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Changing Jobs? Know Your 401(k) Options

If you've lost your job, or are changing jobs, you may be wondering what to do with your 401(k) plan account. It's important to understand your options.

What will I be entitled to?

If you leave your job (voluntarily or involuntarily), you'll be entitled to a distribution of your vested balance. Your vested balance always includes your own contributions (pre-tax, after-tax, and Roth) and typically any investment earnings on those amounts. It also includes employer contributions (and earnings) that have satisfied your plan's vesting schedule.

In general, you must be 100% vested in your employer's contributions after 3 years of service ("cliff vesting"), or you must vest gradually, 20% per year until you're fully vested after 6 years ("graded vesting"). Plans can have faster vesting schedules, and some even have 100% immediate vesting. You'll also be 100% vested once you've reached your plan's normal retirement age.

It's important for you to understand how your particular plan's vesting schedule works, because you'll forfeit any employer contributions that haven't vested by the time you leave your job. Your summary plan description (SPD) will spell out how the vesting schedule for your particular plan works. If you don't have one, ask your plan administrator for it. If you're on the cusp of vesting, it may make sense to wait a bit before leaving, if you have that luxury.

Don't spend it

While this pool of dollars may look attractive, don't spend it unless you absolutely need to. If you take a distribution you'll be taxed, at ordinary income tax rates, on the entire value of your account except for any after-tax or Roth 401(k) contributions you've made. And, if you're not yet age 55, an additional 10% penalty may apply to the taxable portion of your payout. (Special rules may apply if you receive a lump-sum distribution and you were born before 1936, or if the lump-sum includes employer stock.)

If your vested balance is more than $5,000, you can leave your money in your employer's plan at least until you reach the plan's normal retirement age (typically age 65). But your employer must also allow you to make a direct rollover to an IRA or to another employer's 401(k) plan. As the name suggests, in a direct rollover the money passes directly from your 401(k) plan account to the IRA or other plan. This is preferable to a "60-day rollover," where you get the check and then roll the money over yourself, because your employer has to withhold 20% of the taxable portion of a 60-day rollover. You can still roll over the entire amount of your distribution, but you'll need to come up with the 20% that's been withheld until you recapture that amount when you file your income tax return.

Should I roll over to my new employer's 401(k) plan or to an IRA?

Assuming both options are available to you, there's no right or wrong answer to this question. There are strong arguments to be made on both sides. You need to weigh all of the factors, and make a decision based on your own needs and priorities. It's best to have a professional assist you with this, since the decision you make may have significant consequences — both now and in the future.

Reasons to consider rolling over to an IRA:

- You generally have more investment choices with an IRA than with an employer's 401(k) plan. You typically may freely move your money around to the various investments offered by your IRA trustee, and you may divide up your balance among as many of those investments as you want. By contrast, employer-sponsored plans generally offer a limited menu of investments (usually mutual funds) from which to choose.
- You can freely allocate your IRA dollars among different IRA trustees/custodians. There's no limit on how many direct, trustee-to-trustee IRA transfers you can do in a year. This gives you flexibility to change trustees often if you are dissatisfied with investment performance or

In some cases, you have no choice — you need to use the funds. If so, try to minimize the tax impact. For example, if you have nontaxable after-tax contributions in your account, keep in mind that you can roll over just the taxable portion of your distribution and keep the nontaxable portion for yourself.

customer service. It can also allow you to have IRA accounts with more than one institution for added diversification. With an employer's plan, you can't move the funds to a different trustee unless you leave your job and roll over the funds.

- An IRA may give you more flexibility with distributions. Your distribution options in a 401(k) plan depend on the terms of that particular plan, and your options may be limited. However, with an IRA, the timing and amount of distributions is generally at your discretion (until you reach age 72 and must start taking required minimum distributions in the case of a traditional IRA).
- You can roll over (essentially "convert") your 401(k) plan distribution to a Roth IRA. You'll generally have to pay taxes on the amount you roll over (minus any after-tax contributions you've made), but any qualified distributions from the Roth IRA in the future will be tax free.

Reasons to consider rolling over to your new employer's 401(k) plan (or stay in your current plan):

- Many employer-sponsored plans have loan provisions. If you roll over your retirement funds to a new employer's plan that permits loans, you may be able to borrow up to 50% of the amount you roll over if you need the money. You can't borrow from an IRA — you can only access the money in an IRA by taking a distribution, which may be subject to income tax and penalties. (You can give yourself a short-term loan from an IRA by taking a distribution, and then rolling the dollars back to an IRA within 60 days; however, this move is permitted only once in any 12-month time period.)
- Employer retirement plans generally provide greater creditor protection than IRAs. Most 401(k) plans receive unlimited protection from your creditors under federal law. Your creditors (with certain exceptions) cannot attach your plan funds to satisfy any of your debts and obligations, regardless of whether you've declared bankruptcy. In contrast, any amounts you roll over to a traditional or Roth IRA are generally protected under federal law only if you declare bankruptcy.

  Any creditor protection your IRA may receive in cases outside of bankruptcy will generally depend on the laws of your particular state. If you are concerned about asset protection, be sure to seek the assistance of a qualified professional.
- You may be able to postpone required minimum distributions. For traditional IRAs, these distributions must begin by April 1 following the year you reach age 72.[1] However, if you work past that age and are still participating in your employer's 401(k) plan, you can delay your first distribution from that plan until April 1 following the year of your retirement. (You also must own no more than 5% of the company.)
- If your distribution includes Roth 401(k) contributions and earnings, you can roll those amounts over to either a Roth IRA or your new employer's Roth 401(k) plan (if it accepts rollovers). If you roll the funds over to a Roth IRA, the Roth IRA holding period will determine when you can begin receiving tax-free qualified distributions from the IRA. So if you're establishing a Roth IRA for the first time, your Roth 401(k) dollars will be subject to a brand new five-year holding period. On the other hand, if you roll the dollars over to your new employer's Roth 401 (k) plan, your existing five-year holding period will carry over to the new plan. This may enable you to receive tax-free qualified distributions sooner.

When evaluating whether to initiate a rollover always be sure to (1) ask about possible surrender charges that may be imposed by your employer plan, or new surrender charges that your IRA may impose, (2) compare investment fees and expenses charged by your IRA (and investment funds) with those charged by your employer plan (if any), and (3) understand any accumulated rights or guarantees that you may be giving up by transferring funds out of your employer plan.

What about outstanding plan loans?

In general, if you have an outstanding plan loan, you'll need to pay it back, or the outstanding balance will be taxed as if it had been distributed to you in cash. If you can't pay the loan back before you leave, you'll still have 60 days to roll over the amount that's been treated as a distribution to your IRA. Of course, you'll need to come up with the dollars from other sources.

[1] If you reach age 72 before July 1, 2021, you will need to take an RMD by December 31, 2021.

Retirement Account Rollovers

When evaluating whether to initiate a rollover always be sure to (1) ask about possible surrender charges that may be imposed by your employer plan, or new surrender charges that your IRA may impose, (2) compare investment fees and expenses charged by your IRA (and investment funds) with those charged by your employer plan (if any), and (3) understand any accumulated rights or guarantees that you may be giving up by transferring funds out of your employer plan.

****SEP and SIMPLE IRAs are not included in or subject to this limit and are fully protected under federal law if you declare bankruptcy.***

A rollover is the movement of funds from one retirement savings vehicle to another. You may want to make a rollover for any number of reasons — your employment situation has changed, you want to switch investments, or you've received death benefits from your spouse's retirement plan.

There are two possible ways that retirement funds can be rolled over — the indirect (60-day) rollover and the direct rollover (or trustee-to-trustee transfer).

The indirect, or 60-day, rollover

With this method, you actually receive a distribution from your retirement plan and then, to complete the transaction, you deposit the funds into the new retirement plan account or IRA. You can make a rollover at any age, but there are specific rules that must be followed. Most importantly, you must generally complete the rollover within 60 days of the date the funds are paid from the distributing plan.

If properly completed, rollovers aren't subject to income tax. But if you fail to complete the rollover or miss the 60-day deadline, all or part of your distribution may be taxed, and subject to a 10% early distribution penalty (unless you're age 59½ or another exception applies).

Further, if you receive a distribution from an employer retirement plan, your employer must withhold 20% of the payment for taxes. This means that if you want to roll over the *entire* distribution amount (and avoid taxes and possible penalties on the amount withheld), you'll need to come up with that extra 20% from other funds. You'll be able to recover the withheld amount when you file your tax return.

The direct rollover, or trustee-to-trustee transfer

The second type of rollover transaction occurs directly between the trustee or custodian of your old retirement plan, and the trustee or custodian of your new plan or IRA. You never actually receive the funds or have control of them, so a trustee-to-trustee transfer is not treated as a distribution. Direct rollovers avoid both the danger of missing the 60-day deadline and the 20% withholding problem.

If you stand to receive a distribution from your employer's plan that's eligible for rollover, your employer must give you the option of making a direct rollover to another employer plan or IRA.

A trustee-to-trustee transfer is generally the most efficient way to move retirement funds. Taking a distribution yourself and rolling it over may make sense only if you need to use the funds temporarily, and are certain you can roll over the full amount within 60 days.

Should you consider a rollover?

In general, if your vested balance is more than $5,000, you can keep your money in an employer's plan at least until you reach the plan's normal retirement age (typically age 65). But if you terminate employment before then, should you consider a rollover to either an IRA or a new employer's plan? There are pros and cons to each move.

IRA: In contrast to an employer plan, where investment options are typically limited to those selected by the employer, the universe of IRA investments is almost unlimited. Similarly, the distribution options in an IRA (especially for your beneficiary following your death) may be more flexible than the options available in your employer's plan.

New employer's plan: On the other hand, employer-sponsored plans may offer better creditor protection. In general, federal law protects IRA assets up to $1,362,800 (scheduled to increase on April 1, 2022) — plus any amount rolled over from a qualified employer plan or 403(b) plan — if bankruptcy is declared.* (The laws in your state may provide additional protection.) In contrast, assets in a qualified employer plan or 403(b) plan generally receive unlimited protection from creditors under federal law, regardless of whether bankruptcy is declared.

Use this rollover guide to help you decide where you can move your retirement dollars. A financial professional can also help you navigate the rollover waters. Keep in mind that employer plans are not legally required to accept rollovers. Review your plan document.

Some distributions can't be rolled over, including:

- ***Required minimum distributions***
- ***Certain annuity or installment payments***
- ***Hardship withdrawals***
- ***Corrective distributions of excess contributions and deferrals***

In addition to rolling over the assets to an IRA or new employer's plan, or leaving the money in your current employer plan, you may also choose to take a lump-sum cash distribution. However, keep in mind that the distribution will be subject to income taxes and, if you're younger than 59½, a 10% penalty tax, unless an exception applies.

Rollover from:	Rollover to: Traditional/ SEP-IRA	SIMPLE IRA	Roth IRA	Qualitfied Plan (incl. 401(k))	Roth 401(k)/ 403(b)/457(b) Account	403(b) Plan	Governmental 457(b) Plan
Traditional/SEP-IRA - taxable dollars [1]	**Yes [2]**	**Yes [2,5]**	**Yes [3]**	**Yes [7]**	**No**	**Yes**	**Yes [9]**
Traditional IRA - nontaxable dollars [1]	**Yes [2]**	**Yes [2,5]**	**Yes [4]**	**No**	**No**	**No**	**No**
SIMPLE IRA [1]	**Yes [5]**	**Yes [2]**	**Yes [3, 5]**	**Yes [5, 7]**	**No**	**Yes [5]**	**Yes [5, 9]**
Roth IRA [1]	**No**	**No**	**Yes [2]**	**No**	**No**	**No**	**No**
Qualified Plan - taxable dollars (incl. 401(k)) [6, 7]	**Yes**	**Yes [5]**	**Yes [11]**	**Yes**	**No [12]**	**Yes**	**Yes [9]**
Qualified Plan - nontaxable dollars (incl. 401(k)) [6, 7]	**Yes**	**Yes [5]**	**Yes**	**Yes [8]**	**No [12]**	**Yes [8]**	**No**
Roth 401(k) Account [6, 7]	**No**	**No**	**Yes**	**No**	**Yes [10]**	**No**	**No**
Roth 403(b)/457(b) Account [6]	**No**	**No**	**Yes**	**No**	**Yes [10]**	**No**	**No**
403(b) Plan - taxable dollars [6]	**Yes**	**Yes [5]**	**Yes [11]**	**Yes [7]**	**No [12]**	**Yes**	**Yes [9]**
403(b) Plan - nontaxable dollars [6]	**Yes**	**Yes [5]**	**Yes**	**Yes [8]**	**No [12]**	**Yes [8]**	**No**
Governmental 457(b) Plan [6]	**Yes**	**Yes [5]**	**Yes [11]**	**Yes [7]**	**No [12]**	**Yes**	**Yes**

1 Required distributions and nonspousal death benefits can't be rolled over.

2 In general, you can make only one tax-free, 60-day, rollover from one IRA to another IRA in any 12-month period no matter how many IRAs (traditional, Roth, SEP, and SIMPLE) you own. This does not apply to direct (trustee-to-trustee) transfers, or Roth IRA conversions.

3 Taxable conversion

4 Nontaxable conversion

5 Only after employee has participated in SIMPLE IRA plan for two years.

6 Required distributions, certain periodic payments, hardship distributions, corrective distributions, and certain other payments cannot be rolled over; nonspousal death benefits can be rolled over only to an inherited IRA, and only in a direct rollover.

7 May result in loss of qualified plan lump-sum averaging and capital gain treatment.

8 Direct (trustee-to-trustee) rollover only; receiving plan must separately account for the after-tax contributions and earnings.

9 457(b) plan must separately account for rollover — 10% penalty on payout may apply.

10 Nontaxable dollars may be transferred only in a direct (trustee-to-trustee) rollover.

11 Taxable dollars included in income in the year rolled over.

12 401(k), 403(b), and 457(b) plans can also allow participants to directly transfer non-Roth funds to a Roth account if certain requirements are met (taxable conversion).

Six Steps to Consider Before Tapping Your Retirement Savings Plan

You've worked long and hard for years, saving diligently through your employer-sponsored retirement savings plan. Now, with retirement on the horizon, it's time to begin thinking about how to tap your plan assets for income. But hold on, not so fast. You may need to take a few steps first.

Step 1: Evaluate your needs

The first step in any retirement income plan is to estimate how much income you'll need to meet your desired lifestyle. The conventional guidance is to plan on needing anywhere from 70% to 100% of your pre-retirement income each year during retirement; however, your amount will depend on your unique circumstances. While some expenses may fall in retirement, others may rise. So before even thinking about how to tap your plan assets, you should have a concrete idea of how much you'll need to (1) cover your basic needs and (2) live comfortably, according to your wishes.

First, estimate your non-negotiable fixed needs — such as housing, food, and medical care. This will help you project how much you'll need just to make ends meet. Then focus on your variable wants — including travel, leisure, and entertainment. This is the area that you'll have the easiest time adjusting, if necessary, as you refine your income plan.

Step 2: Assess your sources of predictable income

Next, you'll want to determine how much to expect from sources of predictable income, such as Social Security and traditional pension plans. These could be considered the foundation of your retirement income.

Social Security

A key decision regarding Social Security is when to claim benefits. Although you can begin receiving benefits as early as age 62, the longer you wait to begin (up to age 70), the more you'll receive each month.

The Social Security Administration (SSA) calculates your retirement benefit using a formula that takes into account your 35 highest earning years, so if you had some years of no or low earnings, your benefit amount may be lower than if you had worked steadily.

You can estimate your retirement benefit by using the calculators on the SSA website, ssa.gov. You can also sign up for a *my* Social Security account so that you can view your Social Security Statement online. Your statement contains a detailed record of your earnings, as well as estimates of retirement, survivor, and disability benefits, along with other information about Social Security.

Pensions

Traditional pensions have been disappearing from employer benefit programs over the past couple of decades. If you're one of the lucky workers who stand to receive a pension benefit, congratulations! But be aware of your pension's features. For example, will your benefit remain steady throughout retirement or increase with inflation?

Your pension will most likely be offered as either a single or joint and survivor annuity. A single annuity provides benefits until the worker's death, while a joint and survivor annuity generally provides reduced benefits until the survivor's death.[1]

Step 3: Reflect

If it looks as though your Social Security and pension income will be enough to cover your fixed needs, you may be well positioned to use your retirement savings plan assets to fund the extra wants. On the other hand, if those sources are not sufficient to cover your fixed needs, you'll need to think carefully about how to tap your retirement savings plan assets, as they will be a necessary component of your income.

Step 4: Understand your plan options

Upon leaving your employer, you typically have four options:

Keep in mind that taxable distributions from employer-sponsored plans and IRAs prior to age 59½ may be subject to a 10% penalty tax, unless an exception applies.

Qualified withdrawals from Roth 401(k) accounts are those made after a five-year holding period and in one of the following circumstances: the participant has reached age 59½, becomes disabled, or dies.

1. Plans may allow you to leave the money alone or may require that you begin taking distributions once you reach the plan's normal retirement age.
2. You may choose to withdraw the money, either as a lump sum or a series of substantially equal periodic payments for the rest of your life, or you might use other withdrawal options offered by your plan. In its 63rd Annual Survey of Profit-Sharing and 401(k) Plans, the Plan Sponsor Council of America (PSCA) found that other options included installment payments (offered in 55% of plans) and periodic/partial withdrawals (54.5%).
3. You may roll the money into an IRA. You'll want to carefully compare the investment options, fees, and expenses of both your current plan and the IRA before making any rollover decision.
4. If you continue to work during your retirement years, you may be able to roll the money into your new employer's plan, if that plan allows. Again, be sure to compare plans before making any decisions.

If, after assessing your anticipated Social Security and pension benefits, you discover they will not be enough to meet your basic needs, one option may be to use a portion of your retirement plan assets to create another source of predictable income using an annuity.

An annuity is an insurance contract designed to provide steady income over a set period of time or over either your lifetime or that of you and your spouse. According to the PSCA, just 17.2% of retirement plans in their survey offered an annuity. If your plan is not one of them, you may want to consider rolling at least some of your tax-deferred money into an IRA and purchasing an immediate fixed annuity. As noted above, however, you'll want to carefully compare fees and expenses associated with all options before making any final decisions. (Legislation passed in late 2019 has made it easier for employers to offer annuities as an option. This may result in an increase in the percentage of employers offering them.)[2]

Step 5: Compare tax deferred and tax-free

If you have both tax-deferred and Roth accounts, consider that the taxable portion of distributions from tax-deferred accounts will be taxed at your current income tax rate, while qualified withdrawals from Roth accounts are tax-free. For this reason, general guidelines often suggest tapping tax-deferred accounts before Roth accounts to allow those accounts to continue potentially growing free of taxes.

Note that all assets in employer-sponsored retirement savings plans — even money held in Roth accounts — will be subject to required minimum distributions (RMDs). These rules state that minimum distributions generally must begin once you turn age 72; however, you may delay your first distribution up to April 1 of the following year.[3]

Roth IRAs, however, are not subject to RMD rules until after your death. This is just one reason you might consider converting your employer-sponsored retirement assets to a Roth IRA. Keep in mind that a conversion will trigger an immediate tax consequence on the taxable portion of the converted assets, which can result in a hefty bill from Uncle Sam.

Step 6: Seek professional assistance

Determining the appropriate way to tap your assets can be challenging and should take into account a number of factors. These include not only your tax situation, but also whether you have other assets you'll use for income, your overall health, and your estate plan. A financial professional can help make sense of your options in light of your unique situation.

[1] Current federal law requires employer-sponsored plan participants to select a joint and survivor annuity unless the spouse waives those rights. This requirement is not mandated in an IRA, however.

[2] Generally, annuity contracts have fees and expenses, limitations, exclusions, holding periods, termination provisions, and terms for keeping the annuity in force. Most annuities have surrender charges that are assessed if the contract owner surrenders the annuity in the early years of the contract. Qualified annuities are typically purchased with pre-tax money, so withdrawals are fully taxed as ordinary income. Withdrawals prior to age 59½ may be subject to a 10% federal income tax penalty. Any guarantees are contingent on the financial strength and claims-paying ability of the issuing insurance company. It is important to understand that purchasing an annuity in an IRA or an employer-sponsored retirement plan provides no additional tax benefits other than those available through the tax-deferred retirement plan.

[3] The Setting Every Community Up for Retirement Enhancement (SECURE) Act passed in late 2019 raised the RMD age from 70½ to 72, effective January 1, 2020. Anyone who turns 72 before July 1, 2021, (and therefore reached age 70½ before 2020), will need to take an RMD by December 31, 2021.