ED SLOTT'S IRA ADVISOR

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TAX & ESTATE PLANNING FOR YOUR RETIREMENT SAVINGS

When the 2-year Deal is Not Really a 2-year Deal

Acceleration of 2010 Roth Conversion Income

Due in large part to the repeal of the income and filing status restrictions, 2010 saw the Roth conversion floodgates swing wide open. But many clients (including some who were previously eligible) also chose to convert in 2010 thanks to a special tax break. Instead of including all the income from a 2010 conversion in 2010, clients can choose to split the income from a 2010 conversion equally over 2011 and 2012 (which is the default option). Sometimes however, events that occurred after the conversion can alter this 2-year deal, or even eliminate it altogether.

Perhaps the most common reason clients could lose out on the 2-year deal is if any of their 2010 converted funds were withdrawn from the Roth IRA in 2010 and/or in 2011. Although the tax law allows for the deferral of 2010 Roth conversion income equally over 2011 and 2012, it also contains a provision that changes this schedule if funds are prematurely withdrawn from the Roth IRA. Essentially, our lawmakers did not want to allow taxpayers to enjoy the benefits of their conversion income before they were required to pay the taxes on it.

Taxpayers cannot enjoy the benefits of their conversion income before they pay the taxes on it.

To ensure this does not happen, the same law (TIPRA) that allowed for the 2-year split also contained a special clause that accelerates the inclusion of 2010 conversion income if withdrawals of those funds are made prior to 2012. This "acceleration" of income works by moving the conversion income (in an amount equal to the total amount withdrawn) that would have been deferred the longest to the year the Roth funds were distributed. As a result, clients opting for the 2-year deal could still end up with conversion income spread over 2010, 2011 and 2012, over 2010 and 2011 or unequally over 2011 and 2012. Some clients who used the 2-year deal could even end up with all

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