

Mindful Advisory Update

February 21, 2026

201-951-3509

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Dear Investor,

A Roth IRA conversion is among the popular tax strategies for some investors, including early retirees. That means converting part, or all, of a traditional IRA, 401(k), or 403(b), SEP-IRA, or Simple IRA (a non-Roth IRA) into a Roth IRA.

A Roth conversion isn't the right move for everyone, and investors should consult with tax professionals to make sure it's appropriate. But a main reason for doing a conversion is to mitigate against the possibility of taxes increasing. What follows is an attempt to explain the rationale more fully.

(Readers should note that Mindful Advisory, LLC is not an accounting or professional tax firm, and John Coumarios does not have a CPA designation. Readers should also pay attention to the disclaimers and disclosures at the end of this letter. This letter is intended to be educational and not tax advice for any client or prospect.)

What is a Roth conversion?

The conversion strategy is easier to understand if one remembers the purpose of investing a traditional IRA, 401(k), etc.... to begin with.

First, contributions to non-Roth retirement accounts frequently lower one's taxable income by the amount of the contributions. Second, investments in these accounts are protected from taxes on dividends, interest, and capital gains. Then, when distributions in retirement from non-Roth retirement accounts are taxed, the investor, usually no longer employed, can be in a lower tax bracket.

Lower your tax bill annually (in many, but not all, cases) with contributions when you're employed and in a relatively higher tax bracket, avoid taxes on dividends, interest, and gains along the way, and then make taxable distributions to yourself when you're retired and usually in a lower bracket - that's the rationale.

However, a Roth IRA functions a bit differently from non-Roth retirement accounts while also having one similarity. First, distributions from a Roth five years after the contribution is made, and if the investor is older than 59 ½ years old, aren't taxed generally (specific IRS



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rules regarding holding periods and age requirements apply). That's because the money contributed to a Roth doesn't enjoy an income reduction for tax purposes.

Second, a Roth isn't subject to required minimum distributions. An investor can keep money in a Roth for their entire life, and leave it to heirs.

Third, a Roth enjoys one similar tax advantage as a traditional IRA or 401(k) – dividends from stocks, interest income from bonds, and capital gains within the account aren't taxed.

Now that we have a handle on what the differences and similarities are between a Roth and other tax-advantaged accounts, we are better prepared to discuss Roth conversions.

A conversion from a traditional IRA, 401(k), or 403(b) to a Roth IRA means moving money from a non-Roth tax-advantaged account, where distributions are taxed and eventually required, into a Roth IRA where qualified distributions are neither taxed nor required provided they adhere to certain rules.

These rules include two 5-year rules (one already mentioned). One only allows tax-free and penalty-free withdrawals of contributions, but not earnings, after five years elapse for those younger than 59 ½ years old. The other imposes taxes and penalties on withdrawals of each conversion prior to five years elapsing for those younger than 59 ½ years old.

Investors should understand, however, that a conversion from a traditional IRA is a distribution from a traditional IRA, and will be taxed as such. That means doing a conversion while you're still employed, and in a higher tax bracket, may not be advantageous in many cases. Additionally, the tax paid on a conversion is non-refundable; if tax rates were to stay the same or decrease in the future, the investor may have paid taxes earlier than necessary.

Some investors still may choose to do a conversion before retirement if the stock market and the value of the account have dropped significantly so that there's less to convert. But investors have to weigh the value of paying the taxes on even a smaller conversion while they're still in a relatively high tax bracket. They also have to consider if a conversion will increase their taxable income enough to vault them into a higher tax bracket.

Otherwise, when people retire and stop earning income through employment, they often fall into a lower tax bracket. That means most people find early retirement a good time for doing a Roth conversion.

Taxes will be owed on the conversion – but generally at a lower rate than they would have been while the person was still working and presumably in a higher bracket. This is the assumption the strategy relies on.

That's also why a lot of strategies involve converting some traditional IRA money to a Roth incrementally (every year) so that no individual conversion (which counts as a taxable distribution from the non-Roth account or accounts) doesn't vault the investor into a higher tax bracket for a particular tax year.

The primary reason - mitigating against rising taxes

But why do a conversion and pay any taxes at all? If you enjoyed the tax deductions every year on the contributions along the way, you're going to pay taxes on distributions anyway. And if you're paying at a lower rate in retirement, it all may have wound up being a decent deal. Also, why not just wait until you're required to start taking distributions from non-Roth retirement accounts if you have any pensions or other accounts to tap for living in retirement?

That can be a reasonable approach. But what if taxes go up, and you're not in as low a tax bracket as you thought you'd be in at retirement?

Some of the provisions of the Tax Cuts and Jobs Act of 2017 (TCJA) were formally extended into law (119-21) on July 4, 2025, according to the [National Association of Counties](#), but tax laws are highly dynamic and the US has rising debt levels. It's possible a strategy to mitigate against future higher taxes may still be warranted. Tax laws can change.

And that's the primary reason for doing the conversion and paying the tax early in retirement when you're in a lower bracket -- to mitigate the risk of tax increases that may hit your future distributions from traditional IRAs, 401(k)s, etc.... harder than you expected when you're retired.

In other words, while the original rationale for contributing to a tax-deferred account, and then paying taxes on the distributions, was that the distributions would be taxed at a lower rate, that may not pan out.

Future tax rates are subject to legislative change and cannot be guaranteed, of course. Congress could also change the laws governing Roth IRAs as well. But some may want to follow the calculated strategy with some of their traditional IRA or 401(k) money that taxes will increase. That's what is implied in doing a Roth conversion.

Conversion candidates

The best candidates for this strategy have other money in taxable accounts that they can use to pay the taxes on the conversion. It's usually better not to convert traditional IRA money where there aren't other assets to tap to pay the taxes on the conversion.

If all you have is a traditional IRA or a 401(k), meaning you have to reserve some of the conversion to pay the taxes on the conversion, you may not be the ideal candidate. There's an argument that taking money from the conversion to pay for it defeats the purpose of it.

Conversions will cause an investor to incur a tax bill today and some loss of liquidity. They can still be worthwhile, but nobody should take them lightly, or do them without the guidance of a tax professional.

Conversions also may impact the Medicare Income-Related Monthly Adjustment Amount (IRMAA) or specific state and local tax consequences, which may vary by jurisdiction.

Our Dedication to Your Financial Plan: Don't predict, but be prepared

While it's good for investors to know about Roth conversions, investors generally shouldn't seek to alter their financial plans or asset allocations without careful consideration and consultation with a financial professional. The point of sharing my thoughts on markets and financial planning is to provide some education and encourage investors to maintain diversified portfolios and consider a variety of strategies.

In an uncertain world, it is important to focus on what we can control: managing costs, maintaining a well-diversified portfolio aligned with your long-term goals and risk tolerance, and avoiding reactive decisions based on short-term market noise.

Please do not hesitate to contact me if you have any questions or if there have been any changes in your financial situation, including to discuss how the topic of this letter may fit your specific Financial Plan."

Respectfully submitted,
John Coumarios
Mindful Advisory, LLC

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This letter contains 'forward-looking statements.' Due to various risks and uncertainties, actual events or results may differ materially from those reflected or contemplated in such forward-looking statements.

Specific risks of Roth conversions include, but are not limited to, tax liability in the year of conversion, potential for higher-than-expected tax brackets in the future, and 5-year rule complications imposing penalties on distributions prior to five years elapsing on conversions or earnings.

This material does not consider the impact of the Medicare Income-Related Monthly Adjustment Amount (IRMAA) or specific state and local tax consequences, which may vary by jurisdiction.

New Jersey residents should note that New Jersey's treatment of retirement income and Roth conversions may differ from federal treatment; residents should specifically review the NJ Gross Income Tax requirements.

"The decision to convert should be made in the context of your overall financial plan, taking into account liquidity needs and time horizon.

Future tax rates are subject to legislative change and cannot be guaranteed.

Clients executing Roth conversion, and paying taxes may lower Mindful Advisory's assets under management (AUM) and fees derived thereof. Therefore, the Firm may have a conflict of interest in recommending specific distribution strategies that decrease the amount of assets under the Firm's management. While the firm may lose fees, we prioritize the client's long-term financial interest in accordance with our fiduciary duty.

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