ebri.org
Employee Benefit
Research Institute

DCIIA
Defined Contribution
Institutional Investment
Association

FOR IMMEDIATE RELEASE: Oct. 7, 2010
CONTACTS: Jack VanDerhei, EBRI, (202) 775-6327, vanderhei@ebri.org
Stephen Blakely, EBRI, (202) 775-6341, blakely@ebri.org
Lori Lucas, DCIIA, (312) 346-3536, lucas@callan.com
Lew Minsky, DCIIA, (202)367-1124 lew.minsky@dciia.org

New Research from EBRI–DCIIA:

Auto Features in 401(k) Plans Can Be Structured to Give Big Boost to Retirement Savings, Especially for Low-Income Workers

WASHINGTON, DC—A new study released today finds that auto-enrollment and auto-contribution escalation in 401(k) plans—depending on how they're implemented and used—can result in a big improvement in retirement savings, especially for low-income workers.

Specifically, the new research finds that under more optimal use of automatic features in 401(k) plans, the chances of younger employees (with 31–40 years of 401(k) eligibility) hitting an 80 percent pre-retirement real income replacement target (a goal recommended by many financial planners) increases well over 30 percentage points for both lower-income workers (from 45.7 percent to 79.2 percent when the auto features are optimized) and for higher-income workers (from 27 percent to 64 percent).

These findings are part of new research released jointly today by the nonpartisan Employee Benefit Research Institute (EBRI) and the Defined Contribution Institutional Investment Association (DCIIA). The study analyzes the potential impact that auto-enrollment and auto-contribution escalation of workers' contributions in 401(k) plans has on retirement income, and how employers can structure their 401(k) plans for improved benefit to workers.

The full report, "The Impact of Auto-enrollment and Automatic Contribution Escalation on Retirement Income Adequacy," is published in the November 2010 *EBRI Issue Brief* and the *DCIIA Research Report* and is available online at www.ebri.org and www.dciia.org.

The EBRI/DCIIA study finds, for instance, that 401(k) plans are more likely to achieve the results listed above if they have:

- A higher automatic-enrollment contribution rate cap,
- A successful program to reduce automatic contribution escalation opt outs,
- A higher annual auto-contribution escalation rate.

"Auto-enrollment" in 401(k) plans was encouraged by provisions of the Pension Protection Act of 2006 (PPA), which provided legal and regulatory incentives for employers to automatically sign up (or "enroll") new workers in their 401(k) retirement savings plan, as a way to boost participation and individual retirement savings. Workers can still opt out of auto-enrollment, but are required to take affirmative steps to do so; their "default" choice is to participate in the plan. Plans with an "auto-contribution escalation" provision automatically increase workers' annual rate of saving in their plan, to ensure their savings increase with income and salary raises.

"Our simulation models have shown for some time that auto-enrollment and auto-escalation are likely to have a tremendously positive impact on workers' retirement savings," said Jack VanDerhei, EBRI research director and co-author of the study. "Increasingly, we are now able to quantify just how big that impact will be."

"This study helps plan sponsors, policymakers, and plan providers better understand how auto features can be optimized to significantly improve workers' retirement income adequacy," commented Lori Lucas, DCIIA's executive chair of research and DC practice leader at Callan Associates, and the other co-author of the study.

Among the other findings in the EBRI/DCIIA study:

- Increasing the auto-contribution escalation cap had by far the greatest impact of any single factor on increasing the probability of success in the analysis (as defined by participants achieving an 80 percent real replacement rate in retirement), with a projected 16.4 percentage point increase for the lowest-paid workers, and a projected 14.1 percentage point increase for the highest-paid workers.
- Successfully discouraging opt-outs in auto-contribution escalation, ensuring that employees remember and implement deferral levels from their prior 401(k) plan instead of remaining at the auto-enrollment default, and increasing the annual auto-contribution escalation rate from 1 percent to 2 percent individually had a much smaller impact, ranging from 0.4 percentage points to 1.8 percentage points.
- When all four design elements and behaviors are optimized, the probability of success increases 33.5 to 37 percentage points, depending on income quartile.

"Plan sponsors may believe that simply having automatic enrollment and automatic contribution escalation is sufficient to ensure good retirement savings outcomes. These results clearly point to the fact that robust implementation and utilization are key," says Lucas.

About EBRI and DCIIA
EBRI is a private, nonprofit research institute based in Washington, DC, that focuses on health, savings, retirement, and economic security issues. EBRI does not lobby and does not take policy positions. www.ebri.org

The Defined Contribution Institutional Investment Association (DCIIA) is a nonprofit association dedicated to enhancing the retirement security of American workers. To do this, DCIIA fosters a dialogue among the leaders of the defined contribution community who are passionate about improving defined contribution plan design. DCIIA members include investment managers, consultants, law firms, record keepers, insurance companies, plan sponsors, and others committed to the best interests of plan participants. www.dciia.org

###