Hewitt NEWS & Information

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Hewitt Study Shows Nearly Half of U.S. Workers Cash Out of 401(k) Plans When Leaving Jobs

LINCOLNSHIRE, Ill. – Despite the growing need for employees to save for retirement, a significant number of workers participating in 401(k) plans "cash out" of them once they leave their company, according to new research by Hewitt Associates, a global human resources services firm.

Hewitt's study of nearly 200,000 workers who participate in their 401(k) plans found that 45 percent elected to take a cash distribution once they left their jobs. The remainder either kept their savings in their current employer's 401(k) plan (32 percent) or rolled the money over to a qualified IRA or other retirement plan (23 percent).

"Retirement security relies not only on employees saving in their 401(k) plan, but on them actually *preserving* their retirement wealth when they leave their company. Our findings show that too many workers are not looking at their 401(k) savings as long-term in nature, but are instead using termination of employment as an opportunity to spend this money," said Lori Lucas, director of participant research at Hewitt Associates. "With fewer workers tending to remain at one company until retirement, employees may become 'serial consumers' of their 401(k) savings, which can have serious consequences when it comes to their ultimate ability to reach their retirement goals."

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Age Factors into Employee Cash-Out Decisions

Hewitt's study shows a direct correlation between age and tenure and employees' decisions to cash out of their 401(k) plans. The highest incidence of cash distributions was among young employees (66 percent) age 20-29. Employees who were older and more tenured were more likely to preserve their retirement wealth – either keeping their assets in their current employer's plan or rolling it over. Still, more than 42 percent of workers age 40-49 elected to cash out of their 401(k) plans upon leaving their jobs.

"It's disconcerting to see that a number of middle-aged workers still elected to cash out of their 401(k) plans when changing jobs," said Lucas. "It shows that many workers who are closer to retirement can be tempted to consume rather than save when they get the chance. By doing so, they are exposing themselves to significant taxes and possible penalties, and therefore may face having to work longer to make up the savings they lost when they cashed out."

Employees With Smaller Plan Balances More Likely to Cash Out

Not surprisingly, Hewitt's study showed that size of balance was a factor when it came to workers' tendencies to cash out of their 401(k) plans. Nearly three-quarters (72.5 percent) of workers with 401(k) plan balances under $10,000 took a cash distribution. When 401(k) plan balances were between $10,000 and $20,000 at termination, cash-out rates were much lower. Still, nearly a third (31 percent) of these employees elected to take their 401(k) distribution in cash.

"It's disturbing to find that nearly a third of workers with 401(k) balances of this size aren't taking steps to preserve it for the future," said Lucas. "In these cases, employers need to stress the value of compounding, which can be a very powerful tool in showing employees how small balances can make a big impact on their retirement savings. For example, if a 40-year-old employee with a $10,000 balance earned a 7 percent annual return, the money would grow to more than $50,000 by the time he or she retired at age 65."

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About Hewitt Associates

With more than 60 years of experience, Hewitt Associates (NYSE: HEW) is the world's foremost provider of human resources outsourcing and consulting services. The firm consults with more than 2,300 companies and administers human resources, health care, payroll and retirement programs on behalf of more than 300 companies to millions of employees and retirees worldwide. Located in 35 countries, Hewitt employs approximately 20,000 associates. For more information, please visit www.hewitt.com.

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Enabling Employees to Make Easier 401(k) Plan Distribution Decisions

Here are four ways that companies can help employees make better decisions with respect to preserving their retirement wealth:

- **Take the hassle out of the decision-making process.** Provide employees with internal resources that enable them to understand their 401(k) plan distribution options and easily make – and implement – educated decisions. Employees may not understand that they can leave their money in their 401(k) plan. Alternatively, when employees don't want to leave their money in their 401(k) plan, too much paperwork can result in the decision that "it's just not worth it" to roll over their 401(k) balance.

- **Show employees that it's worth the effort.** Make employees aware of the power of compounding – and how even a small balance can grow over time. Illustrate the impact of cashing out on long-term retirement wealth by using tangible examples:

  For example, consider an employee, age 25, who receives a lump-sum distribution of $5,000 upon termination of employment. On a pretax basis, assuming retirement at age 65 and an annual rate of return of 6%, the amount of retirement wealth forfeited by consuming the distribution today would be more than $50,000. If that same worker were to change jobs again at ages 30 and 35, taking a cash distribution of $5,000 each time could result in nearly $120,000 of lost retirement wealth.

- **Communicate clearly.** Hewitt finds that 92 percent of all 401(k) distributions are taken in the first 12 months after termination – and many much earlier than that. It is important to offer the departing employee compelling savings options early on. In fact, employers need to make sure employees understand their savings options before, not after, they leave the company.

- **Establish a formal program.** Hewitt finds that few companies have formal programs in place either to help employees retain assets in the 401(k) plan or encourage rollovers. Employers should consider developing a proactive approach either to encourage workers to remain in the plan after termination or roll over their money into an IRA.