



A unique, but often overlooked, Roth Conversion Option

If you have money in traditional Individual Retirement Accounts (IRAs), you may be concerned about the taxes you'll have to pay¹ when you begin making withdrawals from those accounts. If you are like some retirement savers, you may have heard of a Roth IRA, and considered converting some, or all, of the money you have in your IRA to a Roth. A Roth IRA conversion can help you create a tax-advantaged asset for retirement income for yourself, or tax-advantaged money for your loved ones through your estate.

Life insurance may be able to help. Life insurance protects families in many ways — it provides a source of income at the death of a breadwinner, it provides liquidity for estates with illiquid assets such as businesses, and it provides a source of funds to pay taxes due at death, to name just a few. And, most importantly, the source of funds provided gives you options you might otherwise not have had. One of these options could be to convert to a Roth IRA.

What you need to know about Roth IRA conversions

The advantages:

- A Roth IRA conversion offers potentially significant income tax benefits. First, there are no Required Minimum Distributions from a Roth. Second, once five years have passed and the Roth account owner has reached age 59½, withdrawals are income-tax free.
- Unlike Roth IRA contributions, there are no income limits for Roth conversions.²
- Converting to a Roth is not considered a distribution from your IRA, so if you convert prior to age 59 ½ there will be no 10% early withdrawal penalty.³
- While beneficiaries of inherited Roth IRAs are generally subject to the 10-year withdrawal rule,⁴ their withdrawals are also free of income taxes as long as five years have passed since they inherited their Roth IRA.



One disadvantage: any amounts you convert from a traditional IRA to a Roth IRA will result in taxable income in the year of conversion — which could push you into a higher marginal tax bracket.

For married individuals, you may want to consider funding the taxes on your Roth conversion with life insurance

While converting to a Roth IRA requires sufficient funds to pay the income taxes due in the year the conversion takes place, if you don't have enough available cash, or don't want to sell appreciated investments to generate the cash needed, one strategy to consider is a "deferred" Roth conversion, funded by life insurance.

How could this approach work? Let's say you're married with two adult children, and own a traditional IRA, and you've named your spouse as your primary beneficiary. You purchase a life insurance policy on your own life and name your spouse as your policy's primary beneficiary. When you pass away, your spouse simply rolls your IRA balance into their own IRA, income-tax free, and receives the death proceeds on the life insurance policy income-tax free.⁵ Your spouse could then convert all or a portion of the IRA to a Roth IRA, and use the death proceeds to pay the taxes due on the Roth conversion. Your spouse doesn't even have to decide in advance, but could make the decision after your death based on circumstances at the time.

As a result of this approach

- Your spouse will not have any withdrawals due on the Roth IRA during their lifetime.
- Your spouse can name your two adult children as primary beneficiaries of their Roth IRA. Assuming your spouse dies at least five years after you do, your children will not pay income taxes on withdrawals from their inherited Roth IRAs during the required 10-year withdrawal period.

Considerations

- Any amounts converted from a traditional IRA to a Roth IRA will result in taxable income in the year of conversion — which could push the IRA account owner into a higher marginal tax bracket.
- The IRA account owner needs to be insurable for this strategy to be viable.
- The amount of the insurance premiums should be considered.

What if your spouse dies before you do? To account for that possibility, you and your spouse each purchase life insurance, and each one of you names the other as primary beneficiary. Then, if your spouse is the first to die, you can convert your traditional IRA to a Roth IRA, using the death benefit from your spouse's policy to pay the income taxes due in the year of conversion.

Using permanent life insurance to fund a Roth IRA conversion can be an excellent way to provide yourself with tax-advantaged retirement income, or your loved ones with tax-advantaged assets through your estate. To learn more about the benefits of this approach, contact your Guardian Financial Professional.

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¹ Guardian, its subsidiaries, agents, and employees do not provide tax, legal, or accounting advice. Consult your tax, legal, or accounting professional regarding your individual situation.

² Contributing to a Roth IRA isn't possible for taxpayers whose Modified Adjusted Gross Income exceeds, in 2023, \$153,000 for single income tax filers and \$228,000 for those who are married, filing jointly.

³ Traditional IRA withdrawals are subject to a 10% federal tax penalty if the distribution is made before the account owner reaches age 59½.

⁴ The Setting Every Community Up for Retirement (SECURE) Act of 2019 requires most beneficiaries of inherited IRAs to take their distributions over a 10-year period.

⁵ All whole life insurance policy guarantees are subject to the timely payment of all required premiums and the claims-paying ability of the issuing insurance company. Policy loans and withdrawals affect the guarantees by reducing the policy's death benefit and cash values.

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