

Help! I Think I'm About to Be Fired

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Q. I think I'm going to lose my job. I don't have an emergency fund, but I do have a 401(k), an IRA and a life insurance policy of a cash value of \$10,000. I also have credit cards with no balances and spending limits of \$5,000, \$11,000 and \$12,000. If I need money to hold me over, where should I take it?

A. We're going to assume that unemployment benefits wouldn't cover all of your expenses. Before we dig into the use of your potential resources, you should take a good hard look at your budget.

If you don't have one, it's essential that you create one, because you are going to want to find every possible way to save, said **Claudia Mott, a certified financial planner with Epona Financial Solutions in Basking Ridge, N.J.**

Mott said creating a budget can be done with paper and pencil, a spreadsheet or any of the free financial planning tools that are available online. She recommends you break your living expenses down into two major categories. The first is non-discretionary, or the items you can't live without such as food, shelter and transportation. The second is discretionary, which include the non-essentials, such as restaurants and entertainment. "When times are tough and cash is limited, cutting back is imperative," Mott said. "You need to determine exactly what you will need to have by way of supplemental income." She said it's good to know that you have some financial resources available and it's important to understand what each option costs in terms of taxes, interest and penalties before deciding which makes the most sense to use.

Of the list you provided, the two options that might get you access to money at no cost would be the cash value of your life insurance and the Roth IRA, Mott said. "Cash value can be withdrawn tax-free up to the amount of the premiums you have paid," Mott said. "A call to your insurance carrier should enable you to determine how much of the \$10,000 reflects the basis in your policy and what would be taxable income." If your IRA is a Roth, the contributions you've made can be withdrawn at any time both tax- and penalty-free.

"Because the contributions are made with after-tax dollars, withdrawals are not treated as taxable income," she said. "However, if you are under age 59 ½ the earnings on your principal would be subject to a 10% early withdrawal penalty." A penalty can also be assessed if the age requirement is met but earnings are withdrawn less than five years from the date the contribution is made, she said.

If you need to dip into the other retirement savings accounts, the withdrawals will be reported as taxable income. In addition, if you are under age 59 ½, you will pay a 10% penalty on the value of the withdrawal, Mott said. "There are certain circumstances that might enable you to take a penalty-free hardship withdrawal from your 401(k) if the plan offers them," she said. "You will need to work with the employee benefit department to determine if you would qualify."

Vince Pallitto, a certified financial planner and certified public accountant with Summit Asset Management in Florham Park, N.J., says he would not recommend taking from your 401(k) or IRA because of the taxes and penalties. "That is effectively taking two steps forward and one back," he said.

He prefers a combination approach. "If the expected monthly shortfall is less than \$500 and the prospects of finding a new job are high, then I would say to use a 0% credit card," he said. (Here's a list of the Best Low-Interest Credit Cards in America if you want to see what options could be available for you.) "Hopefully you would get a job before the credit card balance reaches 50% of the cash value of the life insurance policy."

Pallitto says up to 50% of the insurance policy's cash value because you can then use the policy to pay off the cards — if you have to — and still keep the policy intact.

If you do lose your job, Mott said you should consider part-time work to cover at least some of your expenses.

And when you're back working full time, you should make an emergency fund a priority, she said.

"A good rule of thumb for an individual is to set aside three to six months of living expenses in a separate savings account," she said.