

# 5 Ways To Build Your Roth Account

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# Disclaimer

**This presentation is meant for educational purposes only.**

**It is not a specific investment, tax or legal advice.**

**Before taking any action on anything you see in this presentation,  
first consult with your tax, legal or investment advisor.**



# Today's Agenda

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## How to diffuse the tax timebomb

# Tax Treatment of Retirement Savings

## TAX DEDUCTIBLE CONTRIBUTIONS

### PAY TAXES LATER

- Deductible IRA
- 401(k) etc.



## Non-Deductible IRA

## AFTER-TAX CONTRIBUTIONS

### PAY TAXES NOW

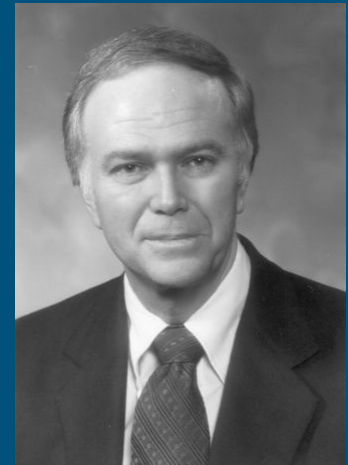
- Roth IRA
- Roth 401(k)



Senator William Roth

# Roth Accounts

The Roth IRA was introduced as part of the Taxpayer Relief Act of 1997 and is named for Senator William Roth.



Senator Bob Packwood

## Post-Tax Retirement Contributions

### No Taxes Forever

Tax-free Growth  
Tax-free Withdrawals\*

# What about Opportunity Cost of paying taxes now?

Hypothetical Savings of \$100,000 in Tax-Deferred and Post-Tax Roth Accounts

Investment assumes 286% growth over 20 years @ 7% compounded annual growth

	<b>Tax-Deferred</b>	<b>After-Tax Roth Account</b>
Current Tax Rate	0%	30%
Investment	\$100,000	\$70,000
Balance over 20 years	\$387,000	\$270,000
Taxes in Retirement	30%	0%
<b>Potential Withdrawal</b>	<b>\$271,000</b>	<b>\$271,000</b>

# **So What Gives?**

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## **RMD (after age 72)\***

## **Uncertainty of Higher Taxes**

(TCJA expires in 2025)

## **Widow's Penalty**



# Other Impacts

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**Large Emergency Withdrawals**

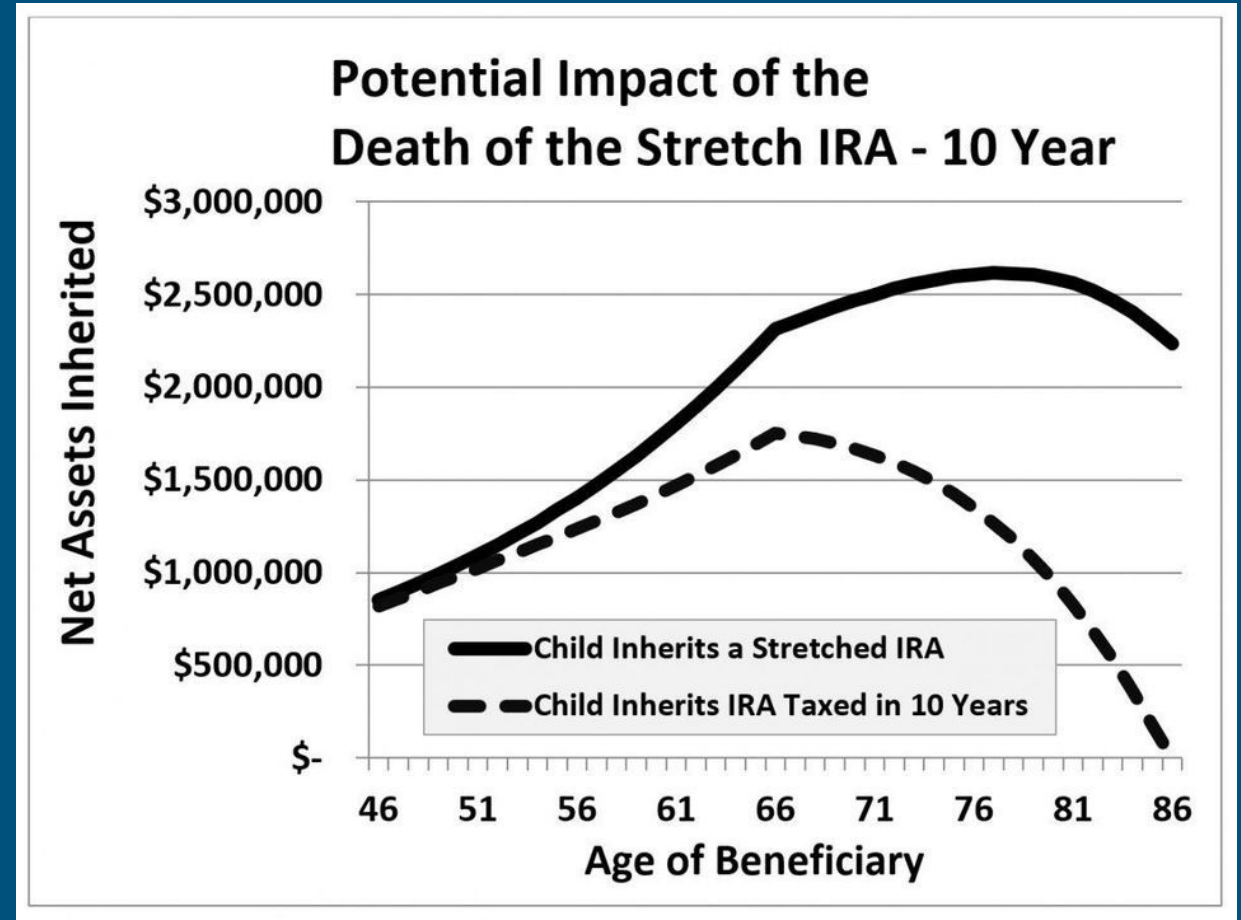
**Medicare Premiums are based on Income**

**50%-85% of Social Security may be taxable in retirement\***

# SECURE Act (Dec 2019)



Heirs must withdraw all the money from the inherited IRA/401(k) in the **next 10 years** and pay taxes!



Source: The Hidden Money Grab In The SECURE Act by James Lange (Forbes, 2019)

# **Roth Rules to Remember**

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**5-year Rule**

**10% Penalty for Withdrawal before age 59 ½\***

**No “Recharacterization” after Conversion**

# Ways to Build Your Roth Account

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## Meet Sam

25 year old, Single

Salary: \$75,000 / year

Employer Benefits:

401(k) Contributions: \$8,000

No Roth 401(k) Option

Other Deductible Benefits: \$2,000

MAGI: \$65,000

## Can Sam contribute to Roth IRA?

Yes, since MAGI is less than \$140,000\*

Maximum Roth IRA Contribution: \$6,000  
(under age 50)

\*Reduced contribution for MAGI \$125K-\$140K

#1 Contribute to Roth IRA (even with an Employer Sponsored Plan)

# Roth IRA Income Limits

2021 Tax Year	Single	Married Filing Jointly
MAGI	\$125,000 - \$140,000	\$198,000 - \$208,000

Irrespective of Employer Sponsored  
Retirement Plans!!

Deductible IRA - \$66K (S) / \$105K (MFJ)

# Roth IRA Contribution Rules

**Must have Earned Income**

includes stipend, internship income

**Contribution Limit of \$6,000 per calendar year 2021**

**Catch up Contribution of \$1,000 over age 50 years**

Total of \$7,000

**Contribute till tax-deadline (April 15, 2022)**

**No Contribution age limit with Earned Income**

SECURE Act of 2019

**Non-working Spouse can also contribute to Roth IRA**

# Meet Chetan & Leena

Ages: 51/ 48, Married, Children

Salary: \$240,000 / year

Employer Benefits:

401(k) Contributions: \$20,000

MAGI: \$220,000

## Income over Roth IRA contribution limit

Maximum 401(k) Contribution: \$26,000

Max 19,500 + 6,500 = \$26,000

Tax Ded. Contribution: \$20,000

**Contribute to Roth 401(k): \$6,000**

**No Income Limit for 401(k) Roth**

#2 Contribute to Roth 401(k) in Employer Sponsored Plan



# Meet Jay & Monica

Ages: 45/45, Married, Children

Total Salary: \$480,000 / year

Employer Benefits:

401(k) Contributions: Maxed out

35% Tax Bracket

MAGI: \$440,000

Not qualified to contribute to Roth IRA

**Non-deductible IRA Contributions of \$6,000 each (No income limits)**

Total = \$12,000 per year

**Convert to Roth IRA ASAP**

**File IRS Form 8606**

#3 Backdoor Roth Conversion

# What's Backdoor Roth Conversion?

- Blessed by IRS and Congress
- No income limit for Deductible IRA contribution: \$6,000
  - Additional \$1,000 catch-up over age 50
- Steps:
  - Contribute to Non-deductible IRA
    - until tax deadline (April 15) for the prior tax year
  - Convert the IRA amount to Roth IRA ASAP (no gains)
  - File IRS Form 8606

# Gotcha!

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No prior IRA account(s) to avoid triggering “pro-rata rule”

**Solution for Rollover IRAs:  
Do Reverse Rollover IRAs into current company’s 401(k)**

## Other Situations

What if you have Traditional IRA account?

What if the current custodian cannot accept reverse rollover?

# Meet Tom

Ages: 55, Single with children

One Salary: \$250,000 / year

Employer Benefits:

401(k) Contributions: Max (\$26,000)

Employer Contributes: \$6,000

MAGI: \$215,000

Not qualified to contribute to Roth IRA

Employer allows "After-Tax 401(k)"

IRS Limit on Contributions: \$64,500

(over age 50)

Total EE+ER Contributions: \$32,000\*

Max After-Tax Contributions: \$32,500

File IRS Form 8606

#4 Mega Backdoor Roth Conversion

# Meet Joe & Ruby

Ages: 62/60, Married, both Retired

Passive Income: \$84,000

Retirement 401(k) Savings: \$1,000,000

Taxable Savings: \$800,000

Taxable Income: \$60,000

Not qualified to contribute to IRA/Roth

Tax Bracket - \$19,901 to \$81,050: **12%**

Next Bracket - \$81,051 to \$172,750: **22%**

**Strategy: convert to top off the bracket**

Fill-up Tax Bracket: \$81K - \$60K = \$21K

Convert: \$21K (Tax = \$2,500\*, 12%)

Additional \$91K (Tax = \$20,200\*, 22%)

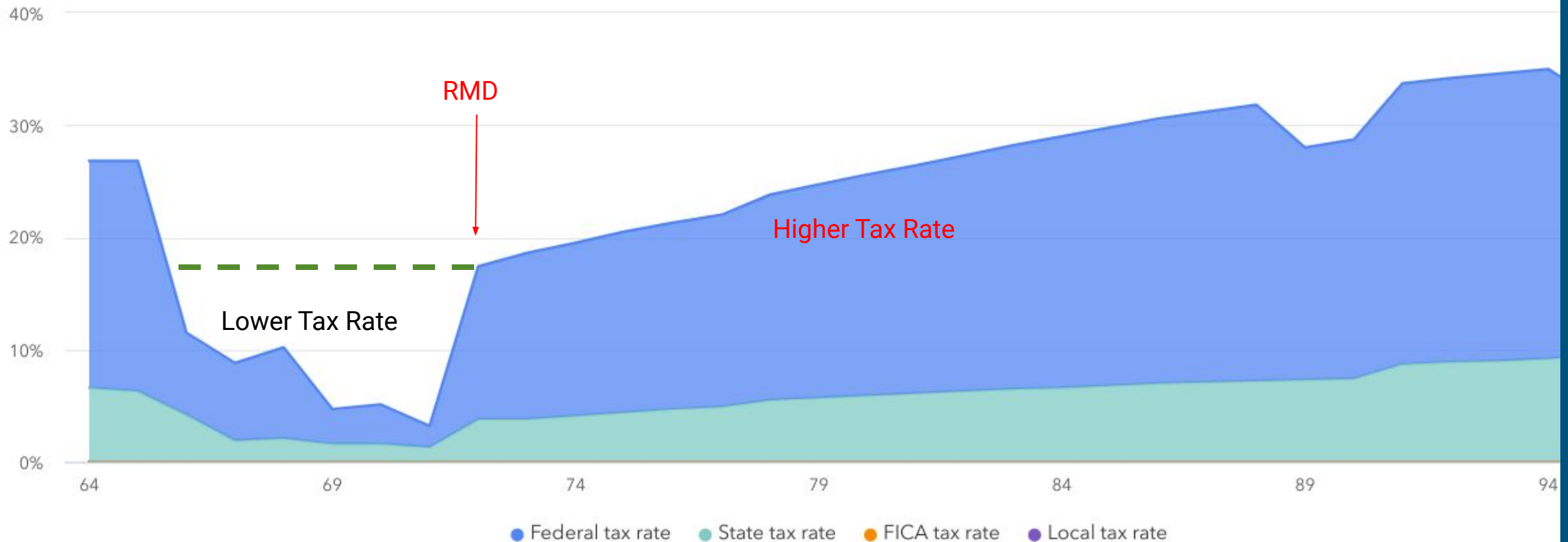
File IRS Form 8606

#5 Roth Conversion from 401(k) or IRA

# Conversion Sweetspot

## Scenarios:

- Gap Year
- Sabbatical
- Job Loss
- Retirement (60-72)



# Roth Conversion Strategy

- Convert IRA and 401(k) accounts to Roth IRA
  - No income limit
- Pay Ordinary Income Taxes on conversion amount
  - Taxes from taxable account to maximize benefits from Roth
  - Beware of penalties paying from IRA if age < 59 1/2

# **Top Reasons not to convert to Roth**

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**Competing Priorities**

**Current Tax Bracket is high**

**Not enough time**

**Insufficient Taxable Funds to pay taxes**

**Heirs will be in a lower tax bracket**



# Summary

Scenario	How to Roth?	Comments
MAGI < \$140K (Single) MAGI < \$208K (MFJ)	Contribute to Roth IRA	Early career years; summer job Lower family income
MAGI > over Roth Limits	Contribute to Roth 401(k)	Higher Income; Employer Plan 401(k) Plan
High Income Tax Bracket	Backdoor Roth IRA Conversion	No other IRA accounts
After-Tax Employer 401(k) Plan	Mega-Backdoor 401(k) to Roth Conversion	Depends on Employer Plan
Lean Years/Lower Bracket	Roth Conversion	Ideally before age 72

# Questions

What should I be doing apart from maximizing 401k contributions?

Can we use not active Roth IRA funds for trading stocks?

Pros and cons of having Roth account personal vs LLC for people who do IT consulting

How will bonds behave in the upcoming period?

# Q & A

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# Thank you!

**Free Initial Consultation**

<https://www.encoverpersonalfinance.com/schedule>

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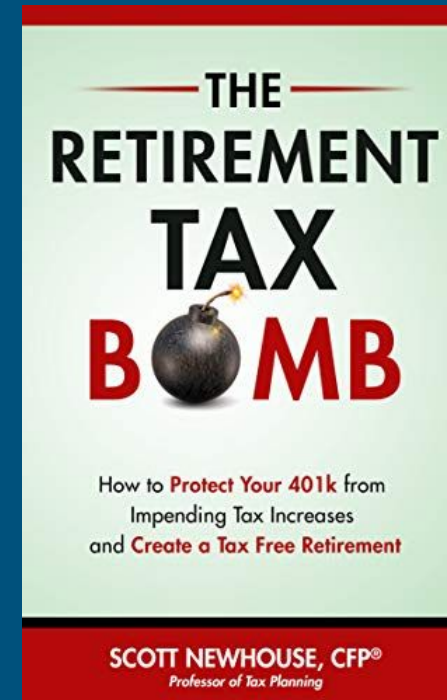
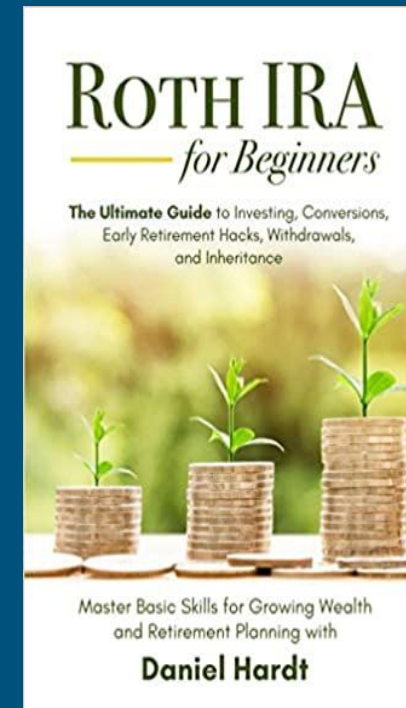
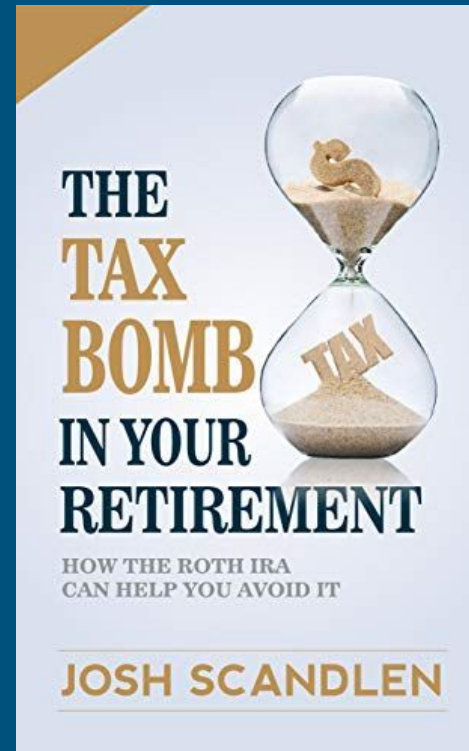
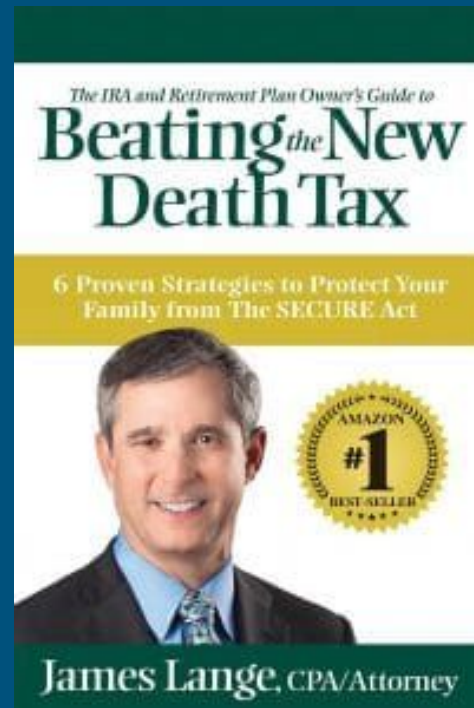
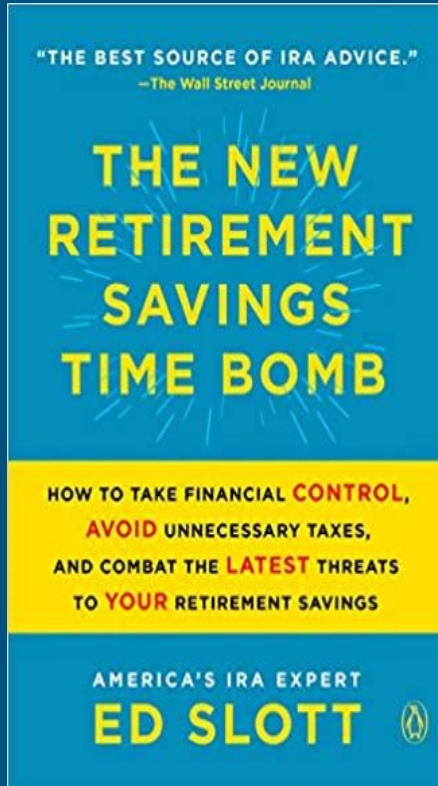
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# Resources



Does SECURE Act favor Roth IRA?