SWEETWATER FINANCIAL ADVISORS GUIDE

5 Questions to Ask Before Rolling Over Your 401(k)

What pre-retirees and those leaving an employer need to know before making this important and irreversible decision.

If you are leaving an employer or approaching retirement, you will likely face a critical decision: what to do with your 401(k). Rolling it over incorrectly — or at the wrong time — can result in unnecessary taxes, penalties, and lost investment options. These five questions will help you make the right choice.

QUESTION 1

Should I roll over to an IRA — and why this is usually the right answer?

For most people, rolling your 401(k) into an IRA is the right move — and the advantages are significant. First, an IRA gives you complete freedom to invest in virtually anything: individual stocks, ETFs, mutual funds, bonds, REITs, and more — compared to the limited menu your employer's plan offered. Second, an IRA consolidates your retirement savings into one account you control, making it easier to manage, monitor, and coordinate with your overall financial plan. Third, an IRA gives your advisor full flexibility to build a portfolio specifically designed for your goals and risk tolerance — not constrained by your former employer's plan options. Fourth, IRAs offer more flexible withdrawal and beneficiary planning options than most 401(k) plans. Potential reasons to consider leaving your money in a former employer's plan might include unusually low-cost expenses (however, ETFs used in an IRA often have very low expense ratios), strong creditor protection, or if you are between 55 and 59-1/2 and may need penalty-free access under the Rule of 55. For the vast majority of people, however, an IRA rollover is the smarter long-term choice.

QUESTION 2

What are the tax consequences — and how do I avoid them?

A direct rollover — where funds move directly from your 401(k) to an IRA — is not a taxable event. No taxes, no penalties, no paperwork headaches. An indirect rollover is where the risk lies: your employer sends you a check for the account balance, withholds 20% for taxes automatically, and you must re-deposit it within 60 days to avoid the full amount being treated as a taxable distribution. Here is the catch — you must deposit the full original amount, including the 20% that was withheld, or that withheld portion is taxed as ordinary income and may incur a 10% early withdrawal penalty if you are under 59-1/2. Always request a direct rollover to your IRA. It is cleaner, safer, and avoids any risk of a costly mistake.

QUESTION 3

Is now the right time to roll over — or should I wait?

Timing matters more than most people realize. If you are between 55 and 59-1/2 and have separated from your employer, you may be eligible for penalty-free withdrawals from your 401(k) under the Rule of 55 — a benefit you lose once you roll over to an IRA. Conversely, the window between retirement and age 73 may be ideal for Roth conversions. The right timing is personal and depends on your age, income, and plans for the money.

QUESTION 4

What can I invest in after rolling over to an IRA — and why does it matter?

This is one of the most compelling reasons to roll over. Inside your former employer's 401(k) you were limited to a preset menu — often 15 to 30 fund options, sometimes dominated by high-cost actively managed funds or target-date funds that may not fit your situation. Inside an IRA, the investment universe opens dramatically. You can hold individual stocks and bonds, low-cost ETFs with very low expense ratios, dividend-paying equities, sector-specific funds, and a wide range of fixed income options. This breadth allows your advisor to build a truly customized, tax-efficient portfolio around your specific goals, timeline, and income needs. The difference in investment costs alone — moving from a 401(k) with average fund expenses of 0.5-1.0% to an IRA using low-cost ETFs — can add tens of thousands of dollars to your retirement over time. Combined with the flexibility to rebalance and coordinate withdrawals strategically, an IRA rollover gives your advisor the full toolkit needed to manage your retirement the right way.

QUESTION 5

Do I need a financial advisor to handle a rollover?

Technically, no. But the real question is whether you want professional guidance on the decisions surrounding the rollover — investment allocation, Roth conversion opportunities, tax-efficient withdrawal sequencing, and Social Security coordination. These decisions are interconnected in ways that are easy to get wrong without experience. A fiduciary advisor who understands your complete financial picture can help you avoid costly mistakes and make the most of this important transition.

Ready to talk through your 401(k) rollover?

Schedule a free 20-minute call — no obligation, just straight answers.

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