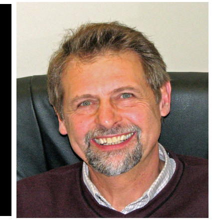
Fiscal Fitness



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Victim of Recent Budget Cuts?

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You may be one of the unfortunate workers who have lost a job due to recent budget cuts; or maybe you quit or changed jobs. Now the question is what do you do with your retirement account? One option is to cash out the account; but if you do that, you could be hit with a 10% penalty for early withdraw and be taxed on the amount (the IRS considers it a taxable distribution).

Other missteps could also cost you money in penalty and taxes. One misstep is if you decide to do an ***indirect rollover*** of your 401(k) (or other qualified retirement plan) into an IRA. An indirect rollover is when your former employer issues a check in your name for your retirement funds. You then have 60 days to deposit those funds into an IRA. If you fail to meet this deadline, the IRS will consider it a distribution, and you will be taxed on the distribution amount at your ordinary income tax rate. You could also be slapped with a 10% early-withdrawal penalty on the distribution if you are younger than 59 1/2 years old. Even worse is your former employer is required to withhold 20% of the distribution for tax purposes. However, this 20% could be refunded to you under the following conditions: you file your income tax return if you meet the 60-day rollover deadline ***and*** you come up with 20% of the money your former employer withheld.

Here's an example: Say you have $100,000 in your 401(k) with your former employer, and you are planning to do an indirect rollover to an IRA. By law your former employer must withhold $20,000 for tax purposes, so they write you a check for $80,000. You then have 60 days to roll over the $80,000 ***plus*** the $20,000 of your own money. Let's say you don't have that kind of money lying around, so you only roll over the $80,000. You will then be taxed on the $20,000 (remember, it is considered a distribution), and you could be hit with the 10% penalty for early withdrawal if you are younger than 59 1/2 years old.

Fortunately, it is easy to avoid these mistakes by doing a ***direct rollover*** (trustee-to-trustee transfer). Set up an IRA account with the new custodian and have your 401(k) from your former employer transferred directly to the new custodian. Two advantages: You won't be tempted to spend any of it because you won't see the check, and there is no requirement to withhold 20% for income taxes; the entire $100,000 is transferred. Even if you need some money to pay unexpected expenses, it's still better to do the direct rollover first. Once the money is transferred, you can withdraw what's needed. You will still pay taxes and possibly the 10% penalty on the amount withdrawn—but you won't need to worry about coming up with your own money. Additionally, you can do as many direct rollovers per year as needed. (For indirect rollovers, only one is allowed per 12-month period.)

Direct rollovers can be facilitated by a financial adviser at Vorpahl Wing Securities. Give us a call. If you have left a job or have been laid off, and you are unsure how to handle your hard-earned retirement account, we can help.