

Roth IRA Conversion – Should you do it?

As of January 1, 2010, the \$100,000 income limitation on traditional IRA to Roth IRA rollovers no longer exists. As a result, one of the hot topics in the financial planning arena is whether or not higher income earning investors, who were previously prevented from rolling their traditional IRA assets into a Roth IRA, should now do so either in part or in full. A key reason to consider a traditional to Roth IRA rollover is to convert IRA assets from a tax-deferred account that is eventually subject to required minimum distributions to a tax free account that is never subject to any required distributions. The added benefit of being able to defer the taxes due on rollovers done in 2010 makes the option of rolling over somewhat time-sensitive and also potentially that much more attractive.

In anticipation of the elimination of the Roth IRA rollover income limitation, we initially addressed some of the pros and cons of rolling traditional IRA assets into a Roth IRA back in our Second Quarter 2009 newsletter. Because this is now such a popular topic, we revisit it here with excerpts from our earlier newsletter.

There are tax implications when rolling assets from a traditional to a Roth IRA. From our 2nd Quarter 2009 newsletter...*Most traditional IRAs contain a combination of deductible contributions (contributions for which the accountholder has already taken a tax deduction) and the tax-deferred earnings on these contributions. In such an instance, the entire amount that is converted from a traditional to a Roth IRA would be taxed at the accountholder's top income tax rate in the year in which it was converted. If the traditional IRA contains a combination of deductible and non-deductible contributions and tax-deferred earnings, then the tax due on the conversion applies only to the deductible contributions and tax-deferred earnings.*

There is, however, a one-time benefit available to those who convert to a Roth in 2010. The tax amount owed as a result of a 2010 conversion can either be paid in full by 4/15/11 or can be split equally – with half paid on the 2011 tax return and the other half paid with the 2012 tax return.

The decision on whether to convert some or all of a traditional IRA to a Roth IRA is not usually straightforward and is often dependent on each investor's particular financial and tax situation. Although a number of variables can come into play, there are several basic factors that should be part of the process of deciding what, if anything, to convert. These factors include:

- > What is your current tax rate and what do you expect your tax rate will be in retirement? If your tax rate will be substantially lower in retirement then it might not make sense to convert.
- > How much can you convert without pushing yourself into a higher tax bracket or causing the Alternative Minimum Tax to apply? A partial conversion may be more tax efficient if a full conversion causes you to jump to a higher tax bracket.
- > Do you have the ability to pay any taxes that may be due on a converted amount without dipping into your IRA?
- > What is your time horizon? How old are you and how far are you from retirement?
- > Is a charitable organization the beneficiary of your traditional IRA? If yes, it probably makes no sense to convert since the charitable organization does not have to pay taxes and thus will not be better off by receiving a tax-free account. Similarly, if the beneficiaries are in lower tax brackets than the IRA owner than it may not make sense to convert.

Although there is a tax deferral benefit open to those who convert to Roth IRA's in 2010, it is also important to keep in mind that, for some investors, converting from a traditional to a Roth IRA may be more tax efficient if done in bits and pieces. Also, even though the income limitation on rollovers no longer exists, the income limitation on contributing to a Roth IRA does still exist. As a result, it appears those whose modified adjusted gross income exceeds the limit and who still want to add to their Roth IRA will have to make an annual contribution to their traditional IRA and then roll this contribution to their Roth IRA.

From our 2nd Quarter 2009 newsletter...*There are several reasons why you may want to consider converting some or all of your traditional IRA to a Roth IRA beginning in 2010. First, there is a concern that income taxes are going up, thus, the notion of tax free income in retirement is becoming more attractive. Second, if you convert before the income tax rates rise then the taxes you will owe on the conversion should be at the older and presumably lower rate. Third, because of the financial market upheaval over the last year and a half, many IRA accounts unfortunately are worth less than they were a year or two ago. This is beneficial from a conversion standpoint because there will be less taxes due as a result of the conversion. ...Fifth, because of the recession, some IRA holders may now find themselves in a lower tax bracket – less dividend income, lower salaries, smaller bonuses, fewer*

News

- Our Annual Holiday Party... Thanks to all the clients who made it out to The Highlands on such a cold day for our eleventh annual holiday party! We were treated to a wonderful performance by a group from the Pennsylvania Girlchoir. Below is a photo from the event. Also, if you would like to learn more about the Pennsylvania Girlchoir or find out where you can hear them again, please visit their website at www.pagirlchoir.org.



January – a Good Time to Ensure Your Financial House is in Order

The beginning of each year is a great time to quickly review your financial and legal documents and ensure that everything is current. Set forth below is a “top 6” list of items you should evaluate at least once a year and possibly more frequently should a birth, death, marriage, divorce, or other major life change occur.

1. Review and, if necessary, update the beneficiary designations on your IRA's, insurance policies, employer-sponsored retirement plans, and any other similar documents. You may also want to consider adding contingent beneficiaries if you have not already done so.
2. Review the contribution history for your IRA. If you have not already made the maximum annual contribution for 2009 (\$5000 or \$6000 if you are age 50 or older), it is not too late. You have until April 15th to make your 2009 contribution. However, if you make a 2009 IRA contribution in 2010, please confirm with the account custodian that the contribution is for 2009.
3. Review and, if necessary, adjust the asset allocation percentages and holdings in your employer-sponsored retirement plan (401k/403b). Among other things, consider whether your account is too heavily overweighted in a particular asset category or individual security – such as stock in the company where you work. You may also want to increase the annual contribution percentage to your 401k/403b provided you are not already contributing the maximum amount.



4. Consider rolling over any old 401k/403b retirement plan accounts held with prior employers. You can easily roll these accounts into your IRA account thereby consolidating your assets and likely reducing the fees and expenses you pay. Once consolidated, you can more easily and efficiently develop and implement a comprehensive investment strategy for retirement.
5. Review the types and amounts of insurance coverage you now have and determine whether these are still suitable given your current and/or anticipated future circumstances.
6. As discussed on the cover page, consider rolling some or all of your traditional IRA into a Roth IRA now that the previous income limitation on doing so no longer exists.

If you have any questions about any of these items or if you would like assistance or guidance with these tasks, please do not hesitate to contact your portfolio manager here at BLB&B Advisors. ■

Qualified Charitable Distributions

The Pension Protection Act of 2006 allowed IRA owners over age 70½ to make tax-free distributions of up to \$100,000 directly from their traditional IRA to a qualified charitable organization. At the same time, this tax-free distribution could be used to help satisfy the IRA-holder's annual required minimum

distribution. The Emergency Economic Stabilization Act of 2008 extended these qualified charitable distributions through December 31, 2009. To date, however, there has not been any further extension of legislation allowing these distributions, thus, for now anyway they are disallowed for 2010. ■



SPOTLIGHT ON TURNING POINTS FOR CHILDREN



With this first issue of 2010, we decided to introduce a new “column” in our quarterly newsletter. In each issue of our newsletter this year, we will feature a different

charitable organization that also happens to be a client of ours. As the kick-off to this new column, we feature Philadelphia-based Turning Points for Children – an organization that has been helping Philadelphia’s children and families since 1835.

Turning Points for Children was the result of the 2008 merger of Philadelphia Society for Services to Children and the Children’s Aid Society of Pennsylvania. These organizations, in turn, can trace their origins to the Inter-Church Childcare Society (founded 1835), Pennsylvania Society to Protect Children from Cruelty (founded 1877), and the Children’s Aid Society (founded 1882).

Turning Points for Children is a 501(c)(3) non-profit organization that provides proven and innovative programs that nurture families with children who are struggling against difficult economic and environmental odds. Their approach includes after-school family programs, teen parent education, assistance to relative caregivers and home visiting services. Turning Points for Children also provides critical resources, life skills and supportive partnerships needed to create stronger families and raise children with the hope for brighter futures.

Last year, Turning Points for Children served well over two thousand Philadelphia families, including more than 3000 children. They provide services through a wide variety of innovative and effective community programs including:

Families and Schools Together (FAST): This program provides parent education and family support services to parents and children by working with schools, mental health and substance abuse providers, and community leaders in order to strengthen families through building partnerships and promoting increased success in school. Families meet once a week for eight weeks and after completion of these sessions, they continue to meet once a month for 22 months. FAST is currently operating in 30 elementary schools in Philadelphia. Two of these schools recently qualified for the Commonwealth of Pennsylvania Educational Improvement Tax Credit (EITC) Program. For further information about the EITC Program, please contact Jack Luke, Director of Development and Communications, at Turning Points for Children (267) 535-1325 or go to www.turningpointsforchildren.org/eitc

Alternative Response System (ARS): This is a new service (Spring 2009) developed by the Department of Human Services

(DHS) to engage families in which there is a moderate level of risk for abuse and neglect. Families in this program have been brought to the attention of DHS through hotline reports, but there is not an immediate safety threat to the children. Social Workers help develop family functioning and work to eliminate any issues or concerns that could place the children at risk for future abuse.

Kids N’ Kin: This program supports families in which children’s biological parents are absent and children are being raised by an extended family member or family friend. Services include home visits, family therapy, legal assistance and supportive services for incarcerated parents.

The Family Project: This program is geared towards pregnant and parenting families with children under the age of 6 who are looking to provide a better life for themselves and their pre-schoolers. Families receive the emotional supports they need through the following services: developmental screening of children and access to early intervention services, if needed; assistance in educational and vocational planning; and, support in locating resources that will further clients’ goals.

Time Out for Teens and Tots: This is a parenting and support program for teen mothers and their children. TTT offers group sessions that build parenting and peer relationships and foster positive and healthy mother/child relationships, individual and family supportive counseling, a Career Directions program that introduces teen mothers to the working world and helps them develop educational and career plans, mother-only and mother-baby educational and cultural special events and developmental screening for children to identify those who may need early intervention services. TTT group sessions are held in five locations throughout Philadelphia.

In 2007, almost 4200 children were abused and neglected in Pennsylvania and 46 children were killed as a result of abuse and neglect. This situation was even worse in 2008 when there were 25,655 reports of suspected child abuse in Pennsylvania. There was also a 39% increase in substantiated abuse over 2007 and 50 children died from abuse in 2008 – six of those children in Philadelphia. (Statistics from the Pennsylvania Dept. of Public Welfare 2008 Annual Child Abuse Report) The need for the critical services provided by Turning Points for Children is ongoing and vitally important not only to the immediate families who receive assistance but also to the Philadelphia community as a whole. If you would like to learn more about Turning Points for Children, you can contact them at (215) 875-3400 or view their website at www.turningpointsforchildren.org. ■

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capital gains, etc. This could translate into lower tax costs on an IRA conversion.

As you can see from this fairly basic article about Roth IRA conversions, there is no simple or easy answer that applies to each investor. Rather, each IRA holder has their own unique set of circumstances and what may be good for one IRA holder may be

detrimental to another. Your portfolio manager here at BLB&B Advisors can walk you through this process and help coordinate with your estate planning attorney and/or accountant as may be necessary. Please do not hesitate to contact us if you have any questions or would like to begin analyzing whether a conversion makes sense for you. ■



Updated IRA Information for 2010

IRA CONTRIBUTION LIMITS FOR 2010

Traditional and Roth IRA: If you are under age 50 you may contribute up to \$5000 to your IRA. If you are age 50 or older you can make up to a \$6000 annual contribution. (Please note, however, that these figures represent your entire allowable annual IRA contribution and are not per account. Thus, if you have a Roth and a traditional IRA you may not make an annual \$5000(\$6000) contribution to each account.)

SEP IRA: An employer may contribute up to 25% of an employee's annual compensation up to a maximum annual contribution limit of \$49,000.

Simple IRA: Employees may contribute up to \$11,500 in 2010 if they are under 50 and up to \$14,000 if they are age 50 or older.

Health Savings Account (single/family): An individual with single coverage may contribute up to \$3050 to a health savings account in 2010 while an individual with family coverage may contribute up to \$6150. For those age 55 or older, the contribution limits are \$4050 for those with single coverage and \$7150 for family coverage.

TRADITIONAL IRA DEDUCTION LIMITS FOR 2010

You may contribute to a traditional IRA whether or not you also have an employer-

sponsored retirement plan through work. If you are not covered by a retirement plan at work, then you will receive a full deduction for your annual contributions to your traditional IRA. However, if you are covered by a retirement plan at work then you may face limitations on your ability to deduct some or all of your annual IRA contributions depending upon your income level.

More specifically, set forth below are the applicable annual income ranges. For example, a single filer with a Modified Adjusted Gross Income (MAGI) of less than \$56,000/year will be able to deduct in full her IRA contribution. However, if this same filer instead has a MAGI of \$59,000/year she falls within the phase-out range and thus will only be able to deduct some of her 2010 IRA contribution as per IRS regulations. Finally, if this same filer has an MAGI of \$67,000 in 2010 her income exceeds the phase out range and she will not be able to deduct any portion of her IRA contribution.

Deduction limits phased out by Modified Adjusted Gross Income (MAGI):

- Single filer: \$56,000 – \$66,000
- Joint filer: \$89,000 – \$109,000

Individual without plan and spouse with plan — deduction limits phased out for MAGI of:

- Joint: \$167,000 – \$177,000 ■

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