

Practice Tips for Rollovers of Roth 401(k) Contributions

Summary	<p>Under the proposed Roth 401(k) regulations, rolling a Roth 401(k) into a new Roth IRA restarts the five-year nonexclusion period. The entire rollover amount including earnings is treated as basis in the Roth IRA. If the Roth 401(k) is rolled into an existing Roth IRA, the rollover is treated the same as a contribution to the Roth IRA, and follows the five-year period that is attached to the receiving Roth IRA.</p>
Client Profile	<p>Participants making Roth contributions to their 401(k) plans who are age 59 ½ or over</p>
Apply the Rules	<p>In order for a distribution of a Roth 401(k) contribution to be a qualifying distribution and receive favorable tax treatment on the earnings, and avoid penalties, the following criteria must be met.</p> <p>The participant must have attained age 59 ½, retired or become disabled;</p> <p>AND</p> <p>The participant must have satisfied the five-year nonexclusion period.</p> <p>If the Roth 401(k) rollover is made to a newly established Roth IRA, the five-year nonexclusion period begins with establishment of the new Roth IRA.</p>
Ask a key question	<p>Are you planning to take a distribution of the entire Roth 401(k) amounts rolled over to the Roth IRA within five years of IRA establishment?</p>
Example	<p>In 2006, Jack, age 58, begins making Roth 401(k) contributions to his employer's 401(k) plan, and does so for the next three years. Now at age 61, he is unhappy with the investment performance and information he receives regarding his account. Jack's retirement plan with his employer allows for distribution of his Roth 401(k) account balance at age 59 ½. He is thinking of rolling it out of the plan. Jack's Roth 401(k) balance is \$68,000, of which \$8,000 is earnings. He currently does not have a Roth IRA, and would like to know the consequences of rolling his balance into the newly established Roth IRA.</p> <p>If Jack rolls his \$68,000 into a new Roth IRA, the five-year nonexclusion period begins again when the Roth IRA is established, even though the Roth 401(k) balance has been in the retirement plan for three years already. If Jack were to distribute the entire Roth IRA within five years of establishment, the \$68,000 (\$60,000 in contributions and</p>

\$8,000 earnings) would be nontaxable to him but any earnings accumulated from the date of the rollover would be taxable.