Make the Most of Your Retirement Plan Distribution

With retirement near, you'll soon need to decide how you want to receive the money you've been accumulating in your retirement plan account. A lot is riding on that decision. Most plans offer several options for receiving a distribution. You'll want to explore all of them and plan ahead so you can make the most of this opportunity.

Keeping Your Money in the Plan

Your plan may allow you to leave your money right where it is. If you leave your money in your plan account, you continue to benefit from potential tax-deferred growth, you avoid the paperwork involved in transferring your money to a new account, and you may be able to keep the same investments. There are no immediate income-tax consequences.

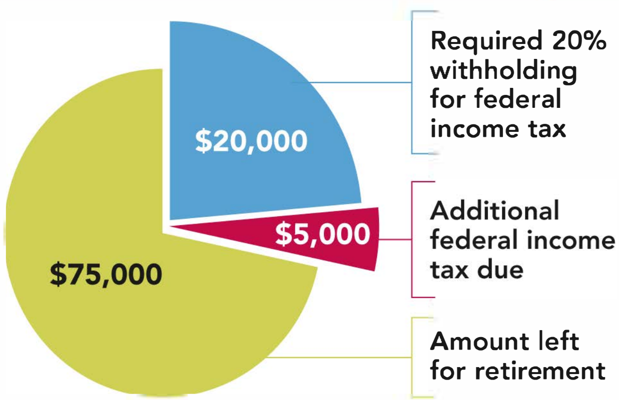
Before you decide to leave your money in your plan, though, review your plan's investment menu to make sure it offers the selection of investments you need for a long-term retirement portfolio. Also, be aware that many plans provide for mandatory distributions of relatively small accounts (up to a $5,000 vested account balance) when employment ends. So you may not be able to keep your plan account long term.

Cashing Out Your Account

You may have the opportunity to take your entire account balance in a single sum when you leave. This option can be appealing because the money will be yours to spend or invest as you see fit. Before you decide to take the cash, be sure to consider the potential impact on your taxes.

To start, the plan is required to withhold 20% of any taxable distribution* and send it to the IRS as a "down payment" on your federal income-tax liability for the year. If your tax bracket is higher, you may owe additional tax come tax time. The pie chart below shows how tax on a $100,000 distribution could break down for a person in a 25% federal income-tax bracket. If you have too much tax withheld, the IRS will refund your overpayment.

DIVIDING UP THE RETIREMENT PIE



This is a hypothetical example used for illustrative purpose only. It assumes a taxable distribution of $100,000 and a 25% federal tax bracket. State and local taxes aren't considered. Your distribution amount and tax results may be different.

Source: SS&C Technologies, Inc.

* Qualified designated Roth account distributions are not subject to federal income tax.

Rolling Over Your Distribution

Rolling over the funds in your plan account to an individual retirement account (IRA) would allow you to continue deferring taxes on your retirement savings. The easiest way to roll over your money is to ask your plan trustee to transfer the funds by a direct rollover to an IRA. You avoid an immediate tax bill.

Another way to roll over your distribution is to have it paid to you. You then have 60 days to complete your rollover to the IRA. Note that your plan will still withhold 20% of the distribution. Unless you make up that missing 20% with other funds and deposit that money in the rollover IRA within 60 days, that part of your distribution will be taxed. In the example above, the individual would have to pay current income tax on the $20,000 withheld and not deposited in the IRA. Also be aware that rolling over pretax plan contributions and earnings to a Roth IRA has tax consequences.

Receiving Installment Payments

Another option you may have is to receive periodic payments starting at retirement. You may be able to choose between receiving payments for a fixed period, such as 25 years, or receiving payments of a fixed amount, such as $300 a month. You also may be able to change your payment amount periodically. You'll pay income tax on your payments in the year you receive them.*

Considering an Annuity

An annuity generally provides monthly payments beginning at retirement that continue for your lifetime (or your lifetime and the lifetime of your spouse or other beneficiary). Your plan may offer an annuity option. Or you can buy an annuity with some or all of your distribution. Annuity payments received from your plan or from an annuity "bought" by rolling over pretax money from your plan to an IRA annuity are generally fully taxed. If you buy an annuity with an after-tax plan distribution, generally only the part of your payment attributable to annuity earnings will be taxed.