

Impact on Retirement Deficits of Cashing Out 401(k) Balances

How important is rolling over defined contribution assets to an individual retirement account (IRA) or another defined contribution plan at job change vs. cashing out to the current state of retirement income adequacy? Using its Retirement Security Projection Model[®] (RSPM), the Employee Benefit Research Institute (EBRI) explores this question by comparing projected retirement deficits of U.S. households in the current state — where there are rollovers into IRAs from defined contribution (DC) plans — vs. a hypothetical state where workers never roll over their DC money to an IRA at job change but instead always cash out assets that are not retained in a defined contribution plan.¹

The baseline RSPM[®] model analyzes retirement income adequacy for various cohorts by simulating households through retirement age, taking into account:

- Social Security.
- Defined contribution (DC) balances.
- IRA balances from rollovers of DC plans.
- IRA balances from contributions to traditional and Roth IRAs.
- Defined benefit (DB) annuities and/or lump-sum distributions.
- Net housing equity.

Under this model, EBRI estimates that the aggregate retirement deficit is \$3.83 trillion for U.S. households headed by those between the ages of 35 and 64.

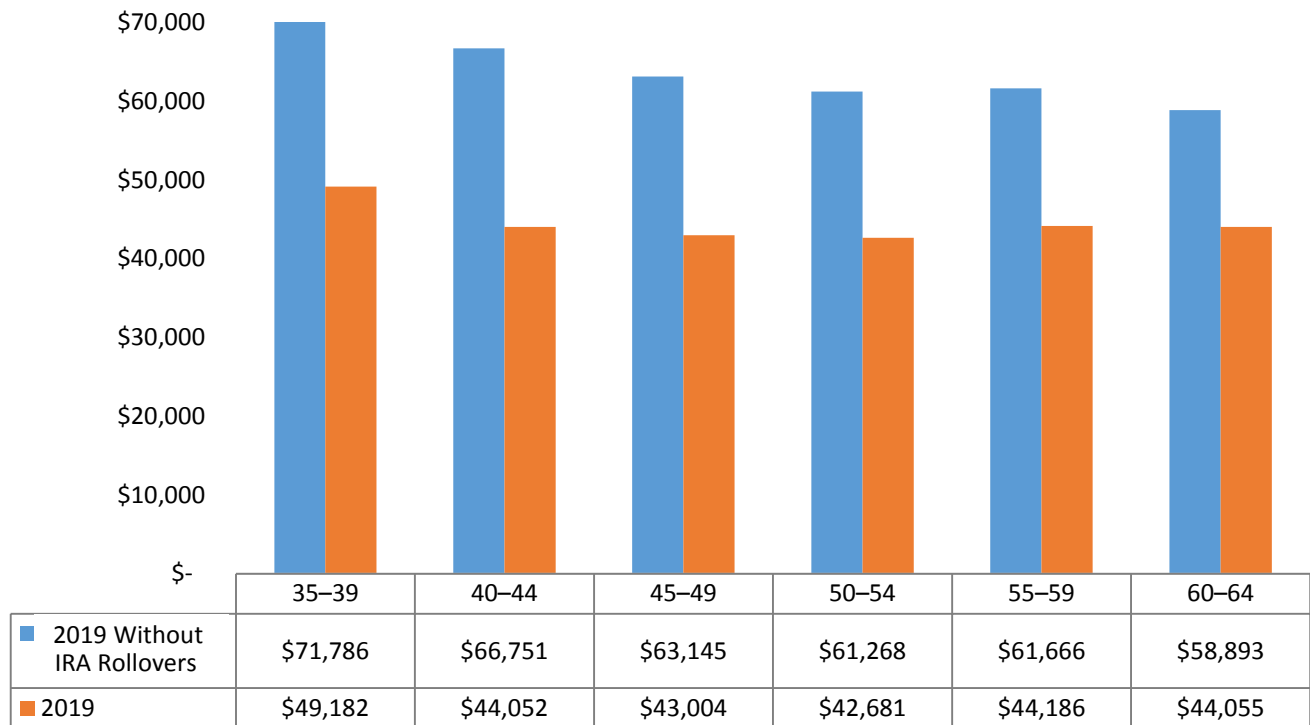
This impact of rollover analysis focuses on five-year age cohorts from age 35 through age 64. It finds that for the youngest workers, the absence of any IRA rollovers has a very material impact on retirement deficits: EBRI projects that the baseline average retirement deficit for that age cohort of \$49,182 would increase by nearly half (46 percent) to \$71,786 if IRA rollovers were assumed never to occur.

A similar magnitude of increase in deficits is seen for those ages 40–54, ranging as high as a 52 percent increase in projected retirement deficit for the ages 40–44 cohort.²

And while the projected increase in retirement deficit is lowest for older workers, it is still material. For those ages 60–64 — who have the lowest opportunity to experience job change (and therefore roll over) due to time remaining in the workforce — the deficit would increase by about a third, from \$44,055 to \$58,893, if IRA rollovers did not occur.

These findings highlight the importance of keeping money in the retirement system — and avoiding leakage at job change — when it comes to retirement deficits for U.S. households.

Average 2019 Retirement Savings Shortfalls,* by Age Cohort: Baseline vs. No IRA Rollovers



Sources: EBRI Retirement Security Projection Model[®] versions 3501 and 3459.

* The Retirement Savings Shortfalls (RSS) are determined as a present value of retirement deficits at age 65.

Previous *Fast Facts* based on RSPM[®] have looked at:

- How much will retirement-reform proposals reduce retirement deficits?³
- How Eliminating Retirement Plan Leakage Can Get Workers On Track for Retirement Success⁴
- How Much Might Defined Contribution Savings Benefit From Auto Portability?⁵
- How Much Would Auto-Portability Help Retirement Reform Proposals to Reduce Retirement Deficits?⁶
- How Much Would OregonSaves Decrease Retirement Deficits in Oregon?⁷

These EBRI publications show the extent to which legislative activity (on either a federal or state-wide basis) and plan design modifications might improve retirement income adequacy for various age cohorts.

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¹ In the “Without IRA Rollovers” scenario, the baseline assumptions are modified to assume there are no FUTURE IRA rollovers when a defined contribution participants changes jobs and that these amounts are cashed out instead.

² While it may seem counterintuitive to have a larger impact for the 40–44 age cohort, the following set of circumstances need to be considered: the 40–44 age cohort has much larger defined contribution plan balances today than do those in the 35–39 cohort; if rollovers are eliminated today, there will be a larger impact on existing defined contribution plan balances for the 40–44 age cohort than the 35–39 cohort. While this phenomenon is also true of cohorts older than age 44, the fact that future (as opposed to current) defined contribution plan accumulations for this group will be sufficiently smaller than those for younger cohorts will result in a net decrease in the impact.

³ *EBRI Fast Facts*, June 19, 2018, #305

⁴ *EBRI Fast Facts*, July 16, 2018, #307

⁵ *EBRI Fast Facts*, July 30, 2018, #309

⁶ *EBRI Fast Facts*, September 4, 2018, #315

⁷ *EBRI Fast Facts*, October 15, 2018, #317

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