Research has shown some employers may choose not to use automatic enrollment and automatic escalation in their 401(k) plans because these features can be sub-optimal for their employees.

**Benchmarking builds better plans**

The reason for this anomaly — despite the fact that such features have been proven to enhance both participation and deferral levels in the broader population — may be industry-specific demographics. In particular, automatic features can be counter productive in companies that have seasonal workforces, even if getting employees enrolled and contributing are key to achieving a solid financial footing.

In broader terms, we believe it is critical that plan sponsors benchmark their plans to others within their industry. Benchmarking participation rates and average deferrals help the sponsor contextualize success for their plan and set appropriate goals. Eligibility and entry dates are two other important competitive areas to compare.

Detailed, plan-specific data may be available through a plan’s advisor or recordkeeper, and more general benchmarking information can be found in the Plan Sponsor Council of America’s (PSCA) annual employer survey (see Figure 1 on next page). Armed with this knowledge, employers can ensure that their plans are competitive within their industries.

**Shortening eligibility**

Given the importance of time in compounding returns, employees should save for retirement as soon as they can. Except for organizations that have large part-time or seasonal employee populations, we support the growing trend toward shorter or immediate eligibility. In fact, 76% of defined contribution plans now offer immediate eligibility, versus 45% in 2001.

Even with immediate eligibility or automatic enrollment, real-world workers must balance plan participation against other financial needs. Intuitively, younger employees may view retirement as a lower priority when they have competing uses for their money, such as repaying student loans, starting a family or purchasing a home.
As a result, plan sponsors may consider reallocating a portion of their communications budget, foregoing traditional, one-size-fits-all efforts in favor of segmented campaigns. This will enable them to target to subsets of employees with specific messages, reinforcing the importance of deferring at the highest level that a participant’s salary and situation can support.

Targeted messages can highlight the importance of allowing assets to grow over time or the value of deferring enough to take advantage of the maximum employer match. Both may help participants separate today’s wants from future needs.

Peers also can have a major impact on behavior. When one or more plan participants have a positive experience, the news can go viral (broadcast via water cooler, company newsletter or intranet), potentially leading to increased participation and contribution levels across the entire company.

**Role of matching contributions**

According to the current PSCA survey, 95.3% of companies make plan contributions on behalf of their employees. Interestingly, research shows that the matching threshold level has a bigger impact on deferral behavior than higher match rates. Although it might seem that the matching rate (i.e., 50% of the first 6% of salary deferred) is the most important factor, participants tend to focus on the matching threshold (in this case, a match of up to 6% of compensation).

Therefore, a matching formula of 50% of the first 6% of compensation may result in higher deferral rates than a formula of 100% of the first 3% of compensation — even though both formulas result in the same maximum employee payout.

**Profit sharing vs. employer matching?**

Is a profit sharing or an employer matching contribution more likely to motivate deferrals? According to the PSCA, fixed matching formulas lead to higher participation rates than discretionary matches. Pure profit sharing contributions are allocated based on a participant’s salary rather than their contributions, and thus have little impact on participation.

As a general rule, we strongly advocate that any plan sponsor that makes a profit sharing contribution without offering a matching contribution should apply part or all of the profit sharing contribution to a matching formula, since matching contributions boost both participation and deferral levels.

The bottom line: proper plan design, when combined with specific participation and contribution goals and a focused communication plan, can dramatically boost employee participation and contribution behavior.

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