

Why Staying in Your Company's 401(k) After Retirement Can Be a Smart Move

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In the 401(k) age, retirement celebrations are capped with a gold watch and a lump-sum distribution -- which retirees often reflexively roll into an IRA.

These days, those reflexes may be out of date.

Employers, financial planners and the 401(k) industry itself are increasingly coming around to the idea that maybe retirees should leave their money in their 401(k) account after they box up their cubicle for good.

There are certainly some caveats you must be aware of -- particularly related to a potential tax time bomb -- but in general the leave-it-in-your-401(k) strategy is backed by some strong reasoning: lower fees that can extend the life of your nest egg; fiduciary protections you don't find in an IRA; access to certain types of low-cost investments you can't get in an IRA; and, increasingly, distribution options that give you access to low-cost immediate annuities that you can't find on your own.

For those reasons, "you're beginning to see a real change in attitude," says David Wray, president of the Profit Sharing/401(k) Council.

- **New options.** Under federal law, you're allowed to keep money in a 401(k) plan if you have more than \$5,000 in your account. But until recently, companies usually wanted new retirees to roll their assets into an IRA to help keep administrative costs down.

That mentality is shifting, with employers recognizing that workers need help not only managing the accumulation of assets during their career, but also with the disbursement and management of those assets in retirement. There's another reason, too: Plan providers generally charge fees based on assets under management. With a mass of baby boomers set to draw down their accounts -- typically worth anywhere from several hundred thousand dollars to more than \$1 million each -- the rapid shrinking of the company 401(k) plan could increase costs to remaining participants.

Already companies are making 401(k) plans more attractive to retirees who might want to stick around. More than a third of employers now allow participants to withdraw their money in installments -- a sharp change from the tradition of requiring full distribution. That gives retirees a new option to better manage income needs and tax issues in retirement.

- **The case for rolling over.** Still, for many 401(k) participants, rolling their balance into an IRA is the better choice. The obvious reason: An IRA offers many more investment options. And if your company plan provides mediocre fund choices, why stick around? "Just because you're paying low fees doesn't mean you should stay if you can get better performance elsewhere," says Joseph Valletta, a partner at HR Investment Consultants, a Baltimore 401(k) consulting firm.

Furthermore, "many retirees don't feel confident managing their own assets," says Kathleen Piaggese, a fee-only financial planner in Scarsdale, N.Y. "They need help they don't typically" find inside a 401(k) plan.

There's also that tax time bomb ticking in many 401(k) plans. If you die while still in the plan, many employers force beneficiaries who aren't spouses out of the plan, with the total value of the account taxed as ordinary income. If your beneficiaries happen to be your kids in their peak earning years, they could face a steep tax bill.

That rule, however, is changing. Hewitt Associates, a human-resources consulting firm in Lincolnshire, Ill., found in a recent survey that between 25% and 30% of companies now allow so-called nonspousal beneficiaries to remain in the plan, "potentially stretching out the value and taxation of your account over many generations," says Stacy Schaus, Hewitt's personal-finance-practice leader. That's the same advantage you'd get by rolling over into an IRA.

- **The case for staying in the plan.** One big reason for staying in the company 401(k): costs. As a participant, you're paying institutional prices, typically far lower than those in an IRA. That might seem trivial when you're talking about hundredths of a percentage point. Over time, though, those added costs can drain your account, meaning your nest egg doesn't last as long as you'd like, or that you can't draw out as much as you might wish.

Consider, for instance, the Pimco Total Return bond fund. An institutional version is available in many 401(k) plans, while a retail version is available in an IRA. The 401(k) investor pays between 0.43% and 0.68% in expenses; the retail investor pays between 0.75% and 1.65% -- and potentially also pays a sales charge of as much as 3.75%.

In rough terms, total 401(k)-plan fees range from about 0.4% to 2.26%, depending on the size of the company, the size of the plan and how the assets are invested, says Mr. Valletta of HR Investment Consultants. In an IRA, those fees are often much higher, particularly if you enlist a pro to manage your money.

You're also getting fiduciary supervision in the 401(k) plan, "people trained and skilled in investment oversight to make sure" the plan operates in the best interests of its participants, says Hewitt's Ms. Schaus. IRAs don't have that protection if you manage your own money.

Another thing: Increasingly, 401(k)-plan participants also have novel distribution options. Hewitt, for instance, has begun offering to the 401(k) plans it administers access to a program designed by Minneapolis-based Hueler Cos., in which retirees can buy an immediate annuity at institutional prices. Unlike traditional 401(k)-plan annuity options, this one allows retirees to annuitize only what they need, not their entire account. And it allows them to comparison-shop for the best available payout.

In an IRA, retirees could annuitize a portion of their nest egg, but would do so at retail prices, ultimately decreasing their monthly income.

Finally, certain investments are available only inside a 401(k) plan, such as stable-value funds, a staple of many retirees' accounts. The funds, essentially money-market accounts with generally better returns, aren't available in IRAs.

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