What To Do With an Old 401(k)

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Weigh the pros and cons of the options to help you decide what makes sense for you.

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 401(k) or 403(b) with that employer. You have several options and it's an important decision.

"Be careful not to make hasty decisions with your workplace savings plan," says John Sweeney, executive vice president of retirement and investing strategies. In particular, beware of cashing out, which often comes with taxes and penalties and can undermine your ability to reach your long-term goals.

Weigh your options.

Because your 401(k) assets are often a significant portion 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. You generally have four choices:

- Leave assets in a previous employer's plan.
- Move the assets into a rollover IRA or a Roth IRA.
- Roll over the assets to a new employer's workplace savings plan, if allowed.
- Cash out or withdraw the funds.

Here are some things to consider about each.

Option 1: Keep your 401(k) with your former employer.

Check your previous employer's rules for retirement plan assets for former employees. Most companies, but not all, allow you to keep your retirement savings in their plans after you leave. If you have recently been through a drastic change such as a layoff, this may make sense for you. It leaves your money positioned for potential tax-deferred investment growth so you can take time to explore your options.

The benefits of leaving your assets in the old plan may include:

- Penalty-free withdrawals if you leave your job in or after the year you reached age 55 and expect to start taking withdrawals before turning 59½.

- Institutionally priced (i.e., lower-cost) or unique investment options in your old plan that you may not be able to roll into or hold in an IRA.
- Money-management services that you'd like to maintain (Note that these services are often limited to the investment options available in the plan).
- Broader creditor protection under federal law than with an IRA.

Some things to consider:

- Typically, employers allow you to keep assets in the plan if the balance is more than $5,000. If you have $5,000 or less, you may need to proactively make a choice to remain. If you don't, some plans may automatically distribute the proceeds to you (or to an IRA established for you).
- You'll no longer be able to make plan contributions or, in most cases, take a plan loan.
- You may have fewer investment options than in an IRA.
- Withdrawal options may be limited. For instance, you may not be able to take a partial withdrawal but instead may have to take the entire amount.

Option 2: Roll the assets into an IRA.[1]

Rolling your 401(k) assets into an IRA still gives your money the potential to grow tax deferred, as it did in your 401(k). In addition, an IRA often gives you access to a wider variety of investment options, such as annuities, [2] than are typically available in an employer's plan. You can also continue growing your retirement savings in a rollover IRA through IRA contributions to the account. Note, however, that in certain scenarios there can be benefits in keeping rollover amounts in a separate IRA.

If you have other accounts at a financial institution that offers IRAs, you often get consolidated statements. This gives you a more complete view of your financial picture, which may make it easier to plan and effectively manage your retirement savings.

Other benefits of rolling over to an IRA may include:

- The option of converting assets to a Roth IRA, which is a taxable event but provides federal tax-free withdrawals of future earnings, providing certain conditions are met[3] (Note that your previous or new employer plan may offer a designated Roth contribution feature in its workplace savings plan and allow participants to convert non-Roth assets into an in-plan Roth account).
- Penalty-free withdrawals for qualifying first-time home purchase or qualified education expenses if you're under age 59½.[4]
- Investment guidance and money management services through a professionally managed account.

But take into consideration that:

- After you reach age 70½, you're required to take minimum required distributions from 401(k), 403(b), or IRA (except for a Roth IRA) every year, even if you are still working. If you plan to work after age 70½, rolling over into a new employer's workplace plan, or staying in the old one, may allow you to defer taking distributions.[5]
- If you need protection from creditors outside bankruptcy, federal law offers more protection for assets in workplace retirement plans than in IRAs. However, some states do offer certain creditor protection for IRAs too. If this is an important consideration for you, you'll want to consult your attorney before making a decision.

A special case: company stock

If you hold appreciated company stock in your workplace savings account, consider the potential impact of net unrealized appreciation (NUA) before choosing between a rollover or an alternative. Special tax treatment may apply to appreciated company stock if you move the stock from your workplace savings account into a regular (taxable) brokerage account rather than rolling the stock (or proceeds) into an IRA. You may want to consider asking your financial adviser or tax accountant for help on how NUA may apply in your situation.

Option 3: Consolidate your old 401(k) assets into a new employer's plan.

Not all employers will accept a rollover from a previous employer's plan, so you need to check with your plan administrator. If your new employer accepts your rollover, the benefits may include:

- Continuing to position your assets for tax-deferred growth potential.
- Continuing to grow your retirement savings through contributions to your new employer's plan.
- Combining plan accounts into one, for easier tracking and management.
- Deferring minimum required distributions if you are still working after you turn age 70½.[5]
- Availability of plan loans (be sure to confirm that the plan allows loans).
- Investing in lower-cost or plan-specific investment options, if available.
- Broader creditor protection under federal law than with an IRA.

But consider this:

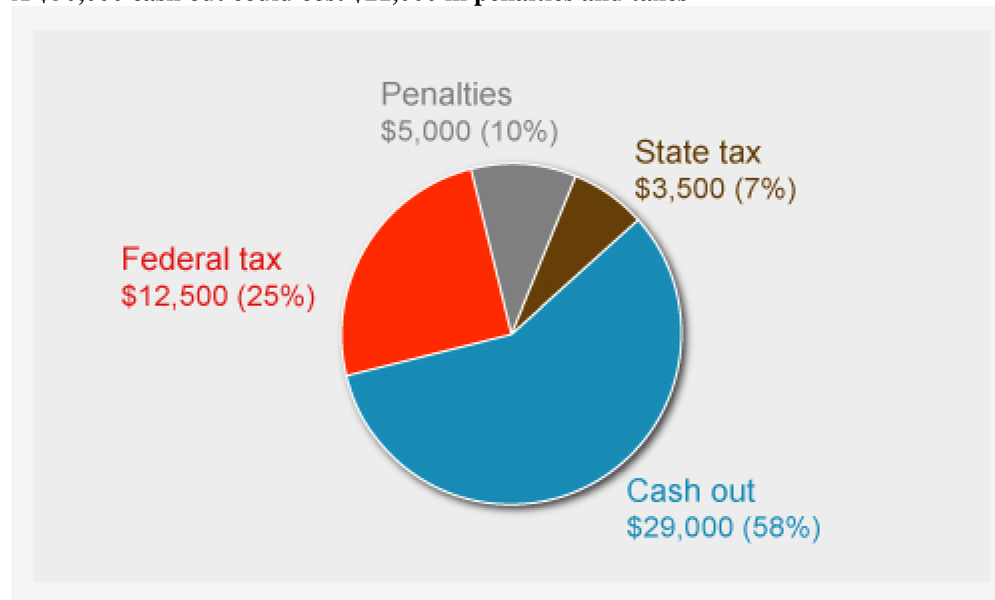
- Your 401(k) may have a limited number of investment options compared with an IRA.
- You will be subject to the new employer's plan rules, which may have certain transaction limits.

Option 4: Cash out.

Taking the assets out should be a last resort. The consequences vary depending on your age and tax situation, because if you tap your 401(k) account before age 59½, it will generally be subject to both ordinary income taxes and a 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.

If you are under age 55 and absolutely must access the money, you may want to consider withdrawing only what you need until you can find other sources of cash.

A $50,000 cash out could cost $21,000 in penalties and taxes



This example assumes the following: A hypothetical 25% federal marginal income tax rate, a hypothetical 7% state income tax, and a standard 10% penalty for early withdrawal. This example is for illustrative purposes only and does not address withdrawals from IRAs. 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. Also, the illustration ignores the opportunity cost of the deferral forgone between early withdrawal and "normal" withdrawal at/during retirement.

A pitfall to avoid

If you choose to roll over your workplace retirement plan assets into an IRA, it is important to pay close attention to the details. To be on the safe side, consider requesting a direct rollover, right to your financial institution. This is also referred to as a trustee-to-trustee rollover, and it can help ensure that you don't miss any deadlines.

Why is this important? If a check is made payable to you, your employer must withhold 20% of the rolled-over amount for the IRS, even if you indicate that you intend to roll it over into an IRA within 60 days. If

that happens, in order to invest your entire account balance into your new IRA within the 60 days, you'll have to come up with the 20% that was withheld. If you don't make up the 20%, it is considered a distribution, and you will also owe a 10% penalty on that money if you are under age 59½. (Later, when you file your income tax return, you will receive credit for the 20% withheld by your employer.)

If you receive the proceeds check in the financial institution's name, you must deposit it into a rollover IRA.

What you should consider when making a decision.

It's important to make an informed decision about what may be a significant portion of your savings. As discussed above, your choice will depend on factors such as your former and current employer's plan rules and available investment options, as well as your age and financial situation. In addition, you may want to think about your investing preferences, applicable fees and expenses, desire to consolidate your assets, and interest in receiving investment guidance. The table below provides a side-by-side comparison of the first three options.

What to do with an old 401(k)? Compare your options.

	Roll over to a Fidelity Advisor IRA	Roll over to the new employer's plan	Leave money in your former employer's plan
Potential tax-deferred growth	✓[1]	✓	✓
Investment options	Ability to invest in mutual funds	Can vary by plan; lower-priced investments may be available	Can vary by plan; lower-priced investments may be available
Continue tax-deferred contributions	✓[1]	✓[2]	
Potential penalty-free withdrawals for qualifying first home purchase and college expenses	✓		
Potential to take penalty-free distributions at age 55[3]		✓	✓

Potential to defer minimum required distributions if you are over age 70½		✓	
Asset protection from creditors	Limited[4]	✓	✓
If you hold appreciated employer stock in your plan	Special tax treatment may be available for your stock (NUA). Consult your tax advisor for more information.		

Be sure to consult the prospectus and offering materials for additional information on fees that may apply.

1. Traditional or Rollover IRA.

2. The new employer may impose a waiting period.

3. You may take penalty free distributions from a qualified employer plan if you terminate employment with the employer sponsoring the plan during or after the year you reach age 55.

4. IRAs are protected under federal bankruptcy law; state law creditor protection of IRAs varies. Consult your legal advisor for more detailed information.

In conclusion, before you make a decision, remember to:

- Speak to a financial professional who can help evaluate your decision based on your complete financial picture.
- Find out your workplace savings plan rules, especially whether you can keep the assets in the plan or roll them into a new employer's plan. Every plan has different rules.
- Compare the underlying fees and expenses of the investment options in your plan with those in an IRA. Also, consider any fees that may be charged by your old plan, such as quarterly administrative fees.
- Evaluate the potential tax impact of any move.

1. Distribution amounts eligible for rollover are generally all pretax contributions (contributions made to your plan that have not yet been taxed) and any investment earnings, both on pretax and any after-tax contributions. You may roll over after-tax contributions (contributions made to your plan that have been taxed). After-tax money in an IRA, including after-tax money rolled in from a 403(b) or governmental 457(b) plan, cannot be rolled from the IRA to a 403(b) or governmental 457(b) plan. Designated Roth contributions under your former employer's plan must be rolled over to a Roth IRA.

2. **Guarantees are subject to the claims paying ability of the issuing insurance company.**

3. A distribution from a Roth IRA is tax free and penalty free, provided the five-year aging requirement has been satisfied and one of the following condition is met: age 59½, disability, qualified first-time home purchase, or death.

4. There is a $10,000 limit on these types of withdrawals.

5. If you are actively employed and own less than 5% of the company you're working for, you can generally delay taking MRDs from that company's 401(k), 403(b), or Keogh until you retire.

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