



THE ULTIMATE **401(k)** GUIDE

HOW TO TAKE CONTROL OF YOUR 401(k) BEFORE AND DURING RETIREMENT

We all know that a 401(k) is one of the most important retirement planning tools we have. You pay into it for decades and will likely need to rely on it, among other income sources, for decades in retirement. The potential tax benefits and power of compound interest can make it a great saving and investment tool for anyone who practices financial discipline and contributes regularly. There are several important things to know about your 401(k), such as how much you can contribute, options for your 401(k) when you leave your job, and how much you are paying in 401(k) fees.



THIS GUIDE WILL COVER:

- 1 OPTIONS FOR YOUR 401(k)
- 2 WHAT TO DO WITH COMPANY STOCK
- 3 HOW TO CONTRIBUTE MORE TO YOUR 401(K)
- 4 HOW TO TAKE ADVANTAGE OF THE CARES ACT 401(K) AND IRA PROVISIONS
- 5 THE SECURE ACT'S 401(K) CHANGES
- 6 WAYS TO MINIMIZE YOUR TAXES

IF YOU LEAVE A JOB FOR ANY REASON, YOU HAVE A FEW OPTIONS FOR YOUR OLD 401(k):

Cash out: You can cash out all or part of your old 401(k), in which case the funds will be taxed as ordinary income.

Rollover into a new 401(k): If you start another job, your old 401(k) can often be rolled over into your new workplace retirement plan without paying tax on funds rolled directly into your new 401(k).¹

Continue with the old 401(k): In many cases, you can leave your money in the 401(k) at your old workplace. However, having multiple retirement accounts can complicate your finances. And your retirement fund will still be at your ex-company.

Rollover into an IRA: If you roll over funds directly into an IRA, you will not owe tax on them. IRAs typically offer many more investment options than workplace 401(k) plans, giving you more flexibility to pursue an investment strategy that suits you specifically.²

¹ <https://www.irs.gov/retirement-plans/plan-participant-employee/401k-resource-guide-plan-participants-general-distribution-rules>

² <https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-termination-of-employment>

WHAT TO CONSIDER:

HOW MUCH OF YOUR RETIREMENT SAVINGS ARE INVESTED IN COMPANY STOCK?

If you plan to roll over your 401(k) into an IRA, first consider how much money you have invested in your previous company's stock. Would you have invested in the company if you didn't work there? If not, then why keep it now? If you do wish to keep it, consider that company stock that has increased in value can be taxed as investment gains at your current tax rate. So how do you sell your company stock without increasing your tax burden?

Using a tax strategy called Net Unrealized Appreciation (NUA), you can move the company stock into a taxable account to potentially lower your tax bill. Distribution of an employer's stock qualifies for this special tax treatment where tax is limited to the cost basis of the stock, not the full market value of the stock. You can then defer income taxes on the NUA until you sell the stock. You may also be able to minimize your tax burden by taking advantage of the long-term capital gains tax rates and getting a step up in basis when you eventually sell or pass on your company stock.

What is Net Unrealized Appreciation? (NUA)

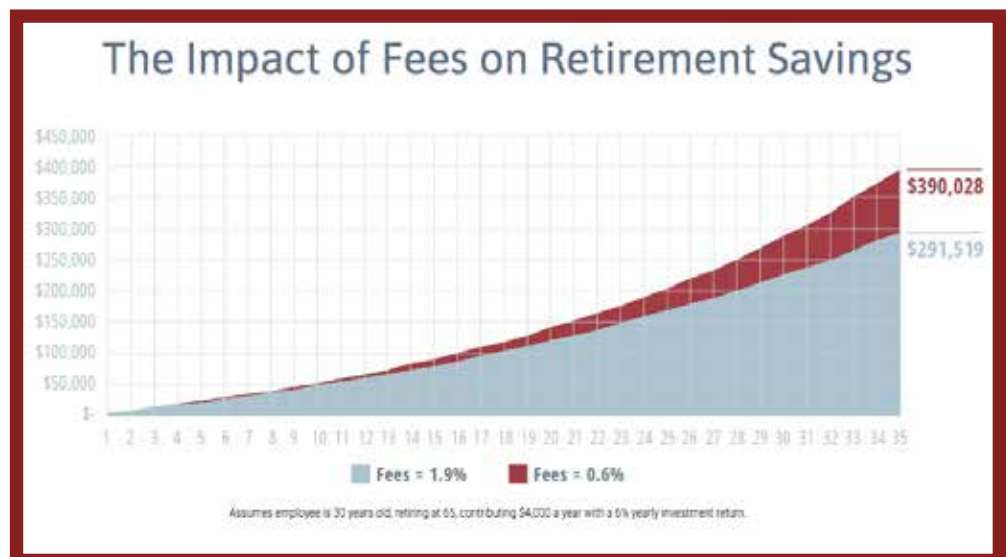
NUA is the difference in value between the average cost basis (what you paid for stock shares) and the market value when the stock is distributed. So, if the cost basis of stock was \$20,000, and the value when it was distributed is \$60,000, then the net unrealized appreciated is \$40,000.

ARE YOU 55 OR OLDER?

In most cases, you must wait until age 59 ½ to withdraw from a qualified retirement plan to avoid the 10% early distribution penalty. However, if you leave your job for any reason during or after the year you turn age 55, you can withdraw from your current 401(k) without penalty. Keep in mind that this rule applies only to the 401(k) sponsored by the employer you leave when you're 55 or older, not 401(k)s from previous employers. There are specific requirements pertaining to taking distributions when you turn 55, which if not followed will result in penalties. These kinds of withdrawals should be discussed with your tax professional prior to taking a distribution.

ARE YOU AWARE OF HOW MUCH YOU'RE PAYING IN 401(k) FEES?

How much of your money goes towards fees? According to the Boston College Center for Retirement Research, paying an annual fee of 50 basis points for 30 years can reduce the purchasing power of savings by one-eighth.³ The size of 401(k) fees varies: 95% of 401(k) participants pay fees, ranging from under 0.5% to more than 2%. 2% might not seem like much, but it can add up over the course of many years. For example, let's compare a 401(k) plan that charges 2% in fees to one that charges 1%. Both start with a balance of \$100,000 and have an expected annual rate of return of 8%. After 30 years, the account paying 2% in fees would grow to \$574,350. Meanwhile, the account paying 1% in fees would grow to \$761,225.⁴



³ https://crr.bc.edu/wp-content/uploads/2009/02/IB_9-3-508.pdf

⁴ <https://cdn.americanprogress.org/wp-content/uploads/2014/04/401kFees-brief3.pdf>

⁵ <https://www.forusall.com/401k-blog/who-are-the-best-401k-providers-for-small-business/>

YOU CAN MAKE “CATCH-UP” CONTRIBUTIONS STARTING AT AGE 50

Starting at age 50, you can contribute more to your 401(k) each year. In 2020, workers under 50 can contribute up to \$19,500 to a 401(k), 403(b), most 457 plans, or Thrift Savings Plan. Workers 50 and over can contribute an additional \$6,500 in 2020, for a total of \$26,000 per year.¹ This can be a good option for workers who want to save more while reducing their tax burden when working.



¹ <https://www.irs.gov/newsroom/401k-contribution-limit-increases-to-19500-for-2020-catch-up-limit-rises-to-6500#:~:text=Highlights%20of%20changes%20for%202020,increased%20from%20%2419%2C000%20to%20%2419%2C500.>

NEW LEGISLATION TO NOTE

THE CARES ACT:

Many 401(k) and other defined-contribution plans allow for loans of up to \$50,000 or half of the vested account balance. Normally these loans can be repaid over a five-year period. The CARES Act has temporarily modified this loan rule: Most 401(k) participants can now borrow up to \$100,000 or 100% of the vested amount – whichever is less – for 2020.

Those who have been diagnosed with the coronavirus, have been laid off, had their hours reduced, or have been furloughed can take an in-service distribution from their IRA. Normally, there is a 10% early withdrawal penalty for those who withdraw from their retirement account before age 59 1/2. The CARES Act waives this penalty for withdrawals of up to \$100,000 for 2020. You can also take up to three years to pay the tax on the distribution. ²

² <https://www.congress.gov/bill/116th-congress/senate-bill/3548/text?q=product+update#toc-H638004C502804947B4CFB9B4B770C2F2>

THE SECURE ACT

Projected Income Disclosures

Part of creating a retirement plan could include figuring out how to turn a lump sum into income for the rest of your life. The SECURE Act requires retirement plan sponsors to state the estimated monthly payments that participants would receive if they used their entire account balance to buy an annuity. And, it allows employer-sponsored 401(k) plans to add annuities as an investment option. While this is helpful for getting a sense of how far your savings could stretch, it only offers a one-size-fits-all solution that may not be right for you. We can sit down with you and figure out how an annuity could fit into your specific retirement plan.



HOW CAN YOUR 401(k) BE USED AS AN ASSET IF IT'S ROLLED OVER?



01 AVOID A HIGHER TAX BURDEN

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While it might be tempting to cash out of your old 401(k) in tough times, this could dramatically increase your tax burden. On the other hand, funds rolled over into an IRA are not treated as withdrawals and are not subject to income tax. You can continue to enjoy tax-deferred growth by rolling over funds directly into an IRA within 60 days of withdrawing from an old account.

GAIN ACCESS TO MORE INVESTMENT OPTIONS

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IRAs tend to have a broader array of investment options and lower administrative fees than 401(k)s. With an IRA, you can invest in practically any stock, mutual fund, ETF, bond, real estate, or security. By consolidating your retirement savings into an IRA, you can gain more flexibility in your investment choices, allowing you to create a retirement plan customized to fit your unique needs. This is important because access to more types of investments could mean more options for mitigating investment risk as you near and enter retirement. If you think having control over your retirement savings is important, consider this: While most 401(k) plans limit the number of times per year you can rebalance your portfolio, an IRA allows you to buy and sell your holdings whenever you want.

SIMPLIFY YOUR FINANCES

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Rolling over your old 401(k) may help you simplify your finances. Instead of keeping track of multiple former workplace retirement accounts, you can roll over your old plan or plans into one IRA and review a single account statement. Also, keep in mind that a communication gap could arise if you keep your old 401(k) with your ex-employer. It could be harder to get in touch with a plan advisor or administrator, or harder for them to get in touch with you if your contact information changes. And in the event that your company undergoes a significant change such as filing for bankruptcy, access to your 401(k) could be temporarily frozen.

04 OPTION TO CONVERT TO A ROTH IRA

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You have the option to convert funds from a traditional IRA, 401(k), or similar qualified retirement account into a Roth IRA. In this case, you would pay tax on the funds converted and then be able to withdraw them tax-free later on. If you think you'll be in a lower tax bracket in the year you lost your job, you might consider a Roth conversion while your tax burden is lower.

Be mindful that unless certain criteria are met, Roth IRA owners must be 59 ½ or older and have held the Roth IRA for five years before tax-free withdrawals are permitted. Please consult a tax advisor before deciding to do a conversion because it cannot be undone.



HOW WE CAN HELP

If the coronavirus recently upended your retirement and financial plans, know that you don't have to go it alone. An advisor can help you figure out a plan for using what you've saved, and help you balance your short-term needs with your long-term financial goals. We're transparent about our costs and fees, and are legally, as well as morally required to act in your best interests. This means that we can go through the myriad of investment options available and help you choose ones that are best suited to your financial needs. We can pursue strategies to help you mitigate risk, minimize taxes, and maximize your Social Security benefit – with all of these elements working together in one cohesive retirement plan. While strategies can give you confidence, there is no assurance that any strategy will achieve its objectives. Our commitment is to provide you with the very highest level of service and to help you achieve your retirement goals!



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