



What You Need to Know About Reversing Roth IRA Conversions

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Did you convert a traditional IRA into a Roth during 2010? Is your Roth IRA now worth less than your traditional IRA at the conversion date due to stock market volatility? If so, you're not alone.

The good news is, you can reverse that Roth conversion! However, you must do so quickly, as the deadline is October 17, 2011.

Conversion of a traditional IRA to a Roth IRA is treated as a taxable distribution from the traditional IRA followed by a contribution of the distributed amount to a Roth IRA. The conversion results in a federal income tax bill, and likely a state income tax bill as well, based upon the value of the traditional IRA on the conversion date. The erratic performance of the stock market subsequent to the conversion may have left you with a Roth IRA that is worth less than the value of the traditional IRA on the conversion date. The end result is that you will pay tax on value that no longer exists.

It doesn't have to be that way! Reversing a Roth conversion avoids paying tax based on the higher value at the time of the conversion. However, subsequently reconverting your traditional IRA into a Roth IRA may be to your advantage. If you get the timing right, you'll convert your traditional IRA into a Roth IRA at a lower tax cost than when you originally converted. Keep in mind that you must wait 30 days from the reversal date to reconvert or to the beginning of the tax year following the year of conversion, if later. Contact your Roth IRA custodian to initiate the reversal.

Already filed your 2010 Form 1040 and paid the tax on the conversion? No problem! Contact us and we'll prepare amended income tax returns to show the reversal and recover any tax paid from the conversion.

Things to consider before you reverse your Roth IRA conversion: Converting a traditional IRA to a Roth IRA in 2010 gave you the option of deferring the income on the conversion to 2011 and 2012 (50% of the income would be reported in each of those years). This should be considered, especially if you expect to be in a lower tax bracket in one or both of those years. This deferral option is not available for conversions that occur in 2011 and beyond. In addition, if the decline in value of the assets in the Roth IRA account is estimated to be temporary, rather than permanent, you may not want to reverse the conversion.