Roth 401(k)
Frequently Asked Questions

What is a Roth 401(k)?
The Roth 401(k) is an optional plan contribution type that first became available to retirement plan participants in 2006. With a Roth 401(k), plan participants can choose to have their salary deferrals made on an *after-tax* basis. This means that, unlike traditional pre-tax 401(k) deferrals (which are not taxed in the contribution year), Roth 401(k) contributions will be subject to current federal and, if applicable, state and local income taxes. So, Roth contributions are subject to tax withholding like regular pay. As with a traditional 401(k), any plan earnings on Roth 401(k) contributions are not taxed while the money is held in the plan. However, when an employee withdraws Roth 401(k) money from the plan, the employee receives both the contributions and any plan earnings *tax free*, assuming certain tax law requirements are met. With a traditional 401(k), the pre-tax contributions and accumulated earnings are generally *taxed* on withdrawal at ordinary income-tax rates. Similar tax treatment applies to the very popular Roth IRA, which has been available for several years to individuals whose income is below certain levels. The Roth 401(k) option makes most of the advantages of Roth IRAs available to *all* eligible plan participants within your retirement plan, no matter what their income may be.

What are the requirements for tax-free treatment of Roth 401(k) distributions?
Generally, withdrawals of Roth 401(k) contributions and any earnings on that money will not be taxed if:

- The money is distributed after the participant reaches age 59½ or on account of death or disability (as defined for Social Security disability purposes) ***and***
- The withdrawal is made after five tax years have elapsed, starting with the year the first Roth 401(k) contribution was made.

If these requirements are not met, the Roth contributions still will not be taxed. However, distributions of Roth 401(k) investment earnings will generally be subject to income tax and, possibly, to a 10% tax penalty as well.

Why would an employee choose to pay taxes now rather than later?
For many employees, making Roth 401(k) contributions will mean more money in their pockets when they retire, after all taxes are paid. Depending on each employee's individual situation, making Roth 401(k) contributions may be very beneficial, even with the upfront taxes. Generally, the decision will depend on several factors, such as the employee's:

- Current age
- Expected retirement age
- Current tax bracket
- Expected retirement tax bracket
- Contribution amount

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The decision requires employees to consider their current financial situation, as well as what they expect their financial situation to be in the future.

Which participants might benefit from a Roth 401(k)?

- Younger and lower paid employees who would pay little tax on their contributions now and who have many years to accumulate potentially tax-free earnings.
- Employees who will be in the same or a higher tax bracket in retirement than they will be during their working years.
- Highly compensated employees who cannot contribute to a Roth IRA due to the tax law's income restriction.
  - Adjusted income limit (AGI) of $139,000 (individuals) and $206,000 (married) (2020).
- Employees who prefer (and can afford) to pay taxes now to gain tax-free treatment for their future plan withdrawals (and not take a chance that tax rates will be higher in the future).

What are the contribution limits for Roth 401(k)?
The $19,500 and $6,500 (for over age 50 catch up) limits (2020) apply to the total of your contributions**,** regardless of whether the contributions are pre-tax or Roth. You may contribute pre-tax or Roth or a mix of both.

Can you contribute Employer match contributions on Roth 401(k) contributions?
If your retirement plan includes employer matching contributions, you can make matching contributions on Roth 401(k) contributions just like you would on pre-tax contributions. All matching contributions are contributed to the same tax deferred employer match account, regardless of whether the employee contributions are made on a pre-tax or Roth basis.

Roth contributions will be made on an after-tax basis, but since you don't have to pay income taxes on employer contributions when they went into your account, you will have to pay federal income taxes when you take a withdrawal.

Can I roll my Roth 401(k) into a Roth IRA?
You can roll-over a Roth 401(k) into a Roth IRA when your employment is terminated or when you retire. You cannot roll-over a Roth IRA into your Roth 401(k) account.

Please contact our office if you wish to discuss this information in more detail. This publication is intended for general information purposes only and does not and is not intended to constitute legal advice. This is not meant to be an all-inclusive summary of all components of auto-enrollments, but merely highlight significant features. The reader must consult with legal counsel to determine how laws or decisions discussed herein apply to the reader's specific circumstances.

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