INVESTMENT ARTICLE

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Recently Retired Or Changed Jobs? What You Need To Know About 401(k) Rollovers

By Robert E. Caplan, MBA, CFA

Major life changes, like retirement or landing a new job can be a big adjustment. Not to mention all the financial considerations that must be managed during these transitions. One major financial decision is whether or not to rollover your employer-sponsored retirement plan. If you decide to rollover your existing plan, there are things you should consider carefully before making a move.

Aside from cashing out the funds in your current plan (which we don't recommend due to potential tax liabilities) there are three rollover options available to you. Each option can provide you with continued potential tax-deferred growth opportunities. The first, if you've changed jobs, is to move the funds into your new employer's retirement plan. The second option is to rollover the money into an Individual Retirement Account (IRA). The third option is to deposit the funds in a Roth IRA.

Depending on your situation, there may be benefits to rolling your funds over to a Roth IRA from a 401(k). Any earnings on after-tax money in a traditional 401(k) are taxed when withdrawn. Earnings in Roth IRAs generally aren't, so you may be able to avoid taxes. In addition, there are no minimum required distributions (MRD) from a Roth IRA during your lifetime.

Other IRA accounts require that you begin withdrawing funds once you reach age 70½.

If you are concerned that your retirement savings are at risk from creditors or possible lawsuits, there is the consideration of what level of creditor protection your selected retirement account provides. Not all retirement accounts offer the same level of protection. Workplace retirement plans and IRAs generally shield your assets in bankruptcy proceedings, but workplace plans generally provide broader protection from other legal claims. Be sure to consult an attorney if legally protecting your assets is a concern.

There are some important questions you need to ask when deciding which is your best option:

What are your investment choices?

Investment options within employer-sponsored retirement plans are typically limited to a selection of mutual funds, exchange-traded funds, individual stocks and bonds. Generally speaking, compared with employer-sponsored retirement accounts, IRAs offer a broader choice of investments. Make sure that the type of account you choose to roll funds over to meets your requirements and offers an array of investment options best suited for your investment needs.

How much will you pay in fees and expenses?

Any retirement account has costs for the investor. These may include administrative fees, management expenses and transaction fees for trades or other account activity. According to a study by the Center for American Progress, the typical 401(k) plan charges 1% of assets managed, but fees vary greatly and can have a significant impact on long-term returns.

What investment guidance and services are available?

As an investor how much financial guidance and service do you require? Does the account you're thinking about offer online tools and services? Many investors prefer to be able to consult directly with a financial advisor that is devoted solely to structuring investment choices based on an individual client, rather than a broad group of employees.

When do you anticipate needing the money?

Each option has different rules for withdrawals, so you need to think about funds you will need in the future. Keeping your investments with your past employer can pose challenges if those plans have restrictions on the frequency or type of withdrawals that former employees can make. The flip side of needing to make withdrawals is age and employment based retirement account withdrawal requirements.

Some employer plans do not require distributions while you are still working. So if you plan to continue working after age 70 ½, you might consider a rollover to your new employer's plan. If you anticipate leaving funds as a legacy, then rolling it into an IRA account or converting to a Roth IRA, will eliminate the tax liability for those who inherit. Consult with your tax adviser to understand the tax implication of these options.

Avoid these rollover mistakes

A common 401(k) rollover mistake is not following the "same property rule." This rule means that you can't take cash distribution from your 401(k), purchase other investments, and then rollover those same funds into a new IRA. The IRS would treat the cash distribution as taxable income, even though the final destination was an IRA account.

Don't miss the 60 day deadline The IRS gives you 60 days to complete your 401(k) rollover to another IRA or qualified plan. If you fail to complete the rollover within that time, the funds will be treated as ordinary income when it comes to tax time.

Follow the one year waiting rule

You may only roll over funds from one 401(k) to another one time per year. This year long period begins when you receive the distribution of your funds.

Keep in mind that this one year rule applies separately to each IRA account. The limit does not apply to transfers from traditional IRAs to Roth IRAs.

The financial advisors at River Wealth Advisors are well-versed in 401(k) options and helping you with your retirement planning.

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