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ICI VIEWPOINTS

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The Facts on Limited Access to Retirement Funds Before Retirement

By Mike McNamee

Third in a series of Viewpoints *postings on key facts about the 401(k) and the American retirement system*

One of the many strengths of the 401(k) system is its flexibility. Policymakers have built into 401(k) plans a careful mix of incentives that help workers save and preserve their savings for retirement—while still allowing limited access to their funds, in case of need, through hardship withdrawals and loans.

Recently, some policymakers and observers have been raising alarms about "401(k) leakage"—claiming that this flexibility is undermining the retirement security of workers who access retirement funds before retirement age. Their concerns are based on estimates that a substantial fraction of 401(k) contributions are "leaking" out.

In a series of posts on retirement, *ICI Viewpoints* is looking at the facts and data surrounding 401(k) plans and the broader retirement system of which they're a part. That requires puncturing myths that sometimes dominate discussions of retirement policy—including these estimates of rampant leakage.

There are three ways that a 401(k) participant can get access to his or her account before retirement—through 401(k) loans, withdrawals, and access to funds during job changes. Let's look at each, based on data assembled by ICI Research and other experts.

401(k) Loan Amounts Are Modest

The EBRI/ICI 401(k) database, which covers more than 64,000 plans, provides a very clear picture of 401(k) loans. As the latest EBRI/ICI study of that database shows, fewer than one in five 401(k) participants have loans outstanding and, in those cases, loan amounts are modest. Among 401(k) participants with loans outstanding, loans on average represent only 14 percent of the remaining account balance.

And if every 401(k) participant with an outstanding loan failed to repay? Overall 401(k) plan assets would fall by less than 2 percent.

That small impact has to be weighed against the benefit that access to loans provides. Research finds that the availability of the loan feature actually boosts participation and contributions in 401(k) plans. This suggests that participants appreciate this flexibility and are more likely to participate in a plan and contribute more if they know they will have access to a portion of their assets if needed.

401(k) Withdrawals Are Rare

Participants in defined contribution (DC) plans, such as 401(k) plans, generally do not tap their accounts through withdrawals while working. Here again, the numbers are clear. The latest data from ICI's DC plan recordkeeping survey, which covered the first three quarters of 2012, finds that only 2.8 percent of DC plan participants took withdrawals, with only 1.4 percent taking hardship withdrawals.

Most Pension Assets Are Preserved at Job Change

Several studies show that most pension assets are preserved at job change. For example, Vanguard's recent examination of its recordkeeping data revealed that about 30 percent of all DC plan participants could have taken their account as a distribution because they had terminated employment in 2011 or prior years. Those workers preserved 96 percent of their plan assets available for distribution.

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A 401(k) participant could take advantage of these opportunities to draw funds from his or her account. But the data clearly suggest that few 401(k) participants are doing that. Instead, most are responding to the incentives these plans offer to save responsibly and work toward a secure retirement. In the coming days, we'll be posting more items on *ICI Viewpoints* regarding the facts of America's approach to retirement.

For more key information on retirement, please visit our Retirement Resource Center or read the other entries in this Viewpoints series:

- No Accident: The Strengths of the 401(k) System
- 401(k) Plans Work in a Balanced Approach to Retirement Security
- The Facts on Limited Access to Retirement Funds Before Retirement
- The Facts on Fees and 401(k)s
- Americans Support Their 401(k)s

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