Common Questions Regarding Cashing Out from Defined Contribution Plans

I have bills to pay. Can I cash out my interest in my former spouse's 401(k)/403(b)/457(b) Plan via QDRO?

Yes, in most cases you can.

If I cash out my interest and I am under the age of 59 ½ will I have to pay the 10% federal tax penalty I have heard about?

No. Pursuant to Internal Revenue Code 72(t)(2)(c) QDRO payments are an exception to the normal penalty rules.

Will I have to pay any taxes on the money?

Yes. You will have to pay ordinary taxes based on your own personal tax bracket. The Plan Administrator will withhold 20% of the funds payable to you for <u>estimated</u> taxes. Your <u>actual</u> taxes will be determined after you file your tax return. Depending on your own personal income tax bracket, the 20% may be an overestimate or underestimate-resulting in a refund or additional tax liability.

I am the account holder. Can I cash out my interest via QDRO and avoid the 10% penalties?

Yes and No. You cannot 'pay yourself' via the QDRO process, however, if your former spouse is cooperative, you can award your former spouse <u>more</u> than he/she is entitled to under the judgment, with an promise that your former spouse return that money to you, less the applicable tax liability.

My judgment says that my attorney is to be paid directly from the QDRO. Can we do that?

Yes and no. Payment from a retirement plan can only be issued to a qualified alternate payee, which means a spouse, former spouse, child, or qualified dependent of the account holder. While attorneys do not fall into any of these categories, from a practical standpoint, an Alternate Payee can 'sign over' their check to whoever they want after receiving the check. This agreement between the attorney and the alternate payee cannot be written into the QDRO document.

Can I cash out my interest from my former spouse's Individual Retirement Account (IRA) and avoid the 10% federal tax penalty?

No. Pursuant to Internal Revenue Code 72(t)(3) the QDRO tax exception does not apply to IRA accounts. You should talk to your CPA to find out if other exceptions apply, such as the first time homebuyers or higher education expense exceptions.

Is it a 'good idea' to cash out my interest in my former spouse's retirement plan to pay my bills or for a down payment on a new house?

David T. Ruegg is an attorney, not a financial advisor. You should seek advice from a financial professional before deciding what to do with your money. If you do not already have a financial advisor, you can ask David for a referral.