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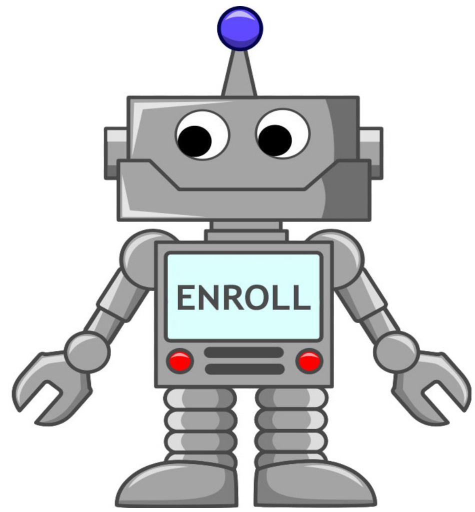
Commco Comments

Timely Information and Updates for Employers and Retirement Plan Sponsors

Retirement Plan Automatic Enrollment

Automatic enrollment allows an employer to automatically deduct retirement plan deferrals from an employee's wages, unless the employee makes an election not to contribute or to contribute a different amount. Employees must be given a notice of automatic enrollment at least 30 days, but no more than 90 days, before their enrollment date.
For plans with immediate eligibility, this requirement would be impossible to meet. In this case employers may provide notice no later than the employee's hire date.



Types of Automatic Enrollment

Basic Automatic Enrollment (Automatic Contribution Arrangement or ACA):

- Employees are automatically enrolled in the plan unless they elect otherwise.
- Plan document specifies the percentage of wages that will be automatically deducted.
- Employees can elect not to contribute or to contribute a different percentage of pay.

Eligible Automatic Contribution Arrangement (EACA):

- Uniformly applies the plan's default deferral percentage to all employees after giving them the required notice.
- May allow employees to withdraw automatic contributions, including earnings, within 90 days of the date of the first automatic contribution.

Qualified Automatic Contribution Arrangement (QACA):

- Uniformly applies the plan's default deferral percentage to all employees after giving them the required notice.
- Meets additional "safe harbor" provisions, including required employer contributions and limits on vesting schedules, which exempt the plan from annual nondiscrimination testing requirements.
- Default deferral percentage must start at no less than 3% and gradually increase (by at least 1% per year) to no less than 6%. The default percentage cannot exceed 10%.

Default Investments if Employee Does Not Make an Election

Employers must choose an investment for employees' automatically deducted salary deferral contributions. You can limit your liability for plan investment losses by choosing default investments that meet certain criteria for transferability and safety, and providing employees with an annual notice informing them of their current investment and their right to make changes.

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What is the maximum default contribution percentage in a QACA plan provision?

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Effects on Plan Participation

In practice, automating salary deferrals has shown both positive and negative impacts to retirement plan contributions and employee retirement readiness.

Automatic enrollment harnesses the tendency to go along with the default option. The good news is this leads to greater participation rates among populations who are less likely to proactively enroll (such as younger and lower-paid employees). The bad news is that employees who would have proactively enrolled in the absence of an automatic enrollment feature tend to save at lower rates when they are default enrolled.

For example, an employee who might have chosen to enroll at a contribution rate of 8% may stick with the plan's much lower starting percentage when given the automatic enrollment option. A 2015 study by The Center for Retirement Research at Boston College found that average salary contributions by automatically enrolled participants were 60-72% (depending on salary level and employment tenure) lower than those of proactively enrolled participants.

Employers can help to minimize this difference by:

- Ensuring that their automatic enrollment provision includes an automatic percentage increase feature.
- Communicating the automatic enrollment as a backup plan and encouraging employees to enroll proactively.
- Providing access to financial education to help employees understand the importance of retirement planning, as well as the effect of various contribution rates on their retirement goals.

If you have questions about automatic enrollment and your company's retirement plan, email us at autoenroll@thecommco.com.