Horrible 401(k)

Horrible 401k & still employed? Here are 4 options to improve your situation

Employees in the United States of America will soon be shocked to learn how much they pay in 401k fees. For boomers with large balances in a plan, high percentage fees translate into really big dollars. Consider a participant with $500,000 in their company's 401k paying 2% in total fees translates into $10,000 a year, each year, causing a real drag on their nest egg. This is going to come as a real shock especially since most people believe they don't pay any fees at all for their 401k. So if you just realized you are paying an arm and leg for your 401k, here are 4 potential ways to cut that bill in half, if not more.

Take the Money and Run

For many participants over the age of 55, the best option, if the plan allows, is doing an In-Service Withdrawal. This option allows the participant to transfer funds from the plan to an IRA rollover, preferably at a low-cost discount brokerage firm and completely escape the 401k plan all of its fees. Additionally, IRA rollovers allow the participant greater flexibility in selecting investments which hopefully will translate into a more diversified portfolio consisting of the best investments with the lowest overall cost. The option to take an In-service withdrawal is plan specific so participants need to contact their provider to learn the caveats. For example, some plans allow participants to take an in-service withdrawal at 55 years of age while others require 59.5. Also, some plans freeze participants from making new contributions for a period of time after the in-service withdrawal so you have to know your plan's rules and create a strategy to maximize your annual 401k contribution for the year. Other points to consider are that your new IRA rollover is not eligible for the Rule of 55. The Rule of 55 allows 401k participants older than 55 but younger than 59.5 to take withdrawals without incurring the 10% penalty, so you should avoid this option if you plan to take distributions prior to 59.5. On a final note, 401k plans allow for participants to be exempted from taking a required minimum distribution once they reach 70.5. This "still working exemption" does not apply to IRA rollovers so this option isn't optimal for high income earners reaching 70.5 who plan to continue working and won't need the money.

Look for an Opening

If you are under 55 and/or your plan doesn't offer an in-service withdrawal, find out if your plan offers a Self Direct Brokerage account. This option is essentially a plan menu options which allows you to keep your money inside the 401k but transferring dollars into a brokerage account. While this option doesn't allow you to escape plan costs, it can help you increase diversification, select better investments and hopefully to decide on low cost index funds. You need to weigh this increased flexibility with any additional administration, gateway and maintenance fees from the plan provider as well as brokerage commissions.

Make the best of the bad

If you are stuck, and no doubt many of you will be, your best option is likely to review your investment options and select only the lowest cost funds, most likely index funds. While you may need to give up some diversification inside your 401k, you should use your other investments outside your company's plan to diversify, building a comprehensive portfolio integrating all your investable assets.

Rock the boat

If you are an activist and feel like picking up a good cause, you always can lobby your employer for a better plan. But be warned, there are often a lot of political, and somewhat unpleasant aspects to why plan sponsors select 401k providers. I'd strongly advise you to walk lightly and always remember that your employment most likely trumps any likely plan improvement you might achieve.