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Should You Take A Pension Lump Sum Distribution?

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If you have ever retired or otherwise left an employer or may be about to, you've probably had to consider what to do with your 401(k) account. Many choose to roll over their 401(k) to a Rollover IRA to enhance investment flexibility. However, how many have ever considered this option for their pension?

Those accepting a buyout, retiring early on their own initiative, or simply leaving an employer for another opportunity, may be able to receive their vested pension benefits as a lump sum distribution. Some may prefer the security of a fixed income stream a pension typically provides. However, a lump sum payment could be advantageous.

By taking a lump sum distribution, you take control of your pension assets to manage as you see fit, while enjoying tax-deferred growth of an IRA. Because lump sum payments are calculated using the very conservative returns of the 30-Year Treasury Bond, exceeding this return over time could likely be accomplished with prudent money management.

If your pension plan is ever taken over by the Pension Benefit Guarantee Corporation, a government agency that assumes the liability of underfunded pension plans, having taken a lump sum distribution may look even more attractive. If the PBGC takes over your plan, the monthly payments you may be expecting for the rest of your life could be significantly reduced. A lump sum payout prior to this event protects you from this risk.

Another consideration is the implementation of the Pension Protection Act in 2008. At that time, a new formula for how lump sum payments are calculated will be phased in that will essentially yield a lower lump sum payment than you would get under the current formula. Therefore, if you are considering taking a lump sum distribution from your pension, take it before January 1, 2008.

More on this subject with illustrations and examples

“Pensions: Lump Sum or Annuity?” - Financial Advisor, September 6, 2006