7 key differences between a Roth 401(k) and a Roth IRA

SAMMONS RETIREMENT SOLUTIONS®

Roth 401(k)s and Roth IRAs share the ultimate goal of tax-free distributions of earnings. While both of these accounts are funded with amounts that have already been taxed, the path to that tax-free goal is paved with different rules for each of these two types of accounts.

Contribution limit

The contribution limit for a Roth 401(k) is more than three times higher than the contribution limit for a Roth IRA. Contributions to a Roth 401(k) and the Roth IRA do not affect each other. Therefore, an individual can make the maximum contribution amount to both accounts if eligible.

Income limits

Roth 401(k) contributions are not subject to any income limits. On the other hand, an individual is eligible to make a contribution to a Roth IRA only if that individual's modified adjusted gross income (MAGI) is below certain amounts. This MAGI is based on the individual's tax filing status, and the amounts may vary by tax year.

Availability

Access to a Roth 401(k) is dependent upon availability through an employer. An individual may not establish a Roth 401(k) plan independently, and must instead rely on an employer to provide access to such an account. Anyone can establish a Roth IRA.

Required minimum distribution

Because Roth 401(k) accounts are subject to required minimum distribution (RMD) rules, you must take your first RMD by the applicable age as set forth by the Internal Revenue Code unless the plan allows RMDs to be deferred past the applicable age until retirement. Roth 401(k) beneficiaries are also subject to RMD rules.

Roth IRA owners are not subject to RMD rules. Roth IRA beneficiaries are subject to RMD rules. An exception applies to spouse beneficiaries who transfer the inherited assets to their own Roth IRAs.

Tip on avoiding Roth 401(k) RMDs:
An individual who does not want to take RMDs from a Roth 401(k) may roll over those assets to a Roth IRA, since Roth IRA owners are not subject to RMD rules. If any RMD is due for the year in which the rollover occurs, that RMD must be taken before the rollover.

Qualified distribution definition and the 5-year rule

Qualified distributions from a Roth 401(k) or a Roth IRA are tax-free and penalty-free. Non-qualified distributions may be subject to income taxes and a 10% early distribution penalty on any taxable amount. The 10% early distribution penalty does not apply if the distribution occurs on or after the date on which the account owner reaches age 59½, or if an exception to the penalty applies.

Qualified distribution definition - A distribution from a Roth 401(k) is qualified if it meets the following two requirements:

1. **The individual has had the Roth 401(k) for at least five years, and**
2. **Is either;**
    - Age 59½ at the time the distribution is made,
    - Disabled,
    - Deceased, in which case the distribution would be taken by a beneficiary.

Roth IRA distributions must also meet these requirements in order to be qualified, but there are two different distinctions.

- The five-year rule for a Roth IRA is determined on an aggregate basis, whereas the five-year period for Roth 401(k)s is determined on a per-employer-plan basis (see below).
- For the second option, a distribution from a Roth IRA is also considered qualified if the five-year period has been met and the distribution is taken for first-time homebuyer purposes. This is subject to a lifetime limit of $10,000.

Continued …

Defining the 5-year period for a qualified distribution

When determining whether or not the five-year period has been met, each of an individual's Roth 401(k) accounts must independently meet this requirement. An exception applies when two Roth 401(k) accounts under different employer plans are combined. Under this exception, if one Roth 401(k) is moved to another using the direct rollover method, the five-year period starts with the Roth 401(k) that was first established and funded. On the other hand, if the movement is done using the indirect rollover method, the five-year period starts when the receiving Roth 401(k) was established and funded.

For Roth IRAs, this five-year period starts with the individual's first Roth IRA.

Recharacterization option: Recharacterization occurs when a contribution is changed from a traditional to a Roth or vice versa. A recharacterization must be done by the individual's tax filing due date plus extension, and must include any net income attributable to the transaction being recharacterized.

Once an individual makes an election to treat an elective contribution as a Roth 401(k) contribution, that election is irrevocable. As such, contributions to a Roth 401(k) may not be recharacterized.

A contribution to a Roth IRA can be recharacterized to a traditional IRA contribution and vice versa.

Reminder: A contribution should be recharacterized to a traditional IRA only if the individual has not reached the applicable age as set forth by the Internal Revenue Code by the end of the year for which the contribution is made. This is because individuals are no longer eligible to make regular contributions to traditional IRAs as of such year.

Awareness of the differences can help with choice

While you can potentially make contributions to both of these types of accounts in some cases, an awareness of these differences—and of course any similarities—can help ensure you choose the account with the features that are more suitable. Awareness can also keep you from choosing an account for which you might be ineligible.

Helping you enjoy a life of living well

We know you want to live well and retire well. But in order to do that, you need your retirement funds to last. As a division of Sammons Institutional Group®, Inc., Sammons Retirement Solutions® specializes in portfolio-management solutions, such as mutual fund IRAs, variable annuities, and fixed and fixed index annuities. Annuities are issued by Midland National® Life Insurance Company. Sammons Institutional Group and Midland National are wholly owned subsidiaries of Sammons® Financial Group, Inc. Through this affiliation, we're a trusted partner positioned to stand strong well into the future.

For more than a century, Midland National has stood by their customers—focusing on providing growth, income, and financial protection. Midland National brings their strong history and proven financial track record to each annuity.

Independent rating agencies have awarded the following ratings:

"A+"

A.M. Best[A,B] (Superior) (Second category of 15)
S&P Global Ratings[B,C] (Strong) (Fifth category of 22)
Fitch Ratings[B,D] (Stable) (Fifth category of 19)

Ratings are subject to change.

Let's work together. Now is the time to work with your financial professional to develop a strong retirement plan you believe in. In the meantime, see if your values align with ours and if our simple, innovative, and straightforward solutions may be right for you. Visit srslivewell.com.

Sammons Institutional Group®, Inc., Sammons Financial Network®, LLC., member FINRA, and Midland National® Life Insurance Company do not give tax, legal, or investment advice. Please consult with and rely on your own tax, legal, or investment professional(s). Taxes are payable upon withdrawal of funds, and a 10% IRS penalty may apply to withdrawals prior to age 59½.

Securities distributed by Sammons Financial Network®, LLC., member FINRA. Insurance products are issued by Midland National® Life Insurance Company (West Des Moines, IA). Sammons Institutional Group®, Inc. provides administrative services. Sammons Financial Network®, LLC., Midland National® Life Insurance Company and Sammons Institutional Group®, Inc., are wholly owned subsidiaries of Sammons® Financial Group, Inc. Sammons Retirement Solutions® and Midland Retirement Distributors® are divisions of Sammons Institutional Group®, Inc.

A.M. Best is a large third-party independent reporting and rating company that rates an insurance company on the basis of the company's financial strength, operating performance, and ability to meet its obligations to policyholders. S&P Global Ratings is an independent, third-party rating firm that rates on the basis of financial strength. Fitch Ratings is a global leader in financial information services and credit ratings. Ratings shown reflect the opinions of the rating agencies and are not implied warranties of the company's ability to meet its financial obligations. The above ratings apply to Midland National's financial strength and claims-paying ability. **A)** A.M. Best rating affirmed on August 29, 2023. For the latest rating, access ambest.com. **B)** Awarded to Midland National® as part of Sammons® Financial Group Inc., which consists of Midland National® Life Insurance Company and North American Company for Life and Health Insurance®. **C)** S&P Global Ratings' rating assigned February 26, 2009 and affirmed on May 24, 2023. **D)** Fitch Ratings' rating affirmed an Insurer Financial Strength rating of A+ Stable on November 30, 2023. The rating reflects the organization's strong business profile, low financial leverage, very strong statutory capitalization, and strong operating profitability supported by strong investment performance. For more information access fitchratings.com.

3288770

28998R-Q REV 01-24