12 Biggest Mistakes When Doing a Rollover of Your Current Retirement Plan

(And How to Avoid Them…)

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When you have retirement money from a former job or are ready to retire, rolling over those funds can present a number of opportunities to make mistakes. If you have a set of guidelines and preventive touch points you can save yourself from crucial and expensive mistakes.

In this report, we will take you through 12 of the most common mistakes that are associated with moving your retirement accounts from a current or previous employer to an account or accounts that you control.

They call this a "Rollover." Sadly, mistakes are commonly made by either you, the owner of the account, or the financial institutions involved with the transfer or "Rollover" of this important money.

These mistakes are easily avoidable, yet are commonly made. They can be very costly and could easily derail even the best of retirement plans.

While nothing in this report is to be thought of as Financial Advice, Tax Advice or Legal Advice it should at least help to give you the bask of knowledge you need to have to be able to navigate these tricky waters and be able to identify whether or not the people you are dealing with know how to successfully accomplish your specific goals.

If you happen to have any questions or concerns you can contact our office at 816.984.0289 or email us. We'll be happy to either answer them for you or point you in the right direction to address them.

Mistake #1

Missing the 60-Day Rollover Deadline

There is a 60-day window when you want to move money from your retirement plan to an IRA rollover account in a tax-free manner. This window begins when your money is transferred from the original account.

How could it happen to me?

Typically, this happens when you have the money sent to you instead of making a direct "Trustee to Trustee" transfer. The clock starts as soon as the money leaves the financial institution then if you encounter any minor problems, issues or roadblocks that eat up time…all of a sudden that 60 day window has shut! It's not just you, one of the financial institutions could make a mistake. They could put the money into a taxable account instead of a rollover account and you don't discover it until after that 60 day window is shut!

What does that mean to me?

If you didn't successfully complete this transaction within that 60 day window the entire amount of the distribution would be counted as taxable income that year and if you aren't yet 59 ½ there is a 10% penalty on top of that!

Well Kurt, how can I avoid it?

Start by requesting a direct transfer of the money. Make sure you are moving it to a trustworthy custodian. Ask your current plan administration to send the money directly to the new custodian. This will keep you from touching the money and that will take away the chance a check gets lost or you let that 60 day window expire. Another bonus with the direct transfer is your current custodian won't withhold 20% for taxes.

If it happens how do I correct it?

Start with a talk to the IRS. The IRS has gotten softer against missing the 60 day deadline if the delay was caused by the financial institution. You should be able to get a waiver, but you'll have to prove it was their fault. You could get a discretionary waiver if the error was due to something like a death or disability, or even a postal error. This is a big hassle so it is always better to do it correctly the first time!

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Mistake #2

Failing to Name the Correct Beneficiary

Naming the incorrect beneficiary on your account happens to be a common and quite major mistake.

How could it happen to me?
Most people under normal circumstances get this correct, but sometimes with more complex financial affairs people are advised by their estate planning attorney to name their beneficiaries in a specific manner. You could run into problems if the financial institution's form won't allow it. That could cause serious issues.

Sometimes following traditional thinking could have you designate it in a way that could delay or create unnecessary costs in transferring it to your heirs. Another key time to make sure you correctly update it is after a divorce or other major life event. It has happened where an IRA went to the ex-spouse because the beneficiary form was never changed.

What does that mean to me?
The wrong folks inherit your money! Or, your beneficiaries could end up paying unnecessary taxes, unnecessarily go thru probate where everything becomes public, it is delayed and have unnecessary costs. Or it could be ALL of those things! This makes an already stressful time even more stressful for your loved ones!

Well Kurt, how do I avoid it?
Make sure you correctly designate your beneficiaries when you set up your account. When life events happen remember that you should review your beneficiary designations to make sure they are still accurate. Even without life events, it is a good idea to review them annually.

If it happens how do I fix it?
Unfortunately, it is too late for you to do anything about it. Sorry to be morbid here, but it is meant to emphasize the importance of getting it correct while you still can!

Mistake #3

Rolling Over Company Stock

If you move stock you own in your employer (former employer) to your IRA Rollover account along with the rest of your retirement assets it can potentially set you up to pay more taxes later. Typically, if your stock has gone up a lot.

How could it happen to me?
An easy mistake can be made if you don't understand how what you are doing will impact your taxes. Company stock can be taxed at lower Capital Gains rates or at typically higher ordinary income tax rates.

If you move the employer stock out of your retirement plan and move it into a taxable account, when you eventually sell it, your net-unrealized appreciation, which is the amount the stock has appreciated versus what you paid for it will be taxed as a capital gain.

If you move your employer stock to an IRA Rollover Account, all the distributions (the money you take out) are taxed at ordinary income tax rates, typically higher rates.

As you can see, it would be easy to overlook this with company stock and just assume you should roll it all over into the Rollover IRA.

What does that mean to me?
You end up paying taxes at ordinary income tax rates (15% to 39.6%) versus long term Capital Gains rates (15%-20%).

Well Kurt, how can I avoid it?
Make sure you check with your tax advisor if you have employer stock in your retirement plan. As you can tell, this isn't just a simple calculation so make sure you get expert guidance on it. You might want to move it if the net-unrealized appreciation isn't much.

If it happens how do I fix it?
Pretty much the only way to take advantage of capital gains tax rates on employer stock is to keep it from going into the IRA.

Mistake #4

Not Paying Off 401k Loans Before Rollover

If you don't pay off your 401k loan (403b, 457) before rolling over your retirement money it would make the outstanding balance on your loan to be treated as a distribution so you'll pay taxes at your highest marginal tax rate plus, if you aren't yet 59 1/2, an additional 10% penalty for early withdrawal.

How could it happen to me?
It is pretty simple, you borrow money from your 401k plan and either you don't have the money to pay it back or you forget about it.

What does that mean to me?
We touched on this before, it is considered a withdrawal or distribution which is subject to income taxes and penalties.

Well Kurt, how can I avoid it?
Pay off your 401k loans before you do the rollover. If you have to it might make sense to borrow the money from another source.

If it happens how do I fix it?
When you have a loan and request a rollover the plan administrator will subtract the loan amount from the rollover amount..

Say you had $50,000 in your account and a $10,000 loan. The amount of the Rollover would be $40,000 and you'd be taxed on $10,000. If you wanted to avoid taxes, use outside money to pay the $10,000 back by depositing it into the IRA Rollover account within 60 days of the money transferring from the current custodian. At that time you would have "technically" rolled over the full $50,000 and would avoid any taxes or penalties on that loan.

Mistake #5

Taking an Indirect Rollover or "Cashing Out"

If you "Cash Out" your retirement account or take cash through an "indirect rollover" you can be subject to taxes and penalties.

How could it happen to me?
It can be tempting to take some or all of the money out to maybe pay off debts or buy something you've always wanted. Some folks will use it during that 60-day window and replace it before that window closes.

What does that mean to me?
Whenever you get your hands on your retirement money there is a big risk of incurring taxes and penalties on the amount taken out. Any cash you take out for what ever reason (other than putting it ALL into a new IRA account within the 60 day window) will be considered a taxable distribution which is reportable on your tax return!

Well Kurt, how can I avoid it?
The easiest and safest way is just don't touch the money. Request a direct transfer of the money and then make sure it is done right!

If it happens how can I fix it?
You have that 60-day deadline so just replace the money you took out. There can be times that period might be longer, depending on your situation, but I wouldn't count on it happening unless you had something extraordinary happen to you during that 60-day period.

Mistake #6

Neglecting to Compare Fees

There are a myriad of options when you leave a company. One way is to roll it over to a new IRA, leave it in the old employer's plan, or move it to the plan at your new employer. Make sure you FULLY understand the fee structure of each option!

How could it happen to me?
Typically, there are two reasons you don't compare fees. You don't pay attention to them or you have some difficulty figuring out how much they are. A lot of the time the fees aren't clearly disclosed so you have to ask a lot of questions don't just trust someone, ask them to show you all of them.

What does that mean to me?
If you pay excessive fees it can destroy your ability to build wealth. A 1% fee structure can reduce your wealth by up to 25% or more over a 40 year work life and a 3% fee structure reduces your wealth up to 56% or more and according to Third Party Research Firm Morningstar and Forbes Magazine the average fees in mutual funds are around 3%.

Well Kurt, how can I avoid it?
Just make sure you understand the fees and they fully disclose them to you.

If it happens how can I fix it?
If you discover you are paying too much in fees consider moving your account to another institution that charges lower fees. You'll likely find that IRA plans have lower fees than 401k plans!

Mistake #7

Failing to Properly Manage Your RMD's

RMD's are also known as "Required Minimum Distributions." Money you have in qualified plans (401k, 403b, 457, IRA) when you reach age 70 1/2 you are required to withdraw minimum distributions each year whether you need the income or not. You'll pay taxes on them. People sometimes forget them because they don't need the money! DON'T LET THAT HAPPEN TO YOU!

How could it happen to me?
It is easier than you think to make a mistake here. If you don't understand the rules for RMD's you may not be aware you must take them. Your financial institution typically sends a reminder, but they can't force you to take the withdrawals, you have to trigger that. Plus you may have other qualified funds with other institutions. For example, if you decided you wanted to take your entire RMD from one account and the other account automatically took out what was required for that amount you would have taken out too much. Ultimately, it is your responsibility.

What does that mean to me?
Failure to take your RMD results in a penalty of 50% of the amount you failed to take. If you had a $500,000 IRA and say the RMD was $18,000 and you failed to take it your penalty would be $9,000 when you file your tax return. Say you only took out $15,000, $3,000 short then your penalty would be $1,500.

Well Kurt, how can I avoid it?
Make sure you start taking your RME when you turn 70 1/2. Determine the value of your IRAs on the last day of the previous year and divide that by the life expectancy factor you can find on the IRS website here. The first year you do have a grace period until April 1, keep in mind your next distribution will need to be taken before December 31st thus resulting in two distributions reported in one year and raising your taxable income.

If it happens how can I fix it?
If you failed to take your RMD on time, take it as soon as you realize your mistake. You might be able to file a Form 5329 with your tax return and ask to have the penalty waived if the oversight was due to a reasonable error.

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Mistake #8

New Account Isn't Ready to Receive Funds

If your new rollover account isn't ready to receive funds, the administrator will be forced to send the check to you. This can also happen when the current administrator has an asinine policy to send the check directly to you! Believe me, it happens.

How can it happen to me?
This can happen if you fail to open an IRA rollover account at the new institution before you requested the transfer of assets or it might be a clerical error on the part of the new administrator or the old administrator.

What does that mean to me?
You'd end up with a check in the mail where they have withheld 20% for taxes. If you fail to open the new account with the new administrator or make other paperwork errors, the check will be cut and sent to you. You then have 60 days to roll it into your new IRA account. Of course you'll also have to replace the 20% that was taken out for taxes with outside funds to avoid a tax hit!

Well Kurt, how can I avoid it?
Open your new IRA account with a reputable custodian then make sure you accurately complete the paperwork with your previous custodian so the rollover happens correctly.

If it happens how can I fix it?
If you miss the 60-day deadline because of an error that is reasonable like this, you could request that the IRA waive the taxes and penalties. If it is clearly not your fault, you might get a waiver. Though you are dealing with the IRS so who knows. This is definitely the case where an ounce of prevention is better than a pound of cure!

You might also talk with the previous custodian, alert them to the error and see if they have provisions that would allow you to send that check back to them and restart the process.

Mistake #9

Forgetting to Consider a Roth IRA Rollover

Deferring taxes can be a good idea, but at some point you HAVE to pay taxes on that retirement plan money. If you roll these qualified funds to a Roth IRA, you pay taxes on the distribution in the year you do it, but the benefit is that future earnings and income will be tax-free! Once you get that tax-hit out of the way, under current tax law you will never have to pay income taxes on that money again.

How could it happen to me?
Most folks don't even consider a Roth when rolling over their money because they are too focused on and don't fully understand the ramifications of Tax-Deferral vs. Tax-Free!

What does that mean to me?
The tax problems happen down the road. People with huge IRA's end up paying huge taxes on their RMD's and then the "Stealth Tax" can come into play creating an UNNECESSARY and COSTLY Tax on your Social Security Income! It can even cause a "surcharge on your Medicare Premiums, or your heirs end up with unnecessary estate taxes! Traditional Financial Planning seems to ignore these costly mistakes so make sure you are aware of them.

Well Kurt, how can I avoid it!
Have a Qualified Financial Professional run a Roth Analysis for you, but make sure they fully understand all the different implications the way your retirement income is structured on taxes, the amount of income you can get, how long that income will last, how to maximize your Social Security benefits and how to avoid unnecessary taxes on your income, Social Security and Estate!

If it happens how can I fix it?
This is one mistake that is simple to rectify. You don't have to do the Roth Conversion at the time you do your rollover, it can be done later! Just make sure there are no extra charges or penalties with the new custodian if you were to roll it over!

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Mistake #10

Not Properly Reporting Your Rollover to the IRS

When you correctly execute the Rollover there won't be any taxes due, but you'll want to make sure you report it correctly. You'll get a 1099-R that shows the total amount of your retirement fund and it will show a taxable amount. Which should be $0 if you did the Rollover correctly. Make sure your taxes reflect this information or it will raise a red-flag with the IRS.

How could it happen to me?
Pretty easily...you'd be surprised at how many people just disregard that 1099-R because they feel there is nothing to do because they did the rollover correctly. It can be complicated if you didn't do the Rollover correctly or you did an Indirect Rollover so the 20% in taxes was withheld. Perhaps you did a partial rollover with company stock then some taxes will be owed. Make sure you or your tax preparer properly reports it.

What does that mean to me?
If you don't match up your tax return with what the IRS received in 1099's you'll get a letter from them requesting the amount of taxes they think you owe!

Well Kurt, how can I avoid it!
Just watch for your 1099 in January and make sure you correctly report it on your return!

If it happens how can I fix it?
If you do make a mistake, try to rectify it immediately. Don't wait for the letter from the IRS. Go ahead and file an amended return!

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Mistake #11

The Dreaded Missing Signature

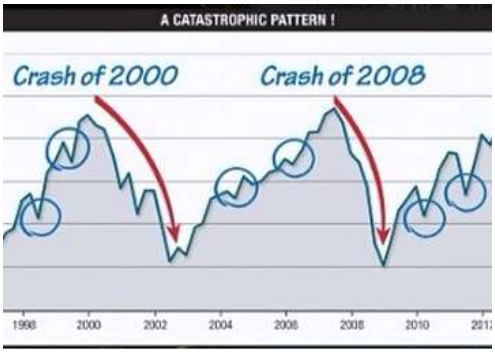
Yep, a missing signature can derail your Rollover in a heartbeat! The custodian can't do anything with your money without the proper signatures so make sure you sign it in the right places.

How could it happen to me?
It might or might not be your fault. Maybe they never asked you to sign or they missed the signature until late in the process and the whole thing came to a screeching halt.

What could it do to me?
If that missing signature is caught too late there's that 60-day deadline that might be missed thus costing you taxes and penalties!

Well Kurt, how can I avoid it!
Pay attention to detail, but more importantly work with competent people to handle your rollover.

If it happens how can I fix it?
Watch your mail, keep communication with the administrator open, even getting names and extension numbers to the people you talk to, keep checking your accounts until you are satisfied that the right amount of money has been moved. Then follow up with your new administrator to make sure they have completed the rollover properly!



Mistake #12

Thinking You Have to be in the Market

There is very little doubt when you look to Roll your 401k over the advice you get will likely be to have your money at risk in the market in stocks, bonds, mutual funds, target date funds, exchange traded funds, variable annuities, etc.

Have you ever wondered why we are constantly advised to put our money at risk of loss and in places that if they accomplish what they say they will we end up paying thousands and thousands of dollars in unnecessary taxes and high fees?

Why would we want our money in places where the retirement income it creates for us in retirement is lower than it could be, it isn't guaranteed and according to recent studies is running out well before our retirement ends?

Is that what you want from your retirement money?

Take advantage of this opportunity to look at other options that might provide more of what you want from your retirement...

- Never lose a penny when the market drops,
- Grab some if not all the gains when the market is up,
- Retirement incomes up to 64% or more higher than traditional plans,
- Eliminate unnecessary taxes,
- Create ever-increasing incomes you can't outlive, etc.

Doesn't that sound more like what you'd want from your retirement savings? Yet traditional planning gives you NONE of those things. Ever wonder why they wouldn't want to help you get what YOU wanted for your retirement?

If the Financial Pros you are talking to aren't familiar with these concepts check out the information at www.MaxMyRetirementIncome.com you just might be surprised at what you find there!

Actual Mistakes

The Rollover process is complicated and the rules can be bungled by people with the best intentions. Here are some examples…

⇒ A woman transferred her IRA to her husband's IRA, she thought that would be a tax-free Rollover, NOPE it was a taxable distribution to her!

⇒ A man took cash out of his IRA, bought stock, and put the stock into another IRA within 60 days. This was a violation of the rule that the same property must be rolled over so that added more than $480,000 to his taxable income that year. All he had to do was simply roll over the cash and then bought the stock in the new IRA he would have avoided the error.

⇒ A man received a check from his IRA in February, immediately deposited into a new IRA. Three months later he did it again—which was a violation the rule that requires a one year waiting period between rollovers from the Same IRA. He could have done a direct trustee-to-trustee transfer that has no limits or he could have done a rollover with a different IRA within the one-year period.

Financial institutions also make errors, but that doesn't mean their clients are exempt from paying the taxes!

⇒ A man asked his current custodian to have his retirement income deposited into his IRA, unfortunately they put it into a regular brokerage account instead. Nine months later he discovered the error and asked the custodian to correct it.
The IRS ruled the income was taxable and also subject to excessive contribution penalties it made no difference who made the mistakes.

If you have money from a previous job don't be afraid of Rolling it Over, just make sure you work with someone that knows what they are doing to get it done correctly and even more important make sure it is someone that knows how to properly position everything to give you all the things you want from your retirement.