



Retirement Plans: A New Source for Business Capital

When it comes to owning and operating a business, finding the right form of financing can be an arduous task. Where do you find the necessary funding to seed a business, buy a new one, or raise additional working capital?

Traditionally, business owners have used bank loans, SBA loans, personal loans, credit cards or home equity to satisfy their funding needs. The biggest downside to these sources of financing is the debt load and corresponding payments. Additional debt can impair your ability to access money in the event that "life happens." This is why the idea of using retirement funds to inject cash into a business has been gaining popularity. Although few know about this new concept, if structured correctly it allows for an individual's retirement account to invest directly into their business venture - without taking a distribution and paying taxes and penalties.

The Background

The IRA and 401(k) was created in 1974 when Congress passed the Employee Retirement Income Security Act (ERISA) to address concerns that private pension funds were being mismanaged and abused. The IRA and 401(k) transferred the responsibility of retirement investing from the employer to the employee. The rules surrounding these plans are complex; however, the laws state that there are only two types of investments into which retirement plans are prohibited from investing: life insurance and collectibles.

New Trend in Financing

Many entrepreneurs have money under performing in tax-deferred retirement plans, such as IRAs or 401(k) plans. In order to fund their business, many of these individuals have taken distributions from their retirement account and paid tens of thousands of dollars in taxes and penalties. There may be a better way to structure this type of business financing in order to avoid taxes and penalties, and it starts by engaging a retirement account facilitator. Retirement Account Facilitators (RAFs), such as Bellevue, WA based Guidant Financial Group, Inc. help structure the specific retirement accounts that enable investment into private businesses. "This investment strategy has been implemented for [more than] 15 years and has been legal since ERISA passed in 1974," says Joe Wishcamper, general counsel for Guidant Financial Group. This industry, bolstered by the stock market performance of recent years, has been growing at a rapid pace as more entrepreneurs pursue owning or financing their business this way. Wishcamper says that "last year [Guidant] structured retirement accounts for about 400 clients. This year [Guidant] will structure retirement accounts for [more than] 800." Another reason a business owner would turn to their retirement accounts for financing may be the added advantages of less business debt and greater long-term potential for their retirement funds. By using retirement money instead of a traditional business or home-equity loan, business owners can avoid costly debt service. This enables more money to be reinvested back into the business instead of toward debt. In addition, because the retirement account owns a portion of the business, some of the profits from the business are returned to the account tax-deferred. If you are looking for financing for your new or current business venture, your retirement account just might be the answer. Something to keep in mind, however, is that you should engage a qualified RAF or attorney when investigating how to use this investment strategy. Wishcamper advised that "any competent retirement account facilitator will work with your CPA, attorney, or other advisor to make sure you understand all the benefits and risks of investing your retirement funds into your business."

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