Reviewing Your Options for a Retirement Plan Distribution

If you are changing jobs, retiring or being terminated from a job, it is natural to undergo stress and anxiety. Usually, these changes are also accompanied by receiving a distribution from your employer’s retirement plan. There are three important decisions that must be made about these distributions.

1. Do you want to pay tax on it now or have it remain tax-deferred?
2. Do you want to leave your funds with your prior employer’s plan, move them to your new employer’s plan or transfer them to an IRA?
3. How do you want the money invested?

If you have been a participant in a plan for a long time and have accumulated a large sum of money, these decisions can have a very large impact on your financial future and that of your family. Considering the decisions carefully is critical.

Check with your human resources or payroll department to learn what your options are and get professional help if you need it.

Pay taxes or not
While your funds were within the qualified plan, any earnings were tax deferred. When you receive the distribution, you have 60 days to roll over your funds to your new employer’s plan (if allowed) or into an Individual Retirement Account. If you don’t act within 60 days, your distribution will be subject to regular income taxes and an additional 10% early withdrawal penalty tax if your are under the age of 59 ½.

If you don’t need the money immediately, it is usually advisable to maintain the tax deferral status.

Where to keep your funds
To maintain tax deferral, the funds must stay in some form of qualified retirement account. Many retirement plans offer the opportunity to leave funds in the plan after employment termination. You may also be eligible to transfer the distribution to a new employer’s plan. The third option is to transfer the funds to an IRA. The choice of where to have your money should be based on the amount of investment control you wish. An IRA probably provides the most flexibility, but also forces you to make more decisions. Costs of administration and asset management should also be considered.

Even if you are currently unsure of your long-term plans, you may want to have the funds transferred into an IRA. You can always make withdrawals later if you choose.
Investing your funds
Your retirement plan distribution may be the largest single sum of money you will ever receive. The investment of those funds should be handled very carefully. Be sure to consider how these funds fit into your overall financial planning efforts.

Be sure to consider your time horizon and risk tolerance when making your investment decisions. If you transfer your distribution to your new employer’s retirement plan, consider the investment options and choose appropriately. If you go the self-directed IRA route, most institutions offer accounts that enable you to choose stocks, bonds, mutual funds, money market funds and other investments. You also have the option of having a professional manage your investments to your risk and investment profile.

Don’t feel that you have to make all the investment decisions immediately or to make them alone. As long as the funds are within another qualified plan or IRA, there should be no taxes due and you can make informed and careful investment choices.

Conclusion
Receiving a lump sum distribution is a major financial event. The choices you make will affect your financial security for years to come. Be sure to evaluate all your options, seek guidance if needed and decide wisely. Your future financial security depends on it.