Will “Auto-Enrollment” Kill the Employer Match?

By Editor Test *Tue, Jan 12, 2010*

By raising participation rates, auto-enrollment will raise the cost of employer-matching efforts and may encourage some employers to reduce or eliminate their match.

Why use a carrot when a stick will suffice?

The trend toward “auto-enrolling” employees into defined contribution retirement plans was supposed to increase participation in these plans and contribute to greater retirement security for more Americans.

But the trend has a negative consequence that somebody must have foreseen: by raising participation rates, auto-enrollment raises the cost of employer-matching efforts and may encourage some employers to reduce their match. It may even undermine the need for an employer match as an incentive to participate.

An article in the December issue of the newsletter of The Retirement Policy Program at the Urban Institute says “firms appear to reduce the rate at which they contribute to 401(k) plans when they adopt auto-enrollment. Auto-enrollment then, will not necessarily raise future incomes for all eligible employees.”

The article’s authors, Barbara Butrica of the Urban Institute and Mauricio Soto of the International Monetary Fund, found that the mean match rate for companies that use auto-enrollment is 44% (median = 46%) of the first 6% of salary, while the mean rate for companies that don’t auto-enroll is 51% (median = 53%).

A seven-point reduction in match rates offsets about 42% of the increase in matching costs caused by auto-enrollment, they said. The article doesn’t discuss whether the higher participation rates associated with auto-enrollment brings benefits to the employer that would justify the expense of higher matching costs.

“Our findings suggest [auto-enrollment] could lead to lower account balances at retirement for those who were already enrolled or would have enrolled anyway,” the authors conclude.