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New Research from EBRI:
Automatic 401(k) Escalation: Likely Impact on Accumulations “Significant”

WASHINGTON—A key provision of 2006 retirement legislation is likely to result in a significant increase in 401(k) accumulations, especially for low-income workers, according to a study released today by the nonpartisan Employee Benefit Research Institute (EBRI) that provides the first estimate of the expected impact of the provision.

The Pension Protection Act (PPA) of 2006 allows employers to automatically enroll workers in the company’s 401(k) plan and to automatically increase a worker’s 401(k) contribution to coincide with a raise or a work anniversary—though the employee can decline both enrollment and the increase. To qualify for nondiscrimination protections, automatic (or default) contributions must be at least 3 percent in the first year and increase regularly. The provision was added in an attempt to boost 401(k) accounts, the primary vehicle for worker retirement savings.

An article in the September EBRI Notes, available at www.ebri.org, says that it will be several years until researchers know how 401(k) participants will react to the automatic escalation of contributions in general and to the specific provisions of the PPA. But under a set of assumptions and scenarios described in the article, automatic escalation was found to increase 401(k) accumulations by these amounts:

- 11–28 percent for 401(k) participants in the lowest-income group.
- 5–12 percent for participants in the highest-income group.

The article uses data from the 2007 Retirement Confidence Survey, fielded several months after the enactment of the PPA, to determine how high workers are likely to allow their automatic 401(k) contributions to go in plans with an automatic escalation feature. This information was added to the baseline assumptions from the EBRI/ICI 401(k) Accumulation Projection Model to come up with the estimated impact of automatic escalation on 401(k) accumulations.

These findings “suggest that the introduction of automatic escalation will result in a significant increase of 401(k) accumulations—especially for low-income workers—compared with estimates previously determined for automatic enrollment,” the EBRI analysis says.

EBRI has done extensive modeling of the retirement income prospects for future generations, with results ranging from very bleak for substantial portions of the U.S. population to fairly positive for 401(k) participants with continuous coverage throughout their working careers.

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