



# Should 401(k) millionaires consider a Roth conversion?

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**Strategic Roth conversions may help families manage future tax risks, boost after-tax retirement wealth, and create greater flexibility in their financial plans.**

## Key points

- Making pretax contributions during high-income years and Roth contributions or conversions during low-income years are strategies that may enhance after-tax growth potential.
- Building wealth in both Traditional and Roth retirement accounts can provide tax diversification, enabling flexibility to manage taxable income and potentially keep more income in lower tax brackets.
- Roth conversions may be especially relevant for families with large retirement balances, those anticipating higher tax rates later in retirement, or those seeking to hedge against possible future tax increases. To be included in 2025 taxable income, Roth conversions must be completed by year-end.
- As with all income tax management strategies, Roth conversions should be evaluated in the context of a comprehensive financial plan. Working with a financial advisor and tax advisor can help families develop an approach tailored to their specific goals and circumstances.

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## Introduction

A recent *Wall Street Journal* article notes that there is a growing number of US households passing the \$1 million mark in their 401(k) accounts, buoyed by a strong savings rate and impressive market gains.<sup>1</sup>

\$1 million doesn't buy as much as it used to, but it's still an impressive figure—and it may come with some significant tax consequences. In fact, some retirement experts refer to large retirement accounts as a "tax bomb," because they can carry a large embedded tax liability for retirees, particularly when Required Minimum Distributions (RMDs) begin, potentially pushing families into higher tax brackets and increasing their overall tax burden.

To understand the impact of this "tax bomb" and identify potential solutions, let's first review how retirement accounts work.

## Tax-deferred growth

Pretax contributions to Traditional IRA or 401(k) accounts may provide valuable tax savings during working years by helping families reduce the income subject to higher marginal income tax brackets. These contributions grow on a tax-deferred basis, allowing dividends, interest, and capital gains to compound without annual taxation.

Unfortunately, these tax benefits don't last forever. Withdrawals in retirement—including both original contributions and investment growth—are subject to ordinary income tax.

Tax-deferred accounts offer the greatest potential value when families benefit from "tax arbitrage," making pretax contributions during high-income years and taking taxable distributions at a lower tax rate during low-income years. While tax-deferred growth is also a tailwind, it's possible to have too much of a good thing.

## The "tax bomb" in retirement

As tax-deferred retirement balances grow, so does their future tax liability. Required Minimum Distributions (RMDs) must begin by 1 April of the year after turning age 73 for those born before 1960, and age 75 for those born in 1960 or later. The IRS requires retirees to take taxable distributions at an accelerating pace, starting at about 3.8%, rising to 5.0% by age 80 and 8.2% by age 90.<sup>2</sup>

For families that wait for RMDs to begin taking from their retirement accounts, this accelerating schedule can push them into higher and higher income tax brackets over time as both account balances and required distribution rates rise.

And the risk of higher taxes can be compounded by life events. For example, when one spouse passes away, the surviving spouse may be subject to higher tax rates as a Single filer—a phenomenon sometimes called the "widow's penalty." In addition, the SECURE Act's "10-year rule" for inherited IRAs requires most non-spouse beneficiaries to fully distribute inherited IRA assets within 10 years—often during their peak earning years—creating significant tax liabilities for heirs.

This lurking problem can be a major headwind for a portfolio's after-tax growth potential. When families take taxable distributions from their retirement accounts at a higher tax rate, it can shrink the "tax arbitrage," reducing or even undoing the benefits of tax-deferred savings.

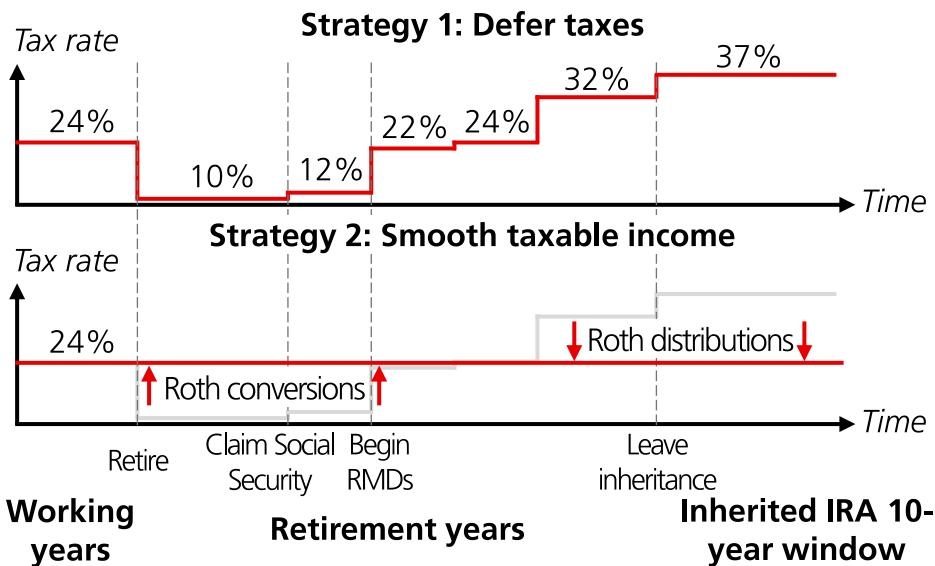
## Introducing Roth Conversions

Roth conversions are one strategy that may help families defuse their retirement account "tax bomb." Roth conversions work by moving a portion of a Traditional IRA or 401(k) into a Roth IRA or 401(k), with the family paying income tax on the converted amount in the current year.

While annual Roth *contributions* are limited, there is no cap on the amount of tax-deferred assets that may be *converted* to Roth accounts each year. Future growth and qualified withdrawals from the Roth account are generally income tax-free.<sup>3</sup>

Figure 1 - Strategic Roth conversions and Roth distributions may help to smooth income

Marginal income tax brackets over time for two retirement withdrawal strategies: Strategy 1 defers taxable withdrawals with an "RMD only" approach, leaving significant tax-deferred IRA assets and therefore large RMDs for heirs during the "10-year window." Strategy 2 aims to smooth taxable income, targeting the 24% marginal income tax rate each year, aiming to alleviate the family's tax burden.



Source: IRS, UBS. Hypothetical example, for illustrative purposes only.

## How to implement Roth Conversions

The timing of Roth conversions is important. Early retirement presents one window of opportunity, as the family's taxable income may be temporarily lower in the years before Social Security and RMDs begin.

A series of partial Roth conversions over several years may be more effective than a single large conversion. This approach allows families to spread the tax impact over multiple years, potentially taking advantage of lower tax brackets to help pull income out of higher tax brackets in future years.

Roth conversions may also help families manage the risk of rising income tax rates in the future. Higher taxes—particularly for high-income households—may be part of the eventual remedy for the US government's fiscal challenges.

The decision to convert depends on the family's current and anticipated future tax rates. Three possible scenarios may apply, relative to the current income tax rate:

- **Scenario 1: Future tax rate is expected to be lower.** A current-year Roth conversion may not be advantageous because the family expects to have an opportunity to do Roth conversions or take taxable distributions at lower tax rates in future years.
- **Scenario 2: Future tax rate is expected to be the same/similar.** A Roth conversion may not directly reduce expected taxes, but it may help to improve tax diversification and help protect against the risk of future tax increases.
- **Scenario 3: Future tax rate is expected to be higher.** Partial Roth conversions may help reduce the tax cost of retirement savings, especially if tax rates increase.

## Conclusion and next steps

When considering partial Roth conversions, it is important to evaluate and coordinate them alongside other sources of income, such as Social Security, pensions, and investment income. Careful planning can help families avoid unintended consequences, such as triggering higher Medicare premiums or the Net Investment Income Tax.

Working with a financial advisor and tax advisor can help ensure that conversion strategies are aligned with overall financial goals. Advisors can help families evaluate the trade-offs, model different scenarios, and determine the optimal timing and amount for Roth conversions.

Some studies suggest that small Roth conversions in early retirement may increase after-tax wealth by approximately 10-15%, boosted by lower income taxes on taxable distributions, reduced Medicare income-related monthly adjustment amounts (IRMAAs), and other tax credits/benefits that would have been phased out at higher levels of annual taxable income.<sup>4</sup>

## Further reading

If you are interested in learning more about Roth conversions and other strategies for managing income taxes in retirement, please refer to the CIO research team's report, [Modern retirement monthly: Managing taxes with a "spending waterfall,"](#) published 25 June 2025.

For information on other planning priorities as we approach the end of the year, please see the CIO Global Investment Management team's report, [Year-end priorities and a preview of 2026](#), published 25 September 2025.

## End notes

<sup>1</sup> Banerji, Gunjan (2025, December 8). *401(k)s Are Minting a Generation of 'Moderate Millionaires'*. The Wall Street Journal. <https://www.wsj.com/personal-finance/retirement/401k-millionaires-382f5c33>.

<sup>2</sup> Internal Revenue Service. (2024). Publication 590-B: Distributions from Individual Retirement Arrangements (IRAs). US Department of the Treasury. Retrieved December 8, 2025, from <https://www.irs.gov/publications/p590b>

<sup>3</sup> Families cannot withdraw earnings from Roth IRA accounts tax- and penalty-free until at least five years after their first Roth IRA contribution, and generally not before age 59½. The five-year period begins on January 1 of the tax year of the first contribution. Withdrawing earnings before meeting both the five-year rule and the age 59½ requirement may result in income taxes and a 10% early withdrawal penalty, unless an exception applies. The original Roth IRA contributions (but not earnings) can be withdrawn at any time, income tax- and penalty-free.

<sup>4</sup> Reichenstein, W. (2020). Optimizing Roth IRA conversions. *Journal of Financial Planning*, 33(2), 38–46. [https://www.financialplanningassociation.org/sites/default/files/2020-09/Feb2020\\_Research\\_Reichenstein.pdf](https://www.financialplanningassociation.org/sites/default/files/2020-09/Feb2020_Research_Reichenstein.pdf)

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