AHWATUKEE FOOTHILLS NEWS

Roth IRAs Make More Financial Sense For Your Retirement

August 5, 2020 by Dr. Harold Wong

Trillions are held in traditional IRAs and 401(k)s. However, this creates a ticking tax time bomb because any money withdrawn is taxed as ordinary income (think wages or profits from any small business you own). You got a tax deduction from your original deposit and your earnings were tax-deferred until you pulled money out (typically in retirement). If you had deposited $250,000 over the decades while working, and were lucky enough for it to be worth $1 million at retirement, all $1 million will be taxed as ordinary income when you spend it.

In contrast, with a Roth IRA, the whole $1 million is tax free if you follow two rules: you wait until age 59.5 or older to withdraw funds; and you have had your first Roth IRA account opened for at least 5 years. You are allowed to convert as much or as little of your traditional IRAs or 401(k)s in any given tax year.

Example: You have $1,000,000 in your traditional 401(k) and decide to convert $500,000 per year over the next two years. Assuming you have no earnings or losses during this period, this will create $500,000 of taxable income in each year. You would either have to pay this tax; or you could invest in alternative energy business equipment and use the 26% tax credit and Section 179 immediate expensing provision to offset the tax. Once you have done the Roth IRA conversion, here are three major benefits:

1. There is no taxation, no matter how much you earn, for the rest of your life and your spouse’s life; and the first 10 years for any heirs (typically kids or grandkids). Imagine that you have $1 million in a Roth IRA when you retire at age 65. Suppose it grows to $4,048,934 when you are 89 (which is only a 6% average compound growth rate). You or your heirs would be able to spend this money with absolutely NO income tax. In contrast, if your $1 million traditional IRA or 401(k) grew to $4,048,934, at a combined federal and state tax rate of 40%, you would owe $1,619,574 of tax.

2. There is no Required Minimum Distributions (RMDs) from a Roth IRA. In contrast, RMDs are required for any traditional tax-deferred retirement account, such as IRAs, 401(k)s, 403(b)s, and the 457 thrift savings plan once you turn 72. If you have been a good saver, you are being forced to distribute $10,000, $20,000, $30,000 or more of annual RMDs and it increases every year. Many of my clients who were good savers don’t need the RMDs to live on and wish they were not forced to take them. They did not want the extra taxable income.

3. When you are retired, you no longer have your job income and every dollar counts more. Example: You are a married couple, age 70 who have $100,000 of taxable income, less $27,400 standard deduction = $72,600 of federal taxable income. They will owe $8,317 of federal tax and about $1,973 of AZ tax. Losing $10,290 to taxes every year might impact your bucket list fun. In contrast, if most of your income was from Social Security and your Roth IRA, you would owe very little tax.

Most people want to have a free and clear house when they retire. The time to pay an expensive mortgage is when you have your job income. The same thinking should apply to your IRAs and 401ks. You want a free and clear retirement account, meaning a Roth IRA when you are retired because there is no tax when you spend that money.

Free Information on Retirement Planning, Solar Business Investments, and Tax Savings can be found at www.drharoldwong.com or www.solarbusinessinvestments.com. **Free Webinar on Solar Business Investments and Tax Savings:** will be held monthly.

Contact Dr. Harold Wong at (480) 706-0177 or harold_wong@hotmail.com to RSVP.

Dr. Harold Wong earned his Ph.D. in Economics at the University of California/Berkeley and has appeared on over 400 TV/Radio programs.