FOR IMMEDIATE RELEASE: John MacDonald, EBRI, (202) 775-6349, macdonald@ebri.org

Jan. 16, 2007

CONTACT: John MacDonald, EBRI, (202) 775-6349, macdonald@ebri.org

New Research from EBRI:

Pension Law Shifts Retirement Plan Participation Equation, Report Says

WASHINGTON—Enactment of the Pension Protection Act of 2006 shows that Congress implicitly endorsed the use of behavioral economics to lead individuals to make better decisions about retirement planning, according to a report published today by the nonpartisan Employee Benefit Research Institute (EBRI).

The report appears in the January 2007 EBRI Issue Brief, available at www.ebri.org, and was written by Jodi DiCenzo, founder of Behavioral Research Associates in Evanston, IL. Behavioral economics seeks to identify the reasons individuals actually make decisions as opposed to how they should make decisions.

In the Issue Brief, DiCenzo says that research by behavioral economists has repeatedly shown that many workers have a tendency to follow the path of least resistance when it comes to retirement planning—even to the extent of making decisions that are contrary to their best interest, such as not participating in an employer-sponsored retirement plan when one is available.

“By and large, individuals are inert—with good intentions, poor follow-through, and bounded rationality,” DiCenzo writes. “Loss aversion and decision-making biases often lead to unfortunate outcomes, including a poorly funded retirement.”

But the Pension Protection Act (PPA) contains a number of provisions, based on behavioral economic research, that are designed to change the equation and overcome worker inertia, the Issue Brief says. These include automatic enrollment of new workers in 401(k) plans and default contribution and automatic deferral increase provisions. Thus, instead of workers passively deciding not to participate they must actively opt out, a change that could produce better retirement outcomes.

“By adopting the auto-enrollment and default contribution provisions in PPA, Congress explicitly placed a priority on helping employers use the path of least resistance to get more workers to participate in 401(k)-type retirement plans, where one is offered,” DiCenzo writes.

Workers may actually benefit from having some decisions taken out of their hands. Among other things, DiCenzo says the PPA’s automatic enrollment provision may increase retirement plan participation rates and contribution rates may increase as workers’ pay rises.

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

###