Destination Financial Freedom

Getting you there

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What's Your Move?
Career Jumpers

As hard as change is to deal with, most people generally agree that change is good. If you have recently had a change in your job situation it is important to be aware of the options available to you regarding your retirement plan with your former employer in order to determine what is best for you. Take a look at some great advice that was listed in the April 2006 edition of Money Magazine.

1. Sit Tight

It may be worth while to keep the plan where it is if there are significant benefits in doing so. If the plan has a variety of low-cost and high-quality investments, you should consider leaving the account there. Some pension accounts, like Colorado's PERA, have matching eligibility that significantly increases at retirement. Make sure you are not giving up any future benefits by leaving early. If the value of your account is less than $5,000 your former employer can push you out of the plan. In this case you should consider the following options. Keep in mind that if you decide to cash the check that your employer sends you, the amount will be taxable and if you are under 59½ you will also have to pay a 10% penalty on top of the regular taxes owed.

2. IRA Rollover

Depending on the institution that you decide to rollover (transfer) your account to, you will most likely have access to more investments than your previous 401(k) plan. In other words you will not be limited to the five-to-twenty funds that are available in your employer's plan. Because of the greater selection available, this could help the investment performance and your account could grow faster. A 401(k) plan is not the only type of retirement plan that you can rollover. Several types of employer's retirement accounts can be transferred into an IRA rollover (there are some exceptions, for example some types of pension plans may not be able to transfer). The transfer must be into a traditional IRA where all annual earnings, such as dividends, interests and capital gains, are tax-deferred but all withdrawals from the account are taxable. One disadvantage to rolling your account into an IRA is that while some employer plans allow for hardship withdrawals or loans from the plan, IRA accounts do not. As mentioned earlier, taxes and penalties may apply. We advise you to use caution when withdrawing funds from an IRA because large withdrawals, whether it is before or after 59½, can bump you up into higher brackets and increase your taxes significantly. It is not recommended to borrow against your IRA because generally the 60-day period is to short of a time span to successfully replenish the account. The money may come out with good intentions to be repaid, however, this may not happen therefore incurring the hefty tax consequences and making less assets available for retirement.

3. Rollover into a New Plan

If your new plan offers good investment choices and you would like to keep your savings consolidated, rolling your old plan into your new employer's plan. Generally, if you are young or your account is small, you might consider consolidating into your current retirement account. By consolidating you will know exactly where your assets are and they can offer more diversification within the new plan. For larger accounts, it is more likely that the investment options in the new plan will not be adequate enough to provide for the additional diversification needs and therefore should be rolled over into an IRA.

4. Cash Out

Typically, a check is mailed to former employees whose accounts are less than $5,000. The question becomes what should you do with the check? You can deposit into an IRA rollover, your new employer's plan or you can put it in your checking account. If you place the check in a retirement account within 60 days of the date on the check there will be no income tax consequences. If you deposit the check into a personal account taxes and penalties will apply. The biggest cost involved in cashing out is the reality that the money will not be invested and therefore not available at retirement. If a 30-year-old cashed in their check of $5,000 today from their previous employer's plan instead of letting it grow 35 more years at 10% annually, $140,000 would be lost.

Please give us a call if you would like to rollover your previous employers plan and keep it working for you!

Marathon Investment Management, Inc., 6565 S. Dayton St. #1200, Greenwood Village, CO 80111
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Pick Me! Pick Me!

Part 1: The Mutual Fund Selection Process

Remember playing kick ball in fifth grade gym class? Two kids would take turns picking who they wanted on their team. There was a systematic approach to this process. Kids who were athletic and played well in previous games would be picked first. Then you picked your buddies because you wouldn't want them to get mad at you. Towards the end you had to settle for whatever was left. This same strategy is often used to evaluate the thousands of mutual funds available to form your "perfect" team. But to get to the Super Bowl you must first review several of the essential investment strategies as covered in *Kiplinger's Mutual Funds 2006* magazine issue. Next month we will cover more specific mutual fund selection strategies.

1. Don't Chase Winners

An investor bought five of the best performing mutual funds on January 1, 2000 for a total $50,000 investment. Many may have believed this was a great opportunity that shouldn't be passed up when on average the five funds were earning 53% annually. However, during the next five years these high flyers lost 61% of their value leaving the initial $50,000 investment at only $19,695. Past performance alone is not the best indicator to use when analyzing investments. In fact, using one factor alone is NEVER the best way to evaluate an investment.

2. Spread Your Risk

Say there is a 25% chance that a boat out to sea will sink. As an investor, would you rather risk putting all $100,000 on one ship or $10,000 on ten different ships? In order to decrease your chance of losses, it is vital to distribute your investments among many funds.

3. Learn How Funds Differ

There are many different types of ships, for example sail boats, yachts, cruise ships, massive distribution ships, etc. There are also many types of mutual funds. These mutual funds work together to soften the investor's bumpy ride. If an investment account is made up of funds that react in the same manner, the ride will become much more turbulent. Each type of mutual fund has its own unique reaction to market changes. Because of this it is very important to compare funds to others that react in the same manner. A sailor cannot compare the speed of a sailboat to that of a massive distribution ship. Compare small cap mutual funds to other small cap funds and international funds to other international funds and so on.

4. Steady Your Nerves

Regardless of short-term volatility it is always a good idea to have some money in stocks if you are investing long-term (more than 10 years). Historically, over 10-year periods, stocks have never lost more than 1% annualized, even through the Great Depression period. Over 5-year periods the S&P 500 Index has made money 90% of the time and it has outperformed bonds and cash 80% of the time. If you stretch the time period to 20 years, the S&P 500 has never lost money and has always done better than bonds and cash.

5. Don't Jump In-and-Out

Market timing has never proven to be a successful way of investing. Not only does it waste a lot of time, it could also rack up a ton of transaction costs that will be hard to make up in the stock market. Short term risks are much greater than holding on for a long ride. Most professionals cannot accurately predict short-term market behavior, which is another reason why diversification is so important.

6. Close Your Ears

It is normal to be protective of your investments because they represent your life goals. However, because of this representation it is easy to let emotions control the situation. The market preys upon emotions - if you listen to them and the media's spotlight news, your investments are bound to suffer. These sources essentially tell you to buy high and sell low - the exact opposite of what needs to be done in order to be successful.

7. Do Nothing

The best part about properly investing is that you don't have to do anything! You don't need to check your account every day or waste time. If you have invested properly with a suitable allocation and sufficient diversification there shouldn't be many reasons for making changes. However, there are times when changes should be made that we will cover in future articles.

8. Be a Bit Above Average

A survey of Swedish drivers revealed that 90% believe they have "above average" driving skills. In reality 44% of the respondents who rated themselves as "above average" are overestimating their capabilities. Many investors also display this same level of self-confidence. The stock market is a very tough and competitive environment. Even the most experienced and educated market professionals continue to learn from its marvels. Beating market averages by one or two percentage points a year can produce significant rewards over a long period of time. A $100,000 investment that earns 10% over ten years will create $260,000. However, the same $100,000 investment earning 11% over ten years will generously produce $25,000 more. That is 25% extra based upon your initial investment!