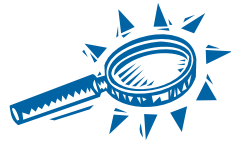




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Blueprint Brief



A closer look at the research in
Blueprint for Opportunity:
Issues that matter • Ideas that work

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In 2001, 60 percent of workers covered by an employer-sponsored pension plan have a 401(k) defined contribution plan. National data shows one out of five workers who have access to a 401(k) plan do not participate.

Research shows that automatically enrolling employees in a 401(k) plan with the option to pull out expands the number of workers, particularly low-wage workers, who enroll.

Two national consulting firms found that 14 to 19 percent of employers nationwide have shifted to auto-enrollment for worker 401(k) pension plans.

Encourage employers to automatically enroll workers in pension plans

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Coloradans will have to rely on the three-legged stool of pensions, personal savings and Social Security to replace their earnings when they retire. Long-term funding concerns over Social Security and cuts in company pension plans have weakened two legs of the retirement stool.

During the past 25 years, defined contribution retirement plans such as 401(k) plans have increased dramatically. In 2001, 60 percent of workers covered by an employer-sponsored pension plan have a 401(k) defined contribution plan.¹

Most 401(k) plans require employees to sign up to participate. National data shows one out of five workers who have access to a 401(k) plan do not participate.² Generally, it is low-wage workers who do not sign up. And some workers are confused about selecting their investment options and never take the initiative to sign up.

One way to increase the number of employees who participate in 401(k) plans is to shift the method of enrollment from requiring workers to opt in, to automatic enrollment that requires them to opt out.

Research shows that automatically enrolling employees in a 401(k) plan with the option to pull out expands the number of workers, particularly low-wage workers, who enroll. According to a study conducted by the University of Pennsylvania, automatic enrollment increases participation from 13 percent up to 80 percent among employees earning a yearly salary of \$20,000 or less, and boosts participation from 19 percent up to 75 percent for Hispanic workers.³

These are the very workers who are likely not saving enough and will be forced to rely on Social Security for most of their retirement income. Enrolling them in a 401(k) plan will increase the likelihood they can live a middle class lifestyle in retirement and have something to pass on to their kids.

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A national study published by the human resources consulting firm Hewitt Associates found 19 percent of employers were automatically enrolling workers in 2005, up from 14 percent in 2003.

Employers can decide how to set up their automatic enrollment program. Most set the default contribution limit at 3 percent of wages, or higher.

Congress included measures to encourage automatic enrollment in 401(k) plans in its comprehensive pension reform legislation. The proposed legislation does not require auto-enrollment, but it does allow employers to supersede any state laws that prohibit the practice.

While there are few Colorado-specific data on automatic enrollment, a national study published by the human resources consulting firm Hewitt Associates found 19 percent of employers were automatically enrolling workers in 2005, up from 14 percent in 2003.⁴ The Deloitte Consulting firm surveyed 426 national businesses in 2004. Of these, 14 percent reported they automatically enroll employees in their plan, while another 14 percent said they were considering adding such an option.⁵

Employers can decide how to set up their automatic enrollment program. The Deloitte study found 55 percent of businesses using auto-enrollment set the default contribution limit at 3 percent of wages, while about 25 percent set it at a higher level. The study also showed that 57 percent of companies invested their employees' auto-enrolled funds in short term money market investments, while 34 percent invested the funds in balanced or lifestyle investments. Employees can override these choices if they wish.

Deloitte also found 5 percent of employers allow workers to establish "step-up" contributions, which automatically increase the amount of wages diverted into their 401(k) plan over time.

Congress included measures to encourage automatic enrollment in 401(k) plans in its comprehensive pension reform legislation (S. 1783 and H.R. 2830), passed in August. That legislation would also shore up the U.S. pension system and strengthen the Pension Benefit Guarantee Corp.⁶ While this legislation does not require auto-enrollment, it does allow employers to supersede any state laws that prohibit the practice.

✓ Encourage Colorado employers to automatically enroll workers in 401(k) pension plans.

Colorado's political, business and community leaders should encourage employers to use automatic enrollment for 401(k) pension plans. We should also educate workers about the value of participating in these plans and of increasing contributions over time to meet retirement needs.

Automatic enrollment is allowed under federal law, and pension reform legislation currently pending before Congress provides additional incentives to do so.

End Notes

- ¹ *The Automatic 401(k): A Simple Way to Strengthen Retirement Savings*, The Retirement Security Project, March 2005.
[http://www.retirementsecurityproject.org/pubs/File/Automatic401\(k\).pdf](http://www.retirementsecurityproject.org/pubs/File/Automatic401(k).pdf)
- ² United States Bureau of Labor Statistics: *Employee Benefits In Private Industry, March 2005*.
<http://www.bls.gov/ncs/ebs/sp/ebsm0003.pdf>
- ³ Brigitte Madrian and Dennis Shea, *The Power of Suggestion: Inertia in 401(k) Participation and Savings Behavior*, *Quarterly Journal of Economics* Vol.

- 116, No. 4 (November 2001): 1149-87.
- ⁴ Hewitt Associates, *Switching On The 401(k) Autopilot*.
http://www.hewittassociates.com/Intl/NA/en-US/KnowledgeCenter/Magazine/vol8_iss2/upfront-hewitt-03.html
- ⁵ Deloitte Consulting, LLP, *2004 Annual 401(k) Benchmarking Survey*.
<http://www.workforce.com/images/benchmarking.pdf>
- ⁶ U.S. Library of Congress, THOMAS Online Legislative Information
<http://thomas.loc.gov/>