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Wye Trust
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Protect your 401(k) money throughout your retirement

According to the Investment Company Institute's 2021 Fact Book, an astounding $11.1 trillion is held in tax-qualified defined contribution plans, such as 401(k) plans. That resource will play an enormous role in the re-tirement security of millions of Americans over the coming years. Accumulating money in a 401(k) is one thing—arrange for salary reductions to fund the plan, evaluate investment choices for the money, check on progress periodically and make adjustments as needed.

Distribution of 401(k) money is another thing entirely—one that raises a host of new and, for most people, unfamiliar issues. Care must be taken to preserve that retirement resource, typically through a rollover to an IRA. The Fact Book reports that IRA assets have reached some $12.2 trillion. That figure includes contribu-tions to traditional and Roth IRAs, as well as employer-sponsored programs built on IRAs, such as SEP IRAs and SIMPLE IRAs, but the bulk of the funding has come from rollovers.

Will you be receiving a lump sum distribution of some or all of your retirement benefits when you retire? A lump sum distribution, from a 401(k) plan or another qualified retirement plan provided by your employer, can be rolled over into an IRA, preserving its special tax status well into your retirement. However, you will have many important choices to make during this process. It's not a hard or complicated process, exactly, but the consequences of your choices will last for the rest of your life, so make them carefully.

Take a direct approach
Most people will opt to roll their lump sums into an IRA in order to avoid current income taxation. There is a wrong way and a right way to handle this.

The wrong way is to accept a check for the amount of the lump sum. If you take this approach, your employ-er will be required to withhold 20% in income taxes on the distribution. You'll either have to be satisfied with an 80% rollover, or you'll have to come up with the difference from other savings sources.

The right way is to arrange a direct transfer from the qualified plan trustee to the trustee of your IRA rollover—there is no withholding requirement with this approach.

IRA investing
During the accumulation years, most people saving for retirement have a significant amount invested in the stock market. That exposure typically falls as one approaches retirement, and it may fall still further in retirement. Retirees need the steady stream of income that bonds can provide.

Still, one needs to keep in mind the probability of eroding purchasing power because of inflation that can oc-cur over the course of a long retirement. Inflation was quite mild for many years, but now that trend has changed. Hopes for a "transitory" inflation have been dashed. Some amount of equity investing may be needed to hedge against these developments.

If you have significant savings in taxable accounts, you won't want to evaluate your investment strategy for the IRA rollover in isolation. You'll need to decide whether your stock investments belong in the IRA rollover or on the taxable side of the ledger. All the distributions from the IRA will be taxed as ordinary in-come, whether they are of interest, dividends, capital appreciation or return of principal. For the sake of tax efficiency, many advisors suggest focusing the IRA on providing steady income (investing primarily in good-quality bonds) and doing the stock investing outside of the IRA. This preserves the benefit of the lower tax rate on realized long-term capital gains, as well as the lower tax rate for most corporate dividends.

Planning the distributions

From age 59½ through age 72, you may withdraw as much or as little from your IRA rollover each year as you please. There's no penalty tax to worry about, but you will have to pay ordinary income tax on most withdrawals. After you reach age 72, a program of required minimum distributions must begin.

Name a surviving beneficiary
You'll want to designate a surviving beneficiary for your IRA rollover. Usually a surviving spouse is named, but another beneficiary may be appropriate, depending upon the composition of family wealth and other family circumstances. The decision can be changed at any time.

We can help
Retirement should be, fundamentally, the moment that you declare your financial independence, a declaration that lasts the rest of your life. Should there be an IRA rollover in this picture? If so, how will the assets be invested? We'll be pleased to offer you our assistance with these important financial planning issues.

We look forward to meeting with you soon to discuss your needs.