Retirement Weekly

Dec. 14, 2012, 5:03 p.m. EST

End-of-year moves for your retirement accounts

By Robert Powell, MarketWatch

It's that time of the year when it's easy to make mistakes with your retirement accounts. There are required minimum distributions, or RMDs, to take, beneficiary designations to change—and the list goes on. To make sure you cover all the bases before 2012 comes to a close, we asked advisers for their best year-end moves to make with retirement accounts.

Here's a look at what they had to say.

What's your exit strategy?

First and foremost, you need to decide what your exit strategy is, said James Johnson, president of All Mark Insurance Services. "What I mean by this is they need to think forward," he said. "Will they be in the same tax bracket when they retire and what do they think will happen to taxes?" He suggests that reader consider watching a video he produced on the subject.

"Once they have decided they will likely be in the same bracket and taxes will be higher, than they need to get moving," Johnson said. "They have only a few days left to take advantage of 2012."

Fill up lower income brackets

If your current income tax bracket is low or zero, then take money from your IRA and recognize taxes at the very low bracket, said Joseph "Big Joe" Clark, the co-founder and managing partner of Financial Enhancement Group. "I have many clients with high six-figure IRAs and very low taxable income. Always be looking to get the money out in the best tax environment possible."

Roth IRA conversion

Consider too a Roth IRA conversion if you have low tax opportunities, he said. The Roth IRA conversion is a year-end vs. an April 15 contribution deadline. "Remember, retirement is not a snap shot like a tax return is," Clark said. "Retirement is a journey and you need to keep both eyes open for opportunities."

Terry Prather, CFP, CHFC, a wealth planner with Payne Wealth Partners, also said a Roth IRA conversion could be useful, especially if you have any tax deductions/credits that will expire at year-end if not used.

Johnson also said you should consider a Roth IRA conversion before Dec. 31, 2012.

"How much?" he asked "Enough to max out your tax bracket."

Now all of this depends on many factors and, he said, "quite frankly you might not be equipped to make these hard decisions and you might need the advice of people specifically trained in these matters."

But know this: "The only way you can screw this up is to not do it," he said. "If you convert to a Roth IRA before the end of the year, you will have all the way up to Oct. 15 of the following year to recharacterize, or in other words, put it back to the IRA no taxes no penalties."

Tom O'Connell, president of Senior Wealth Solutions, agreed: "In general, get as much money out of tax-deferred accounts and into tax-free now, before tax rates go higher," he said.

Reasons to leave money in a 401(k)

According to Hal Rogers, CFP, president of Gold Tree Financial, if you need income from your 401(k) account before you reach age 59½, are separated from service, and are under age 59½, leave those funds in your employer-sponsored account until you reach age 59½.

By doing this, Rogers said, you can take income from your 401(k) without being subject to the 10% penalty tax for early withdrawals. You can't do that with an IRA.

Reasons to move money from a 401(k) to an IRA

If, however, you don't need income from your 401(k) account and/or are over 59½, there is no reason to leave the money in the 401(k) and several reasons to move it, Rogers said.

You have almost infinite investment options in an IRA, said Rogers. By contrast, you have a few limited investment options in your employer-sponsored plan.

In addition, you can control costs in an IRA; you can't in the employer plan.

Rogers also said you can insure income for life with certain investments in an IRA; you can't in an employer-sponsored plan.

There are other reasons to move your 401(k) to an IRA, said Rogers. Those include:

- You can secure professional tactical management services for your IRA; you can't in the employer-sponsored plan.
- You can secure financial, tax, and estate planning services provided by a professional financial planner for your IRA; those services aren't available through investment option providers in the 401(k). This feature alone could prevent inheritance of the plan assets by "unintended heirs", said Rogers.

And services provided by a financial professional can include assuring that the IRA proceeds can be stretched over a period equal to the life expectancy of the plan owner's heirs. That kind of service is generally not provided by 401(k) investment providers that "do not provide tax advice." In addition, Rogers said a professional adviser may be able to help you use strategies available through little-known Tax Code provisions, provisions will allow you to transfer certain 401(k) or Tax Qualified (tax-deferred) ESOP assets to a Non-Qualified brokerage account, thereby avoiding higher income-tax rates associated with distributions from an IRA to which those assets might be rolled to from the employer sponsored plan.

Review your investments

Many people do not take the time to review the investments inside their retirement plans, said Beth Blecker, the CEO of Eastern Planning. "Their money comes in paycheck after paycheck and they do not look to see if the allocation is still right for them and if based on the contributions and gains that it is still accurate," she said.

Blecker's advice: Plan participants should take the time, especially at the end of the year, to look at their allocation and make sure that it is still accurate. "If they are supposed to be 50% in equities and 50% in bonds they should reallocate their account back to the proper allocation," she said. And in a year when equities have risen more than 15% year to date through Dec. 13, she said "it is even more important to rebalance so that they do not take on more risk than they want due to an increase in equities."

Take your investments off autopilot

Dharmesh Vora, the owner and founder of Vora Financial Group, suggests that you take your 401(k) plan off autopilot and start paying attention to the holdings and performance of the plan.

"Most people contribute into their plan because it is the right thing to do for their future, as well as to receive the company match, but without a plan of action," said Vora, who also suggest that you consider hiring a qualified financial adviser for some advice. "Meaning, will the contribution they are making get them to their destination or will they fall short—or do they even know where their destination will be? A good adviser will help their clients create a plan, identify their needs—current and future—help them get to their destination."

Focus on taxes, fees and risk

As for those nearing retirement or already retired, Vora says, you need to focus on risk management first and foremost. “There are three major punctures in the financial tires that could affect some ones retirement journey causing them to fall short of their destination,” he said.

The first is tax: People are paying more in taxes than they should. A good adviser can fix that, he said.

The second is fees: Most people are unaware of the fees that are paying to have their accounts managed. “Paying fees is not the problem,” Vora said. “The question is that are they and their adviser both asleep at the wheel?

And the third is risk. “Most people are taking more risk than they should,” said Vora. “We’ve had two major market corrections with in the past decade. Can people nearing retirement or already retired afford that risk? Instead of a puncture, that was a blowout.”

RMDs and beneficiaries

Prather also said it’s wise to check whether all your required minimum distributions have occurred? “The penalty is severe for missing a distribution,” he said. It’s 50% of the required distribution.

And this isn’t a last-minute thing, but an all-the-time thing. “Always be sure desired beneficiaries are properly designated with the financial institution,” said Prather.