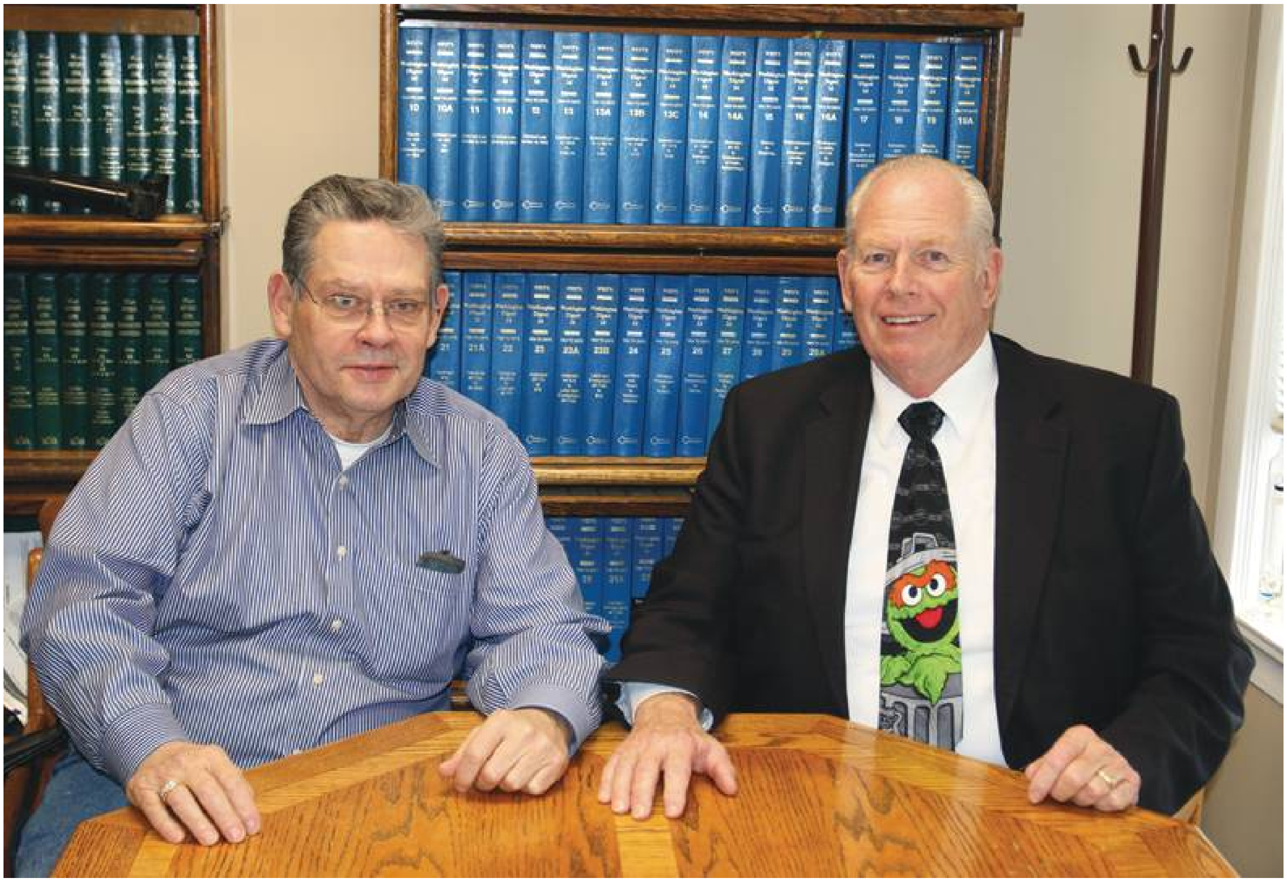
Spokane financial adviser offers alternative use of 401(k)

Baker says clients can convert accounts via in-service rollovers

Samantha Peone February 1st, 2018



-—Samantha Peone

David Baker, of Baker & Associates LLC, and Neil Humphries, of Humphries & Humphries Law PS, are working together on the alternative investment mechanism for 401(k) holdings.

A Spokane financial adviser has started promoting a retirement investment alternative for people who want more control over their employer-sponsored 401(k) funds while still employed.

Many people don't know much about their 401(k) accounts because employers often don't provide many retirement options to worry about, asserts David Baker, financial adviser with Baker & Associates LLC. Baker claims retirement fund investors can apply the funds in their 401(k) accounts better by directing that money into an investment portfolio the client has control over using an in-service alternate rollover.

"The benefit of doing that is you get to choose your own investment," says Baker.

According to the Baton Rouge, La.-based National Pension Corp. LLC's website, which also describes that corporation as a "dedicated ISAR education company," ISAR is a federally compliant retirement fund transaction that enables people to move their existing 401(k) funds into an individual retirement account at any age without penalty or taxes.

Baker and Humphries purchased a training course offered through National Pension Corp. that covered how to correctly facilitate ISAR. National Pension Corp. stopped selling the ISAR training program on Jan. 1, when the company entered into a proprietary agreement with a large broker, says Baker.

ISAR differs from in-service rollovers, which involves some companies enabling individuals to take money out of their 401(k)s for reasons that can include being at least 59 1/2 years old, employment termination, changing jobs, disability, or divorce.

In order to qualify for ISAR, clients must meet two requirements—they must be married, and their 401(k)s must be compliant with the Employee Retirement Income Security Act, says Baker.

To determine whether a 401(k) account is ERISA compliant, account holders should consult their plan administrators, he says.

Baker says clients can use ISAR to invest funds from their 401(k) accounts by following a few steps.

First, clients must move their 401(k) funds into a traditional individual retirement account.

A lawyer then works with clients to prepare the necessary paperwork and ensure ERISA compliance.

Spokane lawyer Neil Humphries is such an attorney.

His firm, Humphries & Humphries Law PS, which does business as Neil Humphries Law Office, shares a little over 1,400 square feet of space on the seventh floor of the Paulsen Center, 421 W. Riverside.

Once the paperwork is assembled, Humphries presents it to a judge. That judge signs an order that's then taken to the planned administrator of the client's 401(k) account.

The 401(k) funds are then transferred to a self-directed custodian, which is a company set up to comply with ERISA regulations that manages investment accounts chosen by the client and his or her financial adviser, says Baker.

Clients can invest in assets such as stocks, bonds, and mutual funds. They also can invest those funds into other assets, such as real estate, gold, silver, or anything approved under ERISA, he claims.

Depending on which investment options a client selects, Baker will either charge commission or a management fee, but not both, he says. His first financial advising meeting with a potential client is free, but he says his rates depend on what investments a client chooses.

Attorneys typically will charge a fee to handle the ISAR-related legal work, and each attorney decides what his or her fee will be, he says.

Humphries normally charges $200 per hour, says Baker.

While the investment strategy is legal under ERISA, he claims, people didn't start using it until about seven years ago. As far as he is aware, Baker claims, he and Humphries are the only two people that currently offer this investment strategy in Spokane.

Because the ISAR process can take time, Baker says he hasn't finalized any client portfolios as of Jan. 23 using that investment strategy. Also, he says he's unsure whether the new government tax laws will impact the investment strategy.

"We still have some work to do before we actually know all the answers to that, and we won't know them all until we get through through at least one tax year," he says.

One benefit to having a 401(k) is that employers can contribute to the account as well, he says. People are still able to keep of that perk through this investment strategy, he asserts, because employee contributions are affected only by current 401(k) investments, not previous ones.

The entire existing 401(K) balance can be withdrawn using ISAR, he says.

By only taking out previous 401(k) funds, people are able to keep their accounts, just without the funds clients transfer to IRAs using this investment strategy, he asserts.

As for actual investments, Baker says the real estate industry can be a strong option.

He claims real estate investments aren't as affected by stock market risks and inflation. He also claims real estate investments can be free of income tax if clients transfer assets to a Roth IRA, although they will pay a one-time tax penalty at the time of each transfer.

A traditional IRA is a tax-deferred account, meaning the account holder pays income tax only on withdrawals, while a Roth IRA is an after-tax account, meaning the deposits are subject to income tax, but withdrawals after retirement generally are income tax free.

"If you're using rental income as part of your retirement package to provide a reasonable or dependable income stream, to me, it's the most stable tool you can use," he says. "It's not subject to stock market risk, it either stays the same or increases over time, and it responds to inflation—as inflation goes up, so does rent go up. I don't know of a better tool."

However, Baker says, a problem arises in that people often don't have enough money in their 401(k)s to invest in real estate.

Baker claims clients can work around that by using a nonconforming loan to borrow up to 70 percent of the real estate purchase price to pay for the property.

A nonconforming loan is a loan that doesn't qualify to be purchased by federally supported Fannie Mae and Freddie Mac to be included in mortgage-backed securities, according to Westlake Village, Calif.-based PennyMac Loan Services LLC.

The advantage of nonconforming loan in this situation is that the loan doesn't factor in the borrower's other assets, Baker asserts—meaning, if something negative happens to the real estate, only the property can be penalized for debt and not other assets clients may have.

Baker claims a competent property manager should be able to return 6 percent or more on a client's investment in real estate.

He refers to the 6-percent-plus return as "leverage" because a real estate tenant essentially would pay back that loan through rent.

Along with being a financial adviser, Baker is a licensed insurance broker in all lines of insurance, and also holds a real estate license. Baker & Associates uses life insurance, annuities, and long-term care insurance and real estate in a financial adviser capacity to help people with their long-term and estate planning, he says.

Baker previously owned a property management company from 1980 to 2012. He and Humphries had worked together in different functions over that time.

Humphries graduated from the University of Washington School of Law and has been practicing since 1966. His practice involves real estate and eviction laws, probate and writing wills, and clients with various business-related issues.

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