

Roth Conversion  
Strategies for

# TAX-FREE RETIREMENT INCOME



# Introduction

## The \$2 Million Mistake

When a couple in their early 60s walks into our office with \$2 million in pre-tax retirement accounts and tells me they plan to defer taxes as long as possible, my honest reaction is: they're probably making a pretty big mistake.

Required minimum distributions on a \$2 million IRA start at roughly \$80,000 a year. Add Social Security (likely \$60,000 to \$70,000 of combined income for a couple at that asset level) and you're at \$140,000 before any pensions, dividends, capital gains, or rental income. That's the floor, not the ceiling. If the accounts grow faster than 4% annually, the RMD percentage increases every year, and the dollar amount can climb into six figures: \$100,000, \$150,000, \$200,000 and beyond.

Now you're permanently stuck in IRMAA Medicare surcharge brackets. 85% of your Social Security is taxable. You're triggering net investment income tax on dividends and capital gains. And the moment one spouse passes away, every threshold in the tax code cuts in half, but the RMDs don't.

This guide is for anyone with significant assets in a retirement account who wants to understand what a Roth conversion actually does, when it makes sense, and when it doesn't. It's not a math problem with one right answer. It's a series of trade-offs most people never see until it's too late to fix them.



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As CEO, Troy is responsible for the vision, execution and delivery of services at Oak Harvest Financial Group.

He is the creator of the Retirement Success Plan (RSP), which is a customized blueprint for coordinating investments, income, taxes, health care and estate planning into a comprehensive plan of action and timeline.

## WHO THIS GUIDE IS FOR

Pre-retirees and retirees with \$500K+ in pre-tax retirement accounts (IRA, 401(k), 403(b)) who want to understand the trade-offs of converting to a Roth, including the people for whom a conversion is the wrong move.





## Chapter 1

# Why “Defer Taxes Forever” Is Itself a Risk Strategy

Most people think of tax deferral as the safe traditional choice, by delaying distributions from any taxable accounts (such as a Traditional IRA or 401k). It feels conservative: pay less now, deal with it later. But deferring large IRA balances into your 70s and 80s isn't conservative. It's a concentrated bet that the tax code, the brackets, the deductions, and the surcharges that exist today will still exist twenty years from now. It also assumes that Congress does not introduce any additional taxes or income-based restrictions in the future. History says they won't.

When you defer, you take on three layers of risk most people never name. Rate risk: tax rates have historically been higher than they are today. Threshold risk: phase-outs, deductions, and IRMAA brackets can be tightened

legislatively without the headline rates changing at all. Surcharge risk: net investment income tax didn't exist before 2013, and new surcharges or means-testing rules can be introduced anytime.

And there's a fourth risk people forget entirely: when you pass the IRA on to your children, the SECURE Act forces them to drain it within ten years, usually during their peak earning years and peak tax brackets. The accounts you spent forty years building can lose 40% to 50% of their value to taxes once inherited.

**\$80,000**

Approximate first-year RMD on a \$2M traditional IRA at age 73, and that number grows every year if the account grows faster than 4%.



### TIP: THE AFTER-TAX REFRAME

When people compare “my IRA balance” against “my Roth balance,” the IRA usually looks bigger. But on an after-tax basis, once you subtract the taxes still owed on the IRA, the gap closes dramatically. The right comparison is after-tax dollars to after-tax dollars, not balance to balance.

## Chapter 2

# When a Roth Conversion Actually Makes Sense

A Roth conversion isn't just about paying less tax over your lifetime, though for the right person, that alone can potentially save hundreds of thousands of dollars. The deeper reason to convert is account composition. Most people focus on diversifying their assets. The bigger lever is diversifying your tax buckets: having money in non-qualified accounts, traditional retirement accounts, and Roth accounts, so you arrive at retirement with the ability to control what shows up on your tax return each year.

Conversions tend to make sense when you have substantial pre-tax balances relative to your spending, you're between retirement and age 73 (the "golden window"), and you have non-qualified savings available to pay the conversion tax without dipping into the IRA itself. They also make sense when you have legacy concerns. The 10-year inherited IRA rule turns a large pre-tax account into a tax problem for your heirs.

Roth conversions don't make sense for everyone. High spenders relative to their balances naturally keep their IRAs in check, because the spending itself prevents the runaway growth that creates the RMD and taxation problem. People with smaller pre-tax balances may never trigger the thresholds that make conversions worth the cost. And some people simply don't want to write the IRS a check today and would rather deal with the tax later. That's a legitimate choice.

| GOOD CANDIDATES                             | POOR CANDIDATES                                 |
|---------------------------------------------|-------------------------------------------------|
| Large pre-tax balances relative to spending | High spenders relative to account size          |
| Income gap between retirement and age 73    | Already at or past age 73 with active RMDs      |
| Non-qualified savings to pay the tax bill   | No taxable account to fund the conversion tax   |
| Legacy goals: children inheriting the IRA   | No legacy concerns; intend to spend down assets |
| Concern about future tax rates and brackets | Believe future tax rates will be lower          |
| Currently in a low or moderate bracket      | Already in the highest brackets year-over-year  |





## Chapter 3

# The Golden Window: Why Calendar Timing Drives Everything

A Roth conversion strategy lives or dies on timing, both at the calendar level (which years you convert) and at the market level (which moments within those years). This chapter covers the calendar lever and the next chapter covers the market lever. Strong conversion plans use both.

The most powerful calendar window for most people is the period between when you stop working and when Social Security and RMDs both turn on. We call this the “golden window.” In the golden window, your earned income has dropped, your Social Security hasn’t started yet, and RMDs are still years away. Your tax brackets are temporarily empty. You have room to convert aggressively at the 12%, 22%, and even 24% brackets, moving large amounts of pre-tax money into a Roth at

rates you’ll likely never see again once Social Security and RMDs start filling those brackets back up.

Starting this strategy early, at age 62 is almost always a better starting point than age 67. Not because the rate changes, but because the runway is longer and the brackets are emptier. The earlier you start, the more you can convert at lower rates over more years. Defer Social Security if your situation allows it, draw from your taxable savings to live on, and use the empty brackets to do aggressive conversions while the window is open.

## 11 years

The typical conversion window, from a retirement age around 62 to the start of RMDs at age 73. Most of a successful Roth strategy is built inside this window. Those born after 1960 have 13 years as RMDs begin at age 75.



### TIP: TAX BUCKET DIVERSIFICATION

The point of having non-qualified savings before retirement isn’t just liquidity. Those dollars let you fund living expenses and conversion taxes during the golden window without pulling from the IRA itself. People who arrive at retirement with everything in their 401(k) lose this lever entirely.

## Chapter 4

### The Market Lever: Converting When Prices Are Down

Calendar timing is the strategic layer. Market timing is the tactical layer that, executed well, can compound the strategy over years. The mechanics are simple. When the market drops, your IRA's account value drops with it, but the number of shares you own hasn't changed. A conversion done at depressed prices moves the same number of shares into the Roth at a lower tax cost. When the market recovers, all of that recovery happens inside the Roth, which is tax-free.

During the COVID drawdown in 2020, we accelerated conversions for clients whose plans called for them. Same in 2022. In both cases, clients converted shares at prices 15% to 25% below where the market had been trading just months earlier. The taxes paid on those conversions were significantly lower than what the same conversion would have cost at peak prices, and the rebound that followed compounded entirely tax-free.

You can't time the bottom perfectly. The market may continue down 5% or 10% after you convert. But waiting for the bottom is the wrong frame. The right frame is: instead of doing one big conversion at year-end at whatever price the market happens to be sitting at, take advantage of the market pullbacks that come during the year. There's almost always a 10% intra-year correction. Catching even some of those pullbacks across a five-to-eight-year conversion plan can meaningfully reduce the lifetime tax cost.

# 10%+

The typical intra-year correction. It happens in nearly every calendar year. Plans that wait for year-end conversions miss this lever every time.



#### MECHANICS: CONVERSIONS ARE IN-KIND

You don't sell the shares to do a Roth conversion. You move them in-kind from the traditional IRA to the Roth IRA. The cost basis carries over for tax purposes, and the shares themselves keep their position. When the market recovers, you own those same shares, just inside the Roth.



# Finding Your Point of Equilibrium

Every Roth conversion analysis prepared, the plan starts with the same input: spending. Not how much you have; not how much you've saved. How much you need to live on, adjusted for inflation, projected across your lifetime. Spending is the be-all and end-all in retirement, and it sets the boundaries of every conversion decision.

Once we know spending, we can solve for what I call the point of equilibrium. That's the IRA balance level where future RMDs, plus Social Security, plus your other sources of income, are roughly enough to cover your inflation-adjusted spending need without producing a large excess, therefore controlling a future "tax bomb". If your IRA balance is higher than the equilibrium level, your future RMDs will exceed what you need to live on, forcing you to pay tax on income you didn't ask for and that just ends up compounding in a taxable account afterward. If your IRA balance is lower than the equilibrium level, you've converted more aggressively than your income picture required, which means you paid taxes earlier than you needed to and gave up the compounding on those tax dollars in the meantime.

Equilibrium is a reference point, not a goal. Reaching it doesn't mean the tax problem is solved. RMDs at the equilibrium level can still push you into IRMAA brackets, can still trigger taxation on a meaningful portion of your Social Security, and can still create real problems for the surviving spouse when one half of the couple passes and the brackets cut in half. Equilibrium tells you where excess RMDs start. It doesn't tell you whether the RMDs you do have are landing you in tax territory you'd rather avoid.

That's why the right amount to convert depends on more than the equilibrium number. It depends on what's most important to you. Some people want to be more aggressive than equilibrium, building larger Roth balances to manage IRMAA, protect the surviving spouse, or pass cleaner dollars to their children. Some prefer to stay closer to equilibrium, keeping more flexibility in pre-tax. Some have legacy goals that override pure tax math. The point of solving for equilibrium is to put a number on the page so the conversation isn't theoretical. Understanding the mathematical component of your decision is enlightening and provides the framework for your Roth conversion decisions. The decision about how far past it (or short of it) to convert is a personal one, and it has to be anchored to what you're actually trying to accomplish.



### EXAMPLE: SOLVING FOR EQUILIBRIUM

If you'll need around \$150,000 of inflation-adjusted income at age 80, and your Social Security plus other income is projected to produce roughly \$80,000, your IRA needs to throw off about \$70,000 in RMDs at that age to cover the gap. Equilibrium is the IRA balance that produces approximately that RMD. RMDs above that level represent excess income you didn't need. RMDs at or below that level may still create their own tax issues. Equilibrium is the starting reference, not the finish line.

## Chapter 6

# The Hidden Thresholds That Make a 22% Conversion Cost 30%

This is the chapter most Roth conversion guides skip. Everyone talks about the 12%, 22%, and 24% brackets. Almost no one talks about what happens when a conversion crosses the other thresholds buried in the tax code. These are where conversions quietly get expensive.

A conversion that looks like a 22% decision on the marginal bracket can effectively cost 28% to 32% once you account for the side effects. The Social Security tax torpedo, IRMAA Medicare surcharges, the loss of the 0% capital gains rate, and net investment income tax are all triggered by the same number, your modified adjusted gross income, and a conversion increases that number directly.

| THRESHOLD                   | WHAT HAPPENS WHEN A CONVERSION CROSSES IT                                                                                                                                                                        |
|-----------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Social Security Tax Torpedo | One extra dollar of conversion can pull 50¢ to 85¢ of additional Social Security into taxation. Effective tax cost on the conversion can rise 6 to 10 percentage points above the headline bracket.              |
| IRMAA Medicare Surcharges   | Cross an income cliff and your Medicare Part B and D premiums jump for the year, sometimes by thousands of dollars. The cliffs are absolute: \$1 over the threshold costs the full step-up.                      |
| 0% Capital Gains Rate       | Long-term gains are taxed at 0% under a specific income threshold. A conversion can blow you past it, turning what would have been a tax-free rebalance into a 15% or 18.8% taxable event.                       |
| Net Investment Income Tax   | An additional 3.8% on dividends, interest, and capital gains kicks in above \$250K modified AGI for joint filers. A large conversion can trigger it on income that would otherwise have been outside the surtax. |

*The takeaway isn't "don't convert." The takeaway is: you should understand every threshold a conversion might cross and the financial impact that could have on your taxable income. A good analysis names each tax threshold, shows you whether your planned conversion crosses it, and lets you see the trade-off. That's the difference between converting blind and converting on purpose and with intent.*



# The Three Most Common Roth Conversion Mistakes

After running these analyses for hundreds of families, the same three mistakes show up consistently. None of them are technical. They're judgment errors people make when they don't have the full picture in front of them.



### MISTAKE 1

## Not Doing Enough

You have a \$2 million IRA and you do a \$25,000 conversion. The account makes 10%, that's \$200,000 of growth in a single year. You converted 1%. You're trying to salt the ocean. Either commit to a meaningful conversion plan or don't bother.

### MISTAKE 2

## Doing Too Much, Too Fast

On the other end: people who convert aggressively all in one year out of fear that taxes will spike. The same outcome could often be achieved over three to five years, staying in lower brackets the whole way and keeping more money compounding. Don't write the IRS one giant check when five smaller ones get you to the same place and at a lower total tax cost.

### MISTAKE 3

## Not Knowing Where the Thresholds Are

The most expensive Roth conversion mistakes come from people who never see the thresholds coming. They look at their marginal bracket, decide a 22% conversion is fine, and don't realize that the same conversion is going to bump them across an IRMAA cliff that adds thousands to their Medicare premiums for a year, or pull a chunk of their Social Security into taxation that wasn't taxable before. The headline rate told them one number. Their actual tax bill told them another. The difference can be five figures, and it's entirely avoidable when the thresholds are visible before you decide. The previous chapter listed the four big ones. The mistake isn't crossing a threshold. It's crossing one without knowing you did.



## Chapter 8

# Your Roth Conversion Action Checklist

Use this checklist before making any conversion decision, whether you work with an advisor or not. If you can't answer all eight questions, you don't have enough information to decide responsibly how much to convert and over what time period.

- 1** Project your RMDs from age 73 to age 90, assuming reasonable growth on the accounts. Most people are stunned by how large these numbers get.
- 2** Compare projected RMDs plus Social Security plus other income against your projected inflation-adjusted spending need at the same ages.
- 3** Identify the point of equilibrium as a reference: the IRA balance that produces approximately the income you need at the ages you need it. Use it as a starting point, not a finish line.
- 4** Confirm you have non-qualified savings outside retirement accounts to pay the conversion tax. Paying tax with IRA money defeats most of the strategy.
- 5** Map every threshold a conversion might cross: income bracket, IRMAA, Social Security taxation, net investment income tax, 0% capital gains rate.
- 6** Model the surviving-spouse scenario. The brackets, deduction, and IRMAA thresholds all cut roughly in half when one spouse passes, so your conversion plan must account for this.
- 7** Decide whether you have legacy goals and to what extent you'd like to maximize inheritance for your beneficiaries. If children will inherit, project their tax cost on a 10-year forced distribution at their likely income levels.
- 8** Build the conversion as a multi-year plan, not a single-year event, and revisit it every year as tax laws, markets, and your situation evolve.

## Our Approach



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CEO of Oak Harvest Financial Group. Host of the weekly retirement planning show on 740 KTRH. Twenty years advising pre-retirees and retirees on the tax, income, and legacy decisions that define a successful retirement.

## Why We Don't Write Multi-Year Roth Plans in Advance

Clients sometimes ask us to map out their entire seven-year Roth conversion plan up front and lock it in. We don't do that, and we're up front about why.

Tax laws change. Markets move. Your spending needs evolve. Your income changes. A conversion plan that was right last year can be wrong this year for reasons that have nothing to do with you. The point of equilibrium shifts. The thresholds shift. The market hands you opportunities (and pulls them away). A conversion plan written once and followed mechanically is a conversion plan that misses the lever it was designed to pull.

What we do instead is run the analysis every year. We look at the current tax landscape, your current account balances, your current spending, the current market environment, and the thresholds you'd cross at various conversion levels. We bring the trade-offs to the surface. Then you decide. The strategy stays the same. The tactics adjust.



## ABOUT OAK HARVEST FINANCIAL GROUP

Houston-based fiduciary registered investment advisor specializing in retirement planning for families with significant pre-tax retirement account balances. We serve clients across the country and currently manage approximately \$1.3 billion in assets. As a Registered Investment Advisor, we are legally required to act in our clients' best interest at all times.

READY TO RUN THE NUMBERS?

# Schedule Your Complimentary Tax Analysis Session

There's no cost, no obligation, and no sales pitch. We'll model your specific situation, identify the thresholds your conversion plan needs to navigate, and show you the trade-offs, so you can make a more intelligent decision anchored to what's most important to you.

**(281) 800-9127**

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