aren't eligible to make a rollover to a Roth IRA if your modified adjusted gross income exceeds \$100,000. Fortunately, that restriction will be a problem only for those who are retiring in 2008 and 2009. In 2010 that condition is removed. And, in 2010 only, you can pay the tax on your rollover over two years—2010 and 2011. Only one restriction will remain: You cannot roll over to a Roth IRA if you are married and file a separate tax return.

Take the direct approach

Whichever IRA choice you make, don't ask for a check and then set up your IRA. If you do, you'll have only 60 days to complete the rollover. The consequences are serious if you miss the deadline. You'll pay the tax on your distribution and, if you are under age 59½, a 10% early withdrawal penalty as well.

Additionally, your check will be less than you expect because a 20% withholding tax applies when you don't arrange for a trustee-to-trustee transfer. If you have the cash, you can replace the amount withheld with your own funds in order to make your rollover whole, and the amount withheld will be credited toward your income taxes for the year. If you don't, you have lost the opportunity for continued tax deferral on 20% of the amount that you have accumulated in your plan account.

Is it almost time for your rollover?

If you are planning to retire or change jobs at any time in the near future, please contact us to discuss your rollover choices and the wide variety of investment options that we can offer you. We'll put everything in place for you, dot all the "i's" and cross all the "t's," providing a seamless transition from your company retirement plan to the Rollover IRA of your choice.

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