Assess Alternative Retirement Withdrawal Strategies

Although the unemployment rate for individuals who are 55 and older is fairly low, some older workers find themselves out of a job in their golden years. AARP reports that the latest unemployment rate for workers age 55 and older is about 4.7%. Losing a job or facing a forced early retirement is not uncommon in the current economic environment. And, unfortunately the average length of unemployment for workers age 55 and older is a little over 51 weeks which is about one and a half times longer than it is for people under age 55.

The good news is many workers have saved a significant amount of money for retirement by investing in 401(k) plans or IRAs. Thus, early retirees may look to withdrawing from retirement accounts as a source of shoring up the gap between the loss of a regular salary and monthly expenses. A financial triage is in order, however, for older workers contemplating dipping into retirement savings.

When you withdraw from a retirement account, taxes have to be paid as the funds contributed into the account went in tax-free. The assumption when investing in such a vehicle earlier in your career, is that you will be in a lower tax bracket when you retire. However, early retirees may encounter penalties, taxes and inconveniences when withdrawing funds from individual accounts. Proper planning may reduce or even eliminate such costs.

There are techniques that early retirees should use to withdraw funds from their tax-sheltered retirement accounts. If you are age 55 or older and you have stopped working, you can withdraw funds from your 401(k) plan or 403(b) account without being subject to the 10 percent penalty that would usually apply to withdrawals from an IRA owned by an individual under age 59 ½. The funds withdrawn, however, will still be subject to taxation.

A person can withdraw contributions from Roth IRAs anytime for any reason without being subject to tax or penalty, irrespective of your age. Why? Because contributions to a Roth IRA differ from contributions to a traditional IRA in that contributions made to a Roth IRA are made with post-tax dollars.

Additionally, if you become disabled to the degree that you cannot participate in substantial gainful activity due to a physical or mental condition, you may qualify for an exemption to the ten percent early withdrawal penalty from your IRA.

If it is necessary to withdraw funds from your IRA to pay for living expenses before reaching age 59 ½, you should ascertain whether you have any qualifying expenses that can be used against the IRA withdrawals to avoid the ten percent penalty. Such qualifying expenses include large out-of-pocket medical bills, costs associated with higher education expenses, or high health insurance premiums if you are unemployed.

Moreover, IRA holders under age 59 ½ can make withdrawals from their account without incurring a penalty if the withdrawals are similar in amount and comply with a certain schedule. This type of withdrawal is called a SEPP withdrawal (substantially equal periodic payment). Under this option, once the periodic payments have started, they must continue for five years or until you reach 59 ½ whichever is last. The downside to this option is if the requisite amounts and timing of the SEPP schedule are not met, then all withdrawals may be subject to the ten percent penalty retroactively.

In some scenarios it can also be advantageous to leave assets in an IRA for the purposes of planning for long term care eligibility. There are some strategies that can be employed under current Texas policy in which the funds in an IRA can be an excluded asset in means-tested benefit planning. Again proper planning is key.

Knowing the rules governing IRAs might influence your decision regarding financing retirement as well as financing long term care. It is best to consult an elder law attorney for advice regarding withdrawing or restructuring a retirement account if the need for withdrawals is in the near future.

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