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Considerations for an old retirement savings account

Here are 4 options for a retirement savings plan with a former employer.

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Key takeaways

- 4 options for an old workplace savings plan: Keep it with your old employer's plan, roll over the money into an IRA, roll over into a new employer's plan (including plans for self-employed and small businesses), or cash out.
- Make an informed decision: Find out your workplace savings plan rules, compare fees and expenses, and consider any potential tax impact.

Changing or leaving a job can be an emotional time. You're probably excited about a new opportunity—and nervous too. And if you're retiring, the same can be said. As you say goodbye to your workplace, don’t forget about your workplace retirement savings plan with that employer, such as a 401(k), 403(b) or 457(b). You have several options and it’s an important decision.

Because your 401(k) may be a big chunk of your retirement savings, it's important to weigh the pros and cons of your options and find the one that makes sense for you.

Here are 4 choices to consider.

1. Leave your money in your former employer's plan

Most companies—but not all—allow you to keep your retirement savings in their plans after you leave.

Some benefits:

- Your money has the chance to continue to grow tax-deferred.
- You can take penalty-free withdrawals if you left your former job at age 55 or older. [1]
- Many offer institutionally priced (i.e., lower-cost) or unique investment options.
- Federal law provides broad protection against creditors.

But:

- If you have up to $1,000 in the plan, the money may be automatically sent to you. If you have up to $7,000 in the plan, the money may be sent to an IRA for you, which you would then need to invest.
- If you choose to keep the money in your former employer's plan, you won't be able to add any more money to the account, or, in most cases, take a loan from the account.
- Withdrawal options may be limited. For instance, you may not be able to take a partial withdrawal; you may have to take the entire balance.
- Some plans may charge a fee to keep your money in the plan.

After you reach age 73, you'll have to take annual required minimum distributions (RMDs). For those born on or after January 1, 1960, RMDs will start at age 75.

If you hold appreciated company stock in your workplace savings account, consider the potential impact of net unrealized appreciation (NUA) before choosing between staying in the plan, taking the stock in kind, or rolling over the stock to an IRA. Rolling over the stock to an IRA will eliminate any NUA.

2. Roll over the money into an IRA

A Rollover IRA is a retirement account that allows you to move money from your former employer-sponsored retirement plan into an IRA.

You can open the IRA with a financial institution. Make sure to research fees and expenses when choosing an IRA provider, though, as they can really vary.

Some benefits:

- Your money has the chance to continue to grow tax-deferred.
- If you're under age 59½, you can withdraw money penalty-free for a qualifying first-time home purchase or higher education expenses.[2]
- You may be able to get a broader range of investment choices than what is available in an employer's plan.
- Rolling over assets can be done by source type. This means you can roll over Roth assets independently to a Roth IRA.
- If you're self-employed or run a small business, you can move your money into a retirement account designed for you—a self-employed 401(k), SEP IRA, or SIMPLE IRA.

But:

- After you reach age 73, unless you were born in or after 1960, you'll have to take annual required minimum distributions (RMDs) from a traditional IRA every year, even if you're still working.
- Federal law offers more protection for money in workplace retirement savings plans than in IRAs. However, some states offer certain creditor protection for IRAs too.

3. Move your money to your new (or current) employer's plan

Not all employers will accept a rollover from a previous employer's plan, so check with your new employer before making any decisions.

Some benefits:

- Your money has the chance to continue to grow tax-deferred.
- Consolidating money into one account can make it easier to manage your retirement savings.
- Many plans offer lower-cost (institutionally priced) plan-specific investment options.
- Federal law provides broad protection against creditors. You may be allowed to defer RMDs even if you're still working after age 73.[3]
- You can take penalty-free withdrawals if you leave your job with the new employer at age 55 or older.[1]
- If you're self-employed or run a small business, you can move your money into a retirement account designed for you—a self-employed 401(k), SEP IRA, or SIMPLE IRA.

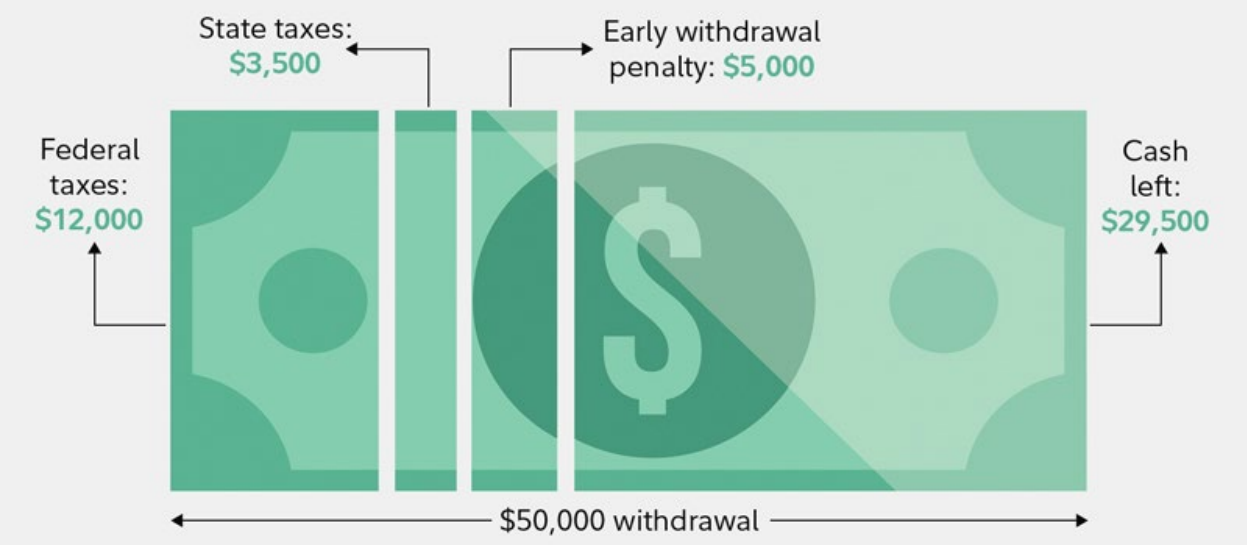
But:

- Make sure to understand your new plan rules.
- Consider the range of investment options available in the new plan.

4. Cash out

Taking the money out of retirement accounts altogether should be avoided unless the immediate need for cash is critical and you have no other options. The consequences vary depending on your age and tax situation. If you withdraw before age 59½, the money will generally be subject to both ordinary income taxes and a potential 10% early withdrawal penalty. (An early withdrawal penalty doesn't apply if you stopped working for your former employer in or after the year you reached age 55, but are not yet age 59½. This exception doesn't apply to assets rolled over to an IRA or to workplace savings plans other than the one belonging to your most recent prior employer.)[1]

A $50,000 cash out before age 59½ could cost $20,500 in penalties and taxes



This example assumes the following: A hypothetical 24% federal marginal income tax rate, a hypothetical 7% state income tax, and a standard 10% penalty for early withdrawal. The penalty is not withheld from the distribution, but rather paid when the employee files their income taxes. This example is for illustrative purposes only. Please note that the 10% early withdrawal penalty does not apply to distributions made to an employee after separation from service after age 55. The withdrawal will still be subject to income taxes.

By taking your money out early, you also won't give your money the chance for potential growth over time. If you have a critical need for cash and no other options,

you may still want to consider withdrawing only what you need if your former employer's plan allows partial withdrawals.

How the rollover is done is important too

Whether you pick an IRA for your rollover or choose to go with your new employer's plan, consider a direct rollover—that's when one financial institution sends a check directly to the other financial institution. The check would be made out to the new financial institution with instructions to roll the money into your IRA or workplace savings plan.

The alternative, having a check made payable to you, is not a good option in this case. If the check is made payable directly to you, your plan administrator is required by the IRS to withhold 20% for taxes. As if that wouldn't be bad enough—you only have 60 days from the time of a withdrawal to put the money back into a tax-advantaged account like a workplace savings plan or IRA. That means if you want the full value of your former account to stay in the tax-advantaged confines of a retirement account, you'd have to come up with the 20% that was withheld and put it into your new account.

If you're not able to make up the 20%, not only will you lose the potential tax-free or tax-deferred growth on that money but you may also owe a 10% penalty if you're under age 59½ (or under age 55 if separating from service in that year or later[1]) because the IRS would consider the tax withholding an early withdrawal from your account. So, to make a long story short, do pay attention to the details when rolling over your old workplace savings plan.

Make the best decision for you

When it comes to deciding what to do with an old workplace savings plan, certain factors may be unique to your situation. That means the best choice will be different for everyone.

- If you decide to roll your funds into another retirement account, make sure the investment mix is aligned to your risk tolerance and time horizon.
- If you opt for an IRA specifically, your rollover money will sit in cash. This means you'll need to take an additional step in order to get invested.
- Remember that the rules among retirement plans vary, so it's important to find out the rules your former employer has as well as the rules at your new employer.
- Compare the fees and expenses associated with the accounts you're considering.

If you find it confusing or overwhelming, speak with a financial professional to help with the decision.

Investing involves risk, including risk of loss.

Be sure to consider all your available options and the applicable fees and features of each before moving your retirement assets.

This information is intended to be educational and is not tailored to the investment needs of any specific investor.

Recently enacted legislation made a number of changes to the rules regarding defined contribution, defined benefit, and/or individual retirement plans and 529 plans. Information herein may refer to or be based on certain rules in effect prior to this legislation and current rules may differ. As always, before making any decisions about your retirement planning or withdrawals, you should consult with your personal tax advisor.

1. There is no penalty for early withdrawals from 457(b) governmental plans, regardless of age. For Public Safety Officers, such as law-enforcement, firefighters, chaplains, rescue squads or ambulance crew, there is no penalty for early withdrawals if you separate from service on or after the year you turn age 50. As well, retired Public Safety Officers may be able to exclude up to $3,000 per year from taxation for distributions used to pay for health, accident, or long-term care insurance premiums.

2. Certain conditions apply in order to meet the requirements of these exceptions. For a first-time home purchase, you and/or your spouse can withdraw up to $10,000 each penalty-free from your respective IRAs. Please note that while penalty-free, taxes may still apply.

3. If you are actively employed and own not more than 5% of the company you're working for (determined as of the year you reach age 73), you can generally delay taking RMDs from that company's 401(k), 403(b), or Keogh until you retire.

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