Make Sure You Know the Ins and Outs of Your 401(k)Plan

Whether you just started a new job, or you’ve been at one for decades, take the time to review your employer’s retirement plan details and make sure you are contributing as much as you can.

Here are a few things to consider:

The Advantages of your 401(k):

- All contributions made to your 401(k) are made with pre-tax dollars, which lowers your taxable income.

- Your 401(k) plan is “portable,” meaning you can take the amount you contributed, plus earnings, with you when you change jobs. The money can be rolled over into an individual retirement account (IRA) or another qualified 401(k) plan.

- Some employers even contribute to or match your contribution. How much is contributed depends on the individual employer’s company policy.

Challenges to Consider:

- You have to decide how much to contribute to the plan and where to invest it.

- The amount that you have in your 401(k) at retirement depends on the amount you invested, how it was invested (e.g. the mix of stocks and bonds), and how long your investments had to grow and increase in value.

- You have to decide what you will do with the money in your plan if you change jobs or when you retire.

Rolling Over Can Avoid Tax Penalties!

If you leave or change your job, you may have the option to receive a lump sum payment. If you take the lump sum, you will have to pay taxes on the payment unless you roll it over into an individual retirement account (IRA) or other eligible plan. (For example, if you are changing jobs and your new company’s retirement plan accepts transfers.)
You can roll all or part of the lump sum payment into an IRA. Your retirement plan can transfer the payment directly to the IRA company.

If the plan directly transfers the lump sum payment to the IRA company, it will not withhold taxes, and you do not have to take any action.

If the plan sends the check to you, however, it is required by law to withhold 20% for income taxes, even if you will not owe that amount on your income taxes. (You must then come up with the dollar amount of the 20% withholding and roll that over, or you will be liable for taxes on that amount.) It is therefore important to be sure your lump sum is directly rolled over to avoid tax penalties.

Taking a loan from your 401(k)

Most plans allow you to take a loan under certain circumstances. Loans are generally not a good idea, and you should understand the risks. Also, you will need to pay the loan in full if you decide to leave the employer. If you do take a loan, you generally have to pay it back within 5 years.

Ask Yourself These Questions and Know the Answers!

- Have you diversified your investments?
- Do you know what the value of your investments is expected to be at retirement?
- Have you planned how you will manage payouts from your plan?
- Have you provided for ways to protect your assets, such as through life, disability income, or long-term care insurance, or by purchasing an annuity?

Divorce and Retirement Benefits

Under all state laws, a pension earned during marriage, which includes 401(k)s, is a joint asset, but it is not automatically divided at divorce. You must ask for a share of the pension at the time of divorce. To do this, you will need to submit a special court order to the retirement plan stating your right to a portion of your ex-spouse’s pension. This is known as a “Qualified Domestic Relations Order” (QDRO).

If you find yourself facing a divorce:

- Check to see if your spouse has more than one pension
- Find out how much of a benefit your spouse has earned from each pension
- Include survivor benefits in the pension court order

Be clear on this critical point: Have all the information about your ex-spouse’s retirement benefits before you divorce. It is nearly impossible to go back to court and ask for a share of your ex-spouse’s benefit after the fact.

To learn more, download WISER’s booklet, Divorce and Retirement: How to Take Control of Retirement Benefits, at www.wisewomen.org