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Rising Hardship Withdrawals Putting Retirement at Risk



A growing number of workers are raiding their employer-sponsored retirement plans to cover emergency expenses, highlighting an alarming trend in employee retirement security. According to Vanguard Group, 4.8% of 401(k) participants took hardship withdrawals in 2024, up from 3.6% in 2023 and more than double the pre-pandemic average of 2%.

Hardship withdrawals can carry significant long-term financial consequences, especially since funds cannot be paid back to the plan. Participants can face taxes, reduced retirement savings, and the opportunity cost of lost compounding growth — particularly if the withdrawal occurs during a market downturn. By implementing proactive strategies, organizations can help workers build financial resilience while preserving retirement funds.

Provide one-on-one financial counseling. There's simply no one-size-fits-all solution when it comes to promoting employee financial wellness. Each worker's situation is unique, and the most appropriate and effective strategies will vary. For some, financial stability might be achieved through highly targeted budgeting interventions or lifestyle changes like moving or downgrading a car. Others may benefit more from debt restructuring or negotiating lower rates on high-interest credit card balances. Personalized financial counseling helps ensure employees receive guidance that's tailored to their specific needs. Individual sessions can be particularly helpful for those who might understandably be hesitant to disclose a financial hardship among their coworkers within a group education setting.

Encourage health savings. Since medical expenses are a significant cause of hardship withdrawals, employers can encourage the use of Health Savings Accounts (HSAs) for workers enrolled in qualified, high-deductible health plans (HDHPs). HSAs enable employees to build a fund to help cover future medical costs, while benefitting from triple tax advantages: tax-deductible contributions, tax-free growth, and tax-free withdrawals for qualified expenses. By providing employer contributions to HSAs and educating employees on their benefits, companies can help reduce the likelihood that workers will need to tap their retirement account for a health-related financial emergency.



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Promote emergency funds. Consider encouraging employees to build emergency savings through pension-linked emergency savings accounts (PLESAs). Under SECURE 2.0, employers can auto-enroll non-highly compensated employees at up to 3% of their salary “unless the participant affirmatively elects a higher or lower percentage,” according to the DOL. The maximum account balance is \$2,500, and participants are permitted to make withdrawals at least once per month. Whether through PLESAs, out-of-plan ESAs, or other personal savings strategies, employees should be encouraged to put aside at least three to six months’ worth of expenses in a low-risk, readily accessible account.

A Lifeline for Struggling Employees

The rise in 401(k) hardship withdrawals sends a loud and clear signal that employees are in need of additional financial support to help manage unexpected expenses. By offering personalized advice, promoting emergency savings, and discussing health savings options, plan sponsors can help employees stay on track with their retirement savings while navigating financial challenges. Taking action now not only helps benefit employees but can also foster a more financially stable, engaged, and productive workforce.

Sources

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