<u>ROTH 401(k) CONTRIBUTIONS,</u>
<u>FROM THE PARTICIPANT'S POINT OF VIEW</u>

February, 2017

We are seeing more employers making a Roth option available in their 401(k) and 403(b) plans. So employees must decide --- do they want to save on a pre-tax (tax-deferred) basis or on an after-tax basis? On an after-tax basis, the participant can create an account which (including the investment gains) is forever free of state and federal income taxes, because all of the taxes are instead paid up front as the dollars are contributed to the plan.

The employee will have to consider a number of factors:

1) Does he expect his marginal tax rate in retirement to be higher than it is today? If so, then Roth 401(k) contributions may make sense. This may happen for several reasons, including:
   a. The individual is already at a high marginal tax rate and feels that in retirement the rates be even higher in order for the U.S. government to meet all its obligations.
   b. The individual might, for example, be a young professional who has every reason to believe that later in life, and even in retirement, he'll be in a higher tax bracket than he is today.
   c. If the participant is experiencing an unusually low marginal tax rate (high deductions, small business write-offs, etc.) compared to what he expects in later years, there may be a one-time opportunity to use the Roth 401(k) account.

2) There are certain estate planning advantages, especially since the required minimum distributions after age 70 ½ do not apply to withdrawals from a Roth 401(k) account that is rolled into a Roth IRA at retirement.

3) What state will he retire in? Some states have no income tax on *retiree* income from qualified plans and pensions. Some states have no income tax *at all*. (In Kentucky, the state exempts the first $41,100 from tax if it comes from qualified retirement plans or IRAs.)

4) If an individual contributes to a Roth 401(k) account now, he has to come up with the cash to pay the tax now. Is that feasible?

5) If cash is available to *maximize* a Roth 401(k) contribution ($18,000 for 2017, plus another $6,000 for someone age 50 or above by year-end) and pay the taxes now, then if the employee chooses <u>*not*</u> to make a Roth 401(k) contribution he needs to decide how to invest the tax savings outside of the plan.

6) A little known fact is that, under some circumstances, if income from retirement plans and IRAs is high enough, Social Security benefits can be scaled back. However, withdrawals from a Roth IRA do <u>*not*</u> come into play in this calculation.

7) Some argue that an individual should pay the tax now, while he can more readily afford it.

8) Some advisors suggest that once you have both a Roth 401(k) and other 401(k) assets, then you should put the more aggressive investments in the Roth account.

9) With a Roth account, an individual may not have control over this year's taxes; but in retirement, when taking money out of a tax-deferred account, he might actually have some control, allowing him to "time" the withdrawal from taxable accounts.

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