ROTH 401(k) GUIDE

Fisher Investments®
401(k) Solutions

Roth 401(k) Plans

You diversify your investment portfolio. It makes sense to also diversify your tax liability. A retirement portfolio that includes a traditional 401(k) and a Roth 401(k) offers both a solid foundation for your retirement savings and an opportunity to cut your taxes and significantly increase your net income over the course of a long life.

Adding a Roth option to your company-sponsored 401(k) plan is a cost-effective way to help your participants tax diversify their investments because it allows you and your employees to contribute post-tax earnings toward retirement—and face no additional taxes on those savings or any investment earnings when the money is withdrawn during retirement.

While a Roth can benefit all types of investors, this feature is especially attractive for highly compensated and younger employees because:

1. A Roth 401(k) has no income cap, so it enables highly compensated employees who make too much money to contribute to a Roth IRA to make contributions to a Roth 401(k).
2. Earnings grow tax-free, so younger employees who have a long time before they retire can benefit more from tax-free earnings growth. For example, if an investment grows by 10% every year, the original contribution will double in size every ~7 years. That growth is never taxed when contributions are made to a Roth 401(k).
3. Younger employees may also pay a lower tax rate now than they will further in their careers.

DIFFERENCES BETWEEN A TRADITIONAL 401(k) AND A ROTH 401(k)

Traditional 401(k)

- Contributions are tax-deferred. Only when it's time to retire will you pay taxes on the money you withdraw.
- Withdrawals are taxed as ordinary income.
- Required minimum distributions are required at age 72.

Roth 401(k)

- Roth 401(k)s approach taxation up front.
- Contributions made to the account after-tax.
- Withdrawals are tax-free.
- Required minimum distributions at age 72 are not required if the Roth 401(k) is rolled into a Roth IRA account.

More on Tax Diversification

As a business owner or plan participant, you have a lot of choices for how to save for retirement. And each type of plan has different taxation rules. Some allow you to invest pre-tax dollars, others allow you to contribute after-tax and pay no taxes when you withdraw your earnings. Which approach is best?

For many plan participants, a diversified approach offers both more retirement income and lower taxes over their lifetime. Specifically, tax diversification means spreading your contributions across tax-deferred and post-tax accounts to increase the after-tax earnings of your investments.

Tax Treatment Table

View the table below to understand the difference in how various types of investments are taxed.

	Individual Accounts		Employer Accounts	
	Brokerage Accounts	Roth IRA	401(k)	Roth 401(k)
Description	A type of after-tax investment account for individuals with none of the tax benefits of an IRA, 401(k) or Roth.	A type of after-tax account available to an individual.	A type of tax-deferred account that is available through an employer.	A type of after-tax account available though an employer.
Income Limits	None	$153K Individual/ $228K Married Filing Jointly	None	None
Contribution Type	After-Tax	After-Tax	Pre-Tax	After-Tax
Personal Contribution Limits	None	$6,500/$7,500	$22,500/$30,000[1]	$22,500/$30,000[1]
Tax Treatment at Withdrawal	Earnings taxed as capital gains	Principal and earnings are tax free[2]	Principal and earnings are taxed as ordinary income	Principal and earnings are tax free[2]
Fed Tax Rate at Withdrawal	0%-20%	0%	10%-39.6%	0%
Subject to RMDs (Required Minimum Distributions)	No	No	Yes	No, if converted to a Roth IRA[3]

Roth 401(k) to Roth IRA Roll Over

If you are leaving a job that provides a Roth 401(k) account, your account can be rolled over to a Roth IRA or Roth 401(k) without incurring taxes.

Often, it's best to roll over your Roth 401(k) to a Roth IRA, rather than to another Roth 401(k) because it allows you to avoid required minimum distributions (RMDs) at age 72.

Using a direct rollover, which transfers funds directly from your current Roth account to your new one, reduces the potential for tax complications.

[1] 2023 employee deferral contribution limit into a Traditional 401(k) and Roth 401(k) is $22,500 < 50 years and $30,000 > 50 years.

[2] This assumes withdrawals are qualified per IRS guidelines.

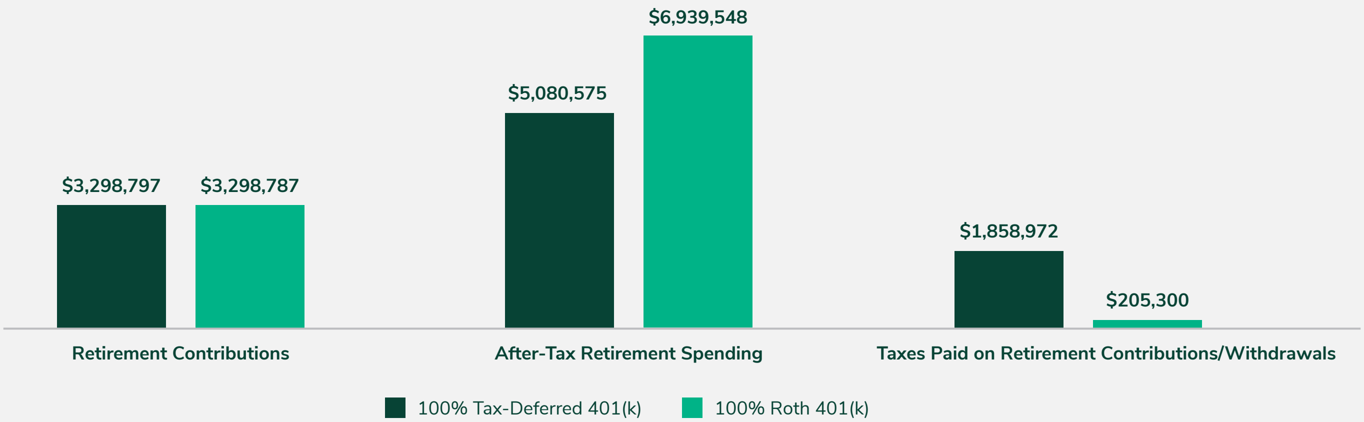
[3] A Roth 401(k) is not subject to RMDs if it is rolled into a Roth IRA after the employee leaves the employer.

Roth 401(k) Case Study

Participant Age: 30
Contribution Period: Ages 30-64
Annual Contribution: $22.5k < 50 years/$30K > 50 Years

Annual Investment Growth Rate: 7%
Withdrawal Period: Ages 65-90

100% Traditional 401(k) vs 100% Roth 401(k) Contributions Strategy



Traditional 401(k) Tax Rate During Withdrawal Period (age 65-90): 24% ages 65-83. 32% ages 84-90.

Roth Tax Rate During Contribution Period (age 30-64): 22% ages 30-52. 24% ages 53-64.

Note: A Roth strategy may not be best for all plan participants which is why it is important to hire a plan advisor that provides one-on-one guidance tailored to the needs of the plan participant.

What if you could have $1.8 MM more in retirement spending without having to increase your contributions? The scenario where the individual invested 100% into an after-tax Roth account resulted in 37% more after-tax retirement spending and -89% fewer taxes paid on the the retirement contributions and withdrawals.

Key Takeaways

- A tax diversification strategy can be an impactful part of retirement planning for plan participants.
- Roth options within the 401(k) are often the only tax-advantaged way for highly compensated employees to save for tax-free retirement income.
- The most efficient way to enable a tax diversification strategy is to add a Roth 401(k) option to a traditional 401(k).

Helpful Resources

Roth 401(k) FAQs
Watch this video to get answers from a Fisher 401(k) Specialist to frequently asked Roth 401(k) questions.

Tax Diversity to Reduce Taxes
What plan participants need to know about tax diversification to reduce taxes and increase retirement income.

Roth 401(k) Case Study
See how to leverage a Roth 401(k) to reduce taxes and increase retirement savings.

Are you leaving money on the table?

When you look at all the money left on the table with an average plan, it's hard to see why anyone would settle for less.

Poor service, which leads to lower savings rates and lower performance, combined with high fees that take a big chunk out of your portfolio, result in less money at retirement. You've worked hard to get to this point. Now's not the time to settle for less.

Contact us today to see how Fisher 401(k) Solutions can help you and your employees create more wealth.

REQUEST FREE CONSULTATION

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