

## Before You Take that Retirement Plan Withdrawal...

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The Coronavirus Aid, Relief and Economic Security Act (CARES Act) makes it easier than ever to take distributions and loans from your retirement plan, with fewer tax consequences. While desperate times call for desperate measures and some personal circumstances may necessitate the need to access retirement plan savings, taking these distributions prior to retirement age should be a measure of last resort - used only when the alternative options (e.g., a payday loan) prove worse. Here are some of the reasons why:

### **WITHDRAWALS TURN “PAPER” LOSSES INTO ACTUAL LOSSES**

Any money lost in your retirement plan this year is not an actual loss until you sell your shares (presumably in retirement). If you still own the underlying investments, and those investments increase in value in the future - as they typically do after a bear market - then the loss wasn't actually a loss at all. However, once a withdrawal is taken, the loss is locked in and can no longer be recovered.

### **WITHDRAWALS DESTROY THE MAGIC THAT IS COMPOUNDING, PARTICULARLY FOR YOUNGER PARTICIPANTS**

Consider the example of a 20-something year old who is tempted to withdraw \$10,000 from his/her retirement account

to help offset the impact of the pandemic. Not doing so means moving back in with his/her parents (assuming COVID-19 doesn't prevent that option). As someone who lived with his mother for six months in his late 20s and understands how bad it can be, I implore the person to move back in with his/her parents! Here's the reason: That \$10,000, and any future 401(k)/403(b)/457 contributions, will help him/her achieve financial freedom sooner than they think. However, if he/she does touch their retirement savings, those dreams of financial independence may be gone, potentially forever. For younger people, small amounts of money become huge amounts of money later on, thanks to the magic of compounding. Don't believe me? [Check this out.](#)

### **WITHDRAWALS ARE OFTEN JUST A BAND-AID FOR AN UNDERLYING FINANCIAL PROBLEM**

Chances are that anyone racing to take retirement plan withdrawal likely has a serious underlying financial issue that the withdrawal will do very little to fix. Someone in this position is unlikely to have an [emergency fund](#) from which to pull during times of need or may be burdened with student loan or other debt. There are many examples of individuals taking plan withdrawals to pay off debt, only to later find themselves in more debt. While the withdrawal may

help in the short-term, it does little to address fundamental income versus expense equations or reinforce the importance of tracking spending, setting a budget, not paying full price, etc. In short, money is the master, instead of being a master of money. No retirement plan withdrawal can cure this particular financial ailment. The good news is that these issues are fairly easy to address, and people who do often live well on far less income than those who don't, which can prove especially useful in tough economic times.

## CONCLUSION

So please, don't take that retirement plan withdrawal if it can be avoided. Find some other ways to reduce expenses, increase income, or both. Here are some relatively simple actions that I took to become a master of my own money. There are countless other suggestions on our Revamping Retirement podcast guest, J. Money's Budgets are Sexy website. If it is absolutely necessary to access retirement funds, loans are far less destructive to an individual's financial future than withdrawals.

## EDITOR'S NOTE

This piece was adapted from a Top of Mind blog post, published on April 2, 2020.

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