



Knowledge is Power

Question of the Month - February

“Hi, Brian – I have heard a lot about the benefits of doing Roth conversions to get more tax efficient. However, someone told me that it is not a good idea because of the lost opportunity cost. What does that specifically mean, and is this a reason not to do Roth conversions? Thank you.”

Rhonda

Every retirement tool and strategy has its advantages and disadvantages and times where it should and shouldn't be used; Roth conversions are no different. But there is no 'lost opportunity cost' to a Roth conversion. This is a myth and not a factor against doing a Roth conversion.

The point argued here is that using funds now to pay the tax upfront on a Roth conversion means losing the future earnings that those funds could have produced, i.e. an opportunity cost. This is simply not true. The main factor here is taxes, meaning the difference between the tax rates paid upfront, now at the time of conversion, versus the projected tax rates, either later in retirement or for beneficiaries. It's all about the tax rates: not inflation, not earnings and certainly not the opportunity cost. If the tax rates are the same both at conversion and later in retirement, the end financial result will be exactly the same, and this is true regardless of how long the funds are invested before being withdrawn in retirement.

To illustrate, let's take a \$100,000 IRA and assume a lifetime earnings rate of 200% and a tax rate of 30%. With no Roth conversion, that \$100,000 would grow to \$300,000, but after the 30% tax rate, the IRA would be worth \$210,000. With a Roth conversion of the \$100,000 today, that \$100,000 would go down to \$70,000. And with the 200% lifetime earnings, it would grow to \$210,000. The result is exactly the same.

The decision whether or not to do a Roth conversion is all about taxes. When can you pay the least amount of tax, now by doing a conversion or later by not? That is the question you need to answer to determine if you or your heirs will benefit by doing a Roth conversion. To learn more about this and get answers to many more questions, join me this weekend on The Retirement Money Matters Show. The show airs on Saturday afternoon at 4 on WFRN (93.7 FM), Sunday morning at 8:00 on WWKI (100.5 FM) or anytime online at www.theretirementmoneymattersshow.com. You can also obtain this information by reaching out to us at Hayes Advisory Group at 452-PLAN (7526), 800-939-1603 or brian@hayesadvisorygroup.com.

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