



Defined Contribution  
Institutional Investment Association

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# Are Partial Distributions For Retirees Right for Your Plan?

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A key design point for a plan sponsor to decide is whether the plan should require retirees to take full withdrawals or permit partial withdrawals. One common misconception is that, in order to create a retirement tier, a plan must allow partial withdrawals. This is not true. There are no specific features that a retirement tier must include. Sponsors will find that as long as they keep in mind the tier's overall purpose — to help participants who are approaching, or in, retirement — a plan can create an introductory retirement tier with retiree-focused components such as education or advice, even if the plan requires full withdrawals.

It may be easier for plan sponsors to decide whether to offer partial withdrawals once they are aware of what others have found to be the pros and cons of doing so.

## COMMON ARGUMENTS GIVEN FOR CHOOSING NOT TO ALLOW PARTIAL WITHDRAWALS AND FAVORING STRATEGIES FOR HAVING RETIREES LEAVE THE PLAN INCLUDE:

- The employer would have to assume continuing fiduciary responsibility for a group of people who are no longer producing for the company.
- Retirees may be a more vocal cohort than active participants regarding plan design and investment structure. This may result in a need to allocate increased resources for research, and for responding to participants' inquiries.
- Having to balance the needs of separated participants with those of currently active participants may require establishing and overseeing broader investment lineups, as well as creating different communication strategies, all of which may take additional plan sponsor resources.
- Paying regular installments to retirees may complicate the ability to change service providers, by making the transition more complex (e.g., there is the possibility of making a mistake with income installments when changing providers); this in turn, the argument goes, could possibly limit which providers the plan sponsor can select.
- A retiree group may complicate future cost benchmarking and cost allocations by raising questions: what portion of costs will be incurred solely with respect to active participants versus separated ones, for instance; and what should be the allocation of costs for active versus separated participants?

## COMMON ARGUMENTS IN FAVOR OF ALLOWING PARTIAL WITHDRAWALS AND STRATEGIES ENCOURAGING RETIREES TO STAY IN THE PLAN INCLUDE:

- A larger asset base generally translates to lower asset management costs for all participants. In this way, younger participants benefit from the plan's scale, thanks to the retained older participants' assets. The larger participant base also makes the plan more attractive to service providers, potentially leading to pricing leverage and enhanced service offerings. Lower fees may also be helpful from a plan sponsor's fiduciary perspective.

- A perception of heightened corporate social responsibility may enhance the company's brand in the eyes of both prospective employees and consumers, points that are of growing importance to plan sponsors.<sup>1</sup>
- Being seen as actively supporting employees may not only increase the appeal of employment at the company; it may also improve current employees' engagement and productivity. Some argue that today's career DC participants of all ages expect decision-making and investment support transitioning into and during retirement.<sup>2</sup>
- A retirement-ready workforce increases management's flexibility, since offering more varied distribution options makes retiring easier for employees and more predictable for plan sponsors.
- By retaining assets in their employer's plan, retirees can access the same robust plan governance and low costs they had when employed, which may improve retirement income. Again, having more satisfied and secure plan participants is good for employers, too.
- Similarly, continuing to provide guidance and access through the plan to services that assist with decision-making may lead to improved retirement outcomes.
- By remaining in the plan, retirees may be more familiar with the investment products offered and the oversight taking place. Therefore, education and communication may not be as daunting a prospect as many assume.
- Plan administration is much more seamless for employers who experience "returning retirees" to part time or full-time work.

Ultimately, plan sponsors will have to weigh these pros and cons and decide what is best for their plan based on their demographics and goals.

This question is one that many plan sponsors are only now beginning to address. There have been a number of surveys that have shown an increasing enthusiasm to keep

terminated employees' balances in the plan including those that terminated due to retirement as well as other service separations. Recent research supports this. For example, a recent Alight survey shows that almost a third of employers prefer that terminated employees keep their balances in the plan, whereas only 5% of employers want terminated employees to leave the plan. The majority of employers (62%) do not have a clear preference (or are undecided).<sup>3</sup>

According to a T. Rowe Price 2018 study, 39.3% of plan sponsors prefer that participants remain with the plan at retirement, 43% have no clear preference or are actively reconsidering a prior preference and 17.8% prefer that participants move their balances out of the plan at retirement. But T. Rowe Price also found that with larger employers the figures were a bit higher with the 39.3% increasing to 50.0%. It's also worth noting that plan sponsors may wish to handle participants who terminate prior to retirement differently than those who separate due to retirement, as the latter may retain other benefit related or retiree association connections to the firm.<sup>4</sup>

Hopefully this series of papers will help plan sponsors make an informed selection.

## ENDNOTES

<sup>1</sup>Denise Lee Yohn, "Reminder: Customers Care How You Treat Your Employees," Harvard Business Review, September 26, 2018, <https://hbr.org/2018/09/reminder-customers-care-how-you-treat-your-employees> (accessed October 2, 2018).

<sup>2</sup>U.S. Government Accountability Office, "401(k) Plans - DOL Could Take Steps to Improve Retirement Income Options for Plan Participants," Report GAO-16-433, August 2016.

<sup>3</sup>Alight Solutions, "Building on the past, working toward the future," 2019 Hot Topics in Retirement and Financial Wellbeing report, January 2019.

<sup>4</sup>T. Rowe Price, June 11, 2018, "Advancing the Way We Think About Retirement Risk and Outcomes"

The Retirement Tier papers are a multi-part series. Other papers in the series may be accessed through the DCIIA website at [www.DCIIA.org](http://www.DCIIA.org)

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