LAW SCHOOL LOANS
Lender Code: 834241
America's Top Law School Lender

Volume I, Issue 2
February 9, 2006

NEWSLETTER

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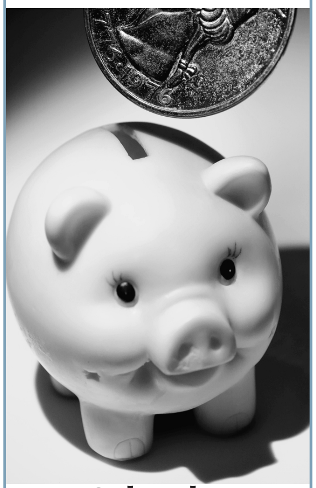

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APATHY, SPENDING SPREE, OR IRA? - DAYANA YOCHIM

Apathy or spending spree — take your pick. Those are the two main choices Americans tend to make when handling money in a former employer's work retirement plan.

But there is an alternative: control.

It's a difficult choice, particularly when faced with a mountain (or even an anthill) of formerly off-limits funds and a circular announcing a plasma-TV sales event. Studies show that 42% of workers give in to temptation and cash out their work retirement plans — 401(k)s, 403(b)s), etc. — when they change jobs. And we change jobs a lot. According to the Department of Labor, Americans move to a new employer once every four years, leaving a trail of money in our former bosses' plans.

But resistance has its perks: It doesn't trigger taxes, nor does it make us suffer through early-withdrawal penalties and fees. And it can pay off big-time in retirement (when, likely, plasma-TV prices will be more reasonable). All it takes is a little bit of legwork to move that money from a former work retirement plan into a self-directed IRA. And as long as it's IRA season and discount brokers are gunning for your business, you might as well get rolling.

What's the rush? For those with a money trail as long as their resume, consider this real-world warning a reader sent to me:

My late ex-husband worked for seven employers in 15 years, acquiring a 401(k) at each. Before he passed away in 2004, leaving no close relatives, he asked me to deal with his estate. His paperwork was chaotic, to put it kindly. I contacted all the trustees I could identify, inquiring about the accounts. Two out of seven responded (one in writing, one by phone), saying he had withdrawn the funds. Some refused to give me any information. Some just ignored me. One kept my letter for over a year, then stuffed it into an envelope and mailed it back to me with no information at all. My advice — roll those 401(k)s into your IRA IMMEDIATELY upon leaving an employer, or you and your heirs may never see the money again!

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TAX BENEFITS ON EDUCATION EXPENSES

When you are paying for law school, it is sometimes difficult to see the light at the end of the tunnel. Law school can be insanely expensive. However, did you know that some of your higher education expenses may help you reduce your federal income tax? The Internal Revenue Service allows tax savings for individuals and families who pay higher education costs. The benefits vary depending on your eligibility, but both deductions, which reduce the amount of income subject to tax before the tax is calculated, and tax credits, which reduce the amount of income tax dollar-for-dollar after the tax is calculated, are offered by the IRS.

Hope Scholarship Tax Credit: One type of benefit offered by the IRS is the Hope Scholarship Tax Credit. This tax credit may be worth up to $1,500 per eligible student for a taxpayer who paid qualified tuition and related expenses. The catch is that the Hope Scholarship Tax Credit only applies to students in their first two years of college. The eligible student must be enrolled at least half time and be working toward a degree or educational credential. This tax credit applies to students who paid for qualified expenses, including tuition and fees, but excluding room and board, books, and transportation.

The Hope Scholarship Tax Credit is designed wto be reduced or phased out as the taxpayer's income increases. For a single filer, the reduction begins with income of $40,000 and the credit is eliminated at $50,000. For joint filers, the reduction

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Although the market for student loan services is extremely broad, our company has chosen to focus on one elite niche: We cater to the particular needs of law students and graduates. On average, a juris doctorate student will have around $100,000 in student loans by the time he or she graduates - a much larger amount than many other kinds of graduate students. A J.D. will also often have questions that only someone with a legal background would think to ask. Established and run by attorneys, Law School Loans is prepared to fulfill the needs of law school graduates at every level. We invite you to visit us at www.LawSchoolLoans.com.

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begins with income of $80,000 and the credit is eliminated at $100,000. Also, the credit may only be claimed by either the student or their parent. It is a "per student" credit intended to be used by parents for dependent students or by independent students.

Lifetime Learning Tax Credit: After completing your first two years of education, you become eligible for a Lifetime Learning Tax Credit to help defray the costs of tuition and related expenses. You may claim a Lifetime Learning Tax Credit of up to $1,000 if the eligible student is enrolled in at least one course. For this type of tax credit, you do not need to be pursuing a degree. Even if you are just taking classes to improve your job skills, you may be eligible for this credit.

The Lifetime Learning Tax Credit equals 20% of the first $5,000 of tuition and related fees paid by the taxpayer. The reduction for this tax credit, based on income, is the same as with the Hope credit. This credit is designed as a "per return" credit. Regardless of the number of dependent students a parent claims on his/her tax return, he/she may only take one Lifetime Learning Tax Credit.

A taxpayer may take only one of the credits for each dependent student each year. For example, if a family has two children in college--one in the second year and one in the fourth year--the taxpayer may claim the Hope credit for one and the Lifetime Learning credit for the other. A taxpayer may also claim the Hope credit during the first two years of college and the Lifetime Learning credit for the remaining years. There is no limit to the number of years you may take the Lifetime Learning credit; so it does apply to graduate-level students as well.

Student Loan Interest Deduction: Students who paid interest on student loans may deduct up to $2,000 of the interest paid. This adjustment reduces the amount of taxable income, and a taxpayer may take this deduction even if he/she does not itemize deductions. Eligible loans include those taken out to pay tuition, fees, living expenses, books, supplies, transportation, and equipment expenses. Most federal and private education loans would be eligible for this type of deduction. However, the student must be the taxpayer, the taxpayer's spouse, or his/her dependent; and the student must be enrolled at least half time and working toward a degree.

This deduction applies to interest paid during the first five years of repayment. Similar to education tax credits, the deduction is reduced as income increases, beginning at $40,000 for single filers and $60,000 for joint filers. If you are a single tax return filer with an income of $55,000 or a joint tax filer with income greater than $75,000, you will not be eligible for this interest deduction.

Employer Provided Educational Assistance: The tax code allows employees to exclude up to $5,250 of employer-provided education benefits from

their taxable income. This means that employers can provide educational benefits such as tuition, fees, books, supplies, and equipment tax free. However, this only applies to undergraduate-level courses.

Education IRAs: Education IRAs (Individual Retirement Accounts) are trusts or custodial accounts designed to help families save for a child's education. The money in these accounts grows tax free until withdrawn. The student benefiting from an education IRA is permitted to withdraw the funds at any time. If the amount does not exceed the student's higher education expenses in a tax year--including tuition, fees, books, supplies, and room and board--the withdrawal will be tax free.

If a student withdraws more than his/her qualified expenses for the year, a portion of the education IRA withdrawal will be taxable. The taxable amount will be considered the same as income and must be reported as earnings. The student's taxable withdrawal may also be subject to a 10% additional tax.

Taxpayers benefiting from a tax-free education IRA distribution cannot take advantage of the Hope Scholarship or Lifetime Learning credit in the same year.

Taxpayers may choose to withdraw funds from a Roth IRA or traditional IRA without penalty if the funds will be used for the higher education expenses of the taxpayer, spouse, child, or even grandchild. A portion of the amount withdrawn will be taxable, but there will not be an additional 10% tax for an early withdrawal as long as the funds are being used for tuition, fees, books, equipment, and room and board for the year.

Student Loan Cancellation: If a borrower takes a community service job--with a nonprofit, tax-exempt, charitable, or education institution that provides loan forgiveness--he/she may not need to include the cancelled amount in his/her gross income for the year. To qualify, the loan must have included a provision for this type of program; and it must have been issued by a qualified lender--including the government, a tax-exempt public benefit corporation, or an educational institution--with the intention of helping borrowers attend educational institutions.

For more information on saving money on your taxes due to educational expenses, contact a tax professional or visit the IRS' website at www.irs.gov. Taking advantage of these programs is one way to begin saving money immediately on your education.

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Apathy, Spending Spree, OR IRA countinued from page 1

With the average 401(k) balance in the $50,000 range, it seems a shame to either fritter away those retirement dollars by cashing out or forgetting about long, lost accounts until it's too late.

Why move?

You may be forced to: Most employer-sponsored retirement plans will force you to move your money (via rollover or direct transfer) if you have less than $5,000 in your account. If you have $5,000 or more, though, you may leave the money in your 401(k) until the normal retirement age specified by that plan.

You'll have more investment choices: Most employer-sponsored retirement plans offer a limited number of investment options. When you roll that money into a self-directed IRA, your choices open up: You've got the entire market (including mutual fund families, money market funds, and ETFs) at your disposal. And, by the way, work retirement plans aren't free to participants. Even if they aren't clearly stated, administrative fees are baked into the plan. With an IRA at a discount-brokerage firm, all of those fees are spelled out up front. (Things to look for include transfer fees, minimum account balances, administration fees, inactivity fees, and trading commissions. Learn more here on opening an account.)

You'll have more freedom in retirement. Uncle Sam has lot of rules for retirees, one of which requires people aged 70 1/2 to begin taking distributions. If your retirement funds are in a 401(k) plan, you are also subject to the distribution rules set forth by the plan administrator. Those tend to be more rigid than those at the companies that manage IRAs. Customer service can also be a factor. Discount brokers tend to act more like banks — focusing on keeping your business. On the other hand, 401(k)s have a captive audience of company employees and a stream of new business whenever anyone is hired. If it's the investment choices within the plan keeping you there, you'll likely have access to the same ones in an IRA.

Roth or traditional IRA?: The IRS allows 401(k) transfers only to traditional IRAs, which are treated similarly in terms of taxes — your contributions are made with pre-tax dollars, and you pay the piper when you withdraw the funds. So the Roth IRA, which requires you to pay taxes now on your contributions so you can avoid The Man at retirement, is off the table.

There is a workaround, however. You can roll your money into a traditional IRA and then convert it to a Roth IRA. That entails paying taxes on everything in your 401(k) — unless you have some after-tax contributions. Depending on the size of your 401(k), converting may or may not be practical. If you can afford to pay the taxes without withdrawing cash from the IRA, then it might be worth it. The prospect of a tax-free retirement is very appealing. If you have to take the money out of the IRA account to pay the taxes, however, it may be best to leave it in a traditional IRA.

And the amount you roll over into an IRA is not limited, since whatever money you stashed in your old 401(k) was already accounted for, tax-wise, in the years in which you put it away. In other words, the rollover amount does not count as IRA investments for the year in which you do the rollover.

Moving money into a new employer's plan: Rolling old 401(k) money into a new 401(k) plan is one option, though not all employers permit transfers from old 401(k)s into the new. There are advantages and disadvantages to doing so, but it all depends on the details of the new plan.

For example, moving money into a 401(k) instead of an IRA preserves your opportunity to take a loan from the plan (for a down payment on a house, for example). That is, if the new plan offers that option. A drawback to going straight from one 401(k) to another would be if the investment choices in the new plan stink (say, if you could pick only company stock) or if the plan fees were outrageous.

If you're chomping at the bit to invest in your new plan because your boss offers to match a percentage of your investing dollars, dream on. You won't get matching funds on your transfer. But still, a good plan has those other lovely qualities mentioned above.

Making a plan-to-plan move: Fool tax expert Roy Lewis explains how it's done:

"Transferring your money to a new employer's 401(k) plan generally can be done in one of two ways. You can take a distribution of the funds from your prior employer and deposit it (roll it over) into the new employer's plan. Second, if the new plan permits it, you can make the transfer through a trustee-to-trustee transfer.

"The trustee-to-trustee transfer option is always preferable because the IRS requires that if you take a distribution, even one that you will roll over to another 401(k) plan, the employer must withhold 20% of the amount distributed for tax purposes. You won't be able to get this money back until you file your tax return for the year in which the distribution took place and claim that amount as taxes withheld. Additionally, if you aren't yet 59 1/2 and don't deposit the distribution check and/or the amount withheld — which must be obtained from sources outside the distribution — within 60 days of the distribution, those amounts will be subject to income taxes and the 10% early distribution penalty."

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When to stay put

We nearly always advocate taking your 401(k) money with you when you leave a job. But there are times when it makes sense to leave the money with your former employer. Consider doing so if:

More on making your IRA A-OK:

Save Like It's 2006
Roth IRAs Often Beat 401(k)s
60-Second Guide to Opening an IRA
It Pays to Ignore Your IRA
Redefining the "R" in IRA

Dayana Yochim owns several of the financial products mentioned in this article but has no shares in any of the big brokerages mentioned. The Fool's disclosure policy has no hidden fees.