Retirement Savings Vehicles

1. Introduction

If you ask yourself why it's important to invest, one of the answers may well be a comfortable retirement. To ensure your retirement matches or comes close to the way you want to live, you will need sources of income. For the average worker, Social Security retirement benefits replace about 40 percent of pre-retirement earnings—and fewer workers today collect monthly pension benefits from a former employer. Fortunately, Congress has created a variety of specialized retirement savings plans to help.

These plans are designed specifically to help you set aside money for your retirement—for living expenses and to pay for the things you want to do when you have the time to do them, such as traveling or learning new skills.

The chief benefit of these retirement plans is the substantial tax advantages they offer—specifically, the potential for tax-deferred or tax-free growth. **Tax-deferred** means you postpone taxes until you withdraw money later on. **Tax-free** means you owe no tax on your investment earnings at all, provided you follow the rules for withdrawing.

In exchange for these tax benefits, there are certain restrictions. For instance, the amount you can contribute to these retirement plans each year is capped, though the limits have regularly increased to encourage savings and keep pace with living costs. In addition, you generally must reach a certain age before you can withdraw your money without penalty. And many of the plans require withdrawals once you reach a specific age—whether or not you actually need the money at the time. For example, if you're using a tax-deferred plan to save for your retirement, you must begin withdrawing at least a certain amount of your savings (what the Internal Revenue Service calls your required minimum withdrawal) by the time you reach age 70½.

Although the various plans have the same ultimate objective—helping you save money for your retirement—they are structured differently. With some plans, especially individual retirement arrangements (IRAs), you must take the initiative to enroll. With others, most commonly employer-sponsored plans, you might be automatically enrolled, putting you on the path to retirement saving unless you decide to opt out.

If you work for a small company or you're self-employed, there's another set of retirement plans such as a Simplified Employee Pension, or SEP, which makes it possible for you to invest for the future. These plans share certain characteristics of individual plans, such as a choice of investments, and some share certain features of larger employer-sponsored plans, such as matching contributions.

Regardless of the plan you're part of—and there may be more than one—participating in retirement savings plans may make the difference between a retirement that's secure and one that is not.

2. Individual Plans

Individual retirement plans, as the name suggests, are accounts you open on your own, separately from a plan your employer might sponsor. With an individual plan, you decide where and how to invest. This includes decisions about your asset allocation, which means spreading your investments among different asset classes, such as stocks, bonds, cash and other investment categories. You must also decide how to diversify your investments within each class to help reduce investment risk, and decide when to sell one investment and buy another one.

When you're ready to stop working and start withdrawing, the value of your account depends on how much you've invested, the investments you chose and how those investments performed. The design of individual plans gives you a lot of authority to make decisions, but also the responsibility for making good ones. That's one of the reasons you might decide to work with an investment professional who has the expertise to help you make these decisions.

IRAs

Perhaps the most widely known personal retirement plan is the individual retirement arrangement (IRA). An IRA may be either an individual retirement account you establish with a financial services company—such as a bank, brokerage firm or mutual fund company—or an individual retirement annuity that's available through an insurance company. Certain retirement plans, including a simplified employee pension (SEP) and a SIMPLE (Savings Incentive Match Plan for Employees of Small Employers) may be set up as IRAs, though they operate a little differently from those you set up yourself. There's more about them in the "Small Business Plans" section below and in IRS Publication 590.

Your IRA provider acts as custodian for your account, investing the money as you direct, and providing regular updates on your account value. Once your account is open, you can select any of the investments available through the custodian. In fact, one of the things to think about in choosing a custodian is the type of investments you are planning to make.

To participate in an IRA, you must earn income, and you can contribute up to the annual limit that Congress sets. That cap is $5,500 in 2017. In addition, if you're 50 or older, you can make an additional catch-up contribution of $1,000 per year. This cap refers to **total** IRA contributions, not to each IRA you may choose to fund. Also, you can't contribute more than you earn. So, for example, if your total earned income is $2,500 for the year, that's the amount you can put into an IRA. If you're divorced, you can count alimony as earned income. And there's an exception to the earned income requirement for nonearning spouses, called a spousal IRA.

You can put money into your IRA every year you're eligible, even if you are also enrolled in another kind of retirement savings plan through your employer. If both you and your spouse earn income, each of you can contribute to your own IRA, up to the annual limit. All IRA contributions for a calendar year must be made in full by the time you file your tax return for that year—typically April 15, unless that deadline falls on a weekend. It may be smarter to spread out your contributions over the year, though, on a regular schedule. That way you don't have to struggle to pull together the whole amount just before the deadline, or risk putting in less money than you are entitled to contribute. Another reason to spread out your contributions over the year is it allows you to take advantage of dollar-cost averaging, a technique that uses regular contributions instead of lump sum investments to manage risk.

When IRAs were first introduced, there was just one basic type, which was open to anyone with earned income. But since then, IRAs have evolved to include a number of variations:

- **Traditional:** There are two categories of tax-deferred traditional IRAs: deductible and nondeductible. If you qualify to deduct your contributions, you can subtract the amount you contribute when you file your tax return for the year, reducing the income tax you owe. If you don't qualify to deduct, the contribution is made with after-tax income.

  Whether you qualify for the deduction, and the amount of your deduction, will depend on your modified adjusted gross income—your income after certain deductions are subtracted--and whether you or your spouse are eligible to participate in employer-sponsored retirement plans through your jobs. Income limitations for a given tax year can be found on the IRS website.

  Earnings on investments in a traditional IRA are tax-deferred for as long as they stay in your account. When you take money out—which you can do without penalty when you turn 59½, and are required to begin doing once you turn 70½—your withdrawal is considered regular income so you'll owe income tax on the earnings at your current rate. If you deducted your contribution, tax is due on your entire withdrawal. If you didn't, tax is due only on the portion that comes from earnings. You can't contribute any additional amounts to a traditional IRA once you turn 70½, even if you're still working.

- **Roth:** Contributions to a Roth IRA are always made with after-tax income, but the earnings are tax-free if you follow the rules for withdrawals: You must be at least 59½ and your account must have been open at least five years. What's more, with a Roth IRA you're not required to withdraw your money at any age—you can pass the entire account on to your heirs if you choose. And you can continue to contribute to a Roth as long as you have earned income, no matter how old you are. Contribution levels for a Roth are the same as those for a traditional IRA in 2017: you can contribute $5,500; if you're 50 or older, you can make an additional catch-up contribution of $1,000.

  However, there are income restrictions associated with contributing to a Roth IRA, which are updated each year and can be found on the IRS website.

  If you're eligible for a partial Roth contribution based on your income, you can put the balance of the $5,500 in a traditional IRA, and you might qualify to deduct that portion.

Which Is Better: Traditional vs. Roth IRA?

The answer to this question will vary from person to person. Assuming you're eligible for either a deductible, traditional IRA or a Roth IRA, here are some factors to consider:

- **Current-year tax benefits**—Depending on your income and employment, contributions to a traditional IRA may be tax deductible, which reduces your taxable income each year you contribute. But if you don't need that tax break now, a Roth IRA can give you more flexibility since you can withdraw your contributions at any time without paying taxes or fees—and you can withdraw your earnings tax-free if your account has been open at least five years and you are 59½ or older.

- **Likely future tax bracket**—If you're young and likely to be in a higher tax bracket when you retire, then a Roth IRA may make more sense. But if you're likely to be in a lower tax bracket after you retire, a traditional IRA is usually the better choice. With a traditional IRA, however, you are subject to minimum required distributions when you reach age 70½.

- **Spousal IRA:** If you're married to someone who doesn't earn income (for example, if your spouse stays home with small children), you can contribute up to the annual limit in a separate spousal IRA in that person's name as well as putting money into your own IRA.

  Your spouse owns the spousal IRA, chooses the investments and eventually makes the withdrawals. A spousal IRA can be a traditional deductible, traditional nondeductible or a Roth IRA, as long as you qualify for the type you select.

- **Deemed or "Sidecar" IRAs:** In some cases, you can make contributions to an IRA through your employer by taking advantage of a deemed or "sidecar" IRA provision.

  In this case, your employer deducts your IRA contributions from your after-tax earnings. All the rules for this account—that is, for contribution limits, withdrawal rules and so forth—are the same as for any other IRA. If you qualify, you may be able to deduct your contribution when you file your tax return.

  You might find a deemed IRA helps you to save. After all, contributions are automatic, so you don't have to remember to write a separate check to your IRA custodian, and you won't be tempted to spend the money on something else. But you might also find that your choices of IRA investments are limited with this option, since they will depend on which financial services company your employer chooses as custodian or trustee of the account.

In addition, if you're not keeping accurate records of your deemed IRA contributions, you might inadvertently go over the contribution limit, which remains the same no matter how many separate IRA accounts you have. That could mean incurring penalties.

- ***my*RA:** This is a type of Roth IRA developed by the United States Department of the Treasury that invests in a United States Treasury retirement savings bond, which will not lose money. Money earns interest until your account reaches $15,000 or 30 years from the day you first fund the account (whichever comes first). At that point, your account balance is transferred to a private-sector Roth IRA, where you can continue to invest your savings and make additional contributions. You can also transfer or roll over your *my*RA to a private-sector Roth IRA of your choice at any time.

  *my*RA accounts cost nothing to open, have no fees, and don't require a minimum amount of savings. The same income limits apply to contributing to a *my*RA as apply to a Roth IRA. While you are allowed to contribute to a *my*RA even if you have access to an employer-sponsored plan, be aware that *my*RA was designed for people who don't have access to such plans and haven't yet started saving for retirement. Also, consider whether the plan available through your workplace offers matching contributions.

Taking Money Out

One important thing is true of all IRAs: Taking out money early is discouraged. In fact, you generally cannot make IRA withdrawals before age 59½ without paying an early withdrawal penalty. The penalty is 10 percent of the amount you withdraw.

There are exceptions, however, if you take IRA money out to meet certain medical expenses, purchase your first home, pay college tuition bills or for certain other reasons listed in the federal tax laws. In any event, before you make any early IRA withdrawals, you should check with your tax or legal adviser to be sure you're following the rules. Even if you do not face a penalty, you will have to pay income tax on any withdrawal you make. The only exception is that you can take up to $10,000 in earnings from your Roth IRA tax-free to buy a first home for yourself or a member of your immediate family, provided you have had the Roth for at least five years.

There is a reason withdrawing early from your IRA comes with penalties. These savings vehicles are specifically designed to help you set aside money for retirement, not for other purposes. By imposing penalties for the early use of these funds, the government hopes that most people will leave their money alone. That way, the money will have time to compound, and will be available to support you in your retirement.

You should also note that unlike certain employer plans, you're not allowed to borrow against your IRA balance.

Required Withdrawals

Just as the IRA rules generally discourage you from taking your money out too early, other rules require that you begin withdrawing from a traditional IRA no later than April 1 of the year following the year in which you turn 70½. And once you do start taking money out, you must take at least your required minimum distribution, or RMD, every year. You're always free to take more than the minimum, but you must take at least that amount, or risk paying a penalty.

Example: You turned 70½ on July 15, 2016. That means you must take your first RMD (for tax year 2016) by April 1, 2017. You must take your second RMD, for 2016, by December 31, 2017, and your third RMD, for 2018, by December 31, 2018—and so on. If you prefer not to take two RMDs during 2017, the IRS will allow you to take your first RMD before December 31, 2016.

Your RMD is calculated based on your age and your annual IRA account balance. To do the calculation, you divide the balance at the end of the year by a number you find in Table III of IRS Publication 590, called the Uniform Lifetime Table. The number you use is the one that corresponds to your age in the year you're making the withdrawal.

Example: You are 72 years old in 2017 and your wife is not more than 10 years younger than you. To figure out your RMD for this year (2017), divide the value of each IRA you own as of December 31 of last year (2016) by the distribution figure found in the appropriate IRS worksheet referenced above. For instance, if an IRA amount at the end of 2016 is $100,000, you would divide $100,000 by 25.6 (which comes from the IRS Uniform Lifetime Worksheet), for an RMD for that IRA of $3,906.25.

However, if you name your spouse as the beneficiary of your IRA and he or she is more than ten years younger than you are, you can use Table II in Publication 590. You find the point in the table where your age and your spouse's age intersect and that's the number you use as the divisor. It will always be higher than the number for your age in the uniform table, which means you will be required to withdraw less each year.

If you fail to keep up with your RMDs, you face a penalty that can be pretty steep: up to 50 percent of the amount you should have withdrawn but didn't, plus the income taxes you would have owed on that amount. Don't assume that if your IRA is invested in mutual funds, and you're receiving distributions from those funds, that you've automatically satisfied your RMD. It could happen, but you can't count on it.

However, if your IRA is an individual retirement annuity, which you would set up with an annuity provider such as an insurance company, your annuity provider assumes the responsibility for ensuring that the income you receive from your annuity meets your RMD.

IRA Rollovers

There are penalties for withdrawing from your IRA before 59½, but there are no penalties for transferring your account from one custodian to another. You might want to do that for several reasons: to be able to make different types of investments, to consolidate several IRAs with a single financial services company or perhaps simply because you move across the country.

In most cases, you roll over a traditional IRA to another traditional IRA and a Roth IRA to a Roth IRA.

There are specific guidelines for handling rollovers. Normally, the easiest way is a direct rollover: You ask your current IRA custodian to transfer the money directly to another custodian where you already have an IRA—either a previously existing one or one you've just opened. Once you fill out the authorization forms, the money will be moved electronically to the investments you have selected in the new account—though not instantly. It may take days or even weeks for the transaction to take effect and you'll want to follow up to be sure that the transfer has actually been completed and the money invested as you've directed.

A direct rollover isn't the only way to handle moving your IRA assets. You can ask for a check for the amount to be rolled over and complete the transaction on your own. But you must deposit the full amount into the new IRA within 60 days. If you don't, regardless of the reason, the IRS considers the money an early withdrawal, so taxes are due as well as a potential 10 percent penalty if you're younger than 59½. What's more, that amount can never be deposited in a tax-deferred account again.

You may also choose to convert a traditional IRA to a Roth IRA. When you convert a tax-deferred IRA to a Roth IRA, all tax-deductible contributions, plus the earnings they've generated, are added to your gross income and taxed at your regular income tax rate. So if you've accumulated a substantial amount in the IRA you're moving, you could face a hefty tax bill.

If you're thinking about moving your assets to a Roth IRA, you should consult your tax adviser to be sure it is appropriate for you. One thing you'll want to consider is how you'll pay the taxes. In most cases, the benefits of converting tax-deferred accounts to a Roth are only realized if the taxes are paid from savings or investments *outside* the retirement fund itself.

Pulling the tax payment from your rollover could be more costly for younger investors. If you are younger than 59½ years old, you could receive a 10 percent early withdrawal tax penalty if the full conversion amount is not deposited in your new Roth account within 60 days.

Another factor is whether you'll keep the Roth IRA open at least five years. If that doesn't seem likely, making the switch is probably not a good idea because you'll owe tax again on the withdrawals since the tax-free withdrawal provisions won't apply.

IRA Beneficiaries

When you open an IRA, you should name a beneficiary for your account. A beneficiary is the person you want to receive the assets you have accumulated when you die. If your IRA custodian permits it, you might also name contingent or secondary beneficiaries—essentially, back-up heirs in case something happens to your first choice, or that person chooses not to take the money. For example, you might name your spouse as primary beneficiary and your children as contingent beneficiaries.

What If You Are a Beneficiary?

If you inherit an IRA, you must take RMDs over your lifetime. When you must start withdrawing depends on whether or not you were married to the owner of the IRA, and whether or not the owner had begun taking RMDs. You can find the information you need in IRS Publication 590, and it's always a good idea to get legal and tax advice, especially if you're uncertain about the rules.

Tax-Deferred Annuities

If you are maxing out on contributions to an employer-provided retirement savings plan, and if you've contributed all you can to an IRA, you might also consider saving for retirement with a nonqualified deferred annuity. Nonqualified here simply means that you purchase the annuity on your own as opposed to selecting one that's offered in a qualified employer plan.

A tax-deferred annuity lets you postpone tax on any earnings as they accumulate and pay tax at your regular rate on withdrawals. However, since you buy the annuity with after-tax dollars, the portion of your withdrawal that comes from your premiums isn't taxed. Like IRAs, there's an early withdrawal penalty if you take money out before you reach 59½—though there may be a provision in your contract allowing you to take a small percentage each year penalty free.

Unlike IRAs, however, you can contribute money from any source to a nonqualified annuity, including investment income or an inheritance. You can put in any amount you can afford, usually up to $1 million per contract—though few people approach that limit.

You can choose a fixed annuity, which means that the insurance company offering the contract guarantees the earnings at a specific rate, subject to the company's ability to meet its obligations. Or, if you prefer, you can choose a variable annuity. In this case, your earnings from the annuity depend on the investment performance of the underlying securities held in the investment funds (also called subaccounts) that you select from among those offered in your contract. As the term "variable" implies, the rate at which you accumulate earnings will depend upon the performance of the underlying investments.

One drawback to tax-deferred annuities, and variable annuities in particular, is that the annual fees for these products may be higher than those for an IRA invested in mutual funds or individual investments, such as stocks and bonds.

3. Employer-Sponsored Plans

Many employers offer retirement savings plans as part of their employee benefits package. Sometimes the employer puts in all of the money that goes into these plans, but more often the employee makes the primary contribution by contributing a portion of his or her current salary.

These savings plans are known as defined contribution plans. What that means is that the amount of money going into the plan—the contribution—is determined, or defined, by a particular formula and is restricted by an annual cap. The retirement income the plan provides is determined by the amount that was contributed, how the money was invested and the return those investments provide over time.

Defined contribution plans are increasingly replacing defined benefit plans, better known as pensions. Where a defined benefit plan is offered, the employer generally has full responsibility for putting money into the plan—an amount typically determined by a formula—and investing that money to provide a retirement income, often calculated as a percentage of your final income.

Defined contribution plans vary, not only by type of plan, but by employer. But they all share some specific characteristics.

Tax Advantages

Employer-sponsored retirement plans all have significant tax advantages. Traditional plans, which are the most common, are funded with pretax contributions. This means the money you put into the plan reduces your current taxable salary, and therefore the income tax you owe now. For instance, if your gross income is $55,000 a year and you defer $4,500 to a traditional 401(k), the income that your employer reports to the IRS is $50,500.

In addition, all the earnings in the account are also tax-deferred. That applies to any capital gains you might have from selling an investment in the account that has gained in value. In fact, you don’t owe any income tax until you withdraw from your account, typically after you retire. At that point, the tax is due at the same rate as you’re paying on your other income. But, by then, compounding generally has allowed you to accumulate substantially more than you would have in a similarly invested taxable account if you’d had to withdraw every year to pay the income tax that was due.

For example, let’s say you choose not to participate in the 401(k), but instead invest $4,500 in a taxable account. Your income tax for the year will be higher since your reported income is still $55,000—and not the $50,500 that would have been reported had you contributed the $4,500 to a 401(k). In addition, if your taxable investment account provides dividends or interest income, you’ll owe tax on those amounts each year—though the rate on the dividends may be lower than your regular rate.

Some employer plans—specifically 401(k)s and 403(b)s—also offer a tax-free alternative, called a Roth 401(k) or a Roth 403(b). If you choose to participate in these plans, your contribution is not tax-deferred and it doesn’t reduce your current income tax. But if your account is open at least five years and you’re at least 59½ when you retire, all your withdrawals are tax-free. (Any employer matching funds, however, will be taxed upon withdrawal because IRS rules require that all matched funds reside in a pre-tax account.)

If you prefer, you can divide your contribution between a traditional and a Roth account, in whatever proportion your plan allows. The one thing you can’t do is move money back and forth between a traditional and Roth 401(k).

Self-Direction

When you participate in a defined contribution plan such as a 401(k) or 403(b), you decide how to invest the money you’re contributing. Your employer is responsible for choosing the investment alternatives offered, but you’re responsible for putting together your portfolio by selecting among them. That’s why these plans are described as self-directed.

A plan menu is likely to include a variety of mutual funds, perhaps some exchange traded funds (ETFs), managed accounts, a real estate portfolio, a variety of fixed-income alternatives and perhaps fixed or variable annuities. Some types of plans also offer what’s known as a brokerage window, which is a brokerage account through which you can select stocks, bonds and other investments. Finally, some corporate plans offer stock in the sponsoring company.

Once you’ve chosen the investments you want, you must also decide what percentage of your total contribution will go into each one each pay period. That’s a process called asset allocation, and it’s an important component to reaching your investment and retirement goals.

Another component is diversification. A sound investing strategy includes a plan to have a mix of different investments—both within and among each of the various asset classes. You don't want to be too heavily concentrated in any one investment type. For example, if your employer offers a dozen stock funds and you choose three, you want to be sure that the funds invest in different types of stock, such as mid- and large company stock or perhaps international stock. And if your company makes its own shares available to purchase for your 401(k) portfolio, you can diversify by limiting the percentage of company stock in your total portfolio.

Your plan may offer a set of target date or lifecycle funds as part of the investment menu. Each of these funds is designed for employees whose projected retirement date corresponds to the date in the fund's name—such as Fund 2025 or Fund 2035. The appeal of these funds is that the individual funds that are included are preselected, reducing your responsibility for allocating your assets and diversifying your portfolio. In addition, the allocation of fund assets gradually adjusts from investments designed for growth to investments designed to produce income as the date in the name draws closer.

Matching Contributions

A match is what it sounds like: For every $X you contribute to your retirement savings plan, your employer will contribute an additional $Y. Some employers voluntarily offer a match. Other employers—like those offering a SIMPLE plan or a money-purchase plan, both of which are discussed in the next section—are required to provide a match. And still others, notably state and local government employers who offer 457 plans, are not permitted to make matching contributions.

When an employer matches your contribution, the amount of the match is based on a specific formula. A typical match is 50 percent of the amount you contribute, up to 5 percent of your salary. So, if you are earning $45,000 and contribute 5 percent of that amount, or $2,250, during the year, your employer would add $1,125 to your account. If you contributed 10 percent of your gross salary, or $4,500, your employer's match would still be $1,125, or 50 percent of 5 percent of your earnings.

If your employer matches contributions, it's smart to contribute at least enough to qualify for the full match. Otherwise, you're throwing away free money, since you're not taxed on your employer's contributions or any earnings those contributions generate until you withdraw from your account. Of course, you can contribute more than the amount that will be matched. In fact, you may want to put away as much as you possibly can each year up to the maximum allowed by the IRS to build up your retirement account.

In some cases, your employer may limit your contribution to a percentage of your salary—say 15 percent—which may mean putting in less than the federal cap. Your plan administrator will provide you with that information if it applies.

As noted earlier, if you participate in a Roth 401(k) or a Roth 403(b) and your employer matches your contribution, those contributions will go into a traditional tax-deferred account. This means the matching funds and their earnings will be taxed as ordinary income when you withdraw them. You still have the right to decide how the matching funds are invested.

Vesting

Vesting is the amount of time you have to work for an employer to be entitled to benefits from a retirement plan. One advantage of a retirement savings plan is that all the money you contribute to it is yours from the moment you put it in, and so are any earnings those contributions generate.

However, you must stay at your job long enough to be able to benefit from the matching contributions your employer makes and the earnings those assets provide. Your plan administrator will tell you how long that period is, though the maximum is six years if vesting is gradual and five years if is not. If you're considering a new job, you may want to think about how close you are to being vested in your old one. It might pay to wait a few months before making a change if a sizeable amount of money is involved.

Portability

Unlike traditional defined-benefit pensions, employer-sponsored retirement savings plans are portable. This means you can take your money with you if you leave your job. You always have the choice of rolling these assets into an IRA, where they continue to have the same tax-deferred growth as your employer-sponsored plan. Or you may be able to move some or all of the money in your account to a new employer's plan if the plan accepts transfers. The advantage is that you don't lose any momentum toward building your retirement account.

Rolling over your 401(k) to an IRA is very similar to moving one IRA to another. You open the account where you want the money to go and notify your plan administrator. Typically, the assets in your account are liquidated and the value is transferred electronically to your new custodian. There may be a delay; this is something you should ask about at the time you authorize the transfer.

While generally not recommended, you can choose to move the money yourself, by asking your plan administrator to write a check to you for the value of your account. You have 60 days to deposit the money from a 401(k) into your rollover

IRA. However, by law, 20 percent of what you're moving must be withheld to pay the taxes that will be due if you don't complete the rollover. Any amount—including the 20 percent that was withheld—that you don't put in the rollover IRA within the time limit is considered an early withdrawal, subject to tax and potentially subject to penalties if you're younger than 59½. To avoid the tax and penalties, you'll have to use money from a savings account or other source to make the full deposit. That's why a direct transfer is often the better choice.

You also have the option of leaving your account with your old employer if its value is $5,000 or more. You might want to do that if the plan is a good one and your new employer doesn't offer anything comparable. If your account value is between $1,000 and $5,000, and you haven't told your former employer how you want the account to be handled, the employer has the right to roll it into an IRA with a financial services company that it chooses. It's probably smarter to pick your own IRA custodian directly.

If your account value is less than $1,000, your employer may cash you out by sending you a check for that amount, less 20 percent that must be withheld to pay the tax that's due on what counts as a withdrawal. You have the right to roll that amount into an IRA, and, if you add the missing 20 percent when you deposit the check you receive, the entire amount remains tax-deferred.

What you probably don't want to do is take the money in your employer plan as cash when you change jobs. Not only will a percentage go to the government in taxes and, potentially, an early withdrawal penalty as well, but you'll be back to square one in setting aside money for retirement.

Taking Withdrawals

You normally can't withdraw from your employer-sponsored retirement savings plan before you retire, even if you are 59½ and could withdraw without a tax penalty.

Your employer will typically offer several alternatives for receiving income, and you can choose the one that you believe will work best for you. You'll receive a document explaining what your options are, and you can either consult with a retirement adviser that your employer provides, or consult one on your own. Among the alternatives may be a lifetime payout, which is similar to a traditional pension, or a lump-sum distribution.

You also have the right to roll over the assets in your account to an IRA, exactly as you do when you change jobs. You might make this choice if you want to postpone taking income or if you want more control over how your money is invested.

Potential Drawbacks of Employer-Sponsored Plans

Along with their advantages, employer-sponsored plans have a few potential disadvantages.

- The plan provider that your employer selects may offer a more limited menu of investments than you would prefer, or the fees may be higher than other providers.

- You may not be eligible to participate right away, as some employers require that you work at their organization for a certain amount of time, such as one year, before you are eligible to enroll.

- Plans might require you to pay some of the administrative costs of 401(k) participation.

Still, the clear-cut benefits of employer-sponsored plans spur many people to participate in them—in fact, some employers even automatically enroll their eligible employees, although those workers can always opt out of participating.

Specific Plans

Employers may sponsor different types of retirement plans, though they normally share many of the same characteristics.

401(k) Plans

Businesses and nonprofit organizations can sponsor 401(k) plans. An employer may offer just a traditional plan or both a traditional 401(k) and a Roth 401(k). Each employer's plan differs in some ways from other plans, but the basic elements are essentially the same. Among the most important are that contributions are deducted directly from your earnings and deposited into your account, you select the investments from the menu your plan provides and you enjoy tax benefits for participating.

Some employers now offer plans with automatic features, including enrollment at pre-set contribution levels into a pre-selected fund. These features can help increase participation rates and allow companies to better help their employees save for retirement. Although automatic features change the defaults so that a new hire doesn't have to remember to sign up, an employee who does not wish to contribute can choose to opt out.

403(b) Plans

Nonprofit employers, including educational institutions, hospitals, museums and foundations, may offer 403(b) plans to their employees. Traditional 403(b)s are tax-deferred salary reduction plans and Roth 403(b)s are tax-free plans to which you contribute after-tax income. These plans resemble 401(k)s in many respects, though they may allow larger catch-up contributions, are less likely to offer matching contributions and their investment menus are typically limited to annuities and mutual funds.

457 Plans

State and local governments may offer 457 plans to their employees. For the most part, these savings vehicles work very much like traditional 401(k)s—they allow you to set aside pretax income in a tax-deferred account. However, there's no Roth version of a 457 plan, and employers do not match contributions. If you're 50 or older, you may have more generous catch-up provisions if you're within three years of the plan's retirement age. Plus, with a 457, you are permitted to make penalty-free withdrawals any time after you retire from your government job, even before you're 59½.

You're able to roll over assets that you accumulate in one type of plan to another. For example, you can move your traditional 401(k) or 403(b) assets to a 457 plan, or vice versa. Your combined assets are subject to the rules of the plan that they're in.

Thrift Savings Plan

If you work for the federal government as a civilian or military employee, you can save for retirement through a Thrift Savings Plan, usually abbreviated as TSP, as part of either the Federal Employees' Retirement System (FERS) or the Civil Service Retirement System (CSRS).

The federal TSP resembles 401(k) plans in many ways. If you have a traditional TSP, you contribute pretax income to your plan through payroll deductions, and your TSP assets grow tax-deferred until retirement, when you start making withdrawals. At that point, you pay taxes at your regular rate on the amounts you withdraw. You can also designate some or all of your contributions as Roth contributions, which are taken out of your paycheck after your income is taxed. When you withdraw contributions and earnings from the Roth balance, you will pay no taxes if you meet holding and age requirements. Your TSP plan assets are portable and your contributions are always 100 percent vested. If you leave your job, you can roll over the money to an IRA.

Similarly, you face withdrawal restrictions. If you're younger than 59½ when you leave your job, you cannot withdraw your traditional or Roth TSP balance without paying a 10 percent penalty. Income taxes are due on the traditional balance unless you qualify for one of the exceptions. If you are 59½ or permanently disabled and the account has been opened at least 5 years, you can withdraw Roth funds tax-free.

You can set aside any percentage of your salary you choose, up to 100 percent, as long as you don't go over the maximum contribution of $18,000 per year in 2017—the same maximum contribution amount as 401(k) plans. If you are a member of the U.S. armed forces and contribute tax-exempt income, separate rules apply, permitting you to put in up to $54,000 in 2017.

If you're a FERS employee, your agency will automatically put an amount equal to 1 percent of your base pay into your TSP account—regardless of whether of you participate in TSP. If you do (and, again, if you are a FERS employee), your agency will match up to 5 percent of the pay you contribute. The match is dollar-for-dollar on the first 3 percent and 50 percent of the next 2 percent. Note that agency matches will always be added to your traditional balance so you will pay taxes when withdrawn. There is no matching for CSRS employees, though their defined benefit plan provides more income than FERS employees receive from their comparable plan. Also, a 2009 law authorized automatic enrollment for new federal civilian employees at a level of 3 percent, which the TSP implemented in 2010.

The major difference between the TSP and a 401(k) is in the type of investments you can make. Customarily, 401(k) plans offer as many investment options as the plan provider chooses to make available—often a dozen or more mutual funds plus fixed-income and other options. Some 401(k) plans even let their participants invest in individual stocks and other securities through a brokerage account, often called a brokerage window, which the participant opens within the plan.

In contrast, TSP participants can allocate their assets among five index fund options, each one identified by a letter, or choose a lifecycle fund, also known as a target-date or "L" fund. The index fund choices are a U.S. Treasury bond fund (the "G" Fund), common stock fund ("C" fund), fixed-income fund ("F" fund), international stock fund ("I" fund) and small-capitalization stock fund ("S" fund).

The L funds are so-called "funds of funds" that combine the five index funds in different mixes to make them appropriate for people whose projected retirement date corresponds most closely to 2020, 2030, 2040 or 2050. There's also an income fund. The combination of funds in each L fund is adjusted regularly, shifting gradually from seeking growth to providing income.

Another difference between the TSP and a 401(k) is the fees that investors typically pay. Few, if any, 401(k) plans offer investment options with lower fees than comparable options available in the TSP.

4. Small Business Plans

If you work for a small company, you may have fewer opportunities to participate in an employer-sponsored retirement plan. In fact, some studies have shown that fewer than 30 percent of full-time workers at small businesses are covered by a retirement plan. But there are some plans that the government has created specifically for these employers.

SIMPLEs

The Savings Incentive Match Plan for Employees, usually called a SIMPLE, is available to companies that employ fewer than 100 people. If your employer offers a SIMPLE and you earn $5,000 or more, you must be included in the plan. Also, your employer must contribute to your account following one of two formulas—either by matching 3 percent of the amount each participating employee contributes, or by contributing 2 percent of each eligible employee's compensation whether or not they participate.

There are two variations of SIMPLEs: the standard SIMPLE IRA and the SIMPLE 401(k). With a SIMPLE IRA, all of the contributions are vested and belong to you from the beginning, so if you leave your job, you can take the money with you. You must, however, wait two years before you can move your account or withdraw any money, or you face a 25 percent penalty on whatever you transfer or take out, which is much steeper than the 10 percent that applies to other employer plans. As the name implies, the SIMPLE 401(k) is set up as a 401(k). So your contributions go into an account that's part of the plan, rather than to an IRA.

In 2017, the contribution limit for both a SIMPLE IRA and SIMPLE 401(k) is $12,500, plus a catch-up contribution of $3,000 if you're 50 or older.

SEPs

If your employer has 25 or fewer employees, your retirement plan may be a Simplified Employee Pension, or SEP, which is an IRA in your name. You're 100 percent vested in all money in your account and you choose the investments from among those offered by the plan provider your employer selects.

You don't contribute. Your employer makes the entire contribution, though the amount may vary from year to year. The annual limit on employer contributions is up to 25 percent of your salary, or $54,000 in 2017, whichever is less. But each eligible employee must be treated the same way. If 25 percent of the boss's salary is added to his or her SEP IRA, then 25 percent of your salary must be added to your account.

Rules on SEP IRA distributions are similar to those for traditional IRAs. Anyone with a SEP is required to start required minimum distributions by age 70½. As with an IRA, you cannot borrow against your account balance. And if you make a SEP withdrawal before age 59½, you'll face a 10 percent penalty and regular income taxes on both the contributions to the account and your investment earnings—just as with a traditional IRA.

Profit-Sharing and Money-Purchase Plans

If your employer has chosen a profit-sharing or money-purchase plan, which are sometimes described as varieties of a Keogh plan, your employer can contribute the full amount to your account, which is up to 25 percent of your salary, or $534000 in 2017, whichever is less.

In a profit-sharing plan, the amount your employer adds each year depends on how well the company has done. The amount could range from $0 to the maximum, but an employer has to contribute to all employees' accounts at the same rate. If the boss gets 25 percent of salary, so do you. If the boss gets 10 percent, you get 10 percent. In a money-purchase plan, your employer is committed to adding a certain percentage of your salary each year—say 5 percent—and can contribute more if it has been a good year.

Distribution rules for these plans are standard. There are penalties for withdrawals before 59½ and mandatory minimum requirements after 70½. You have some flexibility when it comes to account rollovers. For example, you can roll money from other pensions or employer-sponsored retirement accounts into a Keogh. Or, as with a SEP, you can roll the Keogh itself into an IRA, without penalty. And, unlike SEP IRAs and other IRAs, most Keoghs let you borrow from the balance in your account.