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Dialogues » WEALTH STRATEGIES FOR DISCUSSION

You may be eligible for a Roth IRA in 2010. So this can be a good time to look over your investments and cash flow needs, and consider consolidating your accounts and determine what you really want to do with your retirement assets.

FOURTH QUARTER
2009

COURTESY OF THE KING GROUP

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A New Retirement Opportunity: A Second Look At Roth IRAs

Even if an IRA never made sense to you before, you may want to look again. There is a new opportunity to convert a Traditional IRA to a Roth IRA which provides you with tax-free withdrawals, a tax-free inheritance for your heirs and no requirement to take minimum distributions from the account. In order to convert to a Roth IRA, all you need is a Traditional IRA.

If you make less than $100,000, you may convert to a Roth IRA right away. Otherwise, you will have the opportunity to do so in 2010, when everyone, regardless of income, will be eligible to convert to a Roth IRA. So, if you don't have a Traditional IRA, now would be a good time to establish one.

HOW CAN YOU TAKE ADVANTAGE OF THIS OPPORTUNITY?

Start Now: Build up your IRA savings by opening a new Traditional IRA or reactivate an existing IRA by contributing up to $5,000 ($6,000 if age 50 to 70½) for 2009 (and contribute the maximum amount for 2010 early next year). Your spouse, even if non-working, can do the same. Starting to contribute the maximum amount to a Traditional IRA now allows you to accumulate funds to convert to a Roth IRA in 2010, with minimal tax cost. As an added benefit, if you convert to a Roth IRA in 2010, you will have the option of evenly spreading any income that results from the conversion over 2011 and 2012. ■

If you already have a Traditional IRA with another financial institution, we can discuss whether it makes sense to convert that IRA, and how it will impact your tax planning (taxes are due on the amount converted to a Roth IRA). We will also discuss appropriate asset allocation and investment options for your account.

By Morgan Stanley Smith Barney LLC.

Roth IRA Conversion Opportunities

WHY IS NOW A GOOD TIME TO HAVE AN IRA?

Saving within a Traditional IRA can be an excellent way to put additional funds aside for retirement or to help repair recent damage inflicted by turbulent markets on your employer's retirement plan. Whether or not you want to initiate a Roth IRA conversion at a later date, saving for retirement within an IRA can give you control over your investment choices and more flexibility in your beneficiary and distribution decisions. You can also roll over distributions from other retirement plans to your IRA, which is a good way to consolidate your retirement plans in order to manage these funds more effectively.

IS A ROTH IRA CONVERSION RIGHT FOR ME?

The long-term benefits of a Roth IRA conversion, particularly for high-income taxpayers, can be attractive, regardless of age:

- Younger or older investors can benefit from additional years of tax-free compounding in a Roth IRA.
  - The younger investor has more time to allow the account to grow tax-free and to recoup the tax expense of the conversion before retirement.
  - The older investor does not have to take required minimum distributions from a Roth IRA, so any withdrawal amounts can be tailored more closely to actual income needs, or completely eliminated in any year.
- Investors of all ages may benefit from paying taxes on a smaller amount now, rather than waiting to pay taxes on a larger amount at a possibly higher tax rate in the future.
- Any potential inheritance of the Roth IRA can pass to the account owner's beneficiaries income tax free. Beneficiaries will still not need to pay tax on the money.

During your retirement: We can work with you and your tax advisor to help you to manage the investments in your tax-free Roth IRA and your taxable accounts so you can better balance the taxable and tax-free withdrawals you need or want to take from your accounts to your advantage.

WHAT IF I CONVERT TO A ROTH IRA AND THEN CHANGE MY MIND?

If you convert from a Traditional IRA to a Roth IRA, you have a window of opportunity to convert back to a Traditional IRA for any reason. Since it's as if the Roth conversion never took place, you will not owe any taxes. If your situation changes again, you can initiate another Roth conversion using that same account at a later date.

HOW CAN I FIND OUT IF A ROTH CONVERSION MIGHT BE A WORTHWHILE STRATEGY FOR ME?

We can demonstrate what regular contributions to a Traditional or Roth IRA can mean for your future financial security and whether a conversion to a Roth IRA makes sense in your situation. Ask us for a complimentary Roth Conversion Analysis.

> "Saving within a Traditional IRA can be an excellent way to put additional funds aside for retirement."

Consider the following hypothetical illustration: In 2009, a taxpayer age 50 or older opens a Traditional IRA and makes the maximum nondeductible contribution for 2009, and a 2010 contribution at the beginning of 2010, and immediately converts the entire account in January 2010 to a Roth IRA. This results in total contributions of $12,000, and minimal accumulation of interest or dividends. The approximate hypothetical growth and conversion amounts are as shown below.

TRADITIONAL IRA ACTIVITY

Total Contributions to a Traditional IRA	*$12,000
Account Value at Beginning of 2010	$12,360
Amount Converted to Roth IRA	**$12,360
Total Taxable Income from IRA Conversion	$360
Taxable Income Reported in 2011 and 2012	$180

For illustrative purposes only. Not representative of any specific investment.

* $6,000 for 2009 and $6,000 for 2010. 6% rate of return.

**Taxes paid from other funds allow conversion of entire IRA balance

APPROXIMATE VALUES OF THE ROTH IRA OVER 10, 20 AND 30 YEARS, ASSUMING A HYPOTHETICAL 6% ANNUAL RATE OF RETURN

Account Value at the end of 2010	$13,102
Value in 10 Years	$23,463
Value in 20 Years	$42,019
Value in 30 Years	$75,249

For illustrative purposes only. Not representative of any specific investment.

> "We can work with you and your tax advisor to help you manage the investments in your tax-free Roth IRA."

The IRA account earns a hypothetical 6% annual rate of return. At the beginning of 2010, the account holds $12,360, which is converted to a Roth. Assuming no other IRAs are owned, the taxpayer will owe tax on only $360 and can split this amount in half and pay the income tax due over two taxable years—2011 and 2012.

POTENTIAL GROWTH OF CONVERTED ROTH IRA

Assuming a hypothetical 6% annual rate of return, the Roth IRA with a balance of approximately $12,000 could grow to approximately $75,000 in 30 years. If you are eligible to make annual contributions into your Roth IRA, these amounts could be larger.

Distributions from the Roth IRA after age 59½ and after five years from the conversion date are income tax free and completely voluntary. These funds can be withdrawn for expenses during retirement or set aside for inheritance purposes, but there are no specific distribution requirements.

WHAT IF MY EXISTING IRA IS FUNDED WITH A ROLLOVER FROM A RETIREMENT PLAN DISTRIBUTION? CAN THIS ACCOUNT BE CONVERTED TO A ROTH IRA?

Yes. Converting rollovers from a retirement plan distribution to a Roth IRA can be a good way for you to control the management of the taxes and investment of your overall retirement assets:

- » If your adjusted gross income (AGI) is over $100,000 and your existing Traditional IRA contains a retirement plan distribution rollover, you can convert this account to a Roth IRA in 2010 (or thereafter).
- » If you earn no more than $100,000, you can convert now to a Roth IRA.
- » Rollovers from qualified plans, 401(k)s and 403(b)s initiated in 2009 or after, can be rolled over directly to a Roth IRA.

IF MY RETIREMENT ACCOUNTS HAVE TAXABLE AND NONTAXABLE AMOUNTS, CAN ONLY THE NONTAXABLE AMOUNT BE CONVERTED?

If you have Traditional IRAs funded with nondeductible and deductible contributions, withdrawals from any of your IRAs are subject to the "pro-rata rule." Each distribution or amount converted will consist of a percentage of the taxable and nontaxable amount according to the proportion of these funds that exist in the accounts.

Your tax advisor can help you calculate the taxable portion of the conversion. You can also request from us a Roth conversion analysis that will include the amount of any after tax portion of the distribution.

ARE PARTIAL CONVERSIONS FROM TRADITIONAL IRA FUNDS TO A ROTH IRA PERMITTED?

Partial conversions of Traditional IRA funds to a Roth IRA are permitted. You may even choose the particular investments in the Traditional IRA that will be converted to a Roth IRA. One idea is to convert only that amount in a given year that will not push you into a higher tax bracket.

ROTH IRA CONTRIBUTION BASICS

- Contributions are always nondeductible.
- $5,000 annual contribution limit; $6,000 total annual contribution for those age 50 or older.
- If filing singly, contributions are possible if your AGI is no higher than $120,000 in 2009.
- If filing jointly, contributions are possible if your combined AGI is no higher than $176,000 in 2009.
- No age restrictions; taxpayers age 70½ who don't exceed AGI restrictions and who have earned income may contribute.
- Account holder or his/her spouse must have earned income that equals the contribution.

ROTH IRA CONVERSION BASICS

- Through 2009, a conversion from a Traditional IRA to a Roth IRA is available for those who earn less than $100,000.
- Starting in 2010, the opportunity to convert a Traditional IRA to a Roth IRA is available at all income levels.
- Income from a Roth IRA conversion in 2010 can be taxed 50% in 2011 and 50% in 2012. Some taxpayers may wish to pay all the taxes in 2010 if they believe they will be in a higher tax bracket in 2011 and 2012.
- No minimum distributions are required at any age by account holders.

ASK US FOR AN UPDATED FINANCIAL ANALYSIS

Our approach is based on providing a combination of relevant experience and knowledge about your aspirations and circumstances. The difference this makes will be apparent: a clear road map that includes all the pieces of your financial life—accounts, policies and properties—working together to help you achieve what is most important to you and your family. For this reason, we can offer complimentary services, such as a beneficiary audit, a review of your risks and insurance coverage, and help you make your decisions about Medicare and Social Security elections and other sources of retirement income.

This can be a good time to look over your investments and cash flow needs, and consider consolidating your accounts and determine what you really want to do with your retirement assets.

> "Call us for an analysis of your wealth management needs and learn how your retirement assets can help you achieve your financial goals during retirement."

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