

In-plan Roth Conversion

The American Taxpayer Relief Act signed into law in 2013 permits plans to adopt an expanded Roth in-plan conversion feature. If permitted by your plan document, this feature allows you to convert all or a portion of your pre-tax and traditional after-tax money to a Roth account within the plan.

Who is eligible to make an in-plan Roth conversion?

In order to make an in-plan Roth conversion, the Plan document for your retirement plan must permit this option. Only participants who are employees are eligible to convert pre-tax or traditional after-tax money to Roth within the plan.

Are there restrictions on the amount eligible for rollover/transfer?

Yes, the amounts must be 100% vested. Deferrals and safe harbor contributions are always 100% vested.

Can I re-characterize (undo) an in-plan Roth conversion?

No, a Roth in-plan conversion cannot be undone.

What are the differences between an in-plan Roth conversion and a Roth IRA rollover?

Participants must be entitled to a distribution from the plan in order to make an in-plan Roth rollover. In-plan Roth transfers may be made from any fully vested account. There is no requirement that the participant be entitled to a distribution to make the transfer.

What are the benefits of a Roth conversion?

Once the pre-tax assets are converted to Roth, the Roth assets, including earnings, can be withdrawn free of taxes provided that you are age 59½ or older and the account has been established for at least five years.

Tax-free withdrawals could be a significant benefit, especially if you expect to be in the same or a higher income tax bracket at the time of withdrawal than you are at the time of the conversion to Roth. That said, a Roth conversion is not for everyone.

Who might benefit from an in-plan Roth conversion?

You might benefit from an in-plan Roth conversion if you:

- Expect your tax rate to be the same or higher in the future.
- Are interested in tax diversification (owning assets taxed at different rates so that changes in tax rates or taxable income are mitigated).
- Plan to keep the money invested for at least five years before taking a withdrawal.

Who might not benefit from an in-plan Roth conversion?

You might not benefit from an in-plan Roth conversion if you:

- Expect your tax rate to be lower in retirement than it would be at the time of conversion.
- Will need to access your money within five years of the conversion.
- Would find paying the tax owed on the amount of conversion a hardship.

What happens if I withdraw Roth money within five years of the conversion?

If you withdrew Roth assets within five years of the conversion you would owe a 10% federal penalty tax on the portion of the withdrawal attributable to the conversion. In addition, you may also have to pay ordinary income tax as well as the 10% penalty on the portion of the withdrawal that represents Roth earnings, unless you are age 59½ or older.

I have already been making Roth contributions within my plan. Does that count toward the five-year holding period that applies to Roth conversions?

No. Each Roth conversion has a separate five-year holding period for determining whether a withdrawal of converted money is subject to a 10% federal penalty tax. However, one five-year holding period applies to applicable Roth money for the purposes of determining whether earnings may be withdrawn tax-free.

What are the costs of a conversion?

The tax owed on a conversion could be significant. You should consult a tax advisor before deciding to converting to Roth so you can better understand the costs as well as the potential benefits. Here are just some of the factors to be considered:

If you are converting pre-tax money to Roth:

- The conversion amount would be reported as taxable income for the year of conversion and would be due when you pay your taxes for that year. You should consider federal, state, and local income taxes that would apply and tax withholding ramifications. Please consult a tax advisor to discuss the rules apply to you.
- The conversion amount might raise your taxable income sufficiently enough to push you into a higher federal income tax bracket. Income from a conversion could also lead to the imposition of additional tax on investment income (which applies to individuals whose income exceeds certain thresholds).

When would I have to pay taxes on the conversion?

You would have to pay taxes when you file your return for the year in which the conversion was completed.

If you're paying estimated quarterly taxes, you may want to consult with a tax advisor to determine if the conversion will impact your quarterly payments.

Will Sentinel Benefits withhold taxes on a Roth in-plan conversion?

No.

Is Roth money exempt from required minimum distributions?

No. Unlike a Roth IRA, you have to take required minimum distributions (RMDs) from Roth money in your plan. You do not have to take RMDs from a Roth IRA.

To avoid RMDs, you could roll over Roth money to a Roth IRA before age 72. However, unless you have a Roth IRA, this would restart the five-year holding period requirement before you could take tax-free withdrawals of earnings from the Roth IRA conversion account.

What factors should I consider when choosing between an in-plan Roth conversion and a Roth IRA conversion?

Although your plan may permit in-plan Roth conversions, you may also be eligible to convert all or a portion of your assets to a Roth IRA. Only assets that you have access to through a distributable event (such as termination from employment or the availability of in-service withdrawals) can be converted to a Roth IRA. Some of the factors worth examining are the level of creditor protection, investment selection, the costs and fees associated with each account, and the flexibility and control you have over each account.

How do I request a Roth in-plan conversion?

Please contact our Service Center at (888) 762-6088.

ADDITIONAL RESOURCES:

<https://www.sentinelgroup.com/Individuals/Resources/Calculators> (All our online financial calculators)

<https://www.sentinelgroup.com/Individuals/Resources/Calculators/Roth-IRA-Conversion-Calculator> (Roth Conversion Calculator)

[https://www.sentinelgroup.com/Individuals/Resources/Calculators/Roth-\(after-tax\)-Account](https://www.sentinelgroup.com/Individuals/Resources/Calculators/Roth-(after-tax)-Account) (Roth (after-tax) Account or Pre-Tax Account)

<https://www.sentinelgroup.com/Financial-Professionals/Resources/Education/To-Roth-or-Not-to-Roth> (Webinar)
