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Business Blog

Buying A Business With Retirement Funds - Pros & Cons

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Investing in buying a business may be the best funding alternative in today's market.

In light of today's lending difficulties, have you considered purchasing your small business or franchise through a self-directed 401 (k) investment plan? If so, you are not alone. Accessing the funds in one's IRA, 401(k), SEP or other tax-deferred retirement account to as investment capital for a new business is a very attractive option – especially since it can be done without incurring early distribution taxes or penalties.

There are many advantages to this increasingly popular form of "equity" financing. Foremost is using your 401(k) funds to invest in your own business can expedite the ability for a business to rapidly generate and retain more of its gross profits. Since so many investors have lost at least some money in the stock market recently, growing numbers of Americans are choosing instead to invest in their own hard work and reliable management skills. Also, by using this investment strategy, your new business will have a 401(k). You and your eligible employees will be able to defer income from the business to help prepare for future retirement. In addition, many like the avoidance, or lessening of, borrowed capital. In taking on a loan, you are also taking on considerable personal risk, since a lender requires collateral -- your credit, your house(s) and the pledge of all personal assets in the event you are unable to repay the loan.

This is not to say that 401(k) small business investing doesn't come with its own risks, albeit limited ones. By rolling your retirement funds into a self-directed 401(k) investing product, you are effectively using an employee stock option purchase plan. In other words, you are utilizing your retirement funds to purchase privately held stock and invest into your own business. If the business fails, the 401(k)'s investment also fails and, in return, you lose some or potentially all of the value in your company's stock. Think of it as making a bad stock pick -- if the company goes under, so does the stock price. Thankfully, by not getting a loan, none of your other assets, like your home, should be at risk.

Additionally, you don't wind up paying taxes or penalties on the money since the funds were tax-deferred. It would be equivalent to investing in an Enron or MCI WorldCom before their stock prices collapsed. You are out the investments you made, but aren't stuck with any penalties or tax bills.

Less risk, lower overhead, complete control of your investment . . . if these benefits appeal to you, then you owe it to yourself to explore small business financing options through a self-directed 401(k) investing plan.

About The Author: Cyrus Safavian is a 401(k)/Retirment Plan consultant who specializes in assisting individuals utilizing their retirement plan(s) funds to purchase a business (or down payment) without incurring taxes or penalties in the process. Also view the schedule of upcoming FREE online webinars given monthly on this topic. Cyrus can be reached direct at 425-647-5593 for more information.