Automatic Enrollment

Interested in increasing plan participation and avoiding non-discrimination testing failures?

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Automatic enrollment is a plan feature that allows plan sponsors to withhold a set percentage of the employee's compensation and deposit it into the plan account for that employee as a deferral—unless the employee chooses not to participate or elects to contribute a different amount. Employees must be given the opportunity to opt out of participating. The participant must also be allowed to change the election in the future. Some arrangements also go a step further and implement an automatic escalation feature which gradually increases the employees' deferral rate over time with no effort on the part of the employee.

This arrangement takes advantage of a participant's tendency to procrastinate. By getting them enrolled in the plan, the plan will enjoy increased participation and possibly better testing outcomes while the participant saves for retirement without having to make any decisions.

Automatic Enrollment FAQs

Q. Does It Work?

A. Approximately 30% of employees do not participate in their employer's 401(k) plan. Studies claim that automatic enrollment plans could reduce this rate to less than 15%.And U.S. employers are opting for automatic enrollment in growing numbers. According to the Plan Sponsor Council of America, automatic enrollment was used by 50.2% of plans in 2013 (up from 45.9% in 2012). Many employees are confused about retirement planning. Many want guidance. Automatic enrollment makes the tough decisions for them and starts them on the path to a more secure financial future. Having a robust retirement plan usually helps businesses attract and keep talented employees. Automatic enrollment may be just the enhancement you need to get more employees to participate in — and appreciate — the benefits of working for you.

Q. Are there different types of plans?

A. Yes—there are three types of automatic contribution plans.

- Automatic Contribution Arrangement (ACA)—this automatically starts deferrals for participants and can include an automatic escalation feature.
- Eligible Automatic Contribution Arrangement (EACA)—this is the same as a regular ACA plan but has some additional notice requirements. It also allows withdrawal of those automatic deferrals within 90 days on participant request and extends the deadline for ADP testing.
- Qualified Automatic Contribution Arrangement (QACA) - this plan requires automatic escalation as well as a mandatory employer contribution. It has more strict guidelines and less flexibility at the employer level. It does give some relief to testing since the plan is deemed to pass certain testing requirements..

Q. What are the pros?

A. For paternalistic employers, it can feel good to know that you are helping participants save for retirement. By automatically enrolling participants in the plan, you can help them get a great head start on retirement. You may also save your HR department the time and hassle of chasing after participants who are slow to return their enrollment paperwork. And studies show that lower paid employees tend to stick to the default deferral rate, meaning that those that need the most help are receiving that help through this plan design choice. Furthermore, if a plan is struggling to pass non-discrimination tests like the ADP/ACP test, then the addition of more employees deferring into the plan can have a positive effect and may reduce or eliminate refunds to the plan's highly compensated employees.

Q. What are the cons?

A. These types of plans come with increased notice requirements. At least 30 days before a participant entry date, notices regarding the automatic enrollment and investment default must be distributed. Then, the plan sponsor must remember to actually begin the employee's deferral deduction in the payroll system. If the plan has an automatic escalation feature, then the plan sponsor must also track those increases and communicate them to the payroll system in a timely manner. If the plan sponsor fails to automatically start and/or increase the deferrals as stated in the plan and participant notices, then the plan sponsor can be responsible for reimbursing the participant's account for a portion of the missed deferrals, any matching contribution that would have been contributed and the associated earnings on those contributions.