

**“The Power of Suggestion:
Inertia in 401(k) Participation and Savings Behavior”**

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This empirical paper, based on a detailed case study at a large U.S. company, carefully documents and analyzes two important aspects of investor responses to automatic enrollment in 401(k)-type savings plans.

First, the authors provide convincing, systematic evidence that 401(k) participation is significantly higher as a result of the implementation of automatic—but not mandatory—enrollment. In other words, the authors show that if new employees must take action to opt *out* of the company 401(k) plan, rather than take action to opt *in* to the plan, more end up using the plan. Second, they show that a substantial fraction of 401(k) participants hired under automatic enrollment retain both the “automatic” contribution rate, and the “automatic” portfolio allocation, even though only a small fraction of those in the plan prior to the introduction of automatic enrollment made the same choices.

As they explain: “The ‘suggestion’ of 401(k) participation through automatic enrollment leads to large increases in the 401(k) participation rate. The ‘suggestion’ of a 3 percent contribution rate through the automatic enrollment default leads to a dramatic shift in the distribution of contribution rates among plan participants, away from 6 percent and higher contribution levels to 3 percent. And the ‘suggestion’ of the money market fund as the default fund allocation leads to a substantially more conservative investment portfolio, one dominated by the money market fund rather than by stocks.”

They describe automatic enrollment at a fixed, low contribution rate to a conservative investment fund as a “win-lose” approach to changing 401(k) savings behavior: the “win” is that the existence of the automatic enrollment gets more people to save in the plan. The “lose” is that it may result in some people actually saving less: those that would have selected higher contribution rates or a different asset allocation may instead do nothing and “go along with” the automatic choices made for them, rather than take the time to make their own potentially superior choices.

As the authors explain, their results imply that getting the automatic aspect of such plans “right” could have a tremendous impact on the distribution of retirement savings available to individuals. Their important paper clearly qualifies, quantifies, and emphasizes the significance of this issue.