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New Research from EBRI:

The Impact of "Leakage" on 401(k) Accumulations

WASHINGTON—Would restricting preretirement withdrawals from 401(k) plans help or hurt retirement savings in America?

New analysis conducted by the nonpartisan Employee Benefit Research Institute (EBRI) for the ERISA Advisory Council finds that "leakage"—preretirement access to 401(k) plan savings by workers, either through loans, hardship withdrawals, or payout at job change—can have a negative impact on 401(k) accumulations (defined as 401(k) account balances plus IRA rollovers originating in 401(k) plans) at age 65.

Using its proprietary Retirement Security Projection Model® (RSPM), the EBRI analysis found that the combined impact of the three primary types of leakage on 401(k) accumulations at age 65 of younger workers with at least 30 years of 401(k) eligibility reduced the probability of reaching an 80 percent real replacement rate (combining 401(k) accumulations and Social Security benefits) by 8.8 percentage points for the lowest-income quartile and 7.0 percentage points for those in the highest-income quartile. However, the analysis also revealed that approximately two-thirds of that impact was associated with the cashouts that sometimes occur at job change.

However, and as the testimony presented to the ERISA Advisory Council makes clear, it's one thing to quantify the impact of not allowing early access to these funds—and something else altogether to assume that participants and plan sponsors would not respond in any way to those changes, perhaps by reducing contributions, potentially offsetting some or all of the prospective gains from restricting access to those funds.

"This analysis needs to be accompanied by a very strong caveat that there are clear data gaps that will need to be filled," said EBRI Research Director Jack VanDerhei. "For example, we have found in previous research that participants in plans with a loan option have higher contribution rates than those without such access, and a similar relationship may exist with respect to the availability of hardship withdrawals. Removing or restricting these plan options would likely reduce levels of 401(k) participation or access, and that could result in a significant drop in retirement savings for some employees eligible for participation in a 401(k) plan."

Results of EBRI's modeling were presented by VanDerhei at a June 17 hearing of the ERISA Advisory Council at the U.S. Department of Labor. His full testimony on "The Impact of Leakages on 401(k) Accumulations at Retirement Age" is online at www.ebri.org/pdf/publications/testimony/T-180.pdf

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