

BUILDING BLOCKS FOR RETIREMENT

Retirement Planning Essentials

These Leaks Can Deflate Your Retirement Hopes

What's your vision of the ideal retirement? Endless days by the ocean? Spending time with family and friends? Pursuing a new interest or hobby? Whatever your retirement dreams, you know that it will be largely up to you to fund them.



You are already on the right track if you are maximizing contributions to an employer-provided retirement plan. However, you may stand a far better chance of securing a financially secure retirement if you avoid tapping into your retirement savings by taking loans or hardship withdrawals. These are known as plan leaks and they can impede the growth of the assets in your retirement plan and leave you with a smaller sum available for your retirement than you might anticipate.

Plan Loans Can Be Costly

There's little doubt that plan loans are a tempting way to handle a temporary need for cash. You'll repay yourself at a reasonable interest rate, without taxes or penalties. However, plan loans can be far more costly than they seem. Think about the following before you take a loan from your plan:

No tax advantage. Unlike pretax plan contributions, loan repayments are not tax deferred. You will have to repay the loan with money that's already been taxed. Then, when the money is distributed to you at retirement, you'll pay taxes on it again.

The loss of potential earnings. When you take money out of your plan for a loan, you reduce your plan account balance. Essentially, you will have less money working for you and will lose out on future potential earnings. That lost potential could be significant if you take a loan at a time when the markets are in a strong growth pattern.

The temptation to reduce contributions. Could you comfortably repay your plan loan and continue making your regular plan contributions? There is always the possibility that you could find it hard to do both and decide to reduce or stop making regular contributions to your plan. Reducing or stopping contributions while repaying your loan would further reduce your account's growth potential.

Repayment difficulty. If you leave your employer before the loan is repaid, you will either have to repay the entire outstanding amount or allow the loan to become a distribution. In plain English, a distribution means that you will be required to pay regular income taxes on the loan balance and quite possibly an additional 10% early withdrawal penalty if you are under age 59½.

Hardship Withdrawals Can Also Be Problematic

Some plans permit withdrawals from your retirement plan before you reach age 59½ for what's referred to as a "financial hardship." For example, you might be permitted to withdraw money to buy a principal residence, pay medical expenses, or pay college tuition and room and board expenses.

You will have to pay federal income taxes on the amount in the year you receive the money from the hardship withdrawal. And you may have to pay a 10% early withdrawal penalty as well. Most importantly, taking a hardship withdrawal means you will have less money invested for your future. You will lose the potential earnings that money could make over time.

Consider Alternatives

Having an emergency fund of three-to-six-months' worth of living expenses gives you a substantial cushion for those times when you might face a large, unexpected expense and could help you avoid the need to tap into your retirement plan. If you are considering applying for a plan loan or hardship withdrawal, however, make sure you first explore other options and talk to your financial and tax professionals about your situation.

This material is provided solely for informational purposes and does not constitute investment, tax, legal or accounting advice on the matters addressed. Neither Pentegra Services, Inc., its subsidiaries, nor any of their respective employees intend that this material should be relied on as investment advice, which should be sought from a professional advisor. Performance information shown reflects past performance and does not indicate or guarantee future investment results. Current and future results may be lower or higher than those shown. ©2021 Pentegra Retirement Services



701 Westchester Ave, Suite 320E, White Plains, New York, 10604