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by

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**“Disposition of DC Accounts: Who Rolls Over into an IRA?
Who Leaves Money in the Plan and Who Withdraws Cash?”**



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Disposition of DC Accounts: Who Rolls Over into an IRA? Who Leaves Money in the Plan and Who Withdraws Cash?

By Sudipto Banerjee, Ph.D.

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Introduction

It is well known that the private retirement asset landscape in the United States has shifted from an emphasis on defined benefit (DB) (pension) plans, to one where defined contribution (DC) plan designs (primarily the 401(k)) dominate (Olsen and VanDerhei, 1997; Poterba, Venti, and Wise, 2007). Along with this shift in design, individual workers now carry a greater responsibility of managing their retirement savings. This requires making decisions which could seriously affect their retirement security.

A poor decision—for example, withdrawing the money prior to age 59½, incurring a 10 percent penalty in addition to income tax on that distribution—could reduce their retirement assets significantly. IRAs in some cases offer a larger set of investment alternatives than individual workplace retirement plans, but may also bring with them higher investment and/or administrative costs. Consequently, it is of great importance that people make these decisions wisely.

Although the disposition of accounts is an important part of the DC system, the literature on this subject is relatively small (Copeland 2013, 2009, 2006; Sebelhaus, Bogdan and Holden, 2008). My testimony will focus on a study recently published by EBRI which documents the outcome of DC plans using a nationally representative survey (described below) and analyzing how the disposition decisions of older workers correlate with a number of demographic and financial variables.

Data

The data for this analysis come from the Health and Retirement Study (HRS), a study of a nationally representative sample of U.S. households with individuals age 50 and over. It is a biennial longitudinal survey with waves in even-numbered years, beginning in 1992. Data from 2008 and 2010 were used for this study and are combined and used as a single cross-section. In both years, HRS had asked the following question: “When you retired/left the employer, what did you do with the plan?”

- Withdrew the money/received cash settlement/lump sum.
- Rolled over into IRA.
- Left in the plan.
- Converted to/purchased annuity.
- Transferred to new employer.
- Lost benefits.
- Received/ receiving installments/took irregular payments.
- Receiving benefits now.

In 2010, an additional option, “expecting future benefits” was added and 2.5 percent of respondents chose this option. For comparison, this analysis groups them with the “left-in-plan” category. There were 654 responses in 2008 and 726 responses in 2010, resulting in a total sample size of 1,380. HRS-provided individual sample weights were used for the analysis.

Retirement or Job Change? The Outcomes Are Different

The respondents' decisions changed if they retired rather than remained active in the labor force after leaving their current employment. Figure 1 shows the differences in DC plan outcomes: Retirees were less likely to cash out, to roll it over to an IRA, or to leave it in the plan. But as expected, as retirees they were much more likely to receive benefits from these plans. Among those who continued to be in the labor force, leaving money in the prior plan was the most common outcome. More than 1 in 3 (34.8 percent) of those who still remained in the labor force left their money in the plan, compared with 27.0 percent who rolled over their money to an IRA and 18.4 percent who cashed out.¹

By Account Balance

Figure 2 shows how the disposition of DC accounts varied by the amount left in the plan (in 2010 dollars) at the time of separation from the employer. For a large part of the sample (623 observations), the account balance was unknown, and the majority of this group were receiving benefits, but there were some clear trends. First, the percentage of workers cashing out decreased as the account balance increased. For accounts with a balance of less than \$5,000, the cash-out rate was 46.1 percent, compared with 9.6 percent for accounts with a balance of \$100,000 or higher. On the other hand, the choice to rollover to an IRA increased steadily with account balance: Only 13.7 percent of those with an account balance of less than \$5,000 rolled over their assets to an IRA, compared with 47.0 percent of those with an account balance of \$100,000 or higher. There was, however, little difference between the percentage of workers who left their assets in the plan by account balance (between 31.2 percent and 32.0 percent) for account balances less than \$100,000, compared with 25.4 percent for accounts with balances higher than \$100,000.

By Income

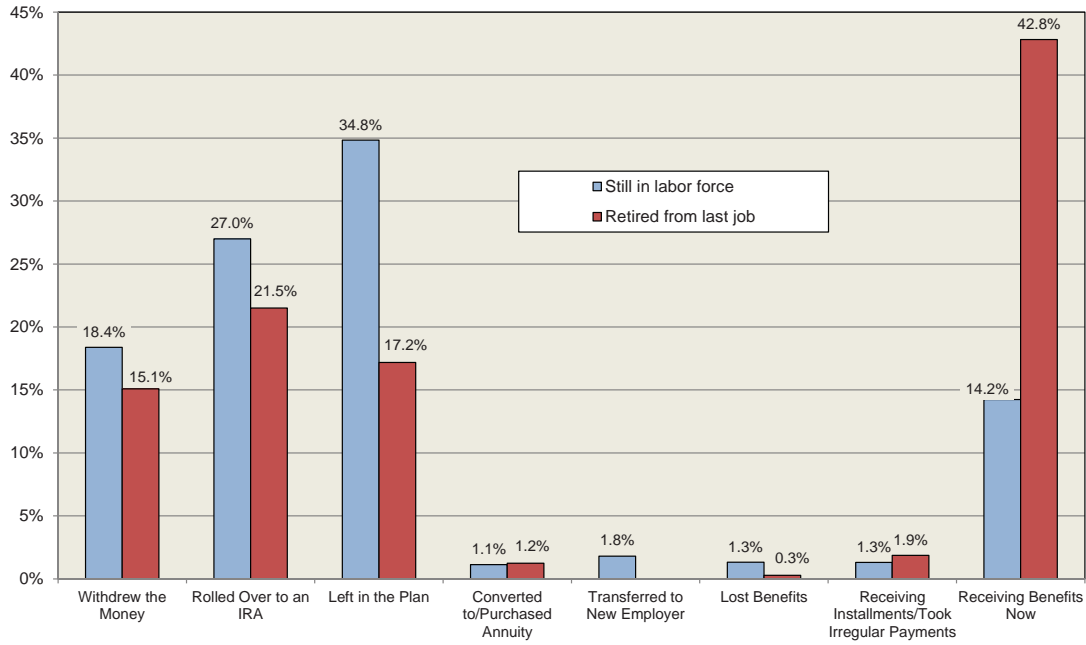
Figure 3 shows the distribution of DC account disposition by wage income (in 2010 dollars) at the time of separation from the employer. There were some trends similar to those illustrated in Figure 2. First, cash outs decreased with income: For example, 30.5 percent of those with annual wage income of less than \$25,000 cashed out, compared with 9.8 percent of those with wage income of over \$75,000. Second, IRA rollovers increased with income: 18 percent with annual wage income less than \$25,000 rolled over their assets to an IRA, while 29.7 percent with wage income of \$75,000 or above did so. Third, the decision to leave money in the current plan did not vary significantly with income: For the three income groups below \$75,000, the percentage of respondents who left money in the plan ranged from 27.1 percent to 26.4 percent, but for individuals with income above \$75,000 this decreased to 20.6 percent.

By Ownership of an Existing IRA

It might be expected that those who already own an IRA should find it easier, or are more inclined to roll over their DC account balance to an IRA. Figure 4 shows that was, indeed, the case: Of those already owning an IRA, 33.7 percent rolled over their DC balance into an IRA, compared with 19.3 percent of those who did not already own an IRA. Also, IRA owners were much less likely to cash out, as 21.4 percent of those without an existing IRA cashed out, compared with 7.2 percent of IRA owners.

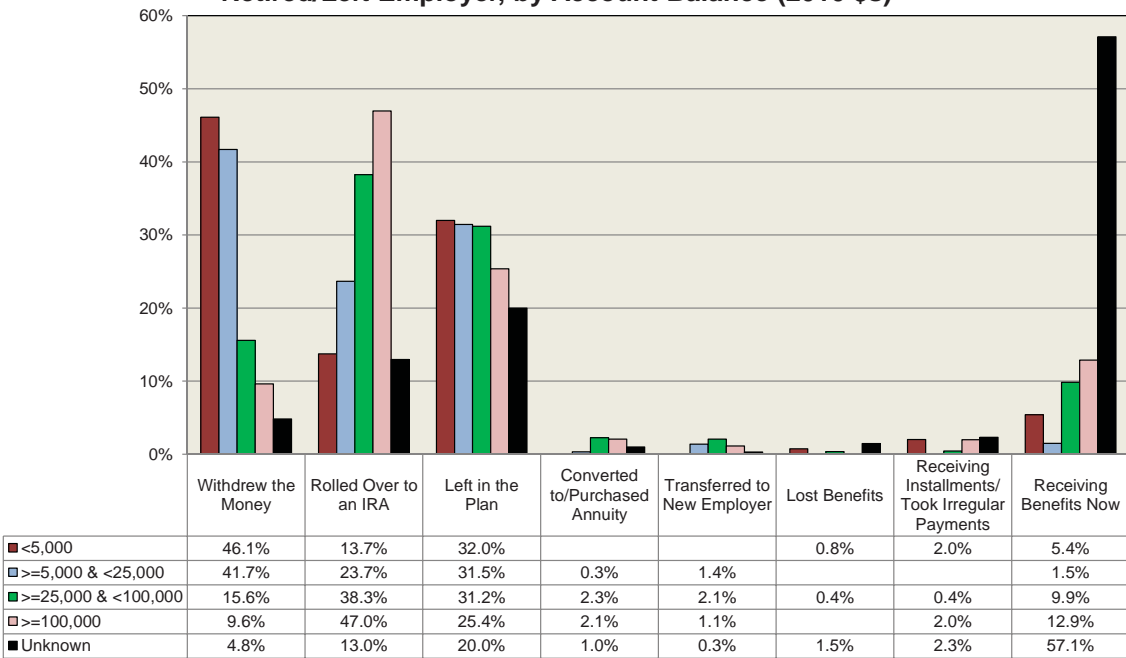
The difference between IRA owners (27.1 percent) and those with no existing IRA (24.8 percent) in terms of the choice to leave the money in the plan was small. So, for the group that left the money in the current plan, neither income, account balance, nor already owning an IRA appeared to influence that decision. This indicates behavioral factors rather than financial factors could be driving some of these decisions, though it might also be a non-decision—a simple case of inertia, leaving the money where it already is, rather than making an affirmative choice, or perhaps deferring any decision until they need the money.

Figure 1
Distribution of DC* Plan Asset Disposition When Respondents Retired/Left Employer, by Labor Force Status



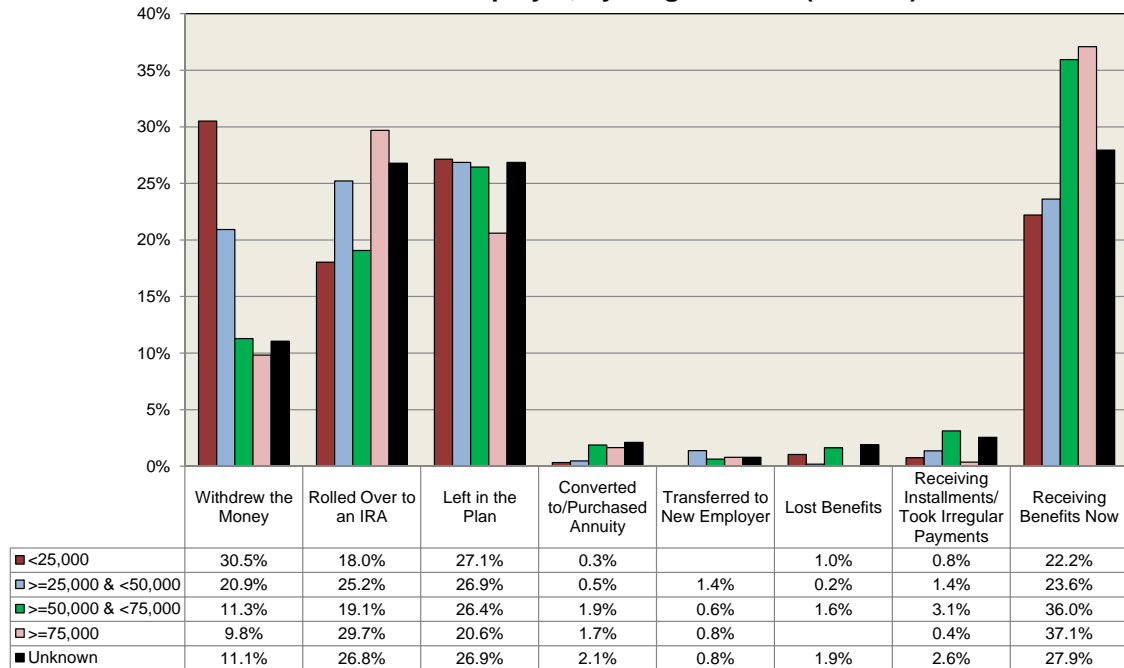
Source: Employee Benefit Research Institute estimates from the Health and Retirement Study (HRS).
 * Defined contribution.

Figure 2
Distribution of DC* Plan Asset Disposition When Respondents Retired/Left Employer, by Account Balance (2010 \$s)



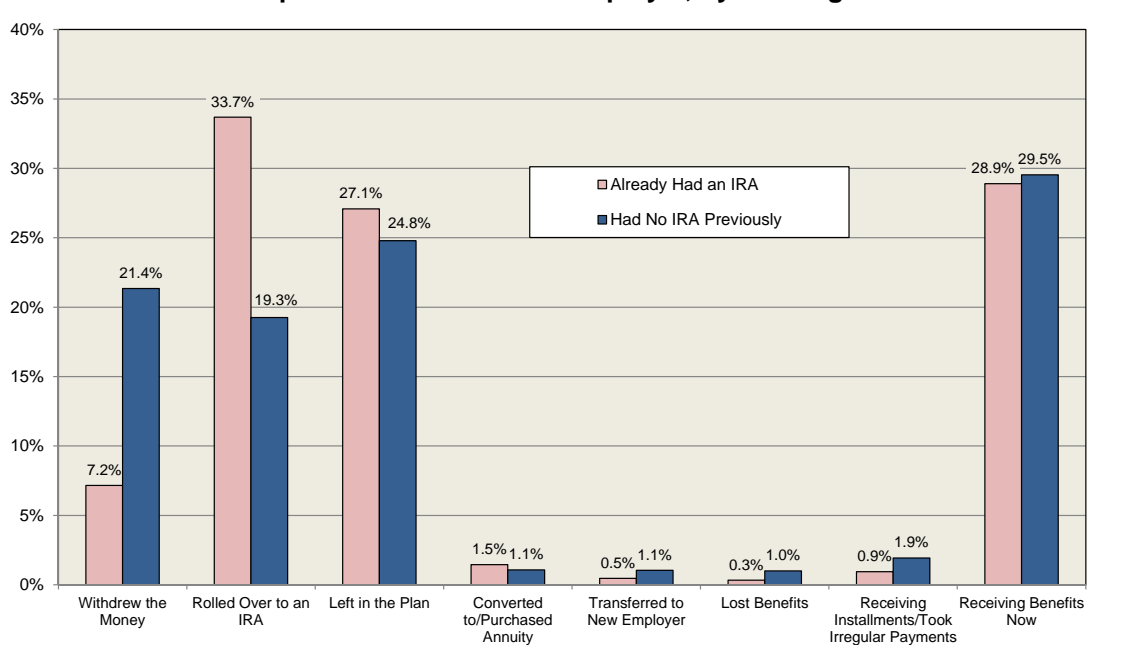
Source: Employee Benefit Research Institute estimates from the Health and Retirement Study (HRS).
 * Defined contribution.

Figure 3
Distribution of DC* Plan Asset Disposition When Respondents Retired/Left Employer, by Wage Income (2010 \$s)



Source: Employee Benefit Research Institute estimates from the Health and Retirement Study (HRS).
 * Defined contribution.

Figure 4
Distribution of DC* Plan Asset Disposition When Respondents Retired/Left Employer, by Existing IRA



Source: Employee Benefit Research Institute estimates from the Health and Retirement Study (HRS).
 * Defined contribution.

By Debt

Figure 5 shows how the decisions varied by the level of debt (credit card balances, medical debts, life insurance policy loans, loans from relatives, etc.) held by the household.² There were two general trends: First, cash outs increased with debt. For example, 12.4 percent of respondents with no debt had cashed out, while 27.3 percent of those with debt between \$3,000–\$10,000 did so, as did 23.8 percent of those with debt of \$10,000 or higher. Second, IRA rollovers decreased as debt levels increased: 27.7 percent of those with no debt decided to roll over their DC account balance to an IRA at the time of job separation, compared with 11.4 percent of those with debt of \$10,000 or more. There was no clear trend with regard to debt and money left in the plan.

By Financial Wealth

Considering the impact of non-housing assets (excluding IRA assets) on the decisions with regard to DC accounts, Figure 6 shows how the decisions varied with the level of financial assets (in 2010 dollars).³ The trends were similar to other financial variables. First, the tendency to choose cash out declined steadily with financial wealth. For example, 32.1 percent of those with zero or negative financial wealth cashed out their DC account balance, but only 8.7 percent of those with financial wealth of \$80,000 or more did so. Second, the tendency to rollover to an IRA increased steadily with financial wealth. While 14.8 percent of those with zero or negative financial wealth chose to roll over their balance, 30.5 percent of those with financial wealth of \$80,000 or more chose to do so. The percentage of respondents leaving money in the plan did not vary much by financial wealth.

Demographic Factors

Gender

Figure 7 shows there was very little separation between men and women in the distribution of DC account outcomes. For both men and women, receiving benefits was the most common outcome (31.1 percent for men and 27.1 percent for women), and an almost identical proportion of men and women (25.8 percent and 25.3 percent for men and women, respectively) left the money in the plan. Cash outs and IRA rollovers were slightly higher among women than men.

Marital Status

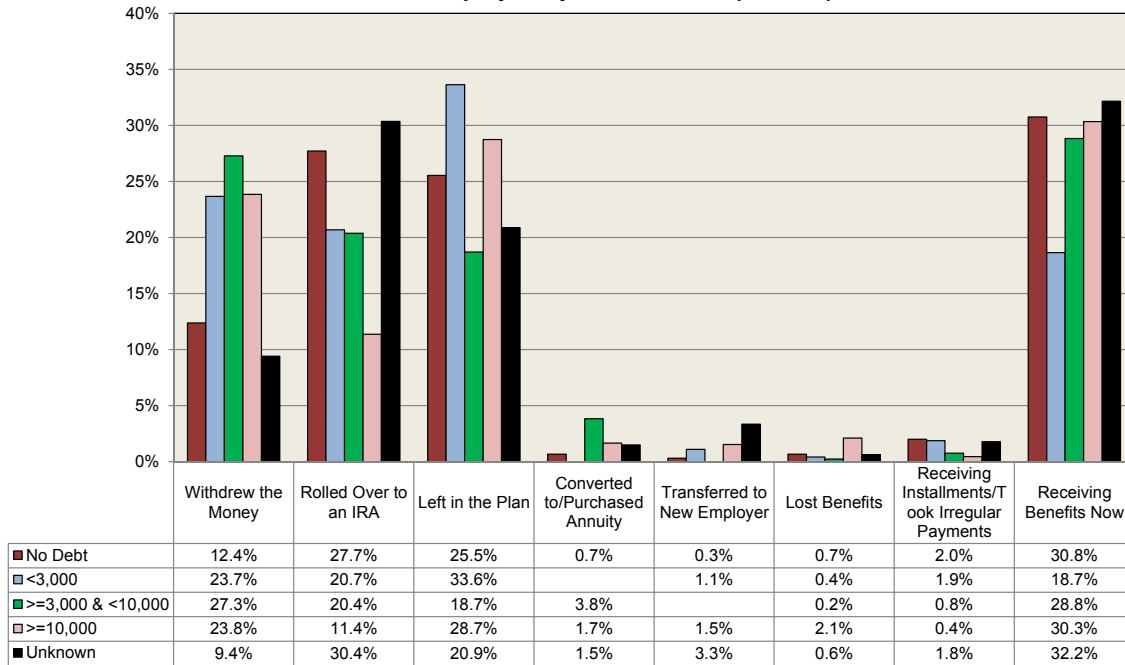
Previous research has shown that married people are generally in a better financial position and thus better prepared for retirement than singles. Figure 8 shows the DC account outcomes for singles and individuals married or living with a partner, and while married/partnered people had lower cash out rates and higher IRA rollover rates than singles, the differences were small. Roughly 1 in 5 (19.8 percent) singles cashed out their DC account balance, compared with 15.3 percent of respondents living in couple household, and IRA rollover rates for singles and married/partnered were 22.9 percent and 24.6 percent, respectively. There was almost no difference in the percentage of respondents opting to leave their DC account in their current plans: 25.8 percent for singles chose to do so compared with 25.5 percent for married/partnered.

Conclusion

A worker's use of his or her DC retirement account balances at the point of separation from a previous employer is one of the most important decisions a DC plan participant faces regarding their future retirement security. This analysis indicates the following:

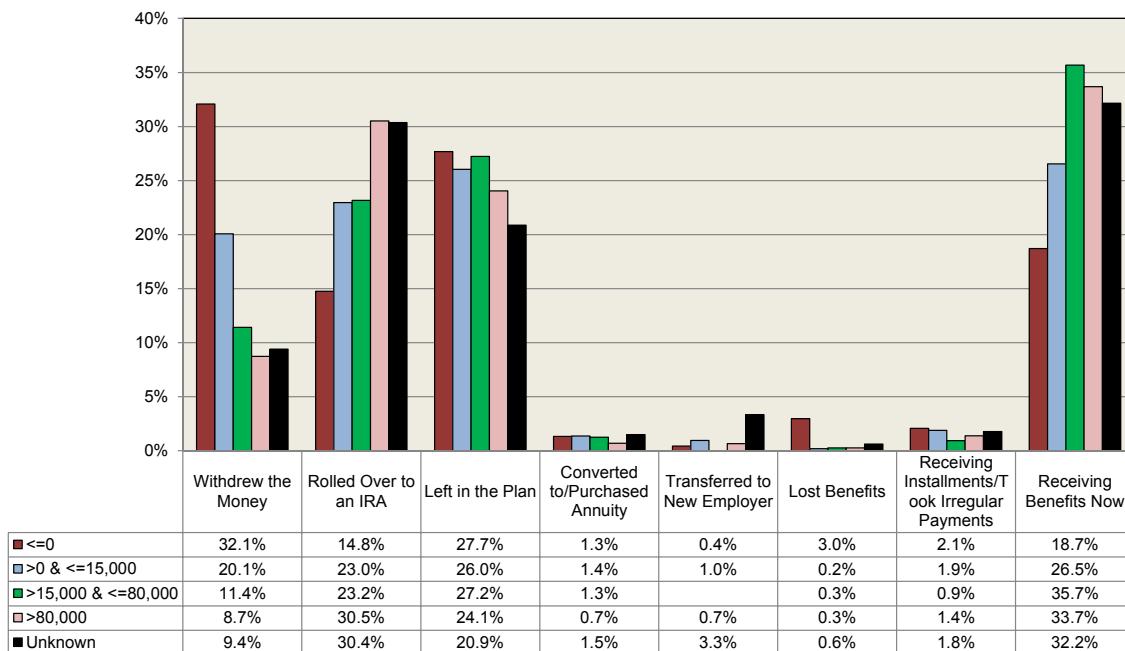
- Leaving the money in the prior plan was the most common outcome for those who remain in the labor force after leaving a job.
- A decision to take cash out of accumulated savings declined with higher account balances, higher incomes, existing ownership of an IRA, and higher financial wealth. The decision to take a cash out also rose with debt levels.

Figure 5
Distribution of DC* Plan Asset Disposition When Respondents Retired/Left Employer, by Level of Debt (2010 \$s)



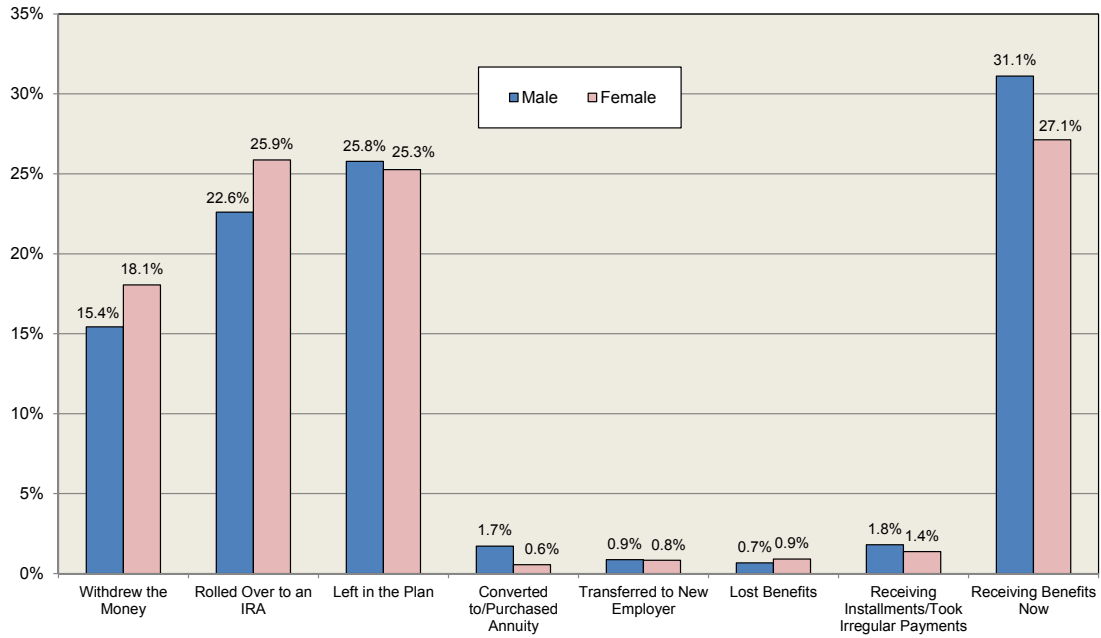
Source: Employee Benefit Research Institute estimates from the Health and Retirement Study (HRS).
 * Defined contribution.

Figure 6
Distribution of DC* Plan Asset Disposition When Respondents Retired/Left Employer, by Financial Wealth (IRA Excluded, 2010 \$s)



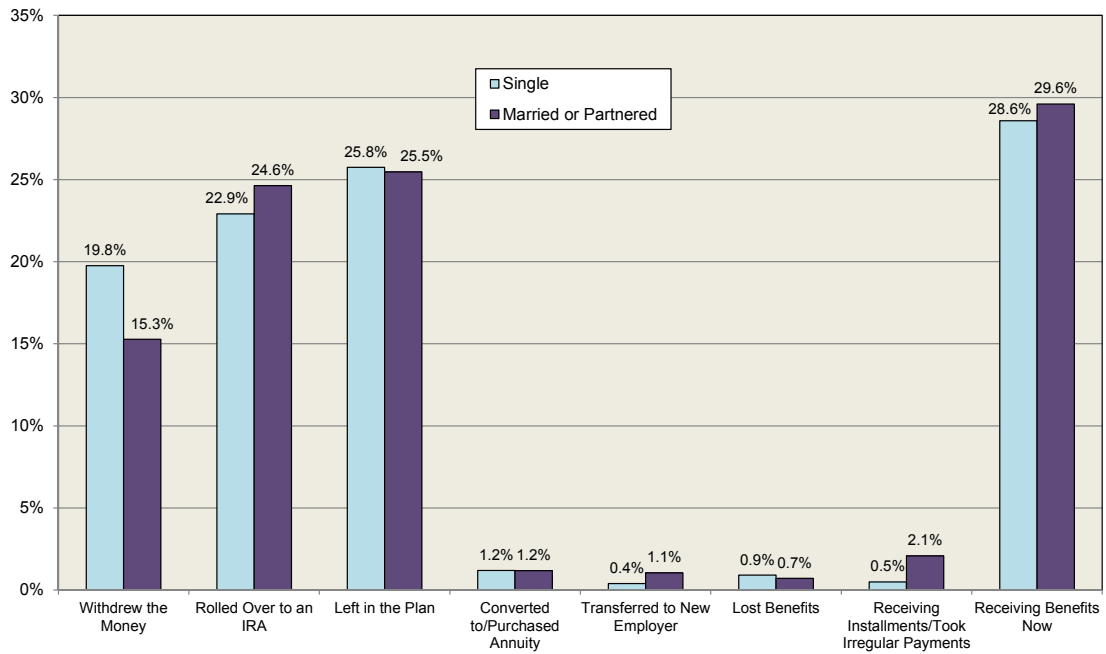
Source: Employee Benefit Research Institute estimates from the Health and Retirement Study (HRS).
 * Defined contribution.

Figure 7
Distribution of DC* Plan Asset Disposition When Respondents Retired/Left Employer, by Gender



Source: Employee Benefit Research Institute estimates from the Health and Retirement Study (HRS).
 * Defined contribution.

Figure 8
Distribution of DC* Plan Asset Disposition When Respondents Retired/Left Employer, by Marital Status



Source: Employee Benefit Research Institute estimates from the Health and Retirement Study (HRS).
 * Defined contribution.

- The decision to rollover those DC distributions to an IRA is the mirror image of the characteristics influencing cash withdrawals. Rollover decisions increased with higher account balance, higher income, previous ownership of an IRA account, and greater financial wealth. They also declined with higher debt.

There is, however, no clear trend with respect to the above-mentioned financial variables and the decision to leave those DC balances in the prior employer plans. This suggests that there may be behavioral factors, such as inertia, driving what might be seen as a “non-decision.” It may also be the case that individuals are deferring the decision until they need the money.

In terms of demographic characteristics, no significant difference was found between men and women in terms of their DC account outcome choices. Married or partnered individuals were less likely to withdraw their assets and more likely to roll over them into an IRA than singles, but the differences were small.

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Notes

¹ Copeland (2013) reported that between 2010 and 2012, among workers 21 and older 21.9 percent cashed out their account balances at the time of job separation. For those between 51 and 60, 61 and 64 and 65 or older the numbers were 17.0 percent, 5.4 percent and 5.5 percent respectively.

² Debt information is collected biennially. So, it is not possible to observe the level of debt for respondents who changed jobs between survey years. For such cases, the average household debt from the adjoining survey years was used.

³ Like debt, financial wealth information is also collected biennially. The last observed level of financial wealth, before the respondent made the DC plan decision, is used here.