UNLOCKING YOUR 401(K) MATCH POTENTIAL: STRATEGIES FOR SUCCESS

Offering matching contributions in your 401(k) plan serves dual purposes: it's a valuable benefit for your employees and a catalyst for their retirement planning journey. However, striking the right balance between affordability and effectiveness is key. Let's explore how you can optimize your 401(k) match to benefit both your organization and your employees.

Deciphering Fixed Matching

Fixed-match formulas, once widespread, are now experiencing a gradual decline in adoption among smaller plan sponsors. While they provide a structured approach to matching contributions, their effectiveness relies on subtle plan design nuances. In contrast, graded matching formulas offer a more tailored approach, potentially enhancing participant engagement by aligning matches with different income levels.

Insights from the Plan Sponsor Council of America's (PSCA's) 63rd Annual Survey indicate a notable shift in preference. While approximately 51.4% of plans with fewer than 50 participants still adhere to fixed-match formulas, this marks a decline from the 72.9% reported two years prior. Larger plans, however, maintain a steadfast preference for fixed formulas, constituting 68.7% of surveyed plans.

The Dynamics of Stretch Matching

Enter stretch matching—a forward-thinking strategy poised to revitalize conventional matching models. This approach incentivizes higher participant savings by offering augmented matches beyond established thresholds. Recent challenges to this theory notwithstanding, its potential to foster increased employee engagement and financial prudence remains promising, assuming participants are motivated to maximize their contributions.

Consider Joe Participant, earning $40,000 annually. A 100% match of a contribution of 4% of pay would give Joe a match of $1,600. A “stretch match” formula of 50% of Joe’s contributions up to 8% of pay would give Joe the same $1,600 match, while also incentivizing him to contribute an additional $1,600 of his pay to the plan. In the first scenario, Joe ends up with $3,200 of total contributions for the year. In the second, Joe finishes the year with $4,800 of total contributions: with no additional cost to the employer.

Evaluating Auto-Enrollment Implications

Auto-enrollment emerges as a critical factor in enhancing plan participation rates. Studies, such as Vanguard's analysis titled “Stretching the Match: Unintended Effects on Plan Contributions,” underscore the significance of this feature. Plans incorporating auto-enrollment demonstrate higher participant engagement, albeit with nuances in interpretation.

The report also highlighted the positive impact of auto-enrollment, based on other studies. “Our research shows that higher initial default deferral rates in automatic enrollment plan designs are the most effective way to raise employee-elective deferral rates,” it concluded.

Navigating these complexities necessitates prudent action. Plan sponsors with voluntary enrollment plans should consider designs integrating 100% match formulas—a counterintuitive yet empirically supported strategy. Additionally, leveraging higher initial default deferral rates within automatic enrollment plans emerges as a potent means to elevate employee savings rates.

Mapping Your Path Forward

So, what's the optimal strategy for your 401(k) plan? Consider leveraging the synergies between stretch matching and auto-enrollment. However, before making any decisions, consult your BMF Advisor or benefits specialist. By conducting a thorough analysis of your plan dynamics and participant demographics, you can craft tailored strategies that align with your organizational goals and foster robust retirement outcomes for your workforce.