

BREAKAWAY
WEALTH MANAGEMENT

401(K) ROLLOVER SERVICES TO CONSIDER

When people are leaving their employer, one of the decisions they need to make is what to do with their 401(k). Here, we will examine each 401(k) option.



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A retirement plan participant typically has four options (and may engage in a combination of these options), each choice offering advantages and disadvantages.

1 Leave The 401(k) in The Former Employer's Plan

If permitted by the retirement plan, a former employee can choose to leave their 401(k) in the plan when they terminate employment. The HR department or retirement plan administrator is a good place to start to see if this option is available. Why would an employee choose this option?

- The new employer may have a waiting period before enrollment and the employee intends to roll over the assets to the new employer's plan.
- The old 401(k) plan has investing options more aligned with the employee's investing strategy.

2 401(k) Portability

Rolling your 401(k) into another employer's plan is possible if the new plan accepts rollovers from another 401(k) plan. This option may make it easier for you to track the performance of your assets, but be sure to evaluate your new employer's plan by examining the investment choices and fees first.

Also, there may be stipulations in the new plan, such as waiting to rollover your 401(k) from your old employer's plan until the next enrollment period, or after you've been employed at your new employer for a set period of time. Contact your HR department for clarification if you intend to rollover your 401(k).

Ownership- In a qualified retirement plan, you are the participant and not the owner, and the plan administrator determines your distribution options in moving your 401(k) assets to another 401(k).



3 Rollover Your 401(k) Assets Into An IRA

You have a few options with a direct rollover:

401(k) into an IRA- You can rollover your 401(k) into your existing IRA, or open a new IRA and initiate transfer paperwork with the help of your former retirement plan administrator or HR department and your financial professional. Usually, the transfer will be electronic, but if you receive a check from the 401(k) plan's custodian, contact your new 401(k) plan custodian or administrator for guidance before thirty days from the date of the check draft or the IRS may consider it an early distribution which is subject to taxes and if applicable the 10% penalty if you're younger than age 59 1/2.

401(k) Roth into a Roth IRA- You can roll your 401(k) Roth into an existing Roth IRA or open a new one. No taxes are due when the money is moved and any new earnings accumulate tax deferred. Earnings are eligible for tax-free withdrawal once the IRA has been open for at least five years and you are at least 59 1/2.

401(k) into a Roth IRA- If your 401(k) plan permits rollovers into a Roth IRA, you can initiate the rollover into your Roth IRA or open a new one. Be aware that you will need to pay taxes on this type of rollover transfer, so it's essential you consult your tax professional prior to converting your 401(k) to a Roth IRA. In addition, if you are required to take a required minimum distribution (RMD) in the year you convert, you must do so before converting to a Roth IRA.

Earnings on the Roth IRA that accumulate after the rollover will be eligible for tax-free withdrawal when the IRA into which your assets are moved has been open for at least five years and you are at least 59½.¹

Why would one consider a 401(k) rollover?

Investment choices- An IRA may offer more investment choices than a 401(k), and you may want to consider a roll-over of part or all of it into an annuity.

Control- You and your financial professional can manage all of your investments in one place. Working with a financial professional enables you with the flexibility to change your retirement portfolio holdings as your situation or the market changes.



Is there another rollover option?

In-service 401(k) distributions- An in-service 401(k) distribution is a rollover into another type of retirement savings vehicle that you initiate while still employed and contributing to your 401(k) plan. Typically, the retirement plan document the employer has in place with the plan administrator, often an HR company or custodian, states if in-service 401(k) distributions are allowable and what amount can be distributed over a set period.

In the case of an in-service 401(k) distribution, the distribution must be made into an IRA or an annuity to avoid paying taxes or a Roth IRA which would be a taxable event. Still, a distribution into a Roth IRA is Age 59 1/2 is the earliest age the law allows for a retirement plan participant to take a 401(k) in-service distribution from their contributions and qualified matching contributions from their employer. However, many retirement plans allow younger employees to exercise an in-service 401(k) distribution if stated in the retirement plan document. Other items to note:

- The event is not taxable, nor is the 10% early withdrawal penalty applicable if it distributes into an IRA or an annuity.
- After the in-service distribution, the employee can still contribute to their 401(k) retirement savings account.

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Cash Out The 401(k)

Cashing out a 401(k) becomes a taxable event since both the contributions and accumulation are taxable, regardless of the employee's age. Also, if the employee is younger than age 59 1/2, they will pay a 10% penalty. The IRS allows penalty-free withdrawals from retirement accounts after age 59 1/2 and requires withdrawals after age 73 (these are called Required Minimum Distributions, or RMDs).ⁱⁱ There are some exceptions to these rules for 401ks and other qualified plans, so it's essential you consult your plan administrator.

Important Disclosures

The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual security. To determine which investment(s) may be appropriate for you, consult your financial professional prior to investing.

All information is believed to be from reliable sources; however LPL Financial makes no representation as to its completeness or accuracy.

This information is not intended to be a substitute for specific individualized tax advice. We suggest that you discuss your specific tax issues with a qualified tax advisor.

Contributions to a traditional IRA may be tax deductible in the contribution year, with current income tax due at withdrawal. Withdrawals prior to age 59 1/2 may result in a 10% IRS penalty tax in addition to current income tax.

The Roth IRA offers tax deferral on any earnings in the account. Withdrawals from the account may be tax free, as long as they are considered qualified. Limitations and restrictions may apply. Withdrawals prior to age 59 1/2 or prior to the account being opened for 5 years, whichever is later, may result in a 10% IRS penalty tax. Future tax laws can change at any time and may impact the benefits of Roth IRAs. Their tax treatment may change.

Annuities are long-term investment vehicles designed for retirement purposes. Gains from tax-deferred investments are taxable as ordinary income upon withdrawal. Withdrawals made prior to age 59 1/2 are subject to a 10% IRS penalty tax and surrender charges may apply.

Sources

- ⁱ Must-Know Rules for Converting Your 401(k) to a Roth IRA
- ⁱⁱ IRS reminds those aged 73 and older to make required withdrawals from IRAs and retirement plans by Dec. 31; notes changes in the law for 2023 | Internal Revenue Service

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