THE DAILY RECORD

August 13 2012 | Volume 123 | Number 216 | Online at TheDailyRecord.com

Changes allow more control over 401(k)s

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While 401(k)s are still where most people keep most of their retirement savings, many of us don't pay much attention to how they are doing until an event like a change in jobs prompts us to take action.

That lackadaisical approach undoubtedly is linked to our busy lives, but it also may have to do with the limited 401(k) choices many companies offer. Many employers reason that if employees have too many investment choices, they will become frustrated and overwhelmed, and employee participation will decline.

Complicating that situation is the fact that declining participation harms highly compensated employees, who are trying to shelter income but cannot contribute to their 401(k), because other employees are not contributing. The ironic result is that employers often respond to this dilemma by reducing employees' investment choices in order to increase employee participation.

Fortunately, recent changes in the law allow most employees to manage their own 401(k) funds or to obtain outside assistance. Individuals also can move their money away from current employers while keeping the same jobs.

That's good news for investors. To take full advantage of these changes in the law, though, individuals can't afford to neglect their 401(k)s. Employees must manage their investments on an ongoing basis. That often can be daunting, because rebalancing the 401(k) portfolio tends to be counterintuitive.

Essentially, you need to sell off asset classes within your portfolio that have outperformed other asset classes for a given period and buy asset classes that have underperformed relative to others. It is really a method of selling high and buying low. Periodic rebalancing reduces risk over long periods of time, but does not guarantee that investment losses will be prevented.

If you don't have the time — and the tolerance for risk — to manage your 401(k), many company 401(k) platforms offer access to advisors who can assist with fund allocation. The good news is that this service is usually free. The downside is that the advisor may simply "advise" — rebalancing the portfolio still may be left up to you.

In addition, you need to recognize that the advisor may be a representative for some or all of the mutual funds in the 401(k). As such, can the advisor truly provide independent advice? Are they evaluating individual needs and building efficient portfolios given each employee's risk tolerance and time horizon, or are they handicapping mutual funds inside of the 401(k)?

Changes in the law also allow employees to go outside of their company to find a wealth manager. This can be done in one of two ways:

- You can use an in-service withdrawal to roll over assets. This allows you to transfer, tax-free, some of your 401(k) funds into an IRA. Obtain advice on the advantages and disadvantages prior to selecting this option.
- You can use a self-directed option within a 401(k). If offered by your employer, this alternative can benefit both the employee and the employer by allowing funds to stay within the company 401(k), but moving them to a separate brokerage account, which gives you access to a different array of investments than those in the 401(k) account.

Alternative investments in a self-directed 401(k) account have become very popular over the past decade and are used extensively by foundations because of their low relative correlation to the stock indices.

Annuities, another option, may have living benefits, thus transferring the downside of investment risk to an insurance company.

In either case, it is essential to select a wealth manager who has the credentials to assist you with advanced planning, including minimizing taxes, improving cash flow, assisting in preventing assets from being unjustly taken, and leaving a legacy to the next generation or a charitable organization. While you will need to pay for these services, it can be done with your pretaxed account, provided you are permitted to do so by your 401(k) or TPA (third party administrator).

Bottom line: don't neglect your 401(k)!

If limited options or indecision on where to allocate funds are causing you to ignore your 401(k), sooner or later that neglect will catch up with you. And your situation won't improve until your funds are properly managed.

So take advantage of the recent changes in the law. Fly solo or obtain outside assistance if you think that will help. But regardless of what option you pursue, don't ignore your 401(k).

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