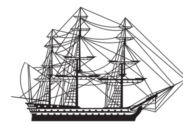
Client Education

Learn About Distribution Options for Your Employer Retirement Plan Assets



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As you plan your retirement, you'll need to decide what to do with the money you've accumulated in your employer-sponsored retirement plan.

Whether you have a pension plan, a 401(k) or 403(b) plan, a SEP, or some combination of these, there are various options for managing the money you've accumulated. Read over this brief guide and work with your financial advisor to determine the best way to receive your retirement benefits.

Your pension benefit options

Traditional pension plans generally provide the option of a lump-sum payment or a fixed monthly payment for life through an annuity. The fixed monthly payment amount is usually based on how long you've worked, how much you've earned, and how old you are when you retire.

Consider your options

Depending on your pension plan, you may have several choices for receiving monthly income payments, and some companies may allow you to take your pension as a single lump-sum payment. Contact your employer's benefits office for information about your options, including the dollar amounts that each option would provide, as well as how to begin receiving your money.

If you've worked for several employers during your career, make sure you check with each employer to determine the distribution options and the pension benefits you qualify for in retirement.

Your financial advisor can help you decide which options will best fit your needs.

Monthly income through an annuity. An annuity is simply a stream of income payments guaranteed for your lifetime or a specified period. If you choose to receive monthly income from your pension plan, you're choosing a lifetime annuity.

The two most common annuity options provide for lifetime payments to a single person (single life annuity) or payments to an additional person upon the death of the annuity owner (joint and survivor annuity). If you're married, you're legally required to choose a joint and survivor annuity, unless your spouse approves a single life annuity in writing.

Be sure you compare your pension plan's annuity options with those of a commercial annuity to see which offers a better deal.

Lump-sum payment. Some defined benefit plans allow you to take money in a lump sum—a one-time payout of everything you're entitled to receive. Another possibility is to set up a lifetime pension for part of your retirement income and maintain a separate investment portfolio to meet your flexible spending needs.

Yet another option is to take your pension as a lump sum and roll it over to a traditional IRA to avoid paying immediate taxes on it. This alternative allows you to use some of the funds to purchase an income annuity, leaving the remainder of your funds in your IRA to use as needed. Once again, consult with your financial advisor to determine the most appropriate payout option for your circumstances.

A comparison of lump-sum and annuity payment options

Annuity payments	Lump-sum payments
Your monthly income is fixed, you have no investment decisions, and your tax planning is straightforward.	You'll face tax issues in deciding how to take the lump sum, and you'll have to make investment and estate planning decisions.
You generally can't transfer your money to another investment or postpone or accelerate payments if your health or financial situation changes.	You control how your money is invested and how fast you spend it. You can roll the money over to a tax-deferred retirement account and have access to the money if needed for an emergency or an investment opportunity.
Most annuities pay a fixed monthly amount. At an inflation rate of 3.5% a year, a fixed income annuity would lose half its purchasing power in 20 years.	Your investments may earn higher returns than an annuity would offer and help you to better keep pace with inflation.
Your benefits don't depend on your investment results, so declining interest rates or falling stock prices won't reduce your income.	If your investments perform poorly, you could end up with less money than if you'd taken a fixed monthly payment.
You can't outlive your money (although after inflation it may not meet all your needs).	You may outlive your money if you live long enough or you don't make good investment or spending decisions.
Your money grows tax-deferred, but you must pay income taxes on your monthly distribution.	If you roll over your lump sum directly to another tax-deferred plan, you'll generally be taxed only as you withdraw the money. But if you don't roll over the lump sum, it's taxable as income in the year you receive it.
Once you (and your beneficiary, if you choose a survivor option) die, all benefits cease and there is nothing for your heirs.	The unspent portion of your lump sum can be left to your heirs when you die.

Your defined contribution plan choices

When it comes to deciding how to handle defined contribution plans such as your 401(k), 403(b), profit-sharing, or money-purchase plan when you retire, you generally have four options, each of which has advantages and disadvantages.

Leave your money in the plan

You may be allowed to leave the money in your employer's plan. Taxes will continue to be deferred until you withdraw your money. And you aren't required to take distributions until April 1 of the year after you turn 70½.

While leaving your money in your employer's plan will prolong its tax-deferred growth, your investment and distribution options are restricted to those in the plan.

Turn your money into an income stream

If your employer plan permits, you can choose to take your distributions in installments. Your payments can be based on a percentage of your account balance or can be fixed-dollar amounts, either of which could run out during your lifetime. Or the payments can be designed to last throughout your lifetime, although the monthly amounts likely will be lower than those of the other two methods.

Another variation would be to buy an income annuity with some or all of the money if you choose to roll over your assets to an IRA.

Roll over your money to an IRA

A rollover is a transfer of money from one investment to another. To maintain the tax-deferred status of your retirement plan money, you can roll your plan assets over to another tax-deferred account, usually a traditional IRA. Beginning in 2008, you also have the option to roll your money over to a Roth IRA. Keep in mind that if you do choose to roll your money over to a Roth IRA, it will no longer be tax-deferred (except for any earnings after the rollover, which will be tax-exempt, not tax-deferred).

Taxes continue to be deferred within a traditional IRA until you make withdrawals. You can delay making withdrawals until April 1 of the year after you reach age 70½. At that point, you must begin taking distributions, which are taxable.

You can roll your assets to an IRA two ways:

A direct rollover. This is the most tax-efficient way to roll over your savings. You instruct your employer to send the money directly from your retirement plan to your traditional IRA. You don't take possession of the assets.

An indirect rollover. You can have the money sent to you, but this method is less efficient than a direct rollover, because your employer is legally required to withhold 20% of the money for taxes.

You must complete the rollover within 60 days and make up the 20% with other assets, or you will owe taxes on the amount withheld. If you make up the 20% withholding tax when you complete the rollover, the amount withheld will be refunded to you when you file your tax return.

On top of the potentially lower costs, another advantage of rolling your assets over to an IRA is the wide range of investment options—mutual funds, stocks, exchange-traded funds, bonds, and cash investments.

An important estate planning opportunity

Depending on your situation, your financial advisor may suggest that you roll your assets over to an IRA so your beneficiaries don't have to deal with adverse tax consequences. With an IRA, your beneficiaries may be eligible to take lifetime distributions. If you leave the money in your employer plan, beneficiaries must usually take a lump-sum distribution and pay taxes in the year of the distribution.

Take your money in a lump sum

Taking your money in a lump sum can be a risky strategy because you must pay ordinary income taxes—as much as 35%, depending on your federal tax bracket—on the entire amount in the year you take the lump sum. If you're under age 59½, you might also owe a 10% federal penalty tax.

It's a good idea to work closely with your financial advisor and your tax consultant before you decide what to do with your defined contribution assets.

A comparison of retirement plan distribution options

Option	Advantages	Drawbacks
Leave your money in the plan	Your assets will keep growing tax-deferred.	You may not be eligible to remain in the plan, and your investment choices will be limited to those in the plan. You must begin making withdrawals once you reach age 70½.
Turn your money into an income stream (through installment payments or an income annuity)	You can create a retirement income stream that you can't outlive.	An annuity will likely involve higher expenses than an IRA. An annuity is irrevocable. Once you purchase an annuity, you can't get your money back.
Roll over your money to a traditional IRA	Your assets will keep growing tax-deferred, and you'll have almost unlimited investment choices. If you're qualified, you can convert the traditional IRA to a Roth IRA. While Roth IRAs offer tax-free withdrawals, you're not required to make withdrawals during your lifetime.	You must begin making withdrawals from a traditional IRA once you reach age 70½. If you convert a traditional IRA to a Roth IRA, you must pay taxes on the conversion.
Take your money in a lump sum	You can use your assets for current expenses or invest the lump sum yourself.	If you spend your retirement assets quickly or make poor investment decisions, you won't have the money available for your later retirement years. Your withdrawal will be subject to federal (and possibly state and local) income taxes. Also, your withdrawal may be subject to a 10% penalty tax if you're under age 59½.

Company stock alternatives

A number of retirement plans let you hold shares of the company's stock in your account. Determining what to do with those shares when the time comes for payout can be tricky.

As you consider your options, you and your financial advisor will want to keep an eye on maintaining the diversification of your portfolio while managing the tax consequences of any stock transfers or sales.

When it comes to dealing with company stock, there are generally three options available.

Reallocate your shares within the plan

In this case you can instruct your plan administrator to sell your shares of stock and add the proceeds to your other plan assets.

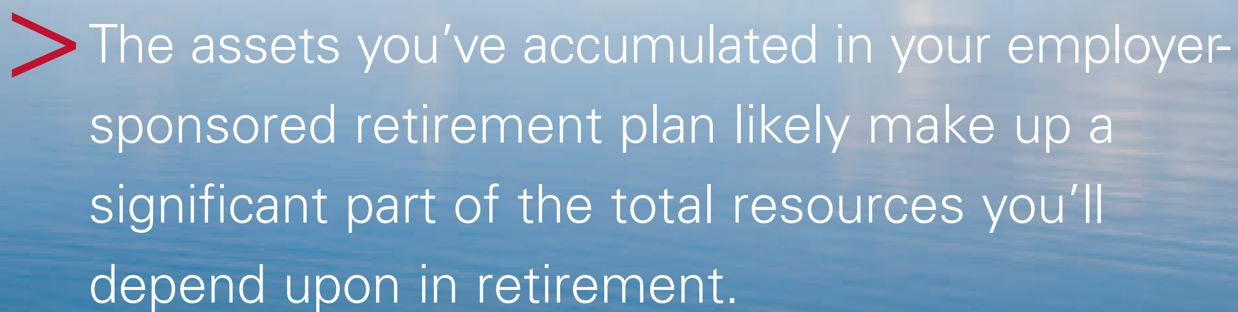
Roll over your shares

You can maintain possession of your stock as part of your retirement savings by rolling over your shares "in-kind" to a brokerage rollover IRA. This option lets you maintain possession of your stock shares, while helping you avoid current taxes on the value of the stock.

Take an in-kind distribution

You can choose not to roll over your stock shares to an IRA by having the plan distribute them directly to you. This option could have significant tax implications, depending on the value of your shares when you take the distribution.

It's very important to talk with your financial advisor and your tax advisor before deciding what to do with your company stock. In addition, you should consult with your company's plan administrator to determine whether the plan has any restrictions on holding shares outside of the employer-sponsored retirement plan.



The assets you've accumulated in your employer-sponsored retirement plan likely make up a significant part of the total resources you'll depend upon in retirement.

As you consider your payout options, work closely with your financial advisor to ensure that your assets are structured to help provide the financial security you plan for in the years ahead.

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