Getting Answers to Questions On IRAs, Roths and Planners

By Terri CullenThe Wall Street Journal Online

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With so many ways to save for retirement, figuring out the best plan of action can lead to a whole lot of confusion and questions.

So it's no surprise then that the Fiscally Fit columns that tend to draw the most reader e-mail are those that deal with individual retirement accounts, Roth IRAs and 401(k)s.

This week, I answer queries relating to recent columns retirement planning. For a kicker, I've also included a letter from a reader who believes she has a good bead on saving and investing but is wondering whether she should get a second opinion from a financial planner. If you've been thinking the same thing, you'll want to check out my response.

So read on for comments and queries from your fellow readers, and send questions of your own to me at fiscallyfit@wsj.com.

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In a recent column, I laid out a few reasons why borrowing from your 401(k) to fund the down payment on a home can be a mistake. Many homeowners wrote in to share their experiences -- for better or worse -- in tapping their retirement savings to buy a house. Two readers offer their thoughts on why it's impossible to make generalizations when it comes to financial planning.

Mark Zumler writes: You did not point out when using your 401(k) savings as a down payment would be prudent. I borrowed some money from my 401(k) when I bought my house here in San Francisco about eight years ago. I made sure that the money would not have to be repaid when I left the company; that was two companies ago. Some 401(k) plans allow this -- you really should advise people to check this option. Considering the increase in home costs (my $400,000 home is now worth around $900,000) I feel I made the right choice.

I certainly agree with you that I lost some compounded interest and tax-free growth, but the funds that I took out did not fall with the rest of the stock market. I think I came out ahead, actually.

Christopher O'Leary writes: For me, your article is five years too late. Although [using my 401(k) savings to purchase a home] has worked out for me due to the great price appreciation I have realized in the short time living on Long Island, N.Y., the money lost to taxes, savings and stock-market appreciation is killing me -- but you can't cry over spilt milk. I made my choice and now I must live with it. It was a costly lesson for me, but now one that I won't make again.

A number of readers, like Mr. Zumler, wrote in to say they felt borrowing from their 401(k)s to buy a home -- or pay off credit-card or car-loan debt -- was one of the smartest financial moves they've ever made. And quite possibly they're right. For them, owning their own homes or being debt free now is worth the sacrifice of some future retirement savings.

As both readers point out, the appreciation in the value of their homes is a big financial plus. But as Mr. O'Leary's experience shows, when you borrow from your 401(k) you risk losing a chunk of your future savings. A sad fact is that some people who spend down retirement accounts to buy a home now will find themselves house rich but savings poor at a time when they need the cash most in retirement. While a home is usually a sure financial bet if you stay in it for the long haul, it's ultimately an illiquid investment. That money is locked up unless the homeowners downsize to less expensive homes, opt for expensive reverse mortgages, or face the fees and/or finance charges that come with borrowing against the equity built up in their homes. Either way, you pay.

So, as I said in my column, if you do decide to borrow from your 401(k) or IRA, plan on repaying the loan and continue to contribute to your retirement accounts to start rebuilding your savings as soon as possible.

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Mark Patterson writes: Regarding your recent article, "Five IRA Rollover Mistakes That Can Crack Your Nest Egg," you listed some common mistakes people make when naming a beneficiary in a rollover, including "naming someone older than you who is a non-spouse (such as a mother or sibling)…" Why is it a mistake to name a parent as a beneficiary? As a

single 28-year-old, all of my investment accounts list my parents as beneficiaries. Whom should I choose, my dog?

It's perfectly fine to name a parent, sibling, partner or close friend as the beneficiary of your holdings if you're not married and have no children, but there are two possible drawbacks. First, you may eventually marry but forget to update the beneficiary information on your IRA -- a mistake far too many account holders make, much to the dismay of spouses. Second, if the parent or sibling you name dies before you or you name a secondary beneficiary, and you later die, the state will ultimately decide how your funds are distributed.

Inheritance laws regarding IRAs are complex, so it's important to make sure you're not creating a financial headache for your loved ones by not putting enough thought into the designation now.

Oh, and for you pet lovers, let me add: While you can't name your dog as a beneficiary on an IRA (pets are considered property) you can include the animal in your estate planning. Many states now allow pet owners to create legal trusts to provide for pet care after the owners have died. To learn more, click here.

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C.J. writes: I have a Roth IRA that is earning so little that when I paid the $90 annual fee last year, I nearly came unglued. My question is: Can I transfer my Roth to the bank where I do almost all my business, and if so, what are the steps necessary to do so?

It's always a good idea to move to another bank or broker if you can avoid paying routine account maintenance fees. Combining all your financial accounts under one roof may also be a smart move because you may be eligible for other freebies and perks typically offered only to the best customers (generally, accounts valued at $25,000 or more).

But in order to avoid confusion, and a run-in with the Internal Revenue Service, you need to do it right. First, open your new Roth IRA account with the bank or broker of your choice, then ask the bank or custodian of your current Roth IRA account to do a direct trustee-to-trustee transfer of the funds to your new IRA account. If you do a direct transfer, there's no need to report the transaction to the IRS. However, if you liquidate the account and then deposit the money into your new Roth IRA account yourself within 60 days, you will have to report the

transfer to the IRS. Miss the 60-day window, and you may owe income taxes on earnings and an early-withdrawal penalty. To be safe, let the financial institutions handle the transfer. After the transfer, be sure your bank or broker has linked the Roth IRA to all of your financial accounts. Read more about IRA transfers and rollovers.

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Amy Hobgood writes: Do you recommend that a couple in their 30s with no consumer debt, a decent retirement savings and a fairly good understanding of personal finances hire a financial adviser? Can you recommend a company?

I strongly feel that every family could benefit from a periodic consultation with an objective financial planner. A planner can help you identify your goals and make suggestions for allocating your savings to get you there. The services of a professional can be even more valuable if your family finances are straining under debt, or if a health emergency or layoff has led to a short-term cash crunch.

If, on the other hand, you feel confident with your financial decision-making, as Amy does, a sit-down with a planner can confirm that you're on the right course to reach your goals and perhaps suggest alternate routes you may not have considered. The peace of mind of knowing you're headed the right way is worth the expense. How frequently you should consult a planner depends on individual circumstances, but as a rule it's a good idea to re-evaluate your finances before or immediately after a major life change (such as a new job or baby, a divorce or a death).

As for finding a planner, one caution: Don't hire a salesperson. Investment brokers, life-insurance and variable-annuity agents, and other so-called financial advisers who work for, or are paid on commission by, financial-services companies are there to sell product. Your best interests come second to their bottom lines. Instead, seek out an objective fee-only financial planner, who is paid hourly or by a percentage of your total portfolio. You can start your search by contacting friends or professionals you know and respect for referrals, or get in touch with one of the networks of fee-only financial planners, such as the Garrett Financial Network (www.garrettplanningnetwork.com) of Shawnee, Kan., or Cambridge Advisors (www.cambridgeadvisors.com) in Franklin, Mich., to find a planner near you. For some estimates of what you should expect to pay,

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Write to Terri Cullen at terri.cullen@wsj.com

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