Access Your Retirement Funds Early Without Penalties

By Dennis J. Rogers, CPA, CFP®

Most people are aware of the age 59 ½ rule that imposes 10% penalty, **in addition** to the tax on withdrawals from a retirement plan. This presents a real dilemma for people who find themselves in need before the "magic age" and have funds available but do not want to get hit with a heavy tax plus a penalty.

There are, however, several exceptions available which can eliminate the penalty. Some of them are not so pleasant like; death, disability, IRS levies, divorce, and excessive medical expenses. If you meet one of these criteria you (or your representative) can file the appropriate form and be exempted from the penalty.

Fortunately, there are also some voluntary and more pleasant circumstances which could let you off the hook for the penalty, as well. The higher education expense exception allows an individual to receive distributions to pay these expenses for the IRA owner, his or her spouse, a child, or a grandchild and avoid the 10% penalty. Tuition at a post-secondary educational institution (including graduate work), as well as room and board, fees, books, supplies, and required equipment are included. [1]

If you have separated from your employer's services and are over 55, you can take a penalty free withdrawal from the employer's plan. These funds **must** come directly from the plan. [2]

The most flexible option is the "substantially equal periodic payments" exception. This one allows you to take payments without penalty at any age. You have to take IRA withdrawals at least once per year based on your life expectancy.[3] These payments have to continue for at least five years or until you reach 59 ½, whichever is longer. After that they can be modified or stopped. An example of how this works would be that a single person age 50 has a life expectancy of 33.3 years on the table. If this person had $500,000 in an IRA the withdrawal amount would be $15,015 ($500,000 ÷ 33.3 years) per year. The payment would have to continue until age 59 ½ to avoid penalties.[4]

Some of the calculations involved and the circumstances for documentation on these exceptions can be quite technical and complicated. You should definitely get professional assistance with this type of transactions.

Dennis J. Rogers, CPA, CFP® is a Registered Principal offering securities and advisory services through United Planners Financial Services. Member FINRA/SIPC. Rogers & Kirby and United Planners Financial Services are not affiliated. He is a partner in a financial advisory practice in Phoenix that focuses on helping clients make smart decisions about their

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[1] Internal Revenue Code §72(t)(7)(A)
[2] Internal Revenue Code §72(t)(7)(A)(v)
[3] Internal Revenue Code §72(t)(7)(A)(iv)
[4] Rev Rul 2002-62

money based on their personal core values. He can be reached at dennis@rogerskirby.com or 602-748-1900.

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