

Threat of defaulting on 401(k) loans haunts employees

The younger they are, the more worried they are.

By **Marlene Satter** | October 30, 2019 at 02:25 PM

As if there aren't enough forms of financial stress for American workers these days, you can add another: Employees are worried over their potential to default on 401(k) loans.

They're happy they have the option to take the loans—don't get them wrong—but they're also worried about how they'll manage to pay them back, according to a new study from fintech firm Custodia Financial and market research firm Greenwald & Associates.

The study, titled "Missing Voices: What 401(k) Borrowers Can Add to the Loan Program Conversation," found that 91 percent of employees find it valuable to have the loan option, 70 percent say that if they lost their jobs they'd have a tough time paying the money back. And the younger they are, the more worried they are; millennials aged 25–34, topped the list, with 69 percent worried about it. Fifty-four percent of those aged 35–44 came next, followed by 49 percent for ages 45–54; 28 percent for ages 55–64; and 44 percent for ages 65-plus.

The three biggest reasons for taking the loan in the first place are just to make ends meet (25 percent), followed by the need to pay off a credit card bill or credit card debt (23 percent) and to pay out-of-pocket medical expenses (22 percent).

And they'd like the chance to have automated loan insurance to cover themselves in case of trouble—a layoff, a disability or death.

According to the report, "[a] 2018 report by Deloitte showed that the average defaulting borrower loses out on \$300,000 of retirement security when taxes, penalties, potential cash-outs, and lost earnings are considered."

That said, it's no wonder that nearly 80 percent of participants find the notion of automated, low-cost loan insurance appealing, with nearly 60 percent saying their bosses should add it.

Younger workers, aged 25–44, are the most in favor. In addition, 67 percent of participants say they'd consider contributing more to the plan if their employer were to add loan insurance.

And among the 70 percent of participants who say they're financially stressed, more than 80 percent say they'd be less so if they had such insurance.

"The survey data and interviews with participants clearly show that 401(k) borrowers are under a great deal of financial stress," Brian Perlman, SVP and financial service practice lead for Greenwald & Associates, said in a statement.

Perlman added, "To illustrate what participants are facing, one woman I interviewed took out a loan from her 401(k) to help her pay out-of-pocket medical costs related to her fibromyalgia. She was later forced to go on disability as a result of her illness and defaulted on her loan. She—and all other participants—needs a better safety net."
