***FOOTE* Notes on Retirement**

**Topic:** 401k as an Equalizing Payment

Scenario

Husband and Wife have agreed upon all terms of the property partition except the method and amount of the equalizing payment. Wife makes $125,000 per year and is keeping $250,000 in assets (some of which is her 401k). Husband makes $30,000 per year and is keeping $150,000 in assets. Both attorneys want to negotiate this issue without extensive litigation. Wife’s attorney suggests an equalizing payment of $50,000 payable through a 401k qdro.

Questions

1. What are the arguments for and against this proposal?

Proposed Answers

Husband’s perspective: He doesn’t want taxable 401k funds as the equalizing payment. If he has to take it, then he wants 30% more to account for the taxes and penalties.

Wife’s response: There are no early withdrawal penalties associated with a QDRO according to IRA regulations, so only taxes should be deducted, if any. Additionally, the liquidation value should account for taxation at Husband’s effective tax rate which is probably 15% after deductions on a $30,000 income. That would be $7,500 max in additional funds.

Husband’s reply: Are you sure about this IRS rule that does not make me pay the early withdrawal penalty because I am only 48 years old? Why should I take that risk? Additionally, if I were to liquidate the $50,000, it would be considered current income which, added to my $30,000/year income, pushes my income to $80,000 and a 25% tax rate. That would be $12,500 in additional funds.

Who is right? Possibly both.