Options for Taking Distributions from a 401(k) Plan

In general, you become eligible to take a distribution from a 401(k) plan upon any of the following events:

- Termination of employment
- Termination of the 401(k) plan
- Attainment of age 59 ½ (assuming the plan contains this provision)

In general, if you are eligible to take a distribution, you can take the following courses of action:

1. Leave the money in the plan. In most cases, if your account exceeds $5,000, the plan cannot force you to take a distribution (except upon termination of the plan). You retain the right to select your investments from among those available to other participants. If you have terminated employment, you cannot add money to your account (since you are no longer working for the company). You have the right to designate a beneficiary. Some plans may assess an extra charge to participants who have terminated employment and leave their accounts in the plan. These charges should be disclosed on the mandatory disclosure documents you receive each year. If you leave your account in the plan, it remains invested and there are no immediate tax consequences. Note that if the balance is less than $5,000, the plan can (based on document provisions) force you to take a distribution. If the account is less than $200, the plan can simply distribute your account to you in cash. The plan might not withhold any amount for federal taxes although you will still owe taxes. If the amount is between $200-$1,000, the plan can force you to take a distribution. You would first be afforded an opportunity to roll this money to another vehicle. If you do not respond to the plan's request, then after 30 days, the money can be distributed to you in cash. The plan will in this case withhold 20% for federal taxes. This withholding may be less than your actual federal tax liability, including the premature distribution excise tax (if it applies). If the

amount is between $1,000-$5,000, then you will be afforded an opportunity to roll your account to another vehicle. If you do not respond, after 30 days the plan can initiate the process to roll this money into an IRA that the plan selects for you. At this point you lose the right to direct your investments. For example, some of these "involuntary" IRA's are invested in a low earning money market. The IRA custodian can charge a reasonable fee. However, relative to the account balance, this fee may seem high. Once this involuntary rollover is made, you would have to contact the IRA custodian if you want to take cash, or roll the money to your own choice of IRA, or another 401(k) plan.

2. Roll over to an IRA with the same investments you have in the plan. Some 401(k) record keepers will allow you to roll over your account to an IRA with the same investments that you have in the plan. The expenses may be different. You should request information about expenses before you make the rollover. If you take this course of action, there is no taxable event. There is no income recognized when your roll over to an IRA.
3. Roll over to an IRA with entirely different investments than you had in the plan. This works exactly the same as option 2 above.
4. Roll over your account to another 401(k) plan. If you terminated employment and took another job, the new company you work for may maintain a 401(k) or similar plan. Most plans let you roll money into the plan from a previous employer or IRA. In fact, in many cases, you can make this rollover even before you have satisfied the eligibility requirements for making your own contributions to the new plan. You will need to check this in advance. As with the other options above, you should compare the fund choices and expenses before you make this move. In some cases, where the rollover is relatively small, the convenience of having your money all in one place may take precedence over having the lowest expenses. As with options 2 and 3 above, the rollover is not a taxable event.
5. Take the money in cash. In this case the amount you take in cash is currently taxable. The 10% premature distribution excise tax may also apply. The plan must withhold 20% for taxes. You can elect a larger amount of withholding. Remember these amounts do not represent the actual tax

liability. The actual tax liability is determined by adding the amount you receive to your taxable income. In addition, the money is no longer set aside for your retirement needs. For this reason, many advisors feel this is almost always a poor choice.

6. Roth Conversion. This is not actually a separate option. Many people use the opportunity of a distribution to analyze if it would be beneficial to convert some of their pre-tax money to a Roth IRA. You would owe taxes on the money converted. A detailed discussion of this option is beyond the scope of this summary. You should always consult a tax advisor before making a Roth conversion.

The rules regarding qualified plans are quite complex. The explanations above are provided as general information and for educational purposes. They should not be relied upon as legal advice, advice on establishing a retirement plan, advice on interpreting a retirement plan, tax advice on how to take a distribution or for any purpose other than general information and education.