Catholic Foundation
1988 - 2016

Can you contribute to both 401k and Roth 401k?

Yes, an individual can contribute to both a 401k and a Roth 401k. The total contribution into both types of deferrals cannot exceed $18,000 for individuals under 50, and $24,000 for those 50 and over. For example, a 30-year-old person could contribute $9,000 into his or her regular 401k and $9,000 into the Roth 401k portion, for a total of $18,000 in 2016.

There are two key factors that should be considered when deciding between making regular 401k contributions vs. Roth 401k contributions—or potentially a combination of both:

- Current taxable income and expected future taxable income
- Discretionary income

Current Taxable Income and Expected Future Taxable Income

Contributing into a regular 401k will help reduce your taxable income: The contributions you make are "pre-tax." Invested assets in these accounts grow tax deferred; the distributions you ultimately take are taxable at ordinary income levels. Making Roth 401k contributions, on the other hand, will not reduce taxable income because contributions are "after-tax." But your investments in a Roth 401k will grow tax free and distributions are tax free as well.

The main reason most individuals contribute to a Roth 401k is they believe tax rates will increase in the future. The thinking here is that contributing into a Roth 401k will help decrease their potential taxes when they start to take distributions from their accounts since distributions from Roth 401ks are tax free.

Discretionary Income

If you're planning to contribute into a Roth 401k (vs. a regular 401k), keep in mind that you will have a higher taxable income at the end of the year. You'll need to budget and have funds available to pay any potential taxes.

Catholic Foundation
1988 - 2016

For example, an individual who earns $100,000 and makes a regular 401k maximum contribution of $18,000 will have a taxable income of $82,000 because regular 401k contributions decrease taxable income. If the same person were to make an $18,000 Roth 401k contribution, he or she would be taxed on $100,000 of taxable income—because these contributions are "after-tax." This would amount to paying approximately $4,500 in additional taxes.

Contributions into Roth 401ks generally favor investors who are younger, with lower taxable incomes. Regular 401k plan contributions favor higher earners because contributions decrease taxable income and allow for individuals to have a higher take-home pay after withholdings.

Please consult your tax advisor before implementing any changes to your 401K.

INVESTOPEDIA
Investing Basics March 24, 2016

Strain, Nickolas

Long Beach, CA

www.halberthargrove.com