Five habits of successful 401(k) plan sponsors

As a plan sponsor, your 401(k) participants depend on you to help create the retirements they envision. The good news is that many of these participants likely recognize the importance of saving for retirement. In fact, with retirement lasting longer than ever, 401(k) millionaires – those with at least $1 million in their retirement accounts – have become increasingly common.

While the rising prevalence of 401(k) millionaires is largely due to the good practices of plan participants and favorable market conditions, it's important to note that 401(k) plan sponsors also play an essential role in helping participants achieve success. Below, we explore how sponsors have helped countless plan participants save for their dream retirements by:

1. AUTO-ENROLLING PARTICIPANTS

Plan sponsors who auto-enroll their participants – allowing them to opt out of the plan instead of having to opt in – often see a much higher savings rate among their participants than other plan sponsors.

A recent study found that since 2008, the average savings rate among employees automatically enrolled in their employer-sponsored retirement savings plan has risen from 4% to 6.7%, and 63% of automatically enrolled participants have increased their savings rate[1] in the past 10 years. A separate study found that participation rates among new hires nearly doubled to 93% under automatic enrollment, compared with 47% under voluntary enrollment.[2]

2. AUTOMATICALLY INCREASING PARTICIPANT CONTRIBUTION RATES

Successful 401(k) participants tend to increase their contribution rates as their incomes increase and their financial needs evolve. While the most diligent savers will make these changes on their own, the most effective plan sponsors automatically increase their participants' savings rates over time.

Research into retirement savings has helped establish the importance of increasing savings rates over time. One study found that participants who are currently contributing less than 3% to a retirement plan are on track to replace only 59% of their income in retirement, whereas those who contribute 10% or more are on track to replace 128% of their income. The same study showed that participants on a defined contribution plan with auto-escalation are on track to replace 107% of their income.[3]

3. OFFERING TARGET-DATE FUNDS

Automatic enrollment programs tend to work better when the qualified default investment alternative

[1] www.planadviser.com/automatic-enrollment-helping-participants-increase-retirement-savings
[2] www,institutional.vanguard.com/iam/pdf/CIRAE.pdf
[3] www.plansponsor.com/increased-savings-rates-auto-escalation-can-boost-retirement-income

(QDIA) is a carefully selected investment option. In many cases, a well-managed target-date fund is the most effective choice for participants. Although not all target-date funds are created equal, they all offer distinct advantages over a do-it-yourself approach, including asset allocation, investment selection and automatic rebalancing as participants near retirement. Additionally, since target date funds are professionally managed, participants don't have to put as much effort into monitoring and adjusting their investment choices over time.

4. OFFERING AUTOMATIC ROLLOVERS

Plan sponsors who offer automatic rollovers help ensure that participants retain access to their hard-earned savings. This is especially important considering that many employees don't realize that switching jobs means their 401(k) accounts can remain with their former employers indefinitely. In fact, a recent study showed 50% of American adults who've participated in a 401(k) or equivalent retirement plan left an account at a previous employer. And nearly a quarter left between $10,000 and $50,000 in these accounts.[4] Other events, such as a participant name change or a plan termination, can also make it difficult for participants to track down their accounts.

In the past, 401(k) participants were required to consent to rolling a balance of less than $5,000 into their new employer's retirement plan. Fortunately, new guidance from the Department of Labor is making it easier for employers to transfer former employees' small-balance 401(k) funds to their new employer's 401(k) plans, provided the employees do not opt out of the transfer.

5. DISCOURAGING EARLY WITHDRAWALS

Participants are more likely to meet their retirement goals when they stay the course and avoid making early withdrawals from their 401(k) plans. While plan sponsors can't prohibit early withdrawals, they can educate participants on the drawbacks of doing so. In addition to the associated taxes and penalties – as well as the risk of not saving enough for retirement – successful plan sponsors can help participants save money and preserve their future retirements by sharing alternative solutions to early withdrawals.

NEXT STEPS:

- **Reevaluate your plan structure.** If you haven't evaluated your 401(k) offerings recently, now is a good time to see how your plan stacks up against the best practices mentioned above.
- **Identify areas to improve and make changes where possible.** While plan adjustments require time, effort and other resources, a reliable retirement plan benefits you and your participants – and helps distinguish you from other employers.
- **Educate your participants on any changes you make.** It's essential to keep employees informed on how they can take full advantage of their 401(k) plans while avoiding unnecessary risks.

401(k) plans are long-term retirement savings vehicles. Withdrawal of pre-tax contributions and/or earnings will be subject to ordinary income tax and, if taken prior to age 59 1/2, may be subject to a 10% federal tax penalty.

All investments are subject to risk, including loss. Asset allocation and diversification does not ensure a profit or protect against a loss. There is no assurance that any investment strategy will be successful.

[4] www.bene itspro.com/2013/05/09/orphaned-401k-accounts-stacking-up/?slreturn=20191021184458

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