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Cramer on Retirement: Should You Buy a Small Business With Your Nest Egg?

BY [Jim Cramer](#) | 10/29/12 - 06:00 AM EDT

[See what Jim Cramer and Stephanie Link are trading today.](#)

By Jim Cramer and Wally Konrad, former senior editor for Smart Money magazine

NEW YORK ([TheStreet](#)) -- The ads are peppered throughout the Internet:

"Buy or start a small business using your retirement savings!"

"Finance a business or a franchise from your 401(k) -- without debt!"

Players like **Guidant Financial** and **IRA Financial Group** have armies of advisers waiting to tell you how to use a little known tax loophole to redirect your nest egg into what may be one of the riskiest investments ever: a small business.

The tax situation works like this. If you invest your 401(k) funds from a former employer to buy or start a business, you will be able to do so without the taxes and penalties associated with early 401(k) withdrawals.

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Jim Cramer and Stephanie

Instead you roll over the money into the business's [retirement plan](#) and use that money to invest in stock in the company. The rollover part means you avoid taxes and penalties. At the same time, buying the stock provides cash to start or buy the business.

Link
actively
manage a
real
portfolio
and reveal
their money

[Where to Hide When Bank Stocks Bomb](#)

The strategy only applies to C corporations (companies that are taxed separately from their owners), and you cannot use the 401(k) money to pay yourself or anyone else a salary. Keep in mind you can't roll over your 401(k) unless you have left your job. Funds from a 401(k) may be used to finance the entire purchase or start-up or can be used in conjunction with [Small Business](#) Administration loans and other financing. Like most tax dodges, this one is complicated. Most people who decide to use it pay a third party like Guidant or one of the other firms to help set up the [new company's](#) retirement plan and administer it each year.

Guidant CEO, Jeremy Ames, says the company has helped 7,000 people [invest](#) in a business since it started 10 years ago. Most bought existing small businesses, while only a few clients use the strategy for start-ups. After two years, 86% to 94% of Guidant clients were still in business; after four years, 60% survived, according to Ames.

[Banks Soon May Ramp Up Risk](#)

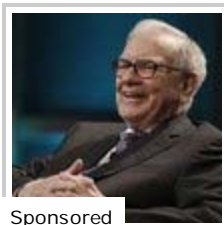
Impressive as that may sound, the truth is this strategy is only appropriate for a tiny percentage of 401(k) savers -- those who are wealthy enough to know they have enough saved for a comfortable retirement and sophisticated enough to buy a business that will thrive.

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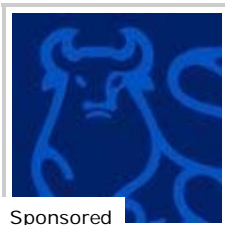
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David Nilssen • a year ago

I appreciate Mr. Cramer covering this small business or franchise financing opportunity because it exposes another great way for people to take ownership over their personal outcomes and invest in an asset they can control. What it fails to point out is that Rollovers for business startups are an extremely important part of small business - and our American economy. Our clients employ almost 50,000 people annually across the United States. As the article pointed out, our clients succeed at a rate much greater than general small businesses. According to FranData* our small business clients generate over \$800M in annual economic output and an additional \$1.3B in indirect annual economic output. That's a total annual economic output of more than \$2.1B. I wish that was the story that Mr. Cramer told.

The article dramatizes a biased perspective by highlighting that an unsuccessful business owner will lose retirement assets if their business does not succeed. Is this an isolated risk? Of course not. Whenever you invest in any asset (even with stocks) - there is risk. Anyone who buys stocks should work with a qualified professional to help them. The same goes for small business. His example where a dry cleaning company didn't do very well fails to point out that the way the business was capitalized didn't contribute the loss. In fact, it likely helped the business mitigate risk because it didn't have any loans. Rollovers for business startups allow an individual to invest a portion of their retirement assets into a business without taking a taxable

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