WHAT IS A ROTH 401(k)?
The Roth 401(k) feature gives you the option to set aside money for retirement on an after-tax basis, where both contributions and earnings continue to grow tax-free. Your money can grow on a tax-deferred basis, and contributions and earnings can eventually—once you have reached age 59 ½ and have held the account for at least five years—be withdrawn tax-free. It is this tax treatment that distinguishes Roth 401(k) contributions from traditional 401(k) contributions, where with traditional 401(k) contributions, which are made on a pre-tax basis and grow tax-deferred until they are withdrawn, Roth 401(k) contributions are taxed at the individual’s ordinary income tax rate when contributed. Aside from these differences, Roth 401(k) contributions are treated the same as traditional 401(k) contributions—normal limits and non-discrimination rules apply. Roth 401(k) contributions are also subject to the same withdrawal restrictions, i.e., death, disability, retirement, hardship, etc. as traditional 401(k) contributions.

WHY CONTRIBUTE TO A ROTH 401(k)?
The Roth 401(k) may offer advantages to those who are currently in a lower tax bracket but who expect to be in a higher tax bracket after retiring. By locking in today’s tax rates, you can create a “hedge” against future tax increases. Another benefit: The Roth 401(k)’s tax-free withdrawals can help highly paid employees better manage their tax situation in retirement. In a Roth 401(k), income taxes are paid at your regular income tax rate at the time that contributions are made, and earnings and withdrawals are not taxed if withdrawals begin after age 59 ½ and if five years have elapsed from the date of the first Roth 401(k) contribution. Taxes and penalties are waived upon death or disability. Similar to a traditional 401(k) contribution, you must generally take minimum distributions from the Roth 401(k) contributions as of the April 1st of the calendar year following the later of (i) the calendar year in which you attain age 70 ½, or (ii) the year in which you retire. However, a Roth 401(k) account can be rolled into a Roth IRA if you leave your job, eliminating the need to take a required minimum distribution.

IS THERE A SEPARATE ACCOUNT UNDER THE PLAN FOR ROTH 401(k) CONTRIBUTIONS?
Yes, a separate account will be maintained for any individual under the plan that elects to make Roth 401(k) contributions. Roth 401(k) contributions must always be kept in a separate account under the plan. You decide what percentage of your retirement plan contributions go to either account. Roth 401(k) contributions and traditional 401(k) contributions will be shown as separate contribution types on your account summary and statement. Also, please note that plan forfeitures, if any, cannot be allocated to a Roth 401(k) account.

HOW DO ROTH 401(k) CONTRIBUTIONS DIFFER FROM TRADITIONAL 401(k) CONTRIBUTIONS?
The primary difference between the two types of contributions has to do with their tax rules. Traditional 401(k) contributions provide for pre-tax contributions and tax-deferred investment growth, but future distributions (withdrawals) are taxable. On the other hand, Roth 401(k) contributions permit after-tax contributions, tax-free earnings, and tax-free qualified withdrawals. Qualified withdrawals are those that are made after you attain age 59 ½ and have held the account for at least five years. (Note that withdrawals are also allowed for certain extenuating circumstances—as defined by the IRS—such as death or permanent disability.)
HOW MUCH CAN I CONTRIBUTE TO A ROTH 401(k)?
You may contribute up to $18,000 in 2026 to a Roth 401(k) and/or traditional 401(k) account, plus an additional $6,000 in catch-up contributions if permitted by the Plan and if you are age 50 or older. Subject to Plan limitations, you can make both Roth 401(k) contributions and traditional 401(k) contributions, subject to the maximum contribution allowable under 401(k) rules, but contributions to a Roth 401(k) account are irrevocable, meaning that once you designate a contribution as a Roth 401(k) contribution, those assets may not be re-directed as traditional 401(k) contributions.

CAN I MAKE BOTH ROTH 401(k) AND TRADITIONAL 401(k) CONTRIBUTIONS?
Yes, you can make both Roth 401(k) contributions and traditional 401(k) contributions, subject to the maximum contribution allowable under 401(k) rules. Please keep in mind that a Roth 401(k) option does not increase the amount of contributions that can be made to a 401(k) plan. In other words, the current 401(k) plan limits will apply to traditional 401(k) contributions and Roth 401(k) contributions in the aggregate. You can elect both Roth 401(k) contributions and traditional 401(k) contributions in the same plan year. There is no limit as to how deferrals can be split between Roth 401(k) contributions and traditional 401(k) contributions. For example, if you elect to defer $100 from each paycheck, you could specify that $50 be designated as a traditional 401(k) contribution and $50 as Roth 401(k) contribution. Roth 401(k) contributions and earnings are maintained as a separate account within the plan and will be shown as two separate items on your quarterly statement.

WILL I STILL RECEIVE EMPLOYEE MATCHING CONTRIBUTIONS?
If your employer provides matching contributions, you can earn a match when you contribute to your Roth 401(k) account, but the matching portion cannot be directed into the Roth 401(k) account. Instead, the matching portion will be directed to your employer matching account.

CAN I CHANGE MY MIND ONCE CONTRIBUTIONS ARE MADE?
Roth 401(k) contributions are irrevocable. Once contributions are made to a Roth 401(k) account, you cannot change your mind and have the money switched over to your traditional 401(k) account. You can, however, decide not to make additional Roth 401(k) contributions in the future. How often you can do so depends on the provisions of your plan.

CAN I MAKE WITHDRAWALS FROM A ROTH 401(k)?
If your plan permits, you can withdraw money from the Roth 401(k) account without paying tax or penalties provided you are at least age 59 ½ and the distribution is made five years or more after January 1st of the first year that you made a Roth contribution to the plan. These are the same rules that apply to Roth IRAs. If your plan permits in-service withdrawals, the same tax penalties that apply to early distributions (prior to age 59 ½) from traditional 401(k) accounts apply to Roth 401(k) accounts. If you apply for a hardship withdrawal, monies will be taken from your pre-tax source first.

If your plan permits, you may also take a distribution of Roth rollover contributions. The taxation of a Roth rollover withdrawal is based on meeting Roth qualifications and the age 59 ½ rule. If you rollover Roth 401(k) contributions into this plan in a direct rollover, then the five-year period will be the earlier of the January 1st of the first year that you made a Roth contribution into the distributing plan or the receiving plan.

As is the case with a traditional 401(k) account, you will need to begin taking minimum distributions after you reach age 70½. This is different than the Roth IRA, which has no distribution requirements.

CAN I TAKE A LOAN FROM A ROTH 401(k)?
If your plan permits, you can take a loan from your Roth 401(k) contributions, as Roth 401(k) contributions are both lienable and loanable. Keep in mind that in the event that you default on loan repayments, earnings on Roth 401(k) contributions will always be taxable, even if you have met the Roth qualifications.
HOW ARE COMPLIANCE TESTING REFUNDS HANDLED UNDER A ROTH 401(k)?
In the event of an ADP test failure, refunds will be paid out of the traditional 401(k) account first, then paid from the Roth 401(k) account.

CAN I ROLL OVER ROTH 401(k) PLAN ASSETS?
You can roll over your Roth 401(k) account to a Roth IRA when you retire or change employers. By contrast, assets in a traditional 401(k) deferral account may only be rolled into a traditional IRA (although a traditional IRA can subsequently be converted to a Roth IRA if desired). In addition, Roth 401(k) plan assets can be rolled into another employer’s Roth 401(k) plan, if available, and plan rules allow.

CAN I ROLLOVER OR TRANSFER THE MONEY IN A TRADITIONAL 401(k) ACCOUNT TO MY ROTH 401(k) ACCOUNT?
There are currently no provisions allowing such a rollover from outside of the plan into your Roth 401(k) account. Because of the unique tax treatment of each contribution type, you cannot switch your Roth 401(k) plan account over to a traditional 401(k) plan account. However, you will be allowed to roll over money from one Roth 401(k) plan account to another qualified plan that permits Roth 401(k) contributions or to a Roth IRA.

However, if your plan allows it, you may complete an In-Plan Roth Conversion. Beginning in 2013, subject to your plan’s provisions, you may convert some of your traditional 401(k) account balance to a Roth 401(k). An In-Plan Roth Conversion allows a participant to transfer an eligible rollover distribution to a Roth 401(k) account within a 401(k) plan. It is simply a transfer from one contribution type to another for tax purposes of the participant. It is important to understand that no actual distribution of funds will occur with In-Plan Roth Conversions. This transaction is purely a transfer from one contribution type to another for tax purposes of the participant. An In-Plan Roth Conversion will result in a 1099-R for the year in which the conversion takes place.

CAN I CONTRIBUTE TO A ROTH 401(k) AND A ROTH IRA?
It depends. While there is no rule specifically preventing you from contributing to both types of accounts during the same year, income limits may restrict or negate your ability to contribute to a Roth IRA. There are significant differences to consider. Some aspects of the Roth 401(k) plan are more generous and some are less generous than those available in a Roth IRA. For example, unlike a Roth IRA, the Roth 401(k) plan has no income restrictions. As a result, the Roth 401(k) plan may be attractive for higher-paid employees who have been unable to contribute to a Roth IRA. The annual contribution limit for the new Roth 401(k) plan is much higher than the Roth IRA ($18,000 for 2016 plus $6,000 catch-up contribution for individuals age 50 and older). On the other hand, the Roth 401(k) plan has one drawback compared with the Roth IRA among people who do not want to be required to take money out of their account. Unlike the Roth IRA, which has no minimum distribution requirements, minimum distributions from a Roth 401(k) account generally must begin as of the April 1st of the calendar year following the later of the (i) calendar year in which you attain age 70 ½, or (ii) the calendar year in which you retire. However, the assets in a Roth 401(k) account can be rolled into a Roth IRA if the employee retires or leaves the company, which would eliminate this requirement.

WHY SAVE AFTER-TAX DOLLARS THROUGH A ROTH 401(k) VS. A ROTH IRA?
The Roth 401(k) feature offers you the opportunity to save more on an after-tax basis than a Roth IRA, which has contribution limits of $5,500 if you have not attained age 50 and $6,500 if you are age 50 or older in 2015. If you have a Roth IRA, or plan to open one, you can still contribute the maximum allowable to the IRA in addition to your Roth 401(k) contributions. In addition, the Adjusted Gross Income limit, which applies to the Roth IRA, does not apply to Roth 401(k).

IS IT BETTER TO CONTRIBUTE TO A TRADITIONAL 401(k) OR A ROTH 401(k)?
That depends on your personal situation. For example, because Roth 401(k)s allow tax-free withdrawals, they may be more appropriate for employees who expect to be in a higher income tax bracket during retirement. High-income earners who make too much to contribute to a Roth IRA may also find the Roth 401(k) attractive, as there are no income limitations for Roth 401(k) participation. The Roth 401(k) option may not be as attractive to someone nearing retirement and expecting to need to tap his or her retirement savings soon.
Traditional 401(k) plans, on the other hand, may be more appropriate for employees seeking a tax break now and/or who expect to be in a lower income tax bracket during retirement. Our Roth 401(k) Calculator is a web-based tool that’s designed to help you determine whether this feature may be right for you. To access the Roth 401(k) Calculator, log on to your Pentegra account and click on the Roth 401(k) calculator under “Tools”.

**WHAT ARE THE DISADVANTAGES OF THE ROTH 401(k)?**

Many employees may not be able to afford the same level of contributions on an after-tax basis as opposed to a pre-tax basis, resulting in decreased savings and a potential loss of employer matching contributions.

You may wish to consult with a financial advisor to determine whether to make Roth 401(k) contributions in lieu of or in addition to traditional 401(k) deferrals.

This material is provided solely for informational purposes and does not constitute investment, tax, legal or accounting advice on the matters addressed. Neither Pentegra Services, Inc., its subsidiaries, nor any of their respective employees intend that this material should be relied on as investment advice, which advice should be sought from a professional advisor. Performance information shown reflects past performance and does not indicate or guarantee future investment results. Current and future results may be lower or higher than those shown.

©2013 Pentegra Retirement Services