

Forbes

The TSP Kicked A Field Goal With The New Modernization Act



The Thrift Savings Plan (TSP) has been a primary retirement savings account for many federal employees. The TSP, as a retirement savings account, features simple, easy-to-understand market indexes with low fees. The potential for matched funds, the ease of contributing and the low-costs have resulted in millions of federal employees using the TSP to build their nest egg.

However, the TSP has been a less than favorable vehicle for retirees who plan on using the money for income or other expenses in retirement. The complexity of the rules for distribution has always run counter to the simplicity experienced during accumulation. The regulations have left

many federal employees confused and dumbfounded.

Recently, Congress stepped in to try to solve some of these issues, and on November 17, 2017, the TSP Modernization Act (PL 115-84) was signed into law.

The new act, which the TSP Board has until November 2019 to implement, has some meaningful improvements for participants.

Here are a few of the upcoming changes to the TSP:

1. Unlimited In-Service Withdrawals At Age 59 ½

Currently, federal employees are able to complete one in-service withdrawal from the TSP after age 59 ½. The option has given many near-retirees expanded options for the transition to retirement as well as the ability to set up meaningful distribution plans ahead of time, instead of having to wait until actual retirement.

Good news: This option just got even better. The Modernization Act will allow for an unlimited amount of in-service withdrawals at age 59 ½. Now near-retirees will be able to successfully use their money to transition to retirement, consider a Roth IRA conversion and have the ability to successfully implement their post-separation plans without the old TSP limitations holding them back.

2. Unlimited Post-Separation Withdrawals

The new law will also allow federal employees to freely withdraw money from their accounts in retirement. For a long time, I have been perplexed on why the TSP would restrict participant access to funds. Once the new law is implemented, participants will be able to use their money without the same limitations.

Here are a few of the restrictions that were not addressed:

1. Limited Choices

The five main funds in the TSP will remain the same under the new law. The funds are simple and low-cost, but the choices inside of the plan have fallen far behind what's available to consumers outside of the TSP. The choices do not include market indexes relating to key asset classes, such as emerging markets, real estate, long-term bonds and commodities. By only offering five funds (and life cycle funds comprised of the five funds) the choices are simple, but they limit the ability to implement a highly diversified portfolio. It's surprising that Congress did not upgrade the TSP funds, considering the leaps and bounds made in the industry by companies that have figured out how to offer more varied options inside of the low-fee space.

2. RMD On Roth TSP

The Roth portion of the TSP is still subject to Required Minimum Distributions. The only way to avoid a required withdrawal after age 70 ½ is to roll the money over to a Roth IRA. A mandatory withdrawal from a tax-free account seems counterproductive.

3. TSP Annuity

The TSP Annuity type also will not change. As an "immediate annuity," the TSP annuity option will still require a full surrender of principal for guaranteed income. This option, in my experience, is rarely appropriate for someone's retirement plan and does not keep up with the evolution of annuities over the last twenty years. I believe TSP participants can find better annuities with more flexibility inside of an IRA over the TSP.

Field Goal Scored

At the end of the day, the TSP Modernization Act will bring about several positive changes to the plan. The flexibility for distributions will allow near-retirees and retirees more opportunities to move from the TSP toward more retirement-appropriate accounts with fewer limitations.

In my opinion, though, Congress missed an opportunity to upgrade the TSP choices, eliminate the Roth RMD and bring the TSP annuity into the 21st century.

Congress scored a field goal for this drive to improve the TSP, when it seemed like a touchdown was going to be scored. I feel an opportunity was missed, but I suppose some improvements are better than none.



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