Avoid Losing Your Home to a Bank Foreclosure

By Daniel Lamaute

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Are you facing the prospect of losing your home in a bank foreclosure? Many who are experiencing a temporary financial squeeze will withdraw cash out of their IRA in order to save their home. Getting a loan from your retirement account may be a smarter way to go than taking an IRA distribution.

As with most people your home and retirement savings probably represent the bulk of your available assets. However, withdrawing money from your retirement accounts, even if it's to protect against a foreclosure, will cause you to lose a big part of your retirement money to taxes. A better strategy is to take money out of your retirement funds by way of a 401k loan. A loan from a 401(k) doesn't trigger any distribution taxes and avoids the 10 percent early withdrawal penalty, as long as you repay the loan.

When you have a job you generally can get a loan from your employer's 401k plan. But once you leave or lose your job, as a rule, you can no longer keep your 401k loan or borrow from the plan.

You may, however, be able to start your own individual 401k plan, called a Solo 401k or Self-employed 401k under new tax laws that became effective in 2002. The paperwork to set up a Self-Employed 401k is easy. You can also transfer any of your IRAs, 401k, SEP plan or other qualified retirement funds to your Self-Employed 401k plan. Most Self-Employed 401k plans allow you to borrow up to 50 percent of your account balance all the way up to $50,000. The 401k loan is tax-free and penalty free.

With a lingering recession, anemic job market, and rising property taxes and fuel bills, experts predict that many more people will default on their mortgage payments and face bank foreclosure action. Small business owners and contract freelancers are especially vulnerable to the economic slump.

The Self-Employed 401k is a qualified retirement plan that can be set up by anyone who has a part-time or full-time business. This retirement plan is similar to 401k plans of large companies. The difference is that the Self-Employed 401k is designed for an individual and as such is less complicated and less costly to maintain. Any person with a business with no employees can set up a Self-Employed 401k plan.

The cost and features of Self-Employed 401k plans will vary depending on the plan vendor. A typical plan will cost less than $200 a year to maintain and allow loans with terms of 5 years or more at an interest rate close to prime rate. The good part is that all of your loan payments including the interest go back to your 401k account. Take caution, however, because not paying your 401k loan on time will trigger IRS tax consequences as if your loan was a taxable distribution.

For more information or to obtain a Self-Employed 401k visit InvestSafe.com.

Daniel Lamaute is a retirement plans expert. Through www.investsafe.com his firm Lamaute Capital provides retirement tax saving tips to individuals and organizations.