



## Roll Misplaying

### Seven Costly Mistakes Workers Make When They Leave a Job

By [Robert Powell](#), MarketWatch

Last update: 10:45 a.m. EDT March 16, 2009

*This update of a column originally published March 11 corrects the professional designation for [Aaron Skloff](#).*

**BOSTON (MarketWatch) -- There's many a slip twixt cup and lip. Most people, conventional wisdom might suggest, would roll their entire 401(k) over to an IRA after they leave their employer. But according to data released last week, many workers only roll a portion of their retirement funds into an IRA.**

According to the Employee Benefit Research Institute, those with \$50,000 or more in their 401(k) roll over on average 72.4% of their balance after leaving their employer while those with \$1,000 to \$2,499 in their 401(k) plan roll over on average just 19.5%.

There are plenty of reasons why someone might roll just a portion over to an IRA. But the consequences, in all but a few cases, can be severe. Uncle Sam will tax the distribution at ordinary income rates, plus assess a 10% penalty.

And that, say experts, is just one of seven easily avoided mistakes workers make after they part ways with their employer:

#### **1. Failing to roll**

The first big mistake is, of course, not doing a rollover at all, according to Beverly DeVeny, the IRA Technical Consultant at Ed Slott and Co. If you don't do a rollover, you'll be taxed. Plus, you'll fall even further behind in your attempt to build a nest egg.

#### **2. Forgetting a direct rollover**

DeVeny says plan participants should take direct rollovers in order to avoid the 20% withholding rules. "But, if withholding has been done, you do have 60 days to replace the withheld amount with personal funds and thus roll over the entire plan balance," she said. Make sure you talk to your HR or employee benefit department about your rollover before transferring any money.

#### **3. Failing to account for plan loans**

If you borrowed money from your 401(k) and there's an outstanding balance on your loan when you leave your employer, beware of this scenario playing out. In some cases, your employer will deduct the loan from the total distribution. You can, of course, replace the "paid off" amount with funds from other accounts and then roll over the entire balance.

But if you don't replace the "paid off" amount, Uncle Sam will view the amount of the loan as a taxable distribution. "If the funds are not rolled over, the participant will owe income tax on the loan balance that was paid off," said DeVeny.

Given what's happened to the market of late, there's another worst-case scenario for which there is seemingly no precedent. If a plan balance is no longer large enough to pay off a plan loan it might be time to call in an attorney or two.

#### 4. Leaving money on the table

"Whether you have a 401(k), 403(b), or 457(b), be sure any profit-sharing and matching has been credited to your account before leaving your employer," said Aaron Skloff, a chartered financial analyst with Skloff Financial Group. This is especially true if you have the ability to time your departure from your employer. According to Skloff, profit-sharing and matching contributions typically aren't made on the same schedule as employee contributions.

What's more, consider your vesting schedule. It would be a big mistake to leave before all the money owed you hits your account or before the anniversary date on your vesting schedule. "You don't want to be a creditor of your former employer," said Skloff.

Read Skloff's other tips at this Web site. <http://www.skloff.com/articles.htm>

#### 5. Failing to consider net unrealized appreciation options

In some cases, you might own company stock in your 401(k). And, as hard to believe as it may sound, that stock might be trading above the price you paid, or your cost basis. If that's true for you, consider taking advantage of the net unrealized appreciation rules, said Skloff.

Instead of rolling your entire 401(k) balance over to an IRA, roll everything but your company stock into an IRA. You would then distribute the stock to a taxable account and pay ordinary income tax on the cost basis of the stock. Then later on, if you sell the stock above the cost basis, you would pay a capital gains tax on the appreciated value -- the difference between the sale price and basis.

The rules can be tricky so be sure to consult with a qualified professional before trying this at home.

#### 6. Eschewing a Roth conversion

It's not so much a mistake to avoid as it is a strategy. Yes, the new buzz phrase of the day is something called "tax diversification." You want to have the ability to withdraw money from accounts that provide you with the greatest after-tax amount of money. That means having a traditional IRA and a Roth IRA. So, for instance, if you don't have a Roth IRA, now might be the time to consider it. Consider doing a Roth conversion with all or some of the money in your 401(k), especially, DeVeney said, if there are after-tax dollars in the plan.

#### 7. Other mistakes to avoid

Make sure you open all your mail. "If the plan sends you a check (either by accident or because you requested it), you only have 60 days to roll it over to another tax-deferred account, said DeVeney.

Make sure all your paperwork is in order, said Skloff. In some cases missing the employer's signature on this or that form could result in big tax problems.

*Robert Powell has been a journalist covering personal finance issues for more than 20 years, writing and editing for publications such as The Wall Street Journal, the Financial Times, and Mutual Fund Market News.*