



Worldwide leaders in public and management accounting

PFP Section

Tax | Retirement | Estate |

Risk Management | Investments

The Latest and Greatest with Roth Conversion Planning

Your Presenter



Robert S. Keebler, CPA, MST, AEP
(Distinguished)

Robert.Keebler@Keeblerandassociates.com

Outline

- Market Volatility & the CARES Act RMD Strategy
- SECURE Act
 - New Post-mortem Payout Rules
 - Roth Conversions as a Solution to Analyze
- Core Roth Conversion Concepts



General Democratic Party Tax Policy Themes

- Additional payroll taxes on high-earners
- Increase the marginal rate imposed on high-income individuals
- Increase the capital gains rate imposed on high-income individuals
- Tax wealth generally; various ideas include an annual wealth tax & greater estate & gift taxes
- Increase the corporate income tax rate

Administrative Issues

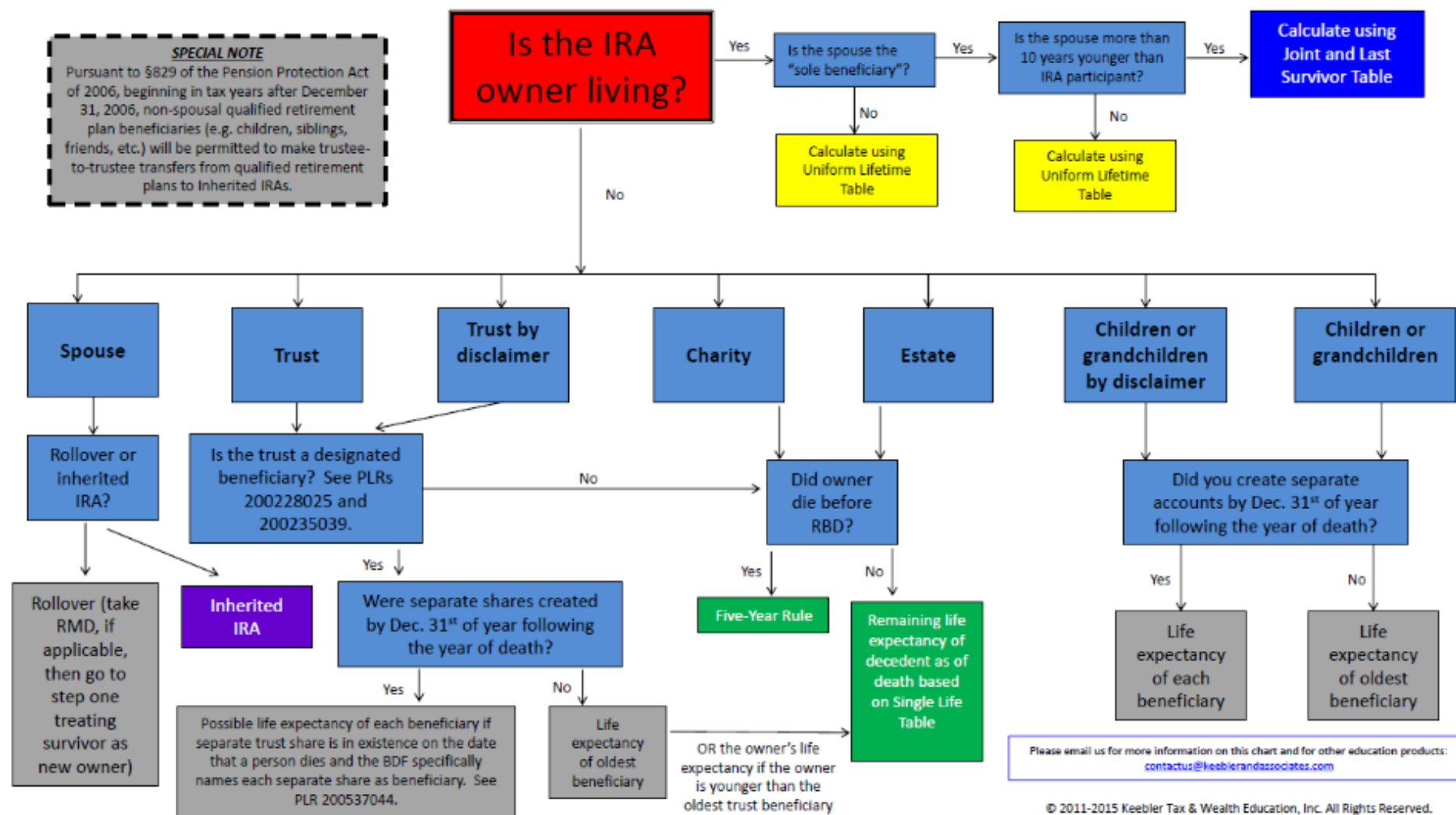
- Estimated taxes
- State and local taxes
- Cash reserves
- Dollar cost averaged conversions

Pre-Secure Law for Post-Mortem Distributions

Stretch Out IRAs - “Inherited” IRA

Objective: Prolong IRA payments over longest possible period of time, thus increasing wealth to future generations

Pre-Secure Bill Distribution Flowchart



Stretch Out IRAs - *“Inherited” IRA*

- An IRA is treated as “inherited” if the individual for whose benefit the IRA is maintained acquired the IRA on account of the death of the original owner.
- Under Pre-Secure law, the IRA assets could be distributed based upon the life expectancy of the beneficiary.

IRC Sec. 401(a)(9)

Stretch Out IRAs - *“Inherited” IRA*

- Two Strategies

- Spousal Rollover
- Inherited IRA

- Advantages

- Rollover delays RMD until spouse’s own RBD
- Inherited IRA provisions allow distributions to occur over many years after the death of the IRA owner

Both Still Available After the Secure Act

Secure Bill – Key Changes

RMDs after Death

EFFECTIVE DATE:

Deaths which Occur After 12/31/19

RMDs after Death

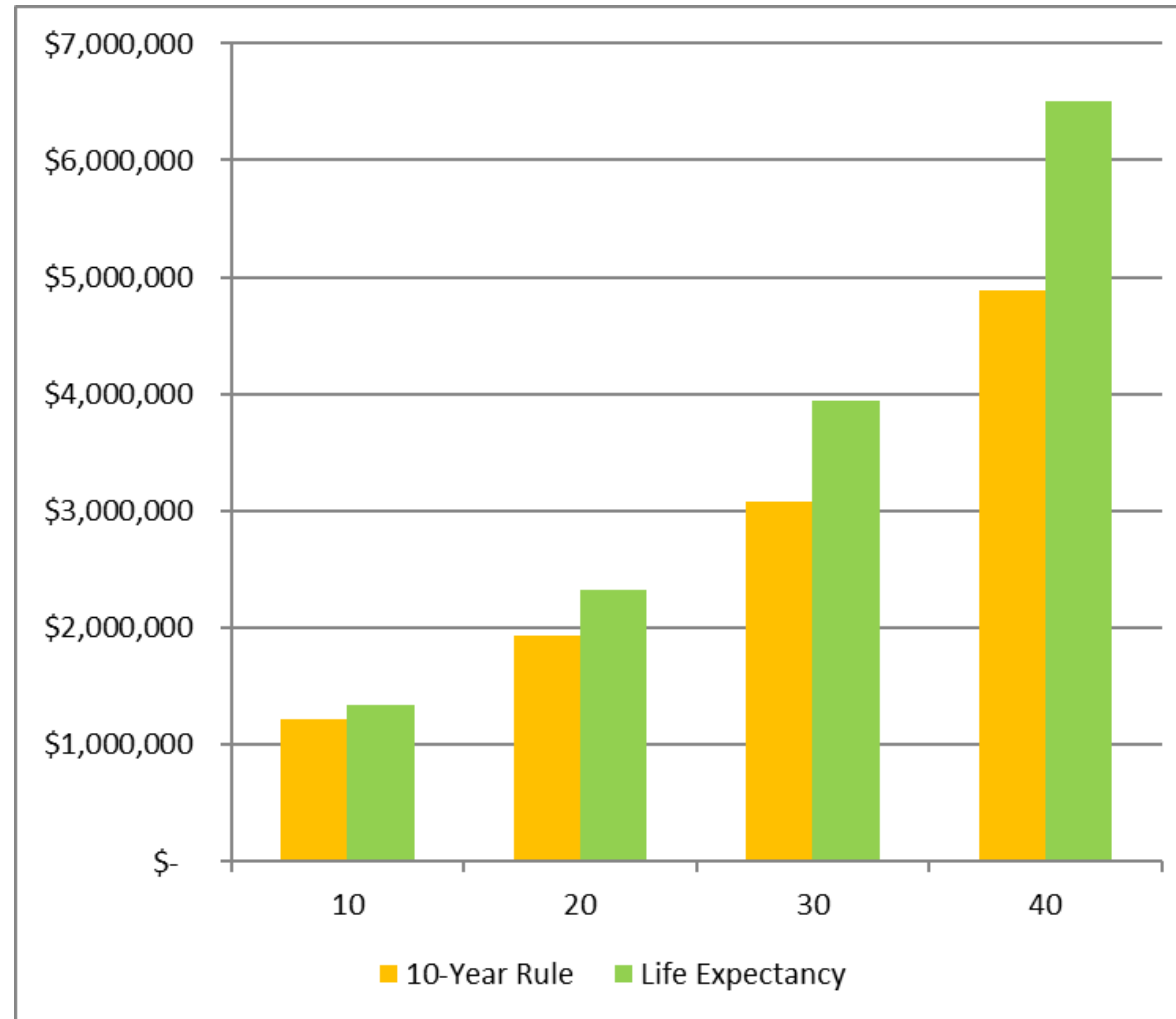
- Basically, requires all IRAs, Roth IRAS, and Qualified Plans to be distributed within 10 years of death

RMDs after Death - Example

Ten-Year vs. Life Expectancy

Age of (Oldest Trust) Beneficiary	40
IRA Balance	\$ 1,000,000
Pre-Tax Growth Rate	6.00%
After-Tax Growth Rate	4.75%
Average Income Tax Rate - Life Expectancy Rule	24.00%
Average Income Tax Rate - Ten Year Rule	28.00%
Distributions Occur at Beginning or End of Period?	End
Lump-Sum Distribution or Amortize Payments?	Amortize

RMDs after Death - Example



RMDs after Death

- Exceptions from the 10-year Rule for certain beneficiaries (“eligible designated beneficiary”)
 - Surviving Spouse
 - The employee’s **Children** under the age of majority (*not grandchildren or any other children*)
 - Disabled
 - Chronically ill
 - Individual not more than ten years younger than employee

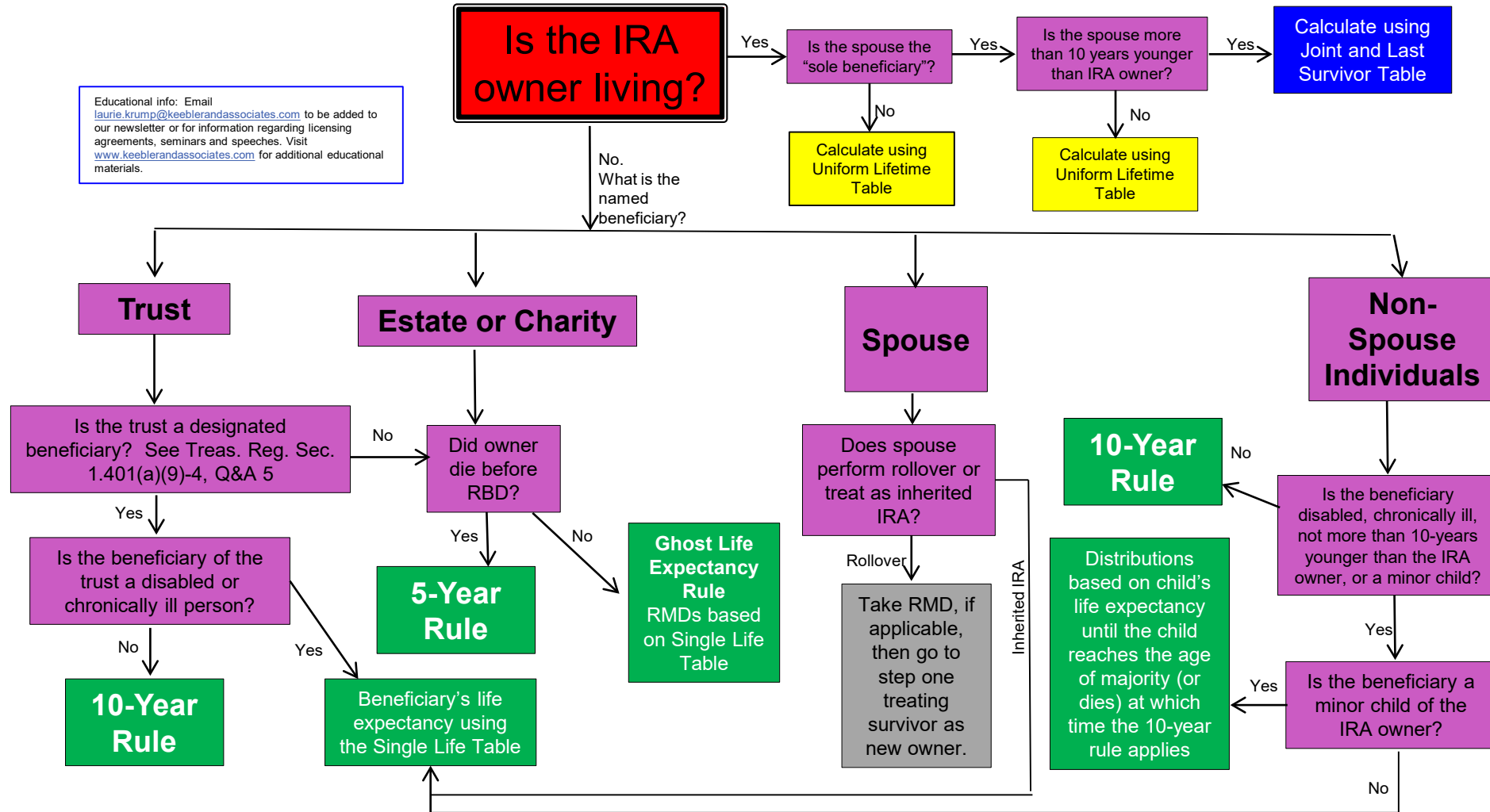


§§ 401(a)(2)(E)(ii)

Secure Act Beneficiary RMD Summary

Tax Terminology	Designated Non-Eligible Beneficiary	Surviving Spouse	Eligible Minor Child	Person Less Than 10 Years Younger	Disabled or Chronically Ill Person
Outright Beneficiary	10-Year Rule	Life Expectancy Rule	Life Expectancy Rule (Until Majority then 10-Year Rule)	Life Expectancy Rule	Life Expectancy Rule
Conduit Trust	10-Year Rule	Life Expectancy Rule	Life Expectancy Rule (Until Majority then 10-Year Rule)	Life Expectancy Rule	Life Expectancy Rule
Designated Beneficiary Trust	10-Year Rule	10-Year Rule	10-Year Rule	10-Year Rule	Life Expectancy Rule
Non-Designated Beneficiary Trust	Before RBD: 5-Year Rule	Before RBD: 5-Year Rule	Before RBD: 5-Year Rule	Before RBD: 5-Year Rule	Before RBD: 5-Year Rule
	After RBD: Ghost Life Expectancy Rule	After RBD: Ghost Life Expectancy Rule	After RBD: Ghost Life Expectancy Rule	After RBD: Ghost Life Expectancy Rule	After RBD: Ghost Life Expectancy Rule

TRADITIONAL IRA RMD FLOWCHART - For Deaths After Effective Date of SECURE Act



Trusts for Disabled and Chronically Ill Beneficiaries

- Life Expectancy Treatment is Available with an “Eligible Designated Beneficiary Trust”
- Need to Draft an Accumulation Trust
- Roth IRAs may work better due to:
 - The difference in the individual and trust tax rates
 - The ability to pay the income tax on conversion out of nonqualified funds
- Two trusts are advisable if the client has both a traditional IRA and a Roth IRA – this avoids “trapping” the taxable IRA income

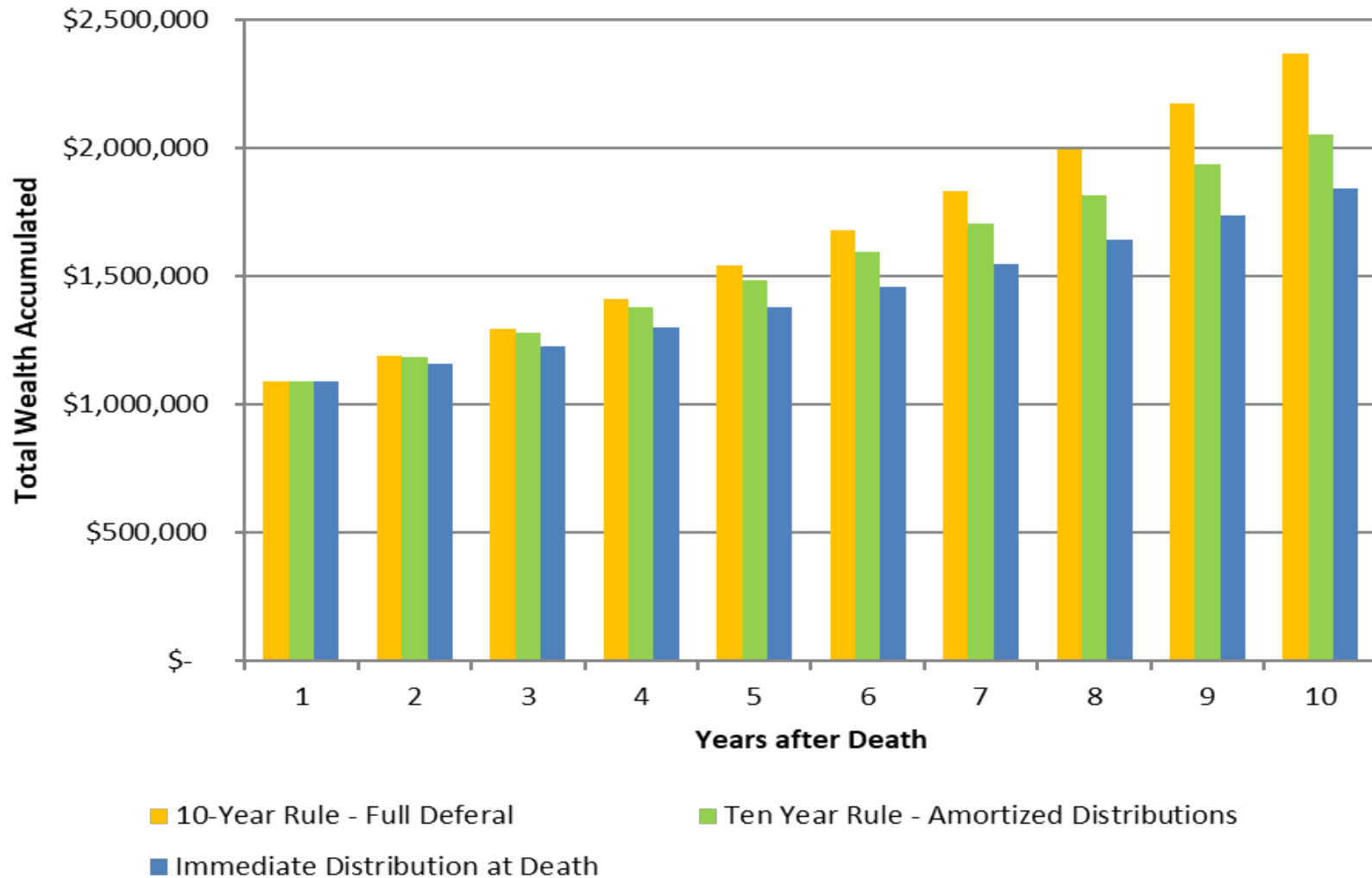
Ten Year Rule - Roth vs. Traditional IRA

- If minimizing income taxation is the only concern, Roth distributions after death should generally be deferred until the end of the Ten-Year period – *“The Roth Reprieve”*
- Growth remains tax-exempt
- Traditional IRA distributions will be tactically withdrawn to manage income tax rates

The Roth Reprieve

- Consider the following example:
 - Connie dies and leaves her \$3,000,000 Roth IRA to her three children equally
 - Each child has a different understanding of the rules, but is responsible and good investor
 - Derek distributes the IRA immediately and reinvests the money in a brokerage account
 - Daniel computes a 10-year level amortization schedule and makes annual transfers from the inherited IRA to his brokerage account
 - David waits the full 10-years to transfer the funds in the IRA to his brokerage account
 - Assume a 6% pre-tax return and a 9% before tax return

The Roth Repeive



Planning Solutions To Analyze

Solutions to Analyze - Overview

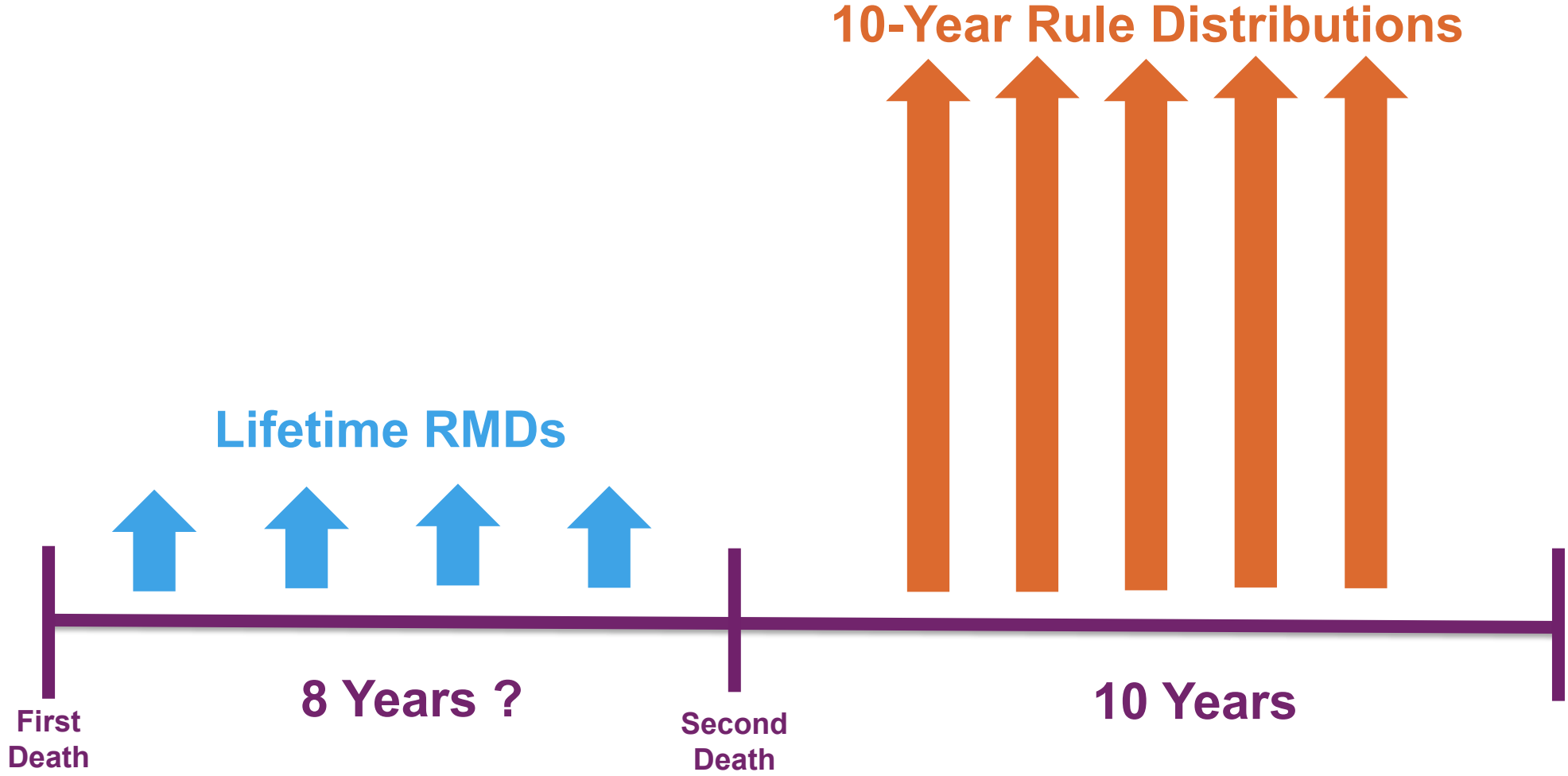
- **Roth conversions**
- Designated Beneficiary - multi-generational spray trusts
- Spousal rollovers and the *new* spousal rollover trap
- IRAs to CRTs
- IRA trusts for state income tax savings
- IRA relocation to life insurance
- Life insurance to offset increased tax-risk of early death
- Combination “hedge” strategies

The New Spousal Rollover Trap – Old Best Practice

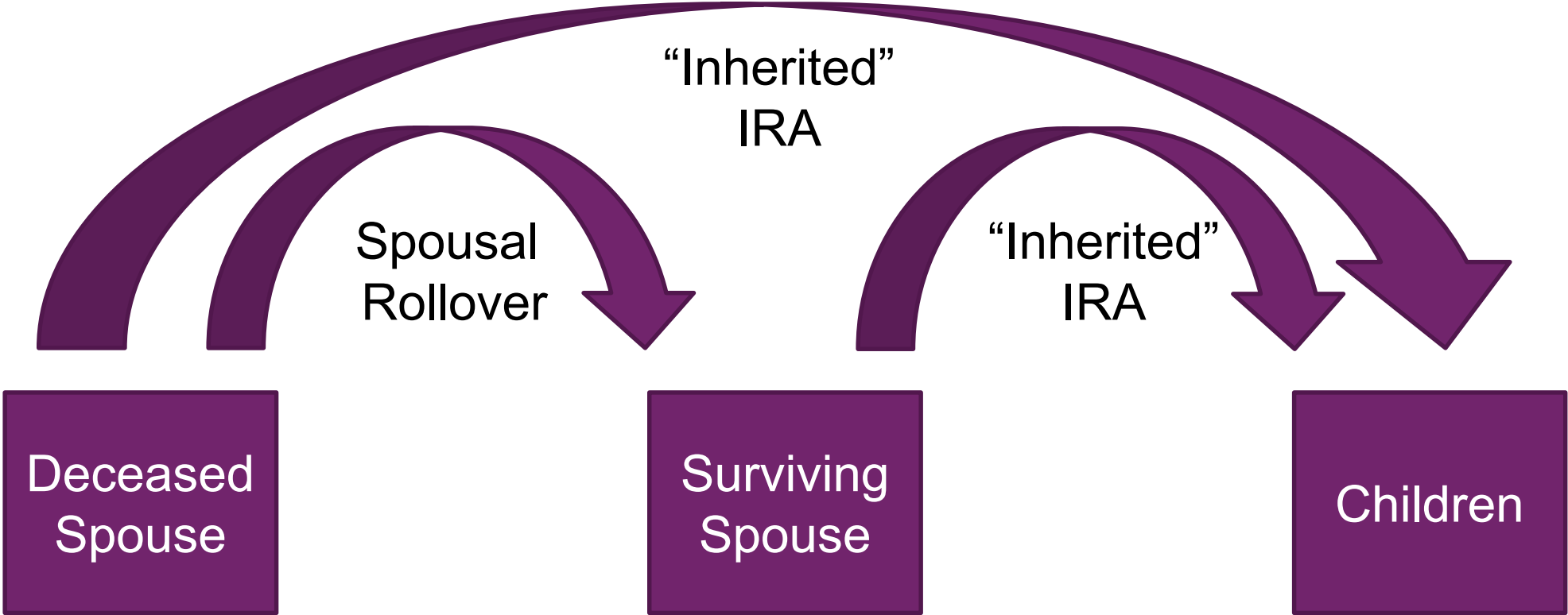


IRC § 408

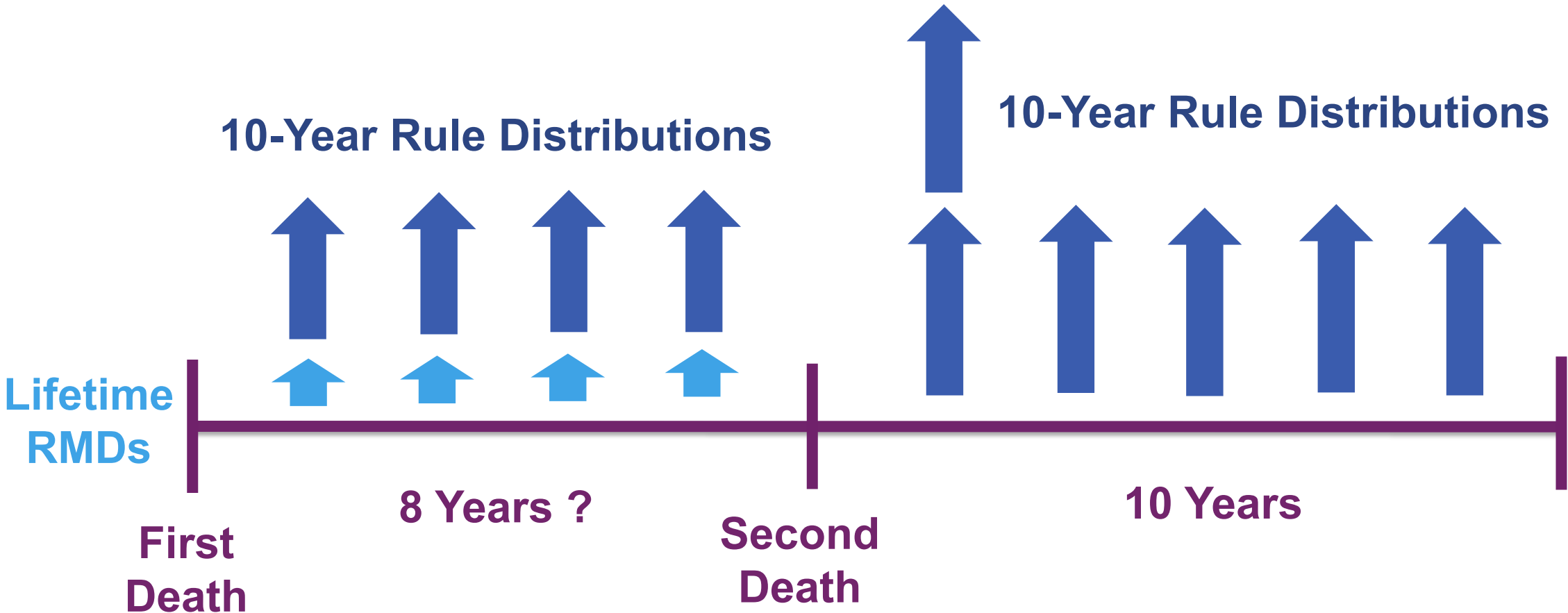
The New Spousal Rollover Trap – Old Best Practice & The New Spousal Rollover Trap



The New Spousal Rollover Trap – Potential New Best Practice



The New Spousal Rollover Trap – Potential New Best Practice



Roth Conversions

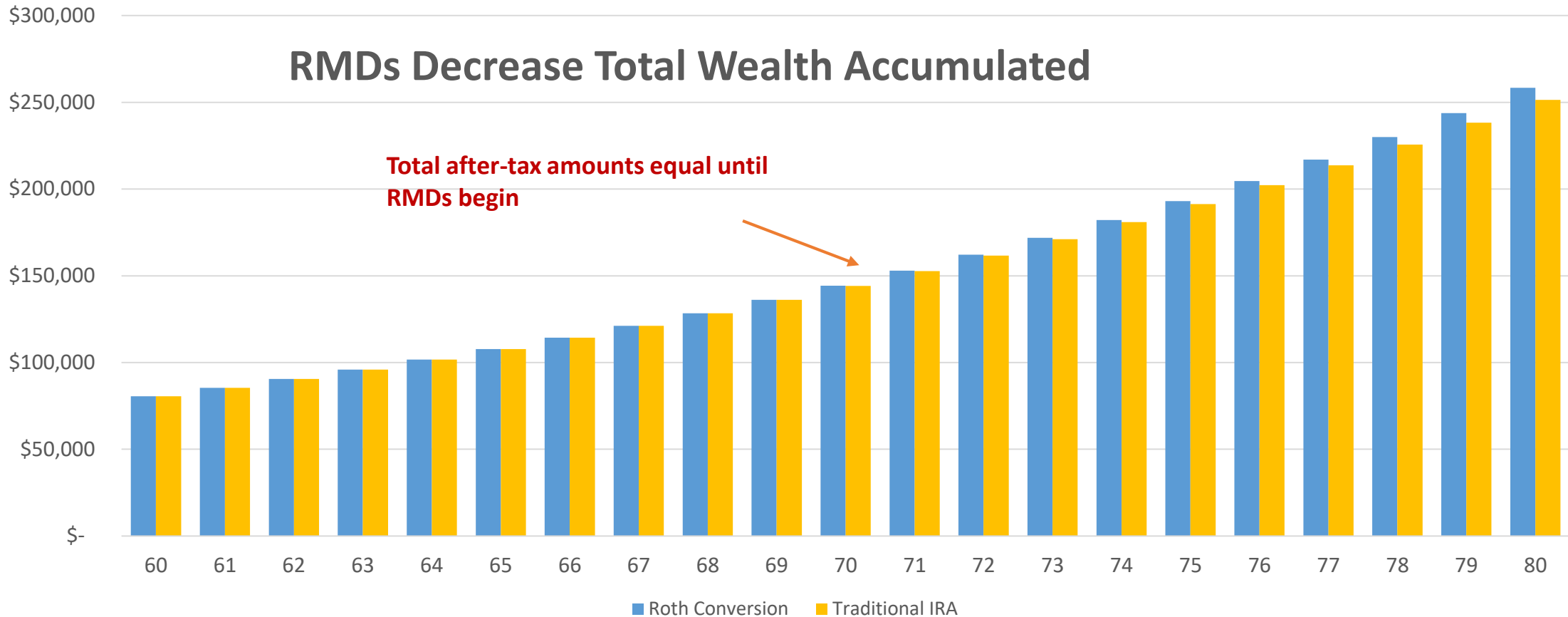
- As it relates to the new 10-year rule, the purpose of Roth Conversions is to spread distributions over many years and lower brackets



General Roth Concepts

- 100% of growth is tax-exempt
- No required minimum distributions at age 72
 - NOTE: Distributions from Roth IRAs cannot be used to fulfill the RMD from a traditional IRA
- RMDs on Inherited Roth IRAs

General Concepts



The graphic compares a \$100,000 Roth Conversion at age 60 to “doing nothing.” It assumes 24% tax rate applies to all distributions/conversions, the conversion tax is paid from the IRA, a 6% pre-tax rate of return, and a 4.75% after-tax rate of return.

General Concepts

- Convertible accounts
 - Traditional IRAs
 - 401(k) plans
 - Profit sharing plans
 - 403(b) annuity plans
 - 457 plans
 - “Inherited” 401(k) plans (see Notice 2008-30)
- Non-convertible accounts
 - “Inherited” IRAs
 - Education IRAs

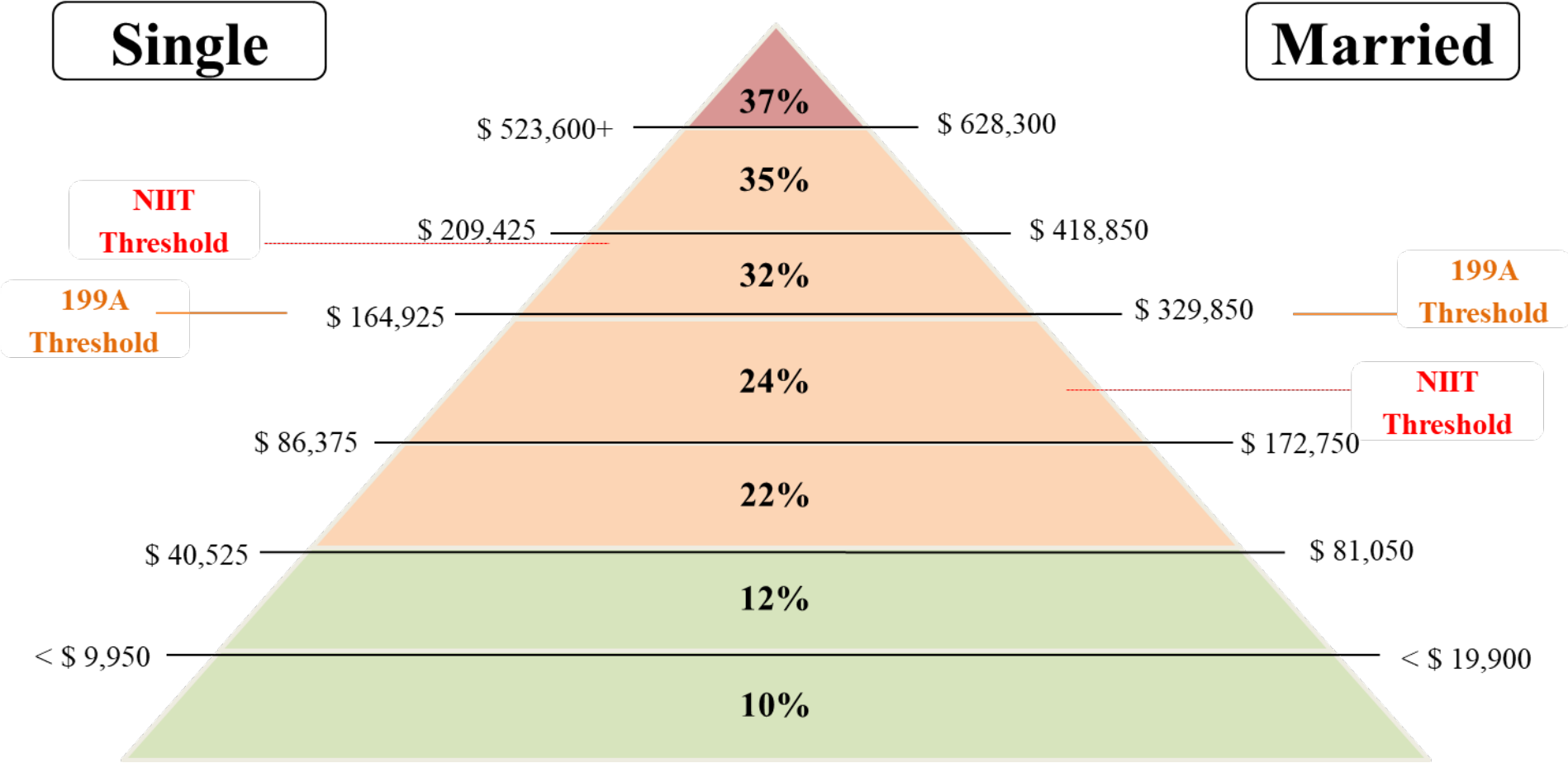
Micro Roth Conversions

- Converting smaller amounts of traditional IRA to reach the top of the income tax bracket to pay a smaller percentage than would the inheritor be taxed at.
- Example:
 - C is married and retired with income of \$50,000 and has a traditional IRA of \$300,000 that he will not need in the future.
 - C's IRA beneficiary is his daughter T who is in the 22% income tax bracket.
 - If C converts \$30,000 of his traditional IRA to a Roth IRA for the next ten years, he will be only paying 12% on income tax because he will be just under the top of his income tax bracket, and thus be transferring \$30,000 more to T, due to paying 10% less on income tax payments than T would have to pay if she inherits the full amount of the traditional IRA.

General Concepts

- Reasons for converting to a Roth IRA
 - Taxpayers have special favorable tax attributes including charitable deduction carry-forwards, investment tax credits, net operating losses (NOLs), high basis non-deductible traditional IRAs, etc.
 - Suspension of the minimum distribution rules at age 72 provides a considerable advantage to the Roth IRA holder
 - Taxpayers benefit from paying income tax before estate tax (when a Roth IRA election is made) compared to the income tax deduction obtained when a traditional IRA is subject to estate tax
 - Taxpayers who can pay the income tax on the IRA from non-IRA funds benefit greatly from the Roth IRA because of the ability to enjoy greater tax-free yields

2021 Tax Brackets



General Concepts

- Reasons for converting to a Roth IRA
 - Taxpayers who need to use IRA assets to fund their Basic Exclusion Amount (BEA) bypass trust are well advised to consider making a Roth IRA election for that portion of their overall IRA funds
 - Taxpayers making the Roth IRA election during their lifetime reduce their overall estate, thereby lowering the effect of higher estate tax rates
 - Federal tax brackets are more favorable for married couples filing joint returns than for single individuals
 - Post-death distributions to beneficiaries are tax-free
 - Tax rates are expected to increase in the near future
 - Impact of the new 3.8% Medicare surtax

General Concepts

- Reasons for converting to a Roth IRA
 - Impact on the taxation of Social Security (age 62+)
 - Impact on part B Medicare premiums (age 65+)
 - Impact on the ACA health insurance premium credit (age 55-64)

Taxation of Roth IRA Conversions

Taxation of Roth IRA Conversions

- When a traditional IRA has non-deductible contributions, a portion of the conversion to a Roth IRA will be non-taxable “basis” to the IRA owner
- In determining the non-taxable portion of a Roth IRA conversion, all traditional IRAs and IRA distributions during the year (including outstanding rollovers) must be combined for apportioning “basis”

— See IRS Form 8606

Taxation of Roth IRA Conversions

Current year non-deductible IRA contributions	\$ 1,000
Prior year non-deductible IRA contributions	6,000
Total non-deductible IRA contributions	<u>\$ 7,000</u>
FMV of all IRAs	\$ 580,000
Outstanding rollovers	20,000
Distributions	-
Roth IRA conversions	100,000
Total value of IRAs, distributions and Roth IRA conversions	<u>\$ 700,000</u>
"Basis apportionment" factor	<u><u>0.0100</u></u>
Gross Roth IRA conversion	\$ 100,000
Non-taxable portion	(1,000)
Taxable Roth IRA conversion	<u><u>\$ 99,000</u></u>

Taxation of Roth IRA Distributions

Taxation of Roth IRA Distributions

- Qualified distributions
 - Not subject to income tax
- Non-qualified distributions
 - Potentially subject to income

Taxation of Roth IRA Distributions

- A Roth IRA distribution will be treated as a “qualified distribution” if both of the following requirements are met:
- The distribution is made:
 - On or after the IRA owner turns 59½
 - To a beneficiary (or the IRA owner’s estate) on or after the death of the IRA owner
 - Because the IRA owner is “disabled”
 - For a “qualified special purchase” (i.e. first-time home buyer)
- A five-year mandatory holding period has passed

CAUTION: If both requirements are not met, then the distribution is a “non-qualified distribution”

Taxation of Roth IRA Distributions

- For purposes of determining a “qualified distribution”, the five-year holding period for all of a participant’s Roth IRAs begins as of January 1st of the first year in which a contribution or conversion was made to any Roth IRA owned by that participant
 - If the participant dies during the five-year holding period, then the five-year holding period “tacks” to the beneficiary (i.e. the holding period of the decedent and the beneficiary combined must be five years)

Taxation of Roth IRA Distributions

- If a distribution is a “non-qualified distribution”:
 - The distribution is first determined to be a non-taxable return of the Roth IRA owner’s previously taxed amounts (i.e. basis)
 - If the distribution exceeds the Roth IRA owner’s previously taxed amounts, the excess distribution will be subject to income tax

Taxation of Roth IRA Distributions

Step 1:
(Non-taxable)

Contributions

- > Regular contributions
- > Rollovers from other Roth IRAs
- > Rollovers from “designated Roth accounts”

Step 2:
(Non-taxable)

Conversions (First-in, first-out basis)

- > Taxable portion of prior conversion
- > Non-taxable portion of prior conversion

Step 3:
(Taxable)

Earnings

Taxation of Roth IRA Distributions

- To the extent that an IRA owner is less than age 59½ at the time he/she receives a non-qualified distribution, the taxable portion of the distribution (i.e. “earnings”) will be subject to the 10% early withdrawal penalty
 - Exceptions to the 10% early withdrawal penalty:
 - Death
 - Disability
 - Substantially Equal Periodic Payments (SEPPs)
 - Medical expenses > 10% of adjusted gross income
 - Health insurance premiums paid by unemployed individuals
 - Qualified higher education expenses
 - Qualified first-time homebuyer expenses

Taxation of Roth IRA Distributions

- To the extent that an IRA owner is less than age 59½ at the time he/she receives a non-qualified distribution, the taxable portion of a previous conversion amount will be subject to the 10% early withdrawal penalty if the distribution is within a five-year period following the conversion
 - The five-year holding period is determined on a conversion-by-conversion basis
 - The five-year holding period for each conversion begins as of January 1st
 - If the year in which the conversion is made the exceptions to that apply to the taxable portion of a non-qualified distribution (i.e. “earnings”) also apply to the taxable portion of a prior conversion amount (e.g. death, disability, etc.)

Taxation of Roth IRA Distributions

- The amount of a non-qualified distribution subject to the 10% early withdrawal penalty is determined as follows:

Gross non-qualified Roth IRA distribution

- *First-time homebuyer expenses*
- *Prior year Roth IRA contributions*

Gross non-qualified Roth IRA distribution subject to 10% tax

- *Taxable portion of prior year Roth IRA conversions > 5 years*
- *Non-taxable portion of prior year Roth IRA conversions*

Net non-qualified Roth IRA distribution subject to 10% tax

Taxation of Roth IRA Distributions

Distribution within 5 years

Distribution beyond 5 years

Age < 59½

Income Tax: Yes (earnings only)

Income Tax: Yes (earnings only)

10% Penalty : Yes (earnings & taxable portion of prior conversion amounts)

10% Penalty: Yes (earnings only)

Age ≥ 59½

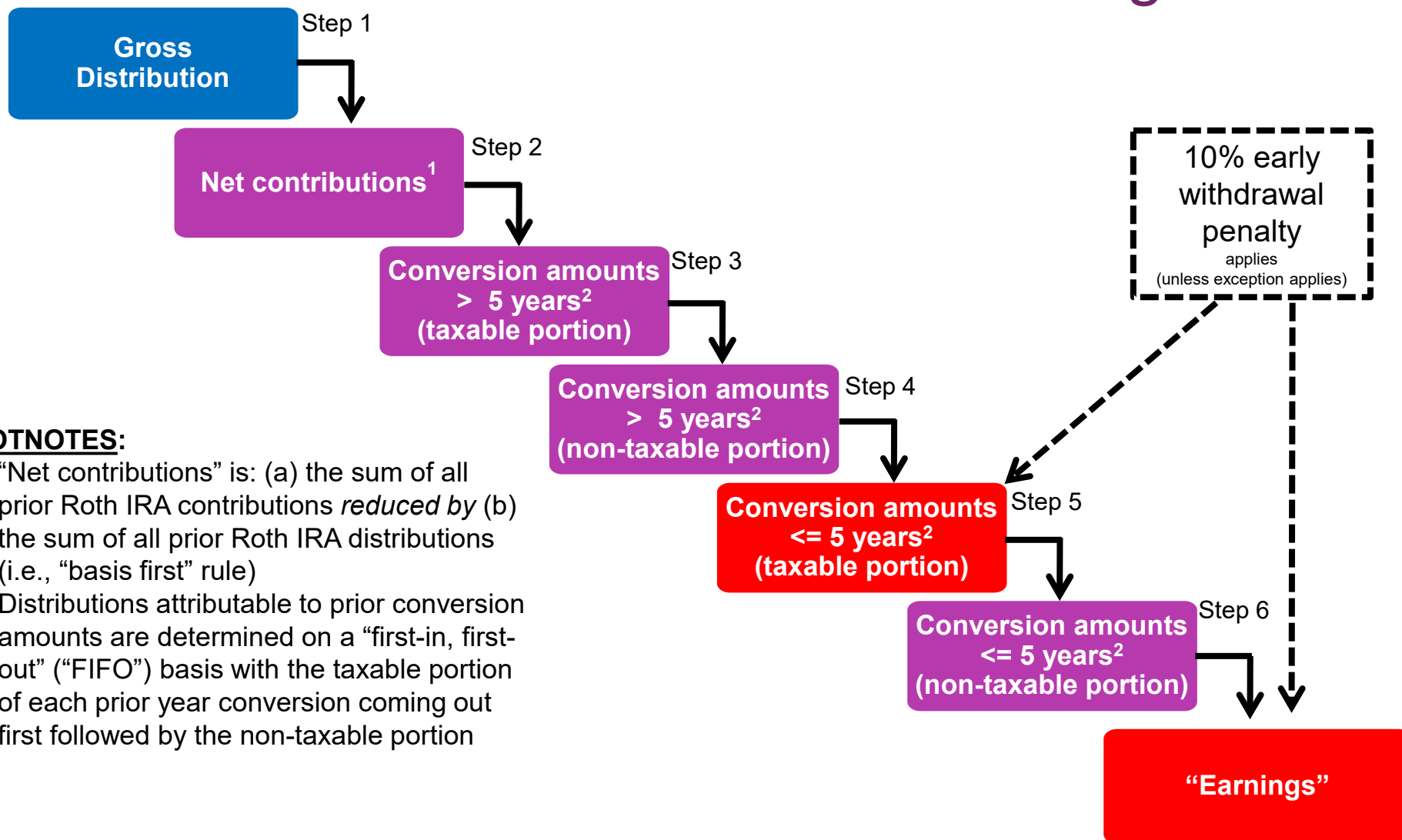
Income Tax: Yes (earnings only)

Income Tax: No

10% Penalty: No

10% Penalty: No

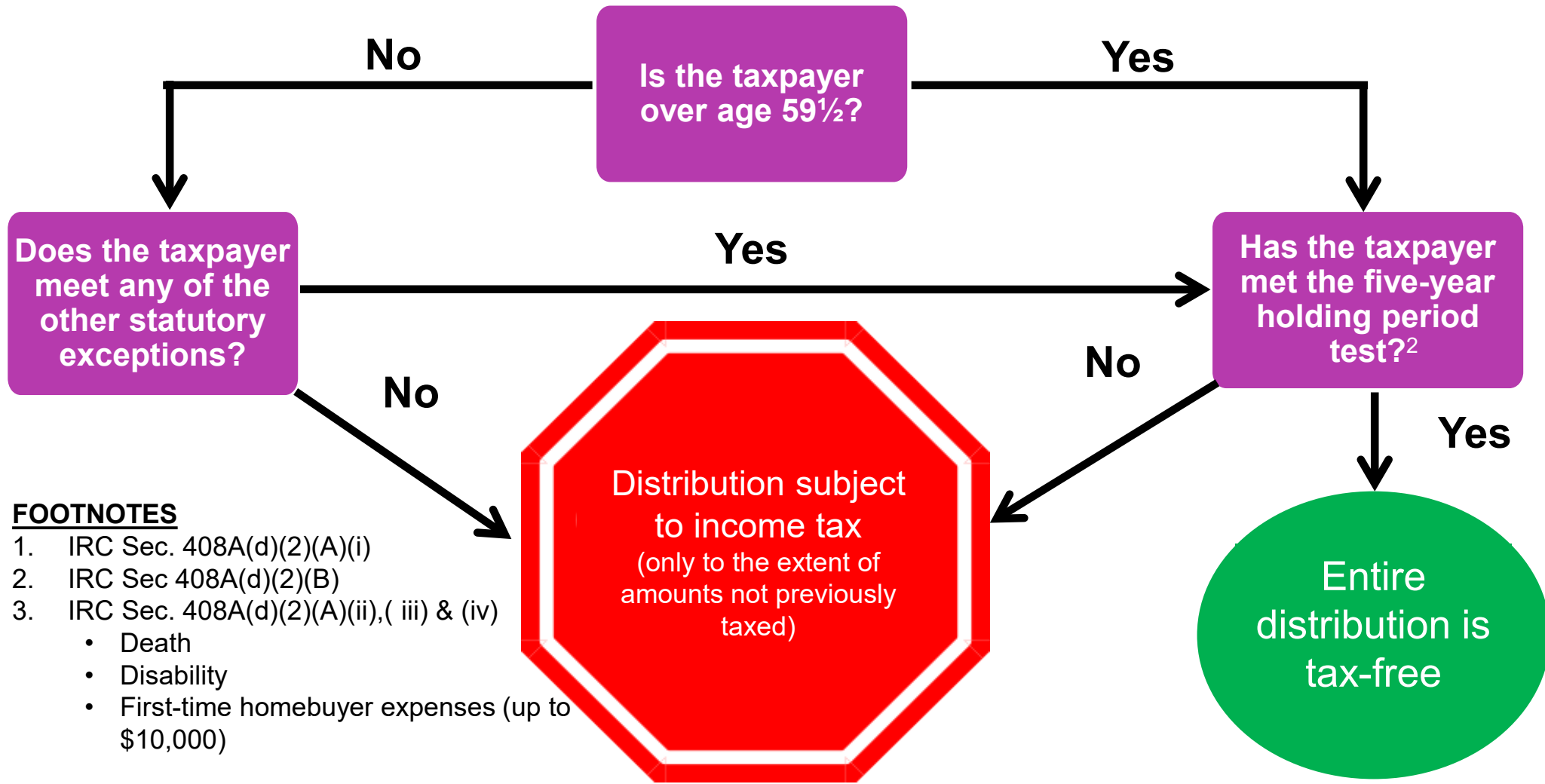
Taxation of Roth IRA Distributions – “Ordering Rules”



FOOTNOTES:

1. “Net contributions” is: (a) the sum of all prior Roth IRA contributions *reduced by* (b) the sum of all prior Roth IRA distributions (i.e., “basis first” rule)
2. Distributions attributable to prior conversion amounts are determined on a “first-in, first-out” (“FIFO”) basis with the taxable portion of each prior year conversion coming out first followed by the non-taxable portion

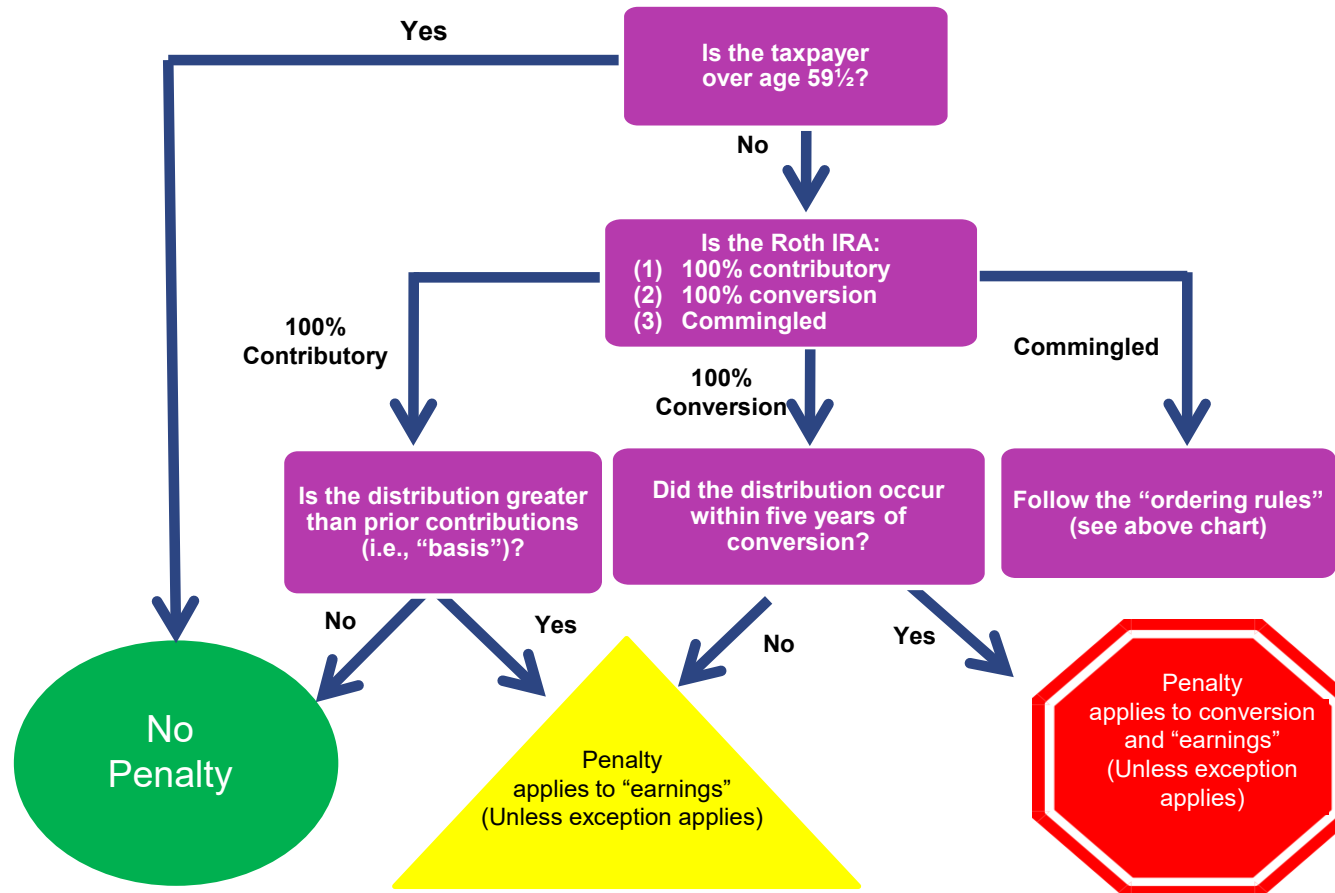
Taxation of Roth IRA Distributions – “Seasoning Rule”



FOOTNOTES

1. IRC Sec. 408A(d)(2)(A)(i)
2. IRC Sec 408A(d)(2)(B)
3. IRC Sec. 408A(d)(2)(A)(ii),(iii) & (iv)
 - Death
 - Disability
 - First-time homebuyer expenses (up to \$10,000)

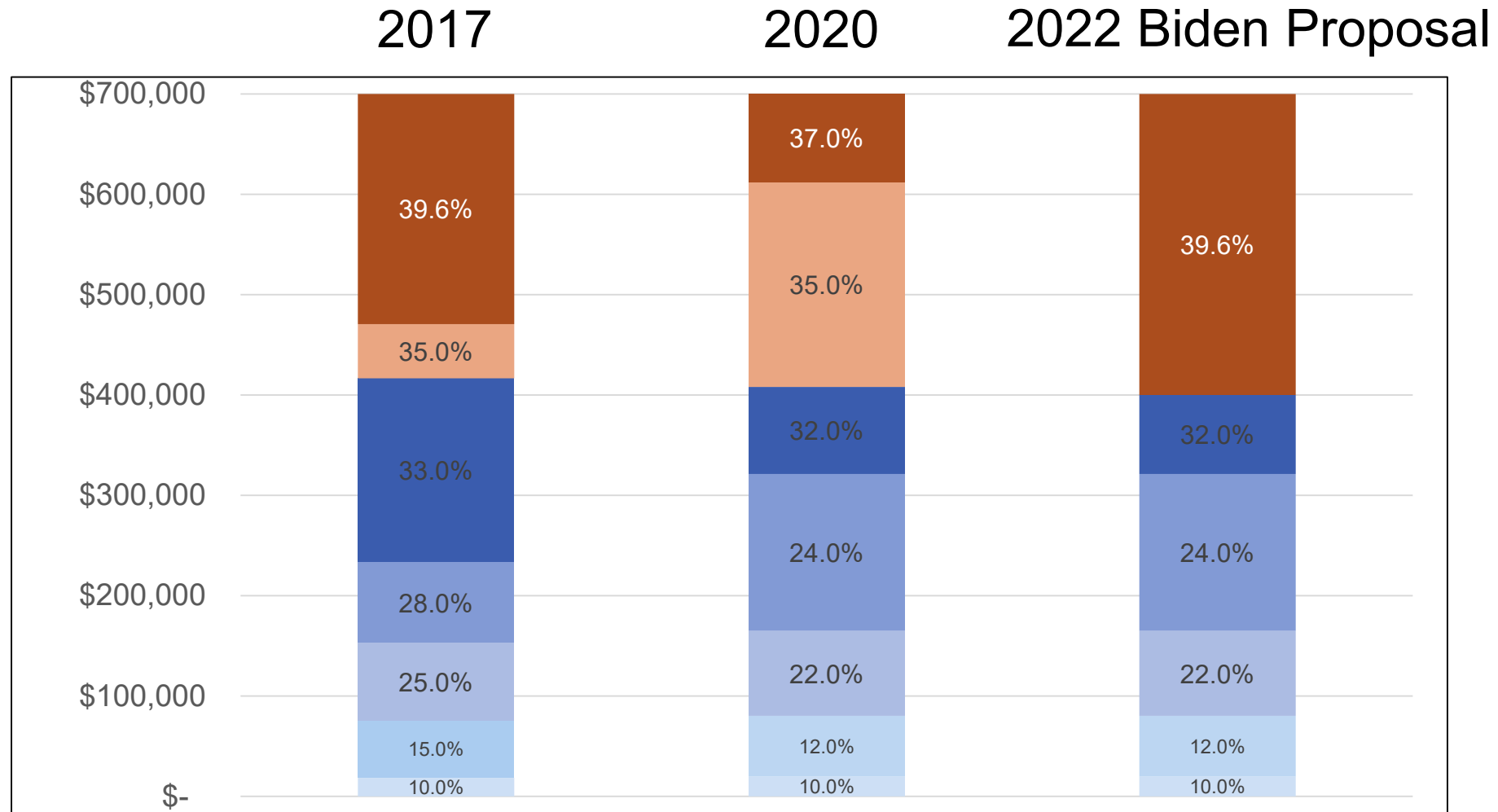
Taxation of Roth IRA Distributions – “Penalty Box Rules”



Exceptions to 10% early withdrawal penalty :

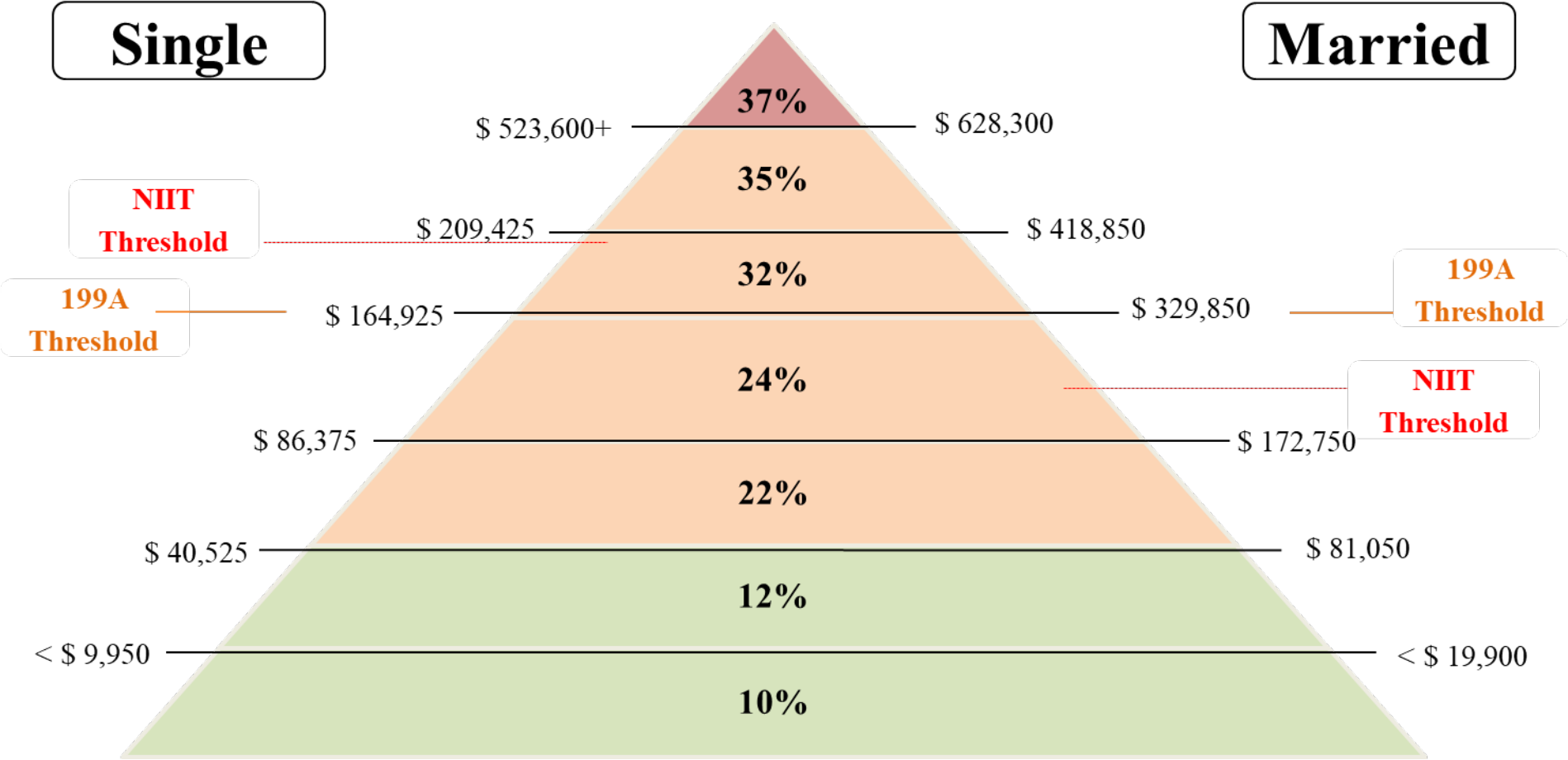
1. Death
2. Disability
3. Series of substantially equal periodic payments
4. Medical expenses greater than 7.5% AGI
5. Health insurance premiums for unemployed individuals
6. Higher education expenses
7. First-time homebuyer expenses (up to \$10K)

Married Filing Jointly



For purposes of this comparison brackets in 2018, 2019, 2020, & 2021 are relatively the same.

2021 Brackets



Mathematics of Roth IRA Conversions

Mathematics of Roth IRA Conversions

- In simplest terms, a traditional IRA will produce the same after-tax result as a Roth IRA provided that:
 - The annual growth rates are the same
 - The tax rate in the conversion year is the same as the tax rate during the withdrawal years (i.e. $A \times B \times C = D$; $A \times C \times B = D$)

Mathematics of Roth IRA Conversions

	Traditional IRA	Roth IRA	Life Insurance
Current Account Balance	\$ 1,000,000	\$ 1,000,000	\$ 1,000,000
Less: Income Taxes @ 40%	-	(400,000)	(400,000)
Net Balance	\$ 1,000,000	\$ 600,000	\$ 600,000
Growth Until Death	300.00%	300.00%	300.00%
Account Balance @ Death	\$ 3,000,000	\$ 1,800,000	\$ 1,800,000
Less: Income Taxes @ 40%	(1,200,000)	-	-
Net Account Balance to Family	\$ 1,800,000	\$ 1,800,000	\$ 1,800,000

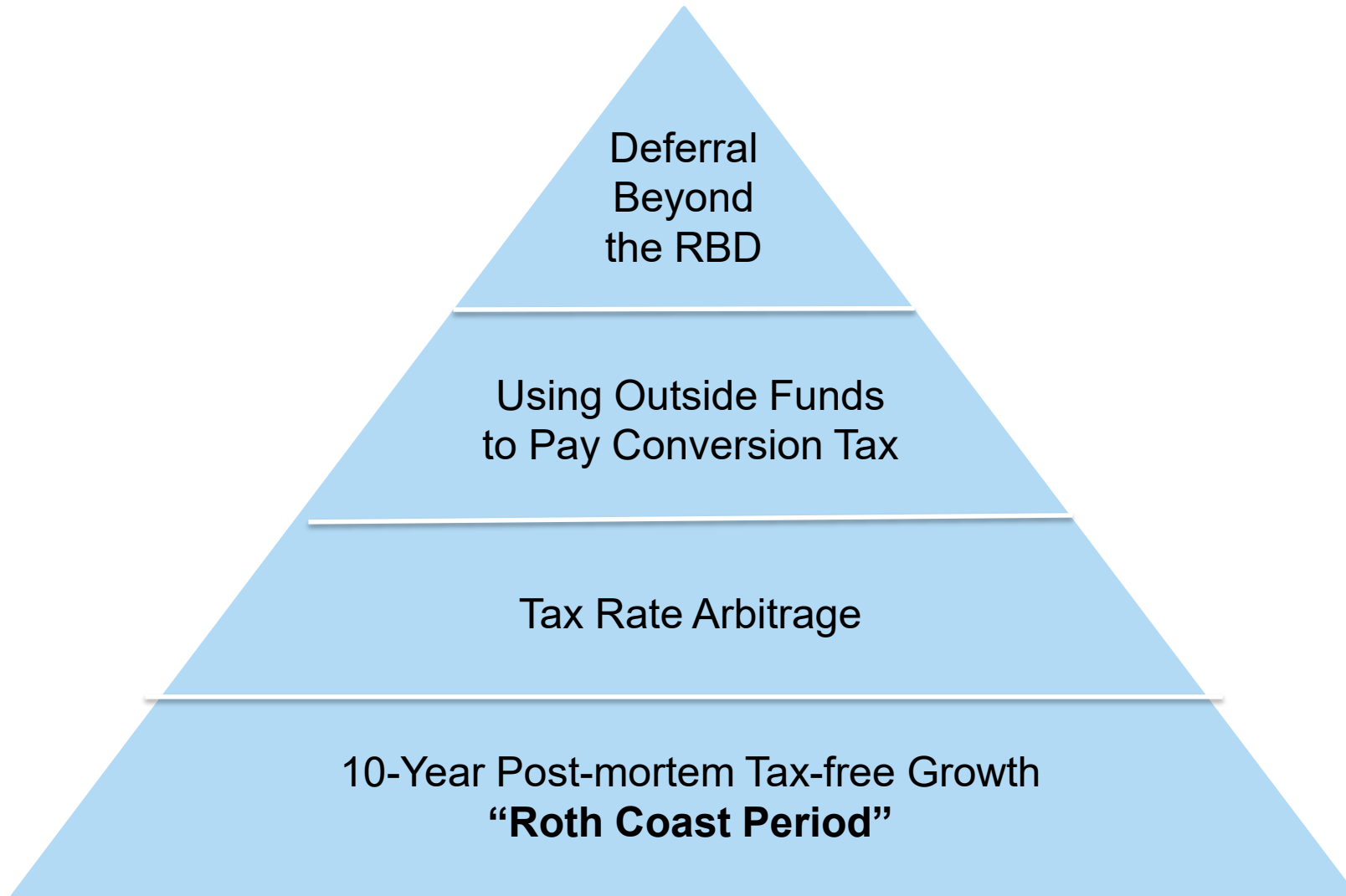
Mathematics of Roth IRA Conversions

- Tactical considerations
 - Unused charitable contribution carryovers
 - Current year ordinary losses
 - Net Operating Loss (NOL) carryovers from prior years
 - Alternative Minimum Tax (AMT)
 - Credit carryovers
 - Dollar-cost averaging to reduce the risk that the amount converted will decrease in value

Mathematics of Roth IRA Conversions

- Critical decision factors
 - Tax rate differential (year of conversion vs. withdrawal years)
 - Use of “outside funds” to pay the income tax liability
 - Need for IRA funds to meet annual living expenses
 - No RMDs
 - Tax-free post-mortem distributions
 - Time horizon
 - Estate tax considerations
 - Ten Year “Roth Coast” period

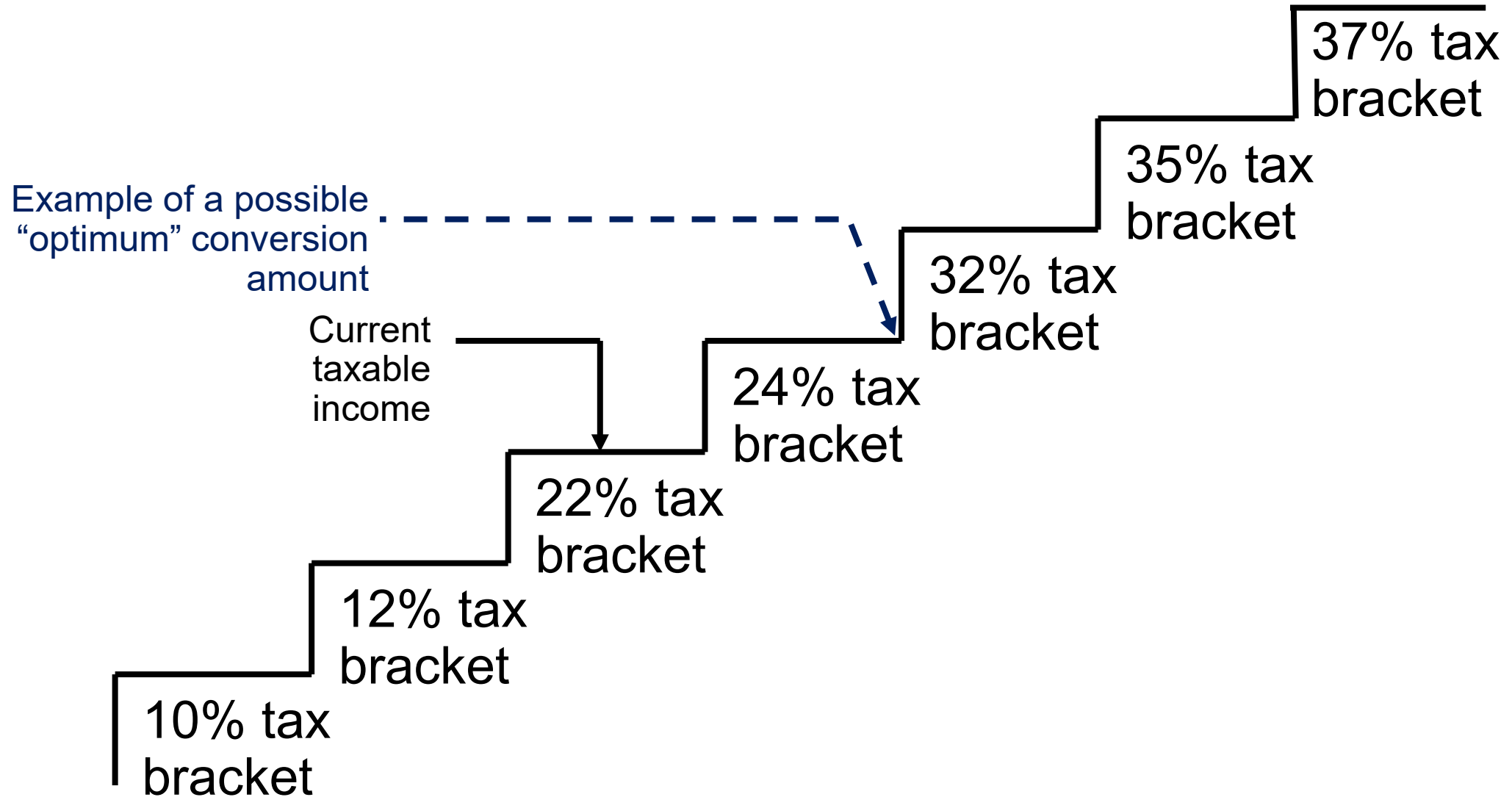
Mathematics of Roth IRA Conversions



Mathematics of Roth IRA Conversions

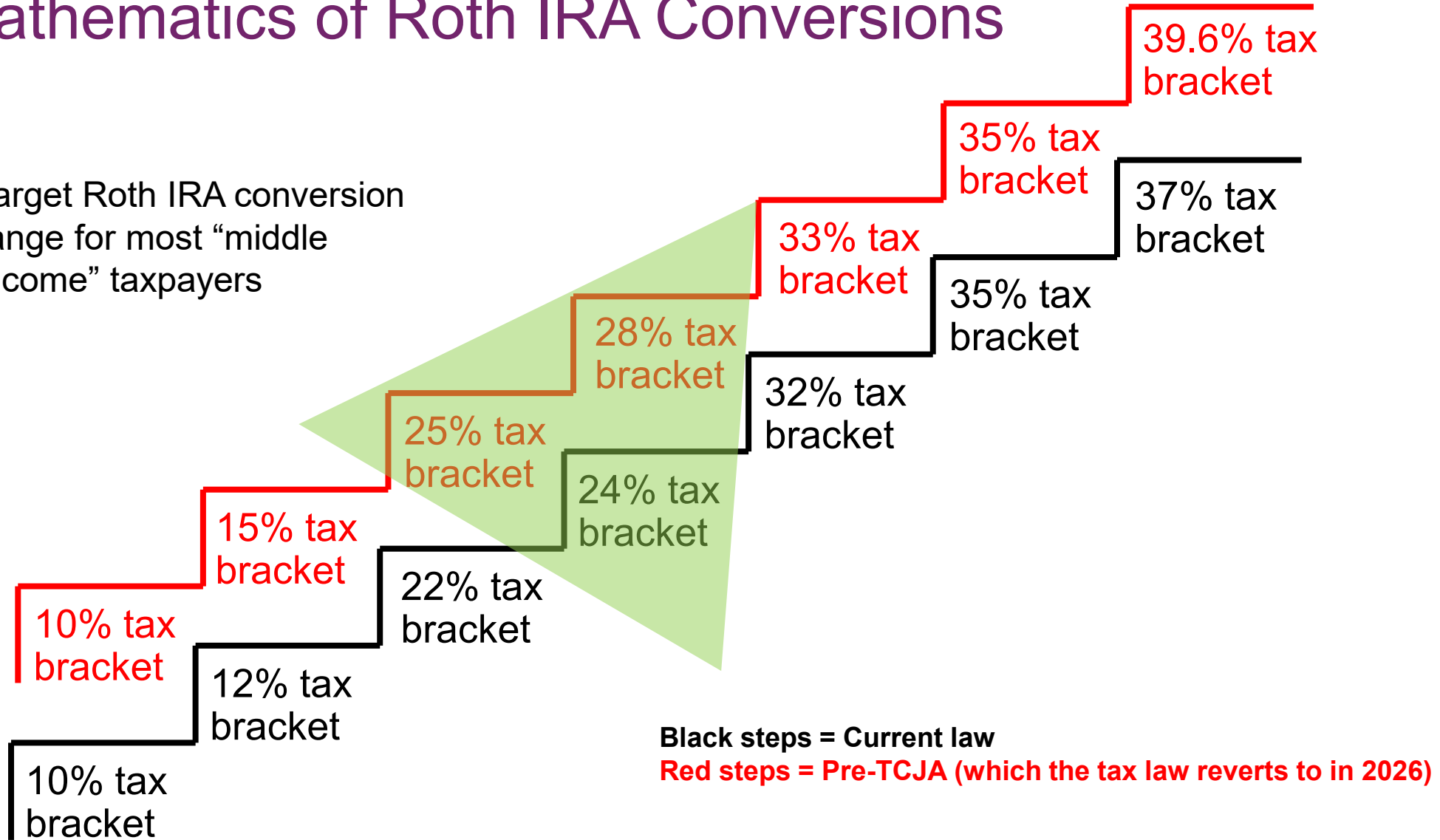
- The key to successful Roth IRA conversions is usually to avoid large jumps in brackets (e.g. converting at a 32% when distributions will likely be subject to a 24% rate will often be ineffective)
- Although brackets are the primary consideration, there are others: capital gains, AMT, NIIT, 199A, etc.
- Timing conversions is critical

Mathematics of Roth IRA Conversions



Mathematics of Roth IRA Conversions

Target Roth IRA conversion range for most “middle income” taxpayers



Mathematics of Roth IRA Conversions

- Tactical considerations
 - Unused charitable contribution carryovers
 - Current year ordinary losses
 - Net Operating Loss (NOL) carryovers
 - Alternative Minimum Tax (AMT) credits
 - Other credit carryovers

Estate Tax Considerations

- “Missing” IRC § 691(c) deduction
 - When a taxpayer dies with an item of Income in Respect of a Decedent (IRD), such as a traditional IRA, in his/her taxable estate the estate (and/or its beneficiaries) must not only pay estate tax on the IRD but also pay income tax on the IRD
 - To prevent double-taxation of IRD, the federal income tax law allows an income tax deduction (on IRS Form 1040, Schedule A), for **federal** estate taxes paid on IRD
 - This is typically known as the “IRC § 691(c) deduction”

Estate Tax Considerations

- “Missing” IRC § 691(c) deduction
 - The dilemma with the IRC § 691(c) deduction is that it only is available for **federal** estate taxes paid on IRD, not state death/estate taxes
 - Thus, the state death/estate tax portion is subject to tax twice (i.e. “missing” IRC § 691(c) deduction)

Estate Tax Considerations

- “Missing” IRC § 691(c) deduction example

IRA balance
 Less: Federal and state income taxes on Roth IRA conversion (40%)
 Taxable Estate

Federal estate tax (40%)
 State death tax (10%)
 Total estate taxes

Post-death traditional IRA balance
 Less: IRC §691(c) deduction
 Post-death traditional IRA balance subject to income tax

Federal and state income taxes on IRA distributions (40%)

Net IRA balance to beneficiaries

	Traditional IRA	Roth IRA
	\$ 1,000,000	\$ 1,000,000
	-	(400,000)
	<u>\$ 1,000,000</u>	<u>\$ 600,000</u>
	\$ 400,000	\$ 240,000
	100,000	60,000
	<u>\$ 500,000</u>	<u>\$ 300,000</u>
	\$ 1,000,000	
	(400,000)	
	<u>\$ 600,000</u>	
	\$ 240,000	\$ -
	<u>\$ 260,000</u>	<u>\$ 300,000</u>

Reconciliation: \$100,000 state death tax x 40% post-death income tax rate = \$40,000 (double-tax component) OR \$400,000 income tax on conversion x 10% state death tax rate = \$40,000 (estate tax savings)

Estate Tax Considerations

- “Fading” IRC § 691(c) deduction
 - Another dilemma with the IRC § 691(c) deduction is that it is only calculated on the value of the IRD at the time of death
 - Thus, post-death appreciation is not sheltered against income tax by the IRC § 691 deduction, resulting in additional income tax being incurred (i.e. “fading” IRC § 691(c) deduction)

Frozen-in-Time

Estate Tax Considerations

- “Fading” IRC § 691(c) deduction example

	No Planning	Roth IRA Conversion at Death
Traditional IRA balance at death	\$ 1,000,000	\$ 1,000,000
Less: IRC §691(c) deduction	-	(450,000)
Taxable portion of Roth IRA conversion	\$ 1,000,000	\$ 550,000
Federal and state income taxes on Roth IRA conversion (40%)	\$ -	\$ 220,000
IRA balance available for future distributions	<u>\$ 1,000,000</u>	<u>\$ 780,000</u>
Total future IRA distributions	\$ 2,000,000	\$ 1,560,000
Less: IRC §691(c) deduction	(450,000)	-
Less: Amounts not subject to income tax	-	(1,560,000)
Taxable portion of future IRA distributions	<u>\$ 1,550,000</u>	<u>\$ -</u>
Federal and state income taxes on future IRA distributions (40%)	\$ 620,000	\$ -
After-tax total future IRA distributions	<u>\$ 1,380,000</u>	<u>\$ 1,560,000</u>

Reconciliation: \$1,560,000 - \$1,380,000 = \$180,000 OR \$620,000 future income tax liability - \$440,000 future value of income tax liability on Roth IRA conversion (i.e. \$220,000 x 2).

Roth Conversions

- 10-year analysis period
- 7% rate of return
- Tax paid from retirement account
- RMDs do not start within period

A positive factor indicates an effective conversion, whereas a negative factor indicates an ineffective conversion

		Rate @ Conversion						
		10%	12%	22%	24%	32%	35%	37%
Rate @ Distribution	10%	0.00	-0.04	-0.24	-0.28	-0.43	-0.49	-0.53
	12%	0.04	0.00	-0.20	-0.24	-0.39	-0.45	-0.49
	22%	0.24	0.20	0.00	-0.04	-0.20	-0.26	-0.30
	24%	0.28	0.24	0.04	0.00	-0.16	-0.22	-0.26
	32%	0.43	0.39	0.20	0.16	0.00	-0.06	-0.10
	35%	0.49	0.45	0.26	0.22	0.06	0.00	-0.04
	37%	0.53	0.49	0.30	0.26	0.10	0.04	0.00

Roth Conversions

- 10-year analysis period
- 7% rate of return
- Tax paid from retirement account
- RMDs do not start within period
- **Sunset distribution rates**

A positive factor indicates an effective conversion, whereas a negative factor indicates an ineffective conversion

		Rate @ Conversion						
		10%	12%	22%	24%	32%	35%	37%
Rate @ Distribution	10%	0.00	-0.04	-0.24	-0.28	-0.43	-0.49	-0.53
	15%	0.10	0.06	-0.14	-0.18	-0.33	-0.39	-0.43
	25%	0.30	0.26	0.06	0.02	-0.14	-0.20	-0.24
	28%	0.35	0.31	0.12	0.08	-0.08	-0.14	-0.18
	33%	0.45	0.41	0.22	0.18	0.02	-0.04	-0.08
	35%	0.49	0.45	0.26	0.22	0.06	0.00	-0.04
	39.6%	0.58	0.54	0.35	0.31	0.15	0.09	0.05

Roth Conversions

- 20-year analysis period
- 7% rate of return
- Tax paid from retirement account
- RMDs do not start within period

A positive factor indicates an effective conversion, whereas a negative factor indicates an ineffective conversion

		Rate @ Conversion						
		10%	12%	22%	24%	32%	35%	37%
Rate @ Distribution	10%	0.00	-0.08	-0.46	-0.54	-0.85	-0.97	-1.04
	12%	0.08	0.00	-0.39	-0.46	-0.77	-0.89	-0.97
	22%	0.46	0.39	0.00	-0.08	-0.39	-0.50	-0.58
	24%	0.54	0.46	0.08	0.00	-0.31	-0.43	-0.50
	32%	0.85	0.77	0.39	0.31	0.00	-0.12	-0.19
	35%	0.97	0.89	0.50	0.43	0.12	0.00	-0.08
	37%	1.04	0.97	0.58	0.50	0.19	0.08	0.00

Roth Conversions

- 20-year analysis period
- 7% rate of return
- Tax paid from retirement account
- RMDs do not start within period
- **Sunset distribution rates**

A positive factor indicates an effective conversion, whereas a negative factor indicates an ineffective conversion

		Rate @ Conversion						
		10%	12%	22%	24%	32%	35%	37%
Rate @ Distribution	10%	0.00	-0.08	-0.46	-0.54	-0.85	-0.97	-1.04
	15%	0.19	0.12	-0.27	-0.35	-0.66	-0.77	-0.85
	25%	0.58	0.50	0.12	0.04	-0.27	-0.39	-0.46
	28%	0.70	0.62	0.23	0.15	-0.15	-0.27	-0.35
	33%	0.89	0.81	0.43	0.35	0.04	-0.08	-0.15
	35%	0.97	0.89	0.50	0.43	0.12	0.00	-0.08
	39.6%	1.15	1.07	0.68	0.60	0.29	0.18	0.10

Roth Conversions

- 10-year analysis period
- 7% rate of return inside retirement account
- 5.5% after-tax rate of return outside retirement account
- Tax paid with outside funds
- RMDs do not start within period

A positive factor indicates an effective conversion, whereas a negative factor indicates an ineffective conversion

		Rate @ Conversion						
		10%	12%	22%	24%	32%	35%	37%
Rate @ Distribution	10%	0.03	-0.01	-0.18	-0.21	-0.35	-0.40	-0.44
	12%	0.07	0.03	-0.14	-0.17	-0.31	-0.36	-0.40
	22%	0.26	0.23	0.06	0.02	-0.11	-0.17	-0.20
	24%	0.30	0.27	0.10	0.06	-0.07	-0.13	-0.16
	32%	0.46	0.42	0.25	0.22	0.08	0.03	0.00
	35%	0.52	0.48	0.31	0.28	0.14	0.09	0.06
	37%	0.56	0.52	0.35	0.32	0.18	0.13	0.10

Roth Conversions

- 10-year analysis period
- 7% rate of return inside retirement account
- 5.5% after-tax rate of return outside retirement account
- Tax paid with outside funds
- RMDs do not start within period
- **Sunset distribution rates**

A positive factor indicates an effective conversion, whereas a negative factor indicates an ineffective conversion

		Rate @ Conversion						
		10%	12%	22%	24%	32%	35%	37%
Rate @ Distribution	10%	0.03	-0.01	-0.18	-0.21	-0.35	-0.40	-0.44
	15%	0.12	0.09	-0.08	-0.11	-0.25	-0.30	-0.34
	25%	0.32	0.29	0.12	0.08	-0.05	-0.11	-0.14
	28%	0.38	0.35	0.18	0.14	0.00	-0.05	-0.08
	33%	0.48	0.44	0.27	0.24	0.10	0.05	0.02
	35%	0.52	0.48	0.31	0.28	0.14	0.09	0.06
	39.6%	0.61	0.57	0.40	0.37	0.23	0.18	0.15

Roth Conversions

- 20-year analysis period
- 7% rate of return inside retirement account
- 5.5% after-tax rate of return outside retirement account
- Tax paid with outside funds
- RMDs do not start within period

A positive factor indicates an effective conversion, whereas a negative factor indicates an ineffective conversion

		Rate @ Conversion						
		10%	12%	22%	24%	32%	35%	37%
Rate @ Distribution	10%	0.10	0.04	-0.25	-0.31	-0.55	-0.63	-0.69
	12%	0.17	0.11	-0.18	-0.24	-0.47	-0.56	-0.62
	22%	0.56	0.50	0.21	0.15	-0.08	-0.17	-0.23
	24%	0.64	0.58	0.29	0.23	0.00	-0.09	-0.15
	32%	0.95	0.89	0.60	0.54	0.30	0.22	0.16
	35%	1.06	1.00	0.71	0.65	0.42	0.33	0.27
	37%	1.14	1.08	0.79	0.73	0.50	0.41	0.35

Roth Conversions

- 20-year analysis period
- 7% rate of return inside retirement account
- 5.5% after-tax rate of return outside retirement account
- Tax paid with outside funds
- RMDs do not start within period
- **Sunset distribution rates**

A positive factor indicates an effective conversion, whereas a negative factor indicates an ineffective conversion

		Rate @ Conversion						
		10%	12%	22%	24%	32%	35%	37%
Rate @ Distribution	10%	0.10	0.04	-0.25	-0.31	-0.55	-0.63	-0.69
	15%	0.29	0.23	-0.06	-0.12	-0.35	-0.44	-0.50
	25%	0.68	0.62	0.33	0.27	0.03	-0.05	-0.11
	28%	0.79	0.73	0.44	0.38	0.15	0.06	0.00
	33%	0.99	0.93	0.64	0.58	0.34	0.26	0.20
	35%	1.06	1.00	0.71	0.65	0.42	0.33	0.27
	39.6%	1.24	1.18	0.89	0.83	0.60	0.51	0.45

Roth Conversions

- 10-year analysis period
- 7% rate of return inside retirement account
- 5.5% after-tax rate of return outside retirement account
- Tax paid with inside funds
- Taxpayer is age 72 and RMDs begin in the first period

A positive factor indicates an effective conversion, whereas a negative factor indicates an ineffective conversion

		Rate @ Conversion						
		10%	12%	22%	24%	32%	35%	37%
Rate @ Distribution	10%	0.05	0.01	-0.21	-0.25	-0.42	-0.48	-0.52
	12%	0.09	0.05	-0.16	-0.21	-0.37	-0.44	-0.48
	22%	0.29	0.25	0.04	0.00	-0.17	-0.23	-0.27
	24%	0.33	0.29	0.08	0.04	-0.13	-0.19	-0.23
	32%	0.50	0.46	0.25	0.20	0.04	-0.03	-0.07
	35%	0.56	0.52	0.31	0.27	0.10	0.03	-0.01
	37%	0.60	0.56	0.35	0.31	0.14	0.08	0.03

Roth Conversions

- 20-year analysis period
- 7% rate of return inside retirement account
- 5.5% after-tax rate of return outside retirement account
- Tax paid with inside funds
- Taxpayer is age 72 and RMDs begin in the first period

A positive factor indicates an effective conversion, whereas a negative factor indicates an ineffective conversion

		Rate @ Conversion						
		10%	12%	22%	24%	32%	35%	37%
Rate @ Distribution	10%	0.34	0.25	-0.16	-0.24	-0.58	-0.70	-0.78
	12%	0.41	0.33	-0.09	-0.17	-0.50	-0.62	-0.71
	22%	0.79	0.70	0.29	0.21	-0.12	-0.25	-0.33
	24%	0.86	0.78	0.37	0.28	-0.05	-0.17	-0.25
	32%	1.16	1.08	0.67	0.58	0.25	0.13	0.05
	35%	1.28	1.19	0.78	0.70	0.37	0.24	0.16
	37%	1.35	1.27	0.86	0.77	0.44	0.32	0.23

Roth Conversions

- 10-year analysis period
- 7% rate of return inside retirement account
- 5.5% after-tax rate of return outside retirement account
- Tax paid with outside funds
- Taxpayer is age 72 and RMDs begin in the first period

A positive factor indicates an effective conversion, whereas a negative factor indicates an ineffective conversion

		Rate @ Conversion						
		10%	12%	22%	24%	32%	35%	37%
Rate @ Distribution	10%	0.08	0.04	-0.14	-0.17	-0.32	-0.37	-0.41
	12%	0.12	0.08	-0.10	-0.13	-0.28	-0.33	-0.37
	22%	0.32	0.29	0.11	0.07	-0.07	-0.13	-0.16
	24%	0.37	0.33	0.15	0.11	-0.03	-0.09	-0.12
	32%	0.53	0.49	0.31	0.28	0.13	0.08	0.04
	35%	0.59	0.55	0.37	0.34	0.19	0.14	0.10
	37%	0.63	0.60	0.42	0.38	0.24	0.18	0.15

Roth Conversions

- 20-year analysis period
- 7% rate of return inside retirement account
- 5.5% after-tax rate of return outside retirement account
- Tax paid with outside funds
- Taxpayer is age 72 and RMDs begin in the first period

A positive factor indicates an effective conversion, whereas a negative factor indicates an ineffective conversion

		Rate @ Conversion						
		10%	12%	22%	24%	32%	35%	37%
Rate @ Distribution	10%	0.44	0.38	0.07	0.01	-0.24	-0.33	-0.39
	12%	0.52	0.46	0.15	0.09	-0.16	-0.25	-0.31
	22%	0.89	0.83	0.52	0.46	0.22	0.12	0.06
	24%	0.97	0.91	0.60	0.54	0.29	0.20	0.14
	32%	1.27	1.21	0.90	0.84	0.59	0.50	0.44
	35%	1.38	1.32	1.01	0.95	0.71	0.61	0.55
	37%	1.46	1.40	1.09	1.03	0.78	0.69	0.63

SECURE Act Life Insurance Strategies

Life Insurance

- Four Strategies
 - IRA Roth Conversion Hedge
 - IRA Relocation
 - Policy on Owner
 - Policy on Spouse
 - Second-to-die policy
 - Source to pay Income Tax
 - Roth Conversion Subsequent to Owner's Death by spouse



Life Insurance – Roth Hedge



*It's a Balancing Act ...
Bet to Live? Bet to Die?*

Life Insurance – Roth Hedge

- The 10-year rule, creates new actuarial risk of early death:
 - Under prior law, qualified accounts can be drawn-down over decades after death capturing deferral and virtually assuring bracket arbitrage.
 - However, a 10-year distribution requirement will unfairly tax those who die when their savings peak around retirement age or shortly thereafter.
 - Life insurance could however offset this risk that family wealth will be lost to tax.

Life Insurance – Roth Hedge

- Roth conversions will be the primary way in which those with large IRAs avoid exposure to higher income tax rates after death.
 - However, the effectiveness of this strategy increases with time.
 - A life insurance policy equal to the difference between the theoretical terminal tax and the terminal tax in the event of early death would offset this risk.

Life Insurance – Roth Hedge

- **Example:**
 - Mary is a 60-year old divorcee and has \$2,000,000 in her qualified plans.
 - Mary's accountant projects her retirement tax-rate to be no greater than 24% with opportunities to undertake Roth Conversions.

Life Insurance – Roth Hedge

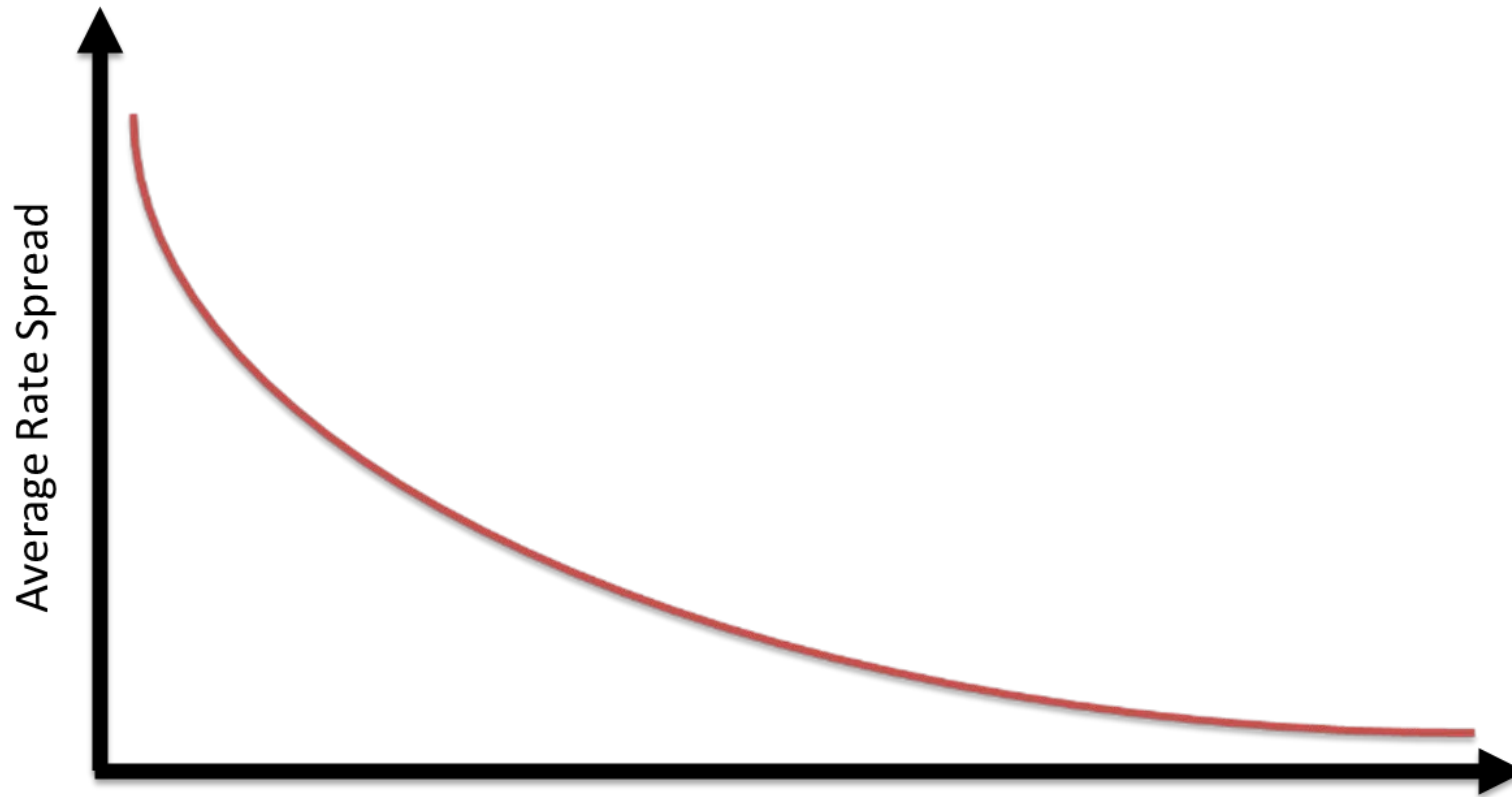
- Example (cont.):
 - With the stretch, RMDs to her only child would generally be subject to a 22%-24% rate.
 - However, with a 10-year rule about 50% of amortized distributions would be subject to a 32% rate.
 - Mary's simple tax-risk of early death is about \$80,000 [$\$2,000,000 \times 50\% \times (32\% - 24\%)$]

Life Insurance – Roth Hedge

- Example (cont.):
 - A more complex calculation could also consider the value of the loss of the qualified accounts:
 - Terminal Tax Deferral
 - Tax-free Compounding of Yield
 - No Roth RMDs During Life
 - Post-mortem Roth Earnings

Life Insurance – Roth Hedge

- Note that the tax-cost of early death will decrease with age for many people



Life Insurance – Roth Hedge

- Therefore, a policy structure with a declining death benefit would best offset the risk
- A whole or universal life product with a term rider may therefore be the best fit

Roth Conversion Subsequent to Owner's Death by surviving spouse

- Determine the likely IRA value at first spouse's death
- Acquire Insurance to pay the Roth conversion taxes at first spouse's death
- Conversions over 1-11 years

Special Consideration for Disability Trusts

Disability Trusts

- Special Lifetime “EBD” Rules
- Roth Conversion Strategies
- CRT Strategies
- Two Trust Strategy

Secure Act: 10-Year Rule - Eligible Designated Beneficiaries

- **Disabled Persons**

- As described in IRC §72(m)(7), “an individual shall be considered to be disabled if they are unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or to be of long-continued and indefinite duration.”
- An individual must provide proof of their disability.
- If an individual is deemed disabled, they are allowed to use the Life Expectancy rule.

Secure Act: 10-Year Rule - Eligible Designated Beneficiaries

- Chronically ill

- As described in IRC §7702B(c)(2), a “chronically ill individual” means an individual who has been certified by a licensed health care practitioner as:
 - Being unable to perform at least two activities of daily living for a period of at least 90 days due to loss of functional capacity,
 - Having a level of disability that is to the level of the bullet point described above, or
 - Requiring substantial supervision to protect such individual from threats to health and safety due to cognitive impairment.
- If an individual is deemed chronically ill, they are allowed to use the Life Expectancy rule.

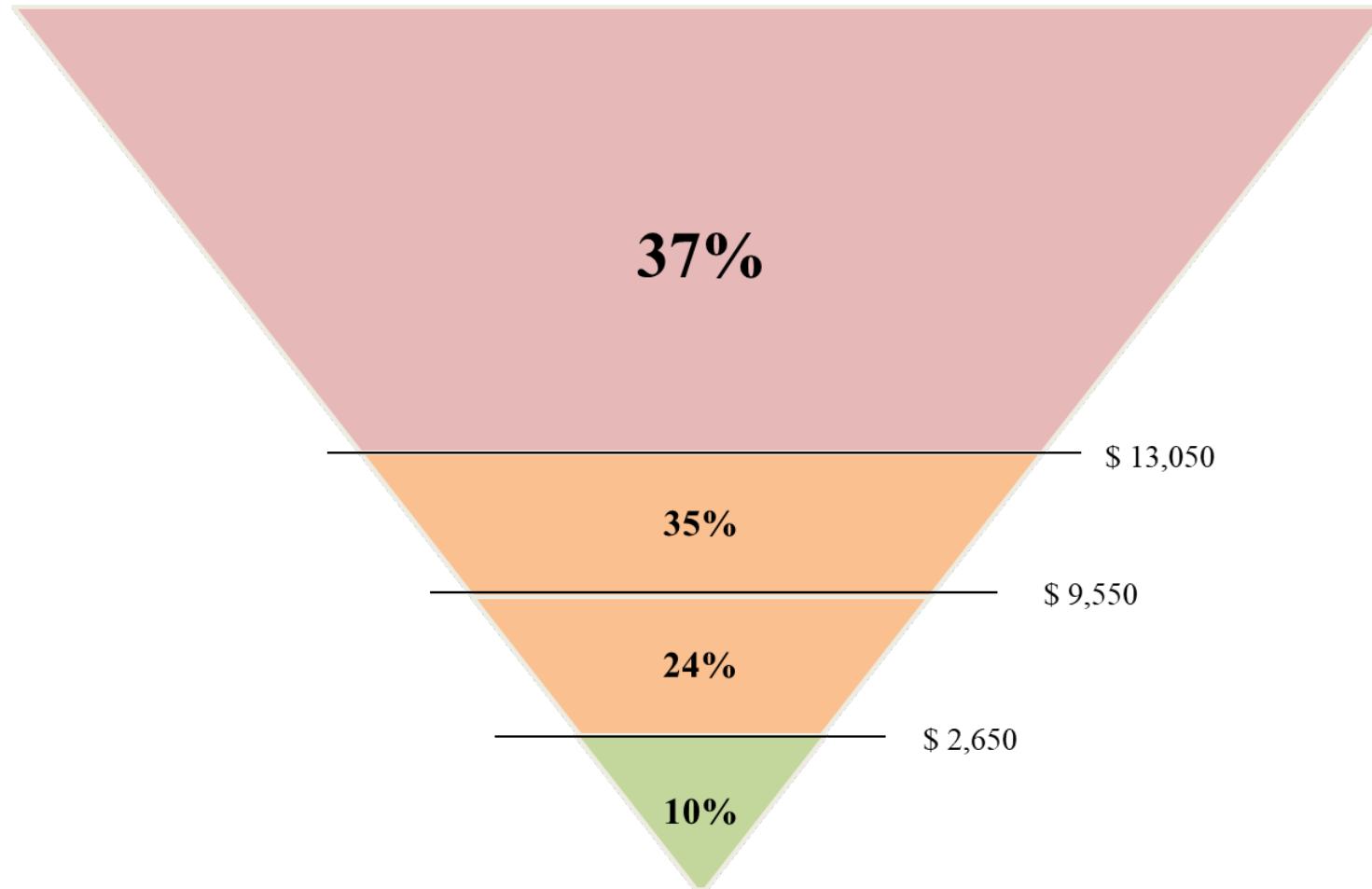
Income Taxation of IRA Trusts

Income Taxation of IRA Trusts

Income taxed to either the trust or the beneficiaries

- If income is accumulated, then the income is taxed to the trust/estate (37% Rate)
- If income is distributed, then the trust/estate gets an income tax deduction and beneficiaries report taxable income
- Roth and Traditional
- IRA income distributed on a pro rata basis

Foundational Concepts - 2021 Ordinary Income Tax Rates for Estates & Trusts

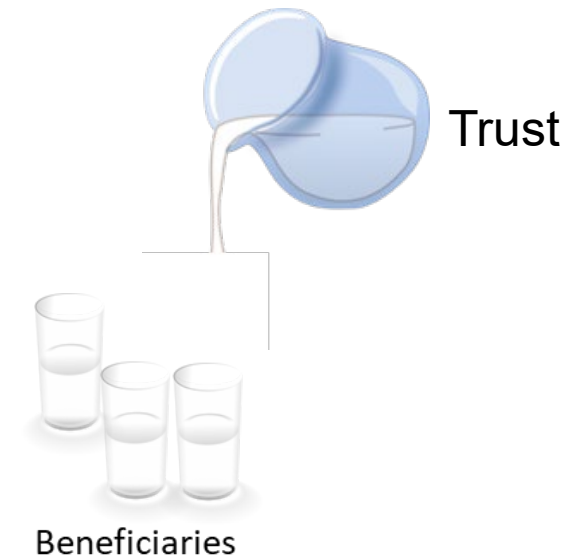


Foundational Concepts – General Tax Rules

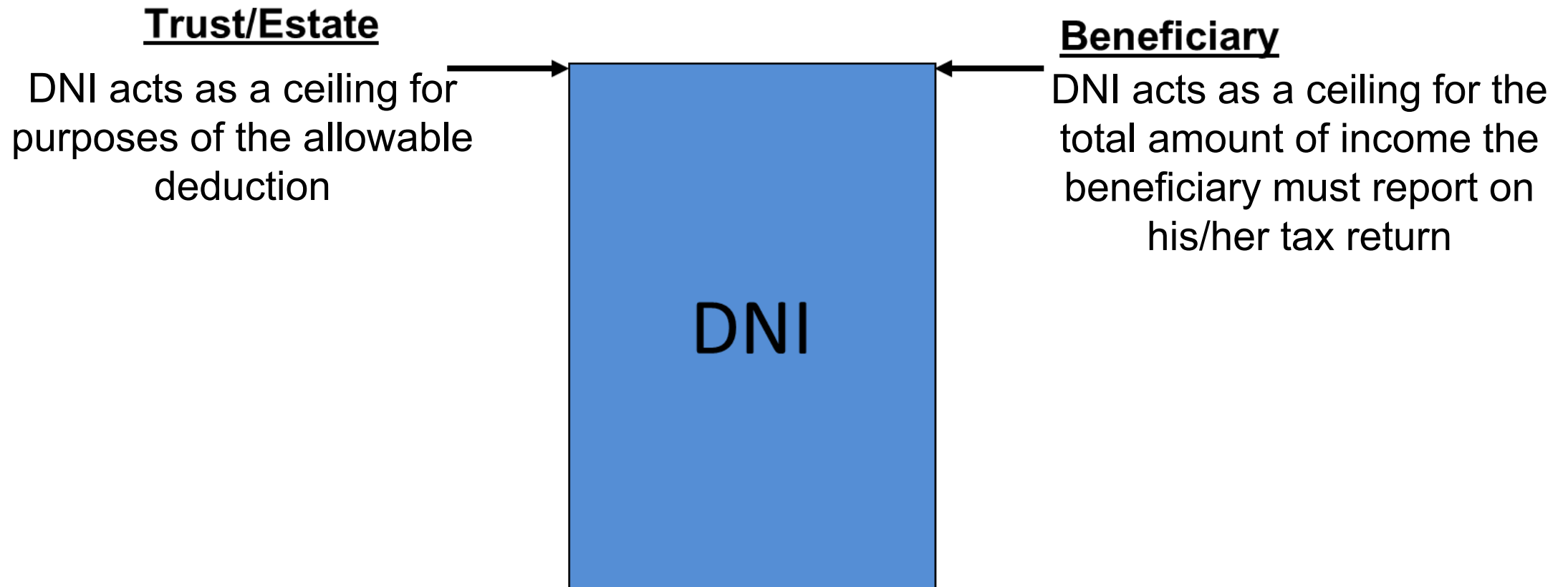
- Two Trust Strategy
 - One Trust for the Traditional IRA
 - One Trust for the Roth IRA

Foundational Concepts – Distributable Net Income (DNI)

- Determines the amount of the trust's or estate's income distribution deduction.
- Determines how much the beneficiaries must report as income on their tax returns.
- Determines the character (e.g. interest, dividends, IRAs etc.) of the taxable income in beneficiaries' hands.



Foundational Concepts – Distributable Net Income (DNI)



Roth Conversions and Disability Strategies

Overview

- Trusts are taxed at a 37% rate
- Parents are likely taxed at a lower rate.

The Objective is to Convert at a 10%
to 24% Bracket Rather than 37%

To be added to our
IRA update newsletter,
please visit:

keeblerandassociates.com/speaking

Upcoming Events

Title	Speaker	Date
AICPA town hall series – PPP and more	Multiple	Every Thursday
The latest and greatest with Roth conversation planning	Bob Keebler	February 23
Financial advice in the age of COVID	Carolyn McClanahan	March 16 and 23
Social Security and Medicare: Maximizing Retirement Benefits	Ted Sarenski	April 20 and 26 (registration coming soon)
Building your tax & financial planning advisory business workshop	Multiple	June 5-6
Advanced PFP Conference @ AICPA ENGAGE	Multiple	June 7-9
Education planning: All you need to know	Ross Riskin	June 21 and 29 (registration coming soon)

Visit <https://future.aicpa.org/home> to register or contact financialplanning@aicpa.org for more information.



AICPA PFP Section

Tax | Retirement | Estate | Risk Management | Investments



Stay in the know

Timely news and forward-thinking ideas



Expand your knowledge & expertise

Technical & practice guides, in-person and online education, hot topic toolkits, PFS credential



Nurture client relationships

Make complex topics simple for clients with Broadridge Advisor



Access professional guidance

Protect your clients, your practice and you



Visit us: aicpa.org/pfp

Contact us: financialplanning@aicpa.org

PFP Section

Tax | Retirement | Estate |
Risk Management | Investments

Your experience counts!

A new pathway to the CPA/PFS
for experienced CPAs

Learn more at
aicpa.org/PFSexperiencedpath



Worldwide leaders in public and management accounting

Thank you

© 2020 Association of International Certified Professional Accountants. All rights reserved. This presentation's images are subject to copyright protection and used under license from third parties. No further use of images is permitted and use of copyrighted images outside the licensed scope constitutes copyright infringement and subjects the user to monetary damages and other penalties.