Expats Convert Traditional IRA to a Roth Tax-Free Using FEIE

Since the passage of FATCA in 2010, Americans have run into roadblocks against foreign banks in establishing retirement accounts. Americans living abroad can continue to contribute to their retirement in U.S. based accounts into IRA accounts. Brian Dunhill, an American financial advisor based in Europe, explains how U.S. expats can continue to contribute to an IRA account without facing the obstacles Americans are facing outside the U.S. in his article that can be read here.

However, Americans currently holding traditional IRA or 401k accounts in the U.S. can begin to move these accounts into a Roth IRA tax-free if they are eligible for the Foreign Earned Income Exclusion (FEIE). It is very simple! If the expat is utilizing the FEIE annually, the standard deduction amount (per the filing status) can be the total amount to be converted into the Roth IRA.

How does this work?

Sounds confusing but it is simple. If the expat earns below the maximum amount allowed for the FEIE ($104,100 is the limit for 2018) and no other (or minimal other income), then the adjusted gross income could be $0. And the standard deduction could be the limit for the IRA conversion to be not taxed. Let's illustrate:

Tax Return Description	**Tax Year 2018**	
	No IRA Conversion	With IRA Conversion
Foreign Earned Income	$80,000	$80,000
Stock Dividends	$100	$100
Traditional IRA convert to Roth IRA	$0	$11,000
Other-FEIE	($80,000)	($80,000)
Adjusted Gross Income	$100	$11,100
Less: Standard Deduction (Single)	($12,000)	($12,000)
Taxable Income	$0	$0
Tax	**$0**	**$0**
Penalty (under 59 1/2 years)	$0	$0

In the illustration, suppose that your salary earned in a foreign company was $80,000 and you earned about $100 from a U.S. brokerage account but you elected for the FEIE thus excluding your foreign salary. In both columns, the taxable income indicates as $0. However, the second column depicts a conversion of $11,000 from the Traditional IRA to a Roth IRA. With the standard deduction, the taxable income is $0. Or in other words, you were able to convert a Traditional IRA to a Roth IRA so that your retirement fund will continue but tax-free!

If you are a married couple filing jointly, the standard deduction is higher thus allowing each taxpayer to move their funds to a Roth IRA. See table below to determine your filing status.

Filing Status	Standard Deduction Amount
Single	$12,000
Married Filing Jointly	$24,000
Married Filing Separately	$12,000
Head of Household	$18,000

Why is this important?

Roth IRA can allow your funds grow without tax considerations at retirement time. However, the Traditional IRA is an account that is pre-tax so you do not pay tax on the funds until you have distributions extended to you. At that time, you will need to report the distributions as taxable income. Using this idea, you can move some of your funds pre-retirement tax-free.

Past 401k and IRA accounts

If you worked in the U.S. before moving abroad and have an opened 401k, or Traditional IRA, you may want to convert these into a Roth IRA but seek the advice of a financial advisor and a tax advisor, but the conversion would need to be accomplished before the end of the year.

If you have questions on this topic, contact us today at info@mirtaxes.com or call us.

Website: www.mirtaxes.com