Rollovers

We don't stay at our jobs as long as we used to. When you change jobs, you are faced with a choice about your 401(k) money. Do you leave the money where it is, move it to a new 401(k), or move it into an IRA?

Of course, there is a fourth option. You could cash out of plan, but that's an expensive proposition. If you cash out, you'll pay income taxes plus a 10 percent penalty if you're under 59½. You'll also lose out on tax-deferred saving.

So, what's the best option? It's an individual choice, but here are some things to consider.

If you are happy with the plan that you have at your previous employer, consider keeping the money in that plan. This may be the case if you have a large amount of money invested in the plan and the funds are performing well.

Some planners would recommend not leaving any money behind at a previous employer's plan saying that it's a good idea to have all of your money in one location for ease of management and for the opportunity to tap the account for a loan or in case of an emergency. In this case, maybe the best option is to move old 401(k) dollars into your new 401(k).

But, what happens if your new employer doesn't offer a 401(k)? In this case, you can leave the money behind or roll it over into an IRA. If you roll the money into an IRA, you will have greater control of the money and more investment options. Most 401(k) plans have a specific selection of mutual funds to choose from. When you choose an IRA, you can select from thousand of mutual funds. Do keep in mind though, that one of the arguments for keeping your money in a 401(k) is that the money is a little more protected from creditors than money in an IRA. This becomes important if you are sued or choose to file for bankruptcy.

Be smart when you rollover your money to avoid taxes and penalties. When you move your money, you'll want to do what is called a "trustee-to-trustee transfer." This means the money will move from one plan to another without touching your hands. You will direct the new plan management to contact the old plan management to have the money moved. You will have to complete the necessary paperwork.

What happens if the old company plan writes a check to you? It can be costly. Your old company will send you a check less 20 percent for income taxes. That's right, your old company will send you only 80 percent of your money and will withhold 20 percent for tax reasons. If you don't plan on keeping the money and you plan to roll it over into a new plan, you then have 60 days to do that. Here's a catch though. When you take the 80 percent and roll it over, you have to come up with the 20 percent missing out of your own funds because you are required to rollover the entire 100% to avoid penalty. If you do that, you will get the 20% back from your old employer, but not until you file your next tax return. If you don't fund the 20% when you rollover the 80%, you will get hit with a 10% penalty in addition to paying taxes.

The bottom line is that when transferring 401(k) funds to an IRA, always let the financial institution make the check payable directly to the receiving firm "For the Benefit Of" (FBO) — you. This will ensure no taxes are withheld and the money is not out of the market for too much time.

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