

fp alpha α

- **Roth Conversion Simulator**
User Guide

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Introduction

FP Alpha Roth Conversion Simulator

To complete a Roth conversion, a client transfers assets from a Traditional IRA into a Roth IRA, expediting the taxes that would eventually be owed on the Traditional IRA distributions. Roth conversions can help lower the future required minimum distribution (RMD) that would be required to be taken from the Traditional IRA at RMD age.

Roth conversions can be a useful strategy when a client believes they will be in a lower tax bracket now than they will be in retirement. Roth conversions may also make sense when a client has a low earning tax year or if the client would like to pass Roth assets on to their heirs.

The Roth Conversion Simulator can assist you in helping the client determine if a Roth Conversion makes sense, as well as the most beneficial timing and dollar amount for the conversion.

Keep in mind that if you utilize the optimization tool within the Roth Conversion Simulator, the simulator will solve for the most optimal result using one of the three variables selected (Minimum Taxes, Heir's Max Benefit or Client's Max Benefit), however the recommendation may not be realistic and/or practical based on the client's unique circumstances.

Section I: Explanation of Inputs

Provided below, you will find a description of each of the inputs available within the Roth Conversion Simulator tool. Each of these inputs can be adjusted to match the specifications of the client's financial situation. Keep in mind that many of these inputs will pre-populate based on your answers in the client's questionnaire.

Profile Inputs

Filing Status

Select the client's current tax filing status. Based on your selection, the simulator applies the appropriate tax bracket for calculations.

Current Age

Age is pre-filled using the profile of the client in the general questionnaire. For joint households, the age of the client listed first in our system is used, though this input can be edited if you wish to use the age of the co-client.

Retirement Age

Select the client's target or historic retirement age. At the client's retirement age, the Retirement Taxable Income will replace the current Taxable Income. In addition, the field, IRA Distribution After Retirement Age, will be applied.

Life Expectancy

You may choose a different age as the final year of this calculation. At the age of your selection, the accumulation will stop, and the Client Max Benefit and Max Value to Heir will be determined.

IRA Inputs

Beginning Traditional IRA Balance

Enter in the aggregate value of all of the client's tax deferred retirement accounts, including Traditional IRA, 401k, 403b, etc. (including spouse accounts). Note that if the client has inherited IRAs, these values should be excluded from the total entered.

Beginning Roth IRA Asset Value

If your client already has a Roth IRA account(s), list the aggregate balance(s) here.

Investment Rate of Return

This is the rate at which all of the investment portfolios will grow. This includes the Traditional IRA(s), Roth IRA(s), and the simulation created hypothetical taxable account.

Supplemental Withdrawal After Retirement

This value represents the amount of money the client needs annually in retirement from their retirement accounts to cover expenses. If left at \$0, the simulator will remove only the RMD amount. If above \$0, we will take the higher of the input amount or the client's RMD. Additionally, if RMD is higher, we will spend the amount requested by the user and then save/invest the difference.

Income Inputs

Pre-retirement Income

This is the client's ordinary income from their return. The simulator will use this annual income until the designated retirement age. If the client is already older than the retirement age, then this input will not be used at all. Note that this input is pre-filled from the most recent tax return uploaded for the client.

Pre-retirement Income Growth Rate

This is the rate at which the client's current income will grow each year. Most advisors stick with a 3-5% growth rate.

Retirement Taxable Income

This is the client's estimated annual income during retirement. The simulator will use this annual income starting at the designated retirement age. Do NOT include RMDs or any other supplemental withdrawals in this field (the simulator will do this for you). It is recommended that the advisor include the taxable portion of all estimated pensions, annuities, social security and other retirement income streams the client may receive.

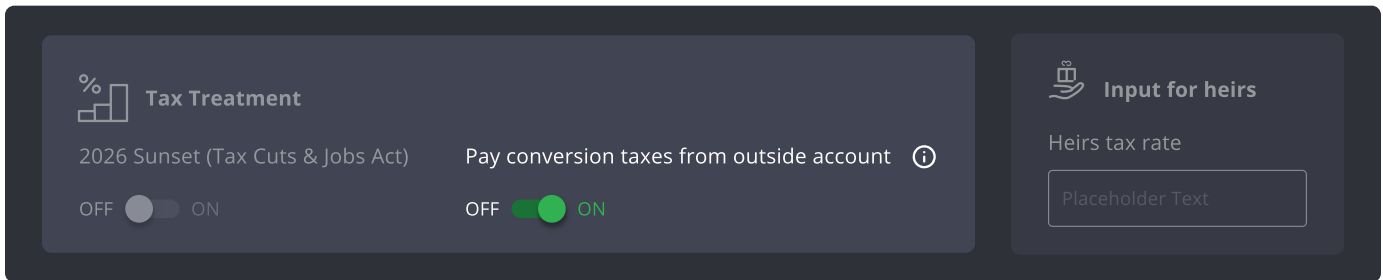
Retirement Income Growth Rate


This is the rate at which the Retirement Taxable Income will grow each year starting from the year the client is set to retire. Most advisors stick with a 3-5% growth rate.


Tax Treatment Toggles

Conversion Tax Paid from Outside Account


If this option is selected, the projector assumes the taxes due on the simulated Roth conversion will be paid from an outside source. In this case, the conversion tax liability is still included in the simulation — it is grown in a placeholder account and then used to reduce the net portfolio balance accordingly. This ensures the impact of the conversion taxes is reflected in the overall projection.



 **Tax Treatment**

2026 Sunset (Tax Cuts & Jobs Act) Pay conversion taxes from outside account 

OFF ON OFF ON

 **Input for heirs**

Heirs tax rate

*Note: Required Minimum Distribution (**RMD**) taxes are always included in both scenarios.

Section 2: How to model a Roth Conversion

There are 2 primary ways to model Roth Conversions within the simulator.

Option 1, manual adjustment, allows you to manually input the details for the Roth Conversion you would like to model. You can specify custom inputs for conversion amount, number of years to convert that amount and the conversion kick-off age.

Option 2, optimize, allows you to utilize FP Alpha’s proprietary Optimize Function to solve for the most optimal scenario for 3 different variables: Client’s Max Benefit, Heir’s Max Benefit or Minimum Taxes . Both methods of modeling the Roth Conversion are explained below.

Option I: Model a Roth Conversion using Manual Adjustments

Step 1 – Enter Inputs on the Roth Conversion Assumptions page

Step 2 – Click Continue

Once all inputs have been entered, click Continue in the upper right corner.

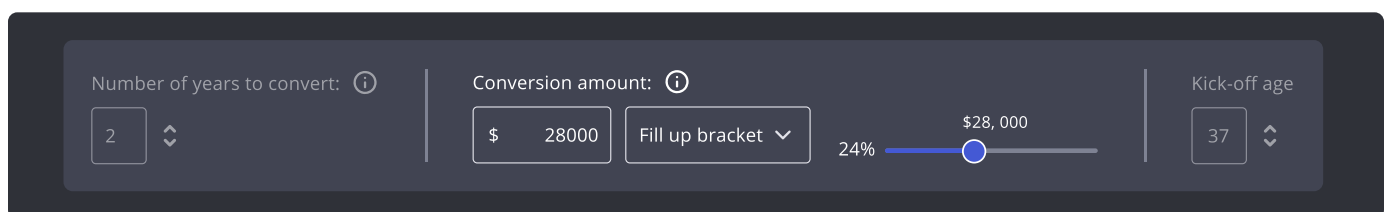
Step 3 – Determine the number of years to convert

This input allows you to indicate the number of years that the simulator is assuming a Roth conversion takes place. Use the arrows to increase or decrease the number of years to convert. You can also type in the number of desired years.

Step 4 – Determine the annual Roth Conversion amount

In order to manually adjust the amount for the Roth Conversion, drag the blue toggle to the right or left to increase or decrease. You can also type in the desired conversion amount and the toggle will adjust automatically.

Note that the percentage displayed in this section represents the marginal tax bracket based on the Current Taxable Income plus the conversion amount. If you would like to maximize the client’s conversion amount to fill up their current tax bracket (or a higher tax bracket), this can be accomplished by clicking the “fill up bracket” dropdown.



Step 5 – Determine the Kick off Age

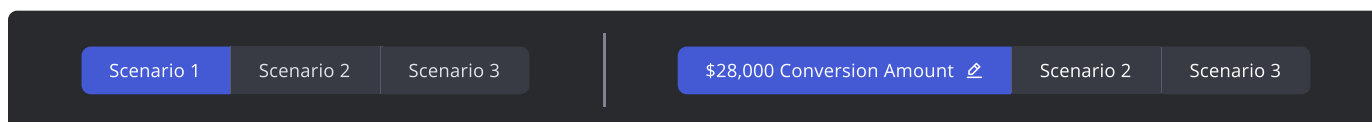
Input the client’s age that you would like the simulator to begin modeling the Roth Conversions.

Step 6 – Review the Roth Conversion Outputs

The simulator will adjust the Roth Conversion outputs at the bottom of the screen, according to the values that were input. You will see a preview of the Total Conversion Amount, Taxes for Conversion, Taxes for Distributions/RMDs, Total Taxes Paid, Client Benefit and Savings to Heirs.

Step 7 – Add in a 2nd and/or 3rd scenario if desired

In the upper left corner, you have the ability to toggle between 3 different scenarios. You can also add a custom name for each of the three scenarios. If you would like to compare multiple scenarios, repeat steps 4 – 7 above.



Step 8 – Click Continue

Once you are satisfied with the initial outputs, click continue in the upper right corner to view a detailed breakdown of the Roth Conversion based on your inputs. Note that the Scenario you have selected in the upper left corner, will determine which scenario is being modeled on the detailed breakdown screen.

Step 9 – Review the Year by Year Roth Conversion Outputs

This page displays a year by year breakdown of the Net Portfolio Balance, Traditional IRA Balance, Roth IRA Balance, Hypothetical Taxable Account, Withdrawals, Taxes Paid, Conversion Amount, Income Amount, RMDs, Value to Heirs and Medicare Part B & D Additional Premium. Each of these columns shows the total value with a Roth Conversion and without a Roth Conversion. (See Section 3 for a detailed breakdown of what is included in each of these columns.)

Step 10 – Visualize balance and conversion graphics

Click each Column Header to display the corresponding line graph above. The Taxes Paid column and the Value to Heirs column can be particularly useful when sharing recommendations with clients.

Step 11 – Adjust inputs as needed

Based on your findings in the year by year Roth Conversion breakdown, you can adjust the inputs by selecting Go Back in the upper right corner. You can also revisit your current assumptions by clicking View Assumptions in the upper right corner.

Step 12 – PDF Report

Once you are satisfied with your inputs and outputs, click Download PDF to generate a report to share with the client. The report provides information on the scenario you have selected on a summarized basis and with a year by year breakdown., On the final page of the report, you will find

a summary comparing each of the 3 scenarios in terms of Client Benefit, Savings to Heirs and Total Taxes Paid.

Step 13 – Model Proposed Conversion in Tax Projector

Once a recommended Roth conversion amount is determined using the Roth Conversion Simulator, the advisor should then do further analysis in the Tax Projector to determine the detailed tax consequences of the proposed roth conversion.

- For example, a Roth Conversion may help the client save on taxes in the long run but income thresholds could trigger additional unfavorable implications such as taxable social security or credits the client qualifies for based on AGI.

Step 14 – Share your recommendations with the client

Keep in mind, if a client decides to move forward with a Roth Conversion strategy, it may make sense for them to make quarterly estimated tax payments in the tax year impacted by the conversion.

Option 2: Model a Roth Conversion Using the Optimize Function

Step 1 – Enter Inputs on the Roth Conversion Assumptions page

Use the client’s information to enter each of the inputs on the Roth Conversion Assumption page. Keep in mind that some of the information will prepopulate if you completed the Tax Planning Questionnaire.

Step 2 – Once all inputs have been entered, click Continue in the upper right corner.

Step 3 – You can use the Roth Conversion Simulator’s Optimization feature to optimize for any of the following three variables:

Client’s Max Benefit: When this variable is selected, it will show the optimal conversion amount in order to maximize the client’s total portfolio value after taxes at death.

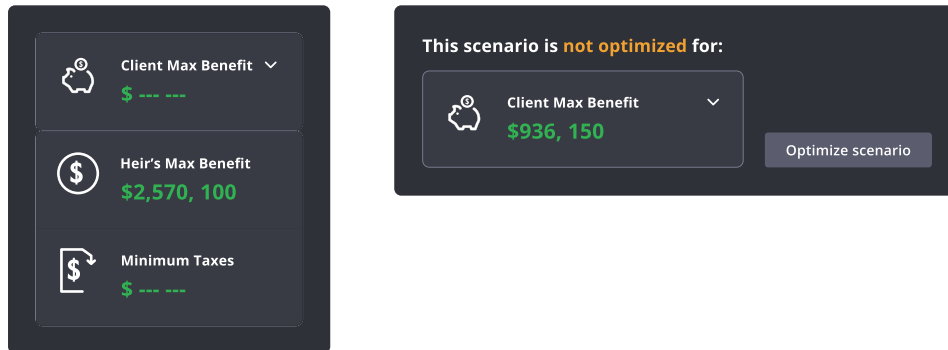
Heir’s Max Benefit: When this variable is selected, it will show the optimal conversion amount in order to maximize the amount that can be passed along to heirs at the client’s death.

Minimum Taxes: When this variable is selected, it will show the optimal conversion amount in order for the least amount of tax to be paid over the client’s lifetime.

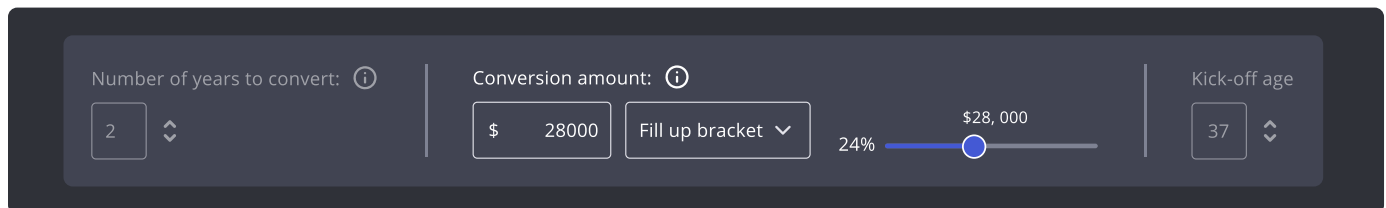
Depending on the variable you would like to solve for, select the corresponding option from the drop down. To do this, click the arrow next to Client Max Benefit. This will display the drop down to allow you to select Heir’s Max Benefit or Minimum Taxes.

Once you have selected the variable you would like to solve for, click Optimize Scenario.

If you would like to maximize the client's conversion amount to fill up their current tax bracket, this can be accomplished by clicking the Maximize button.



Note that the percentage displayed in this section represents the marginal tax bracket based on the Current Taxable Income plus the conversion amount. If you would like to maximize the client's conversion amount to fill up their current tax bracket (or a higher tax bracket), this can be accomplished by clicking the "fill up bracket" dropdown.

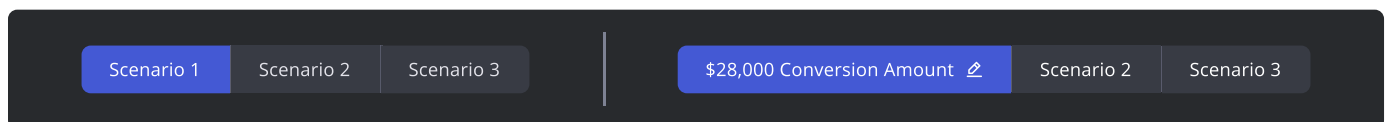


Step 4 – Review the Roth Conversion Outputs

The simulator will adjust the Roth Conversion outputs at the bottom of the screen, according to the values that were input. You will see a preview of the Total Conversion Amount, Taxes for Conversion, Taxes for Distributions/RMDs, Total Taxes Paid, Client Benefit and Savings to Heirs.

Step 5 – Add in a 2nd and/or 3rd scenario if desired

In the upper left corner, you have the ability to toggle between 3 different scenarios. If you would like to compare multiple scenarios, repeat steps 4 – 7 above. Keep in mind that the 2nd and 3rd scenario can be used to optimize for a different variable.



Step 6

Once you are satisfied with the initial outputs, click continue in the upper right corner to view a detailed breakdown of the Roth Conversion based on your inputs. Note that the Scenario you have selected in the upper left corner, will determine which scenario is being modeled on the detailed breakdown screen.

Step 7 – Review the Year by Year Roth Conversion Outputs

This report displays a year by year breakdown of Total After Tax Portfolio Balance, Traditional IRA Balance, Roth IRA Balance, Taxable Account, Taxes Paid, Conversion Amount, Income Amount, Value to Heirs and Medicare Part B & D Additional Premium, Withdrawal Account, Marginal Tax Rate. Each of these columns (with the exception of the conversion amount column) shows the total value with a Roth Conversion and without a Roth Conversion. See Section 3 for a detailed breakdown of what is included in each of these columns.

Step 8

Click each Column Header to display the corresponding line graph above. The Taxes Paid column and the Value to Heirs column can be particularly useful when sharing recommendations with clients.

Step 9

Based on your findings in the year by year Roth Conversion breakdown, you can adjust the inputs by selecting Go Back in the upper right corner. You can also revisit your current assumptions by clicking View Assumptions in the upper right corner.

Step 10

Once you are satisfied with your inputs and outputs, click Download PDF to generate a summary report to share with the client. The report provides information on the scenario you have selected on a summarized basis and with a year by year breakdown. On the final page of the report, you will find a summary comparing each of the 3 scenarios in terms of Client Benefit, Savings to Heirs and Total Taxes Paid.

Step 11

Once a recommended Roth conversion amount is determined using the Roth Conversion Simulator, the advisor should then do further analysis in the tax projector to determine if the conversion amount is recommended.

- For example, a Roth Conversion may help the client save on taxes in the long run but income thresholds could trigger additional unfavorable implications such as taxable social security or credits the client qualifies for based on AGI.

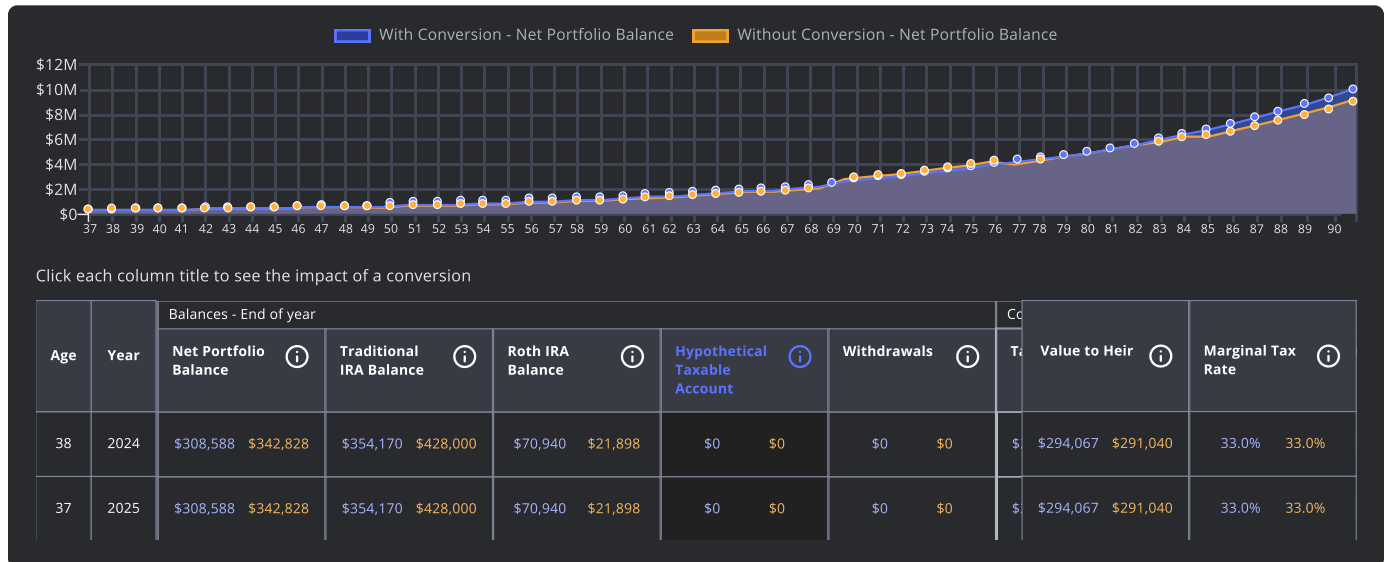
Step 12 – Share your recommendations with the client

Keep in mind, if a client decides to move forward with a Roth Conversion strategy, it may make sense for them to make quarterly estimated tax payments in the tax year impacted by the conversion.

Section 3: Explanation of Year by Year Breakdown

Note that for each of the columns described below, the blue number shows the estimated value based on proceeding with the Roth Conversion and the orange number shows the estimated value based on proceeding without a Roth conversion.

Click each Column Header to display the corresponding line graph. The Taxes Paid column and the Value to Heirs column can be particularly useful when sharing recommendations with clients.



Net Portfolio Balance

This column shows the client’s estimated **Total Portfolio Balance** on an after-tax basis year by year. This amount is calculated by taking the portfolio’s end of year balance, plus growth less any distributions each year.

We use end of year balances for all accounts for consistency and we reduce the portfolio by the opportunity cost of conversion taxes paid from an outside account if that tax treatment toggle is on (see *pay conversion taxes from outside account for more details*).

Keep in mind that you can adjust the *Investment Rate of Return* of the portfolio by clicking **Go Back** until you arrive at the initial input screen

Traditional IRA Balance

This column shows the client’s estimated Traditional IRA Balance on a year by year basis. This column will include all of the client’s tax-deferred money. The client will be required to take Required Minimum Distributions (RMDs) from this account and these RMDs are being calculated automatically by the system. As funds are converted to the Roth IRA, the Traditional IRA balance will decrease.

If necessary, this is also the account that will liquidate second (upon depleting the taxable account) when satisfying Supplemental Withdrawal After Retirement defined by the user on the initial input screen. If you need to adjust the Supplemental Withdrawal After Retirement input or the initial value of the Traditional IRAs by clicking Go Back until you arrive at the initial input screen.

Roth IRA Balance

This column shows the client's estimated Roth IRA Balance. As funds are converted to the Roth IRA, this balance will increase. Upon conversion, taxes are taken out of the total amount being converted (if toggle for Pay conversion taxes from outside account is off). The remaining portion is deposited into the client's Roth IRA. Any distributions (principal and interest) from the Roth IRA are received by the client on a tax-free basis.

If necessary, this is also the account that will liquidate third (upon depleting the taxable account and the Traditional IRA) when satisfying Supplemental Withdrawal After Retirement defined by the user on the initial input screen. Keep in mind that you can adjust the Investment Rate of Return of the portfolio or the initial value of the Roth IRAs by clicking Go Back until you arrive at the initial input screen.

Hypothetical Taxable Account

This column shows the client's estimated Taxable Account Balance on a year by year basis (a hypothetical account we create within the simulator that starts at \$0.). Keep in mind the taxable account is the account that will capture all RMD distributions (and future growth of those RMDs) from the Traditional IRA.

If necessary, this is also the account that will liquidate first when satisfying Supplemental Withdrawal After Retirement defined by the user on the initial input screen. If you need to adjust the Supplemental Withdrawal After Retirement input, click Go Back until you arrive at the initial input screen.

Taxes Paid

This column shows the client's estimated Taxes Paid each year. Keep in mind this includes all taxes paid on liquidations such as the conversion, RMD's and additional IRA distributions.

Conversion Amount

This column shows the amount of Roth Conversion that is completed and the year in which the conversion(s) take place.

Income Amount

This column shows the amount of income received by the client on a year by year basis (uses income inputs on Page 1). This figure also includes all Roth conversions, RMDs, and supplemental withdrawals.

Value to Heir

This column shows the total amount of all accounts that will be passed on to the client's Heirs at the end of the simulation. Keep in mind that if you need to adjust the Heir's Tax Rate, you can click Go Back until you arrive at the initial input screen.

Medicare Part B and D Additional Premium

This column shows the additional Medicare Part B and D Premium for the client. This is a relevant consideration as the additional premium can be triggered once the client's income hits certain thresholds. Note that this is only for one client, even if running a joint scenario.

Withdrawals

This column shows the total net amount withdrawn each year (after taxes) and accumulating (and growing by investment rate of return) over time. If you would like to adjust the annual gross supplemental withdrawal amount, click Go Back until you arrive at the initial input screen.

Marginal Tax Rate

This column shows the client's marginal tax rate percentage based on income, Roth conversions and supplemental withdrawals.

