MFS HERITAGE PLANNING® > LIFE EVENTS

401(k) Plan Choices for Job Changers

When you change jobs, it can be for any number of reasons. Regardless of what triggers a job change, such an event creates a perfect opportunity to reevaluate your long-term financial plan. After all, this is one of the few times — aside from actual retirement — that you will be faced with making decisions about what to do with the money you have been saving in your 401(k) plan. Reviewing your situation at this transitional time can help you feel better about your new job, and get you refocused on your long-term savings plan.

When you leave an employer, you are likely to have several options. You may

- stay invested in your previous employer's plan if your balance meets the plan's minimum
- invest your assets in the new employer's plan
- take your distribution in cash
- roll over assets to an IRA

First and foremost, you should know that by taking a cash distribution from your 401(k) plan, you will incur a tax liability and may be subject to possible penalties that will significantly lessen your after-tax payout. Although taking that distribution in cash to pay off bills or to start a new business venture may seem like a good idea, it will ultimately leave you with a smaller nest egg. On the other hand, leaving your investments in your old employer's plan may limit your investment choices and distribution options.

As you can see, there are many pros and cons associated with each option. Following is just a summary of those options. Your financial advisor or investment professional will be able to help you make the right decisions based on your individual situation.

KEY POINTS

When you leave a job, you can

- stay invested in your current plan
- roll assets into another qualified plan with your new employer or an IRA
- take a 401(k) distribution in cash

While making choices,

- look at the whole picture of your current plan
- understand all the requirements of a new plan
- be aware of any financial penalties associated with taking a cash distribution
- make sure the new plan or IRA offers investment and distribution options that fit your needs
- compare the fees, expenses and services of your old employer's plan with those of your new employer's plan and a rollover IRA

If you do a direct rollover,

- you will have no current exposure to taxes or penalties
- assets can remain invested and can potentially continue to grow tax deferred

This material should be used as helpful hints only. Each person's situation is different.
You should consult your investment professional or other relevant professional before making any decisions.

NOT FDIC INSURED • MAY LOSE VALUE • NO BANK GUARANTEE

Choice 1 — Stay invested in your previous employer's plan

Unless your balance is less than the plan's cash-out minimum, you generally will be able to leave the money right where it is. You should ask yourself the following questions:

- Am I happy with my investment choices?
- Am I limiting my access to these assets now that I am no longer with the company?
- Do I have any after-tax contributions in this plan?

You might be satisfied with the performance of the investments within your previous employer's plan — investments that may not be available to you in a your new employer's plan. In addition, your employer may pay some of the fees involved in having an account, so an employer plan may be cheaper than other options, such as an IRA. There are two types of after-tax contributions to a 401(k). One type is a Roth 401(k). The tax treatment of a Roth 401(k) is very similar to a Roth IRA in that withdrawals are tax free if you follow specific IRS rules. Some plans allow you to make additional after-tax contributions which may grow tax deferred but any potential earnings are taxable when withdrawn. If you have this type of after-tax money, you may want to roll the contributions into a Roth IRA. In a Roth IRA, qualified withdrawals are tax free.

Before you decide to move your nest egg, it is important to look at the entire picture, including any changes you might have made to your financial strategy. It is quite possible that, despite there being several advantages to leaving the money where it is, your previous employer's plan may not be in line with your revamped financial plan.

Choice 2 — Invest your assets in your new employer's plan

Let's say you have looked over your new employer's retirement plan and, having decided it does fit your long-term strategy, you choose to move your assets. Doing so will ensure that your retirement assets remain tax deferred. It also will keep your assets in a centralized location.

That is the good news. The bad news is that your new company may not allow you to participate in its plan right away. Some plans have a service requirement that new employees must complete before they are eligible to participate. Some plans do allow new employees to make rollover contributions to the plan even though they have not met the eligibility requirements for starting to make salary deferral contributions. But if the plan does not allow immediate rollovers and you are looking to transfer assets immediately upon leaving your previous employer, this may pose a problem.

Therefore, while you are waiting out the time requirement to place pretax assets into your employer's new plan, you might consider converting your money into a rollover IRA (see Choice 4).

Choice 3 — Take your distribution in cash

Let's assume you have saved diligently and are well on your way to establishing a nice nest egg for retirement. However, the possibility of taking that money in cash when you change jobs is enticing. The new kitchen, along with the luxury import car, would be an excellent addition to your everyday life. But before you have a check for the entire distribution (or even part of it) made out to you, there are a few things you should keep in mind.

By having the check made out in your name, you could be handing over almost one-third of your account to the government. When a distribution is not directly rolled over into an IRA or another qualified plan — as is the case when it is taken in cash — the employer automatically withholds 20% of the money for federal taxes.

If you are younger than age 59½, you may be hit with an additional 10% federal tax penalty. However, this penalty tax does not apply if you separate from your service after age 55. To make matters worse, taxpayers in the 22% bracket or above will have at least another 2% taken from the now-dwindling nest egg. In short, you may compromise your strategy of building for a comfortable retirement.

If, after taking the distribution in cash, you decide you would like to roll it into another plan or IRA, you can still do so. However, you must reinvest 100% of the amount distributed, including the amount withheld for taxes, within 60 days of the date you receive the distribution to avoid taxation.

The bottom line is that before taking the cash you should think long and hard about all your hard work and the sacrifices you have made only to now be penalized and taxed. And if you are still tempted, a meeting with your financial advisor or investment professional will likely quell any remaining doubts you might have about the effect even a small cash distribution can have on your retirement income.

Choice 4 — Roll your assets into an IRA

Of the four distribution choices discussed here, rolling over assets to an IRA may offer the most investment flexibility and less exposure to taxes and penalties than taking cash.

A direct rollover is a lump-sum distribution that is transferred into an IRA or other qualified plan. When changing jobs, you should request a check for the amount you wish to roll over from your 401(k) and have it made out to the trustee of the new plan or IRA (qualified plans include 401(k), 403(b), pension and profit sharing plans). Please note that unless you are taking the distribution in cash, the check should never be made out to you.

Once you have completed the rollover, you can leave your money in the IRA or you can decide later to roll it over to a new employer's plan when you are eligible to participate in it. Keep in mind, however, that there may be fees associated with establishing and closing the IRA and that indirect IRA rollovers (where an IRA is distributed payable to you and redeposited in a plan or IRA within 60 days) are allowed only once in a 12-month period.

The key is to roll your assets into a vehicle that offers a wide variety of investment choices that meet your financial objectives. Among the most popular choices for traditional IRAs, for example, are mutual funds. Allocating IRA assets among mutual funds offers investors professional, full-time management, diversification (to help reduce risk) and the flexibility to move from one fund to another as investment needs change. Keep in mind, however, that the principal value and return of mutual funds will fluctuate with changes in market conditions and your investment may be worth more or less than you originally paid upon withdrawal.

Take your time and invest wisely

What you do with your 401(k) assets when you change jobs is an important financial decision. The best thing you can do when faced with these four choices is to think things over carefully.

In most cases, you will not be required to make a decision immediately, which leaves you plenty of time to meet with your financial advisor or investment professional. He or she can help you decide the best way to invest those assets to try and help maximize your income at retirement.

One of the benefits of retirement accounts is creditor protection. The level of protection will vary based on account type and in some cases, state law. A qualified plan, such as a 401(k), is protected by a federal law (ERISA). This protects your 401(k) from almost all claims by creditors, bankruptcy and court judgments (the IRS and divorce proceedings are two exceptions). An IRA has similar protection if you declare bankruptcy but does not have the same federal protection from creditors or court judgments.[1] Your state may offer additional protection to an IRA.[2]

There are advantages and disadvantages to an IRA rollover, depending on investment options, services, fees and expenses, withdrawal options, required minimum distributions, tax treatment, and your unique financial needs and retirement goals. Please be aware that rolling over retirement assets into one IRA account could potentially increase fees as the underlying funds may be subject to sales loads, higher management fees, 12b-1 fees, and IRA account fees such as custodial fees. For assistance in determining if a rollover to an IRA is appropriate for you, consult your investment professional.

[1] The amount of money in your IRA that is protected in bankruptcy is limited to $1,512,350 (until March 31, 2025) plus any amount rolled over from a qualified plan. (source: federalregister.gov).

[2] A nonspouse beneficiary who inherits an IRA does not get the same level of creditor protection as the original owner, in most cases. The level of protection, if any, varies under state law.

This material is provided for general and educational purposes only and is not investment advice. The investments you choose should correspond to your financial needs, goals, and risk tolerance. Please consult an investment professional before making any investment or financial decisions or purchasing any financial, securities or investment related service or product, including any investment product or service described in these materials.

Before investing, consider the fund's investment objectives, risks, charges, and expenses. For a prospectus or summary prospectus containing this and other information, contact your investment professional or view online at mfs.com. Read it carefully.

Contact your financial advisor or investment professional for more information or visit mfs.com.

MFS® does not provide legal, tax, or accounting advice. Any statement contained in this communication (including any attachments) concerning U.S. tax matters was not intended or written to be used, and cannot be used, for the purpose of avoiding penalties under the Internal Revenue Code. This communication was written to support the promotion or marketing of the transaction(s) or matter(s) addressed. Clients of MFS should obtain their own independent tax and legal advice based on their particular circumstances.

MFS FUND DISTRIBUTORS, INC., MEMBER SIPC, BOSTON, MA

HP_LE401JB_FLY_5_24
15817.17