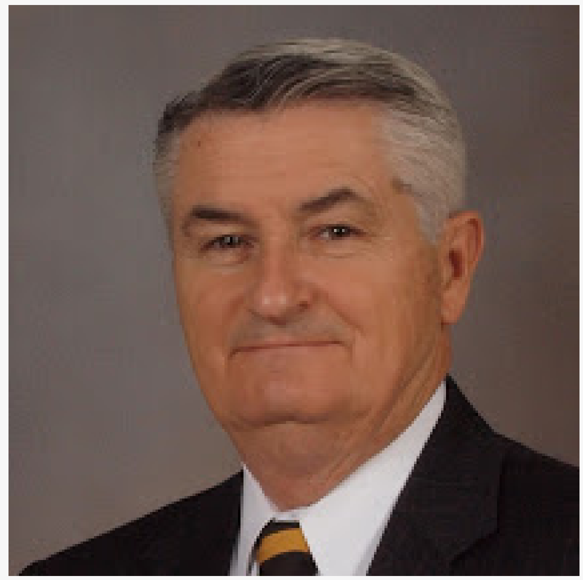
What to Do with Your 401(k) When You Leave a Company According to Jim McEnerney: Part II



KANSAS CITY, KS, UNITED STATES, January 23, 2020 /EINPresswire.com/ -- Welcome back to this two-part article, in which financial whiz Jim McEnerney of the investment advisory firm The McEnerney Group explains what can be done with 401(k) funds that are associated with a previous position. In Part I of this post, McEnerney discussed two of the four options for dealing with an old 401(k): leaving it where it is or moving the funds to your current employer. Today, we're taking a look at the other two options.

Option 3: Indirect Rollovers

What can you do if you don't want to leave your 401(k) where it is, with your former employers, nor transfer the money to an account associated with your current job? A new 401(k) might not even be possible; perhaps you have decided to work as a freelancer or independent contractor, your new employer doesn't offer it, or you're retiring.

An indirect rollover is one way to go, explains Jim McEnerney, but it's a bit (OK, a lot) tricker than its direct counterpart. With this option, you receive a check for the amount in your account, but then you're obliged to take care of moving the funds into the new 401(k) or to an IRA. Fail to do so in a timely fashion, and you'll be on the hook for income tax as well as a 10% penalty tax.

In addition, your former employer will deduct 20% of the distribution for taxes, and therefore you will be responsible for covering the shortfall in order to roll over the entire amount of your assets. You'll get it back come tax time, but it may represent a hardship to part with that much cash even temporarily.

However, Jim McEnerney says, it doesn't really make any sense to take this option if you're moving savings into a new 401(k); there's just too much risk that something will go awry. If you can afford to front yourself that 20%, however, consider establishing an IRA. All of your separate 401(k) retirement accounts, if you have more than one, can go into the IRA. So can future savings. An IRA will also afford you more freedom to invest your money as you wish.

Option 4: Taking a Cash Distribution

Lastly, you can opt to cash in the 401(k). It is a tempting option, to be sure, but it's really a hail mary; unless you are facing a true financial hardship that could be solved with an infusion of cash — we're talking eviction, foreclosure, or repossession here, not "it's been a while since I've had a vacation" or "wouldn't a new Range Rover be nice" — don't even consider a cash distribution.

According to Jim McEnerney, here are a few reasons to avoid this scenario, and they're all very good ones. First, this is your retirement we're talking about here. Even if your financial future is bright, and you anticipate being able to sock away plenty of money to replace your existing 401(k) by the time you are ready to retire, you will still be losing the interest and dividends that your savings are currently reaping.

On top of that, you will have to pay taxes on your funds if you take the cash value. The sudden spike in your "income" may also be significant enough to push you into a higher tax bracket. If you are under the age of 59½ , the IRS will also slap you with a 10% penalty tax. In some situations, you could see the value of your 401(k) plummet, slashed almost in half by taxes and fees when all is said and done. If you truly need the money, you may be willing to forfeit that amount; otherwise, it's just a dumb decision, plain and simple.

Wrapping Up

Naturally, there are many factors to consider when making a decision about an old 401(k) account. No one solution will be right for everyone. Jim McEnerney recommends doing plenty of research, speaking with your financial manager, and exercising caution before making your choice.

No matter which of these alternatives you opt for, be sure you understand all of the potential penalties, tax burdens, requirements, and restrictions. The last thing you want is to pay taxes or face a financial penalty because you rushed through the decision.

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