

Making the Most of Your Retirement Accounts

Should you roll over employer-held accounts?

provided by Jude Wilson RFC, MBA

The current economy has an increasing number of individuals finding themselves suddenly without jobs and/or taking early retirement packages. What you do with your 401(k) plan when you leave your job deserves some careful consideration. Typically, it makes the most sense to roll your company plan into an IRA, yet a variety of factors will determine what type of IRA is best for you. Even if you aren't planning on leaving your job anytime soon, if your employer is no longer making matching contributions to your 401(k), then you might consider looking at some rollover IRA alternatives.

Rolling over a 401(k) or IRA involves some careful tax planning. If you choose not to roll your plan over into an IRA and take the cash instead, then you'll be severely penalized if you are under age 59 1/2. To avoid paying a 10% penalty and having the distribution count toward your taxable income, funds must be directly rolled over into a new 401(k) or IRA within 60 days. Checks made out directly to you will require the payee to withhold 20% of the taxable amount and you will have to incur an additional 10% penalty on the withdrawal if you are under age 59 1/2.

Whether or not you should roll your money into an IRA depends on a few factors. For example, if your company retirement plan holds some appreciated company stock, you may be better off not rolling these funds into an IRA, but rather withdrawing the shares and holding them in a taxable account. This will ensure that you'll be taxed only on the amount the plan paid for the stock, rather than the price at which the stock has appreciated. This assumes you take the shares as a lump sum distribution, usually meaning you completely liquidate all of your company retirement accounts. While you'll be taxed at ordinary income rates (as high as 35%), the net unrealized appreciation when the shares are distributed to you (the difference between market value and the plan's cost for the shares) will qualify for the 15% maximum long-term capital gains rate (which is 0% if you in the 10-15% tax bracket). And, capital gains tax is deferred until you sell the shares. Additional appreciation will qualify for the 15% rate as long as you hold the shares for more than a year.

Additionally, if you already have an IRA, we can help ensure that you have the IRA that is most beneficial for you and your situation. For

example, you may be best served by moving your money from a traditional IRA to a Roth IRA if you are in a certain income tax bracket. While both traditional IRAs and Roth IRAs have the same contribution limits, Roth IRAs offer tax-free and penalty-free withdrawals of contributions and allow you to make withdrawals from earnings that are tax free (if you are over 59 1/2 and have held the account for more than five years). You will however, pay tax on earnings and pretax contributions when you convert to the Roth, instead of paying taxes upon later withdrawals. This means you will have to have enough years until retirement to make up for what you may lose in taxes on the conversion.

Converting to a Roth IRA may also make more sense for you if you plan to leave your

IRA to your heirs. Unlike with traditional IRAs, your heirs will not be required to take minimum withdrawals, meaning the money may be left in the account to continue to grow. You may also reduce your taxable estate by the amount of income tax you pay to convert, potentially reducing estate taxes for your heirs.

As your financial advisor, I am available to help you make changes to investment accounts as you go through various changes in your life. I can help guide you through the many considerations involved in selecting the right IRA for you as each family's situation is unique. Call my office today if you would like to discuss whether you should roll over your 401(k) or IRA. Or you may consult your tax professional for specific tax advice.

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