AUTOMATIC CONTRIBUTIONS MADE EASY: EMPLOYER GUIDE AND BEST PRACTICES

Installment #1	Basics of Automatic Contribution Arrangements

What is an Automatic Contribution Arrangement?

Traditionally, employees in a 401(k) plan must affirmatively elect the amount of deferral they want to contribute to the retirement plan. Absent any action on their part, no deferrals will be contributed to the plan on their behalf. The automatic deferral arrangements are designed as a negative election to counteract employee inertia and instead automatically enroll the employee into the plan with a stated deferral rate unless the employee opts out. The employer chooses the stated default rate in the plan document and participants always have the option to opt out of the stated deferral rate or choose an alternate rate. Increased plan participation usually results which enhances overall retirement savings and the increased deferral rates can have a positive impact on the employer's ADP non-discrimination testing.

Different Types of Automatic Enrollment Features

There are three primary types of automatic enrollment features, each with its own rules and benefits. Additionally, a fourth type has been introduced for plans that must comply with the SECURE 2.0 Section 101 mandate, which takes effect on January 1, 2025. If your plan falls under this mandate, we have already notified you separately about the necessary requirements and action plan to ensure compliance. The chart below outlines each available type of automatic contribution arrangement, as selected in the plan document:

	ACA	EACA	EACA Mandate eff 1/1/2025	QACA
Min Default Rate	any %	any %	3%	3%
Max Default Rate	any %	any %	10%	10%
Escalation	optional	optional	required 1% per year increase up to at least 10% but not more than 15% if the starting default is less than 10%	required 1% per year increase up to at least 6% but not more than 15% if the starting default is less than 6%
Notice Requirement	Yes	Yes	Yes	Yes
When provision can be added to the plan	anytime	generally at the beginning of the plan year. can be added mid year if restricted to new employees only but lose 6 month extended testing window.	Affected plans established after 12/29/2022 must have the provision effective no later than 1/1/2025. New plans established after 1/1/2025 need to comply as of the plan establishment date.	subject to safe harbor rules
Special withdrawal of initial Automatic contributions allowed?	No	Yes, between 30 and 90 days of first contribution	Yes, between 30 and 90 days of first contribution	Yes, between 30 and 90 days of first contribution
Employer Contribution Requirement	None	None	None	Safe Harbor Contribution Required - 3.5% match or 3% nonelective minimum. Unique to QACA, can apply a 2 year vesting schedule to the safe harbor

Notice Requirement

Plans with an automatic contribution arrangement are required to provide participants with a formal notice prior to automatic contributions being deducted from their paycheck. Eligible plan participants are required to receive the notice at least 30 days prior to any automatic deferral contributions being withheld and at least 30 days prior to the start of each plan year. MVP will provide this notice each year that the automatic contribution feature remains in effect.

Escalation

Auto escalation is simply a stated increased in employee deferral rates which happens automatically via a set rate and at a set time as prescribed by the plan. Employers can choose to apply an escalation feature to the automatic contribution arrangement. If so elected, the escalation provisions are contained in the plan document. Most commonly, the increases occur annually in increments of 1 percent up to a stated maximum percentage defined by the plan. With the QACA provision, annual escalation will be required if the initial default rate is set less than 6 percent and with the EACA mandate, annual escalation will be required if the initial default rate is less than 10%. To reduce administrative burden, we recommend limiting the escalation timing to one specific day of the year for all employees, usually the first day of the plan year.

Special Withdrawal Provision for automatic contributions

Plans utilizing the EACA or QACA automatic contribution arrangements can choose to allow a special withdrawal provision whereby participants who were caught off guard by the automatic enrollment contributions can request a withdrawal of their contributions within 90 days after the first contribution is made. Any corresponding matching contributions attributable to such deferrals will be forfeited and no additional deferral contributions will be withheld for the participant until which time the participant makes an affirmative election. Such withdrawals are exempt from the 10% early withdrawal penalty. Plans subject to the EACA mandate are required to offer this withdrawal feature starting in 2025. In our experience, one of the best ways to avoid the need for these withdrawals or the participant frustration that generally precedes them is a good communication strategy for newly eligible participants.

Communication is Key

One of the best ways to mitigate problems with an automatic enrollment plan is through a comprehensive communication strategy which serves to ensure that the participants understand the auto enrollment features and process. Employees will need to understand how the auto enrollment will work, what steps need to be taken to opt out of the auto enrollment, and in what time frames those steps are required. The required notice will serve to explain the automatic contribution arrangement, the default percentage and other required information about the structure. Separately, the employer should provide the enrollment materials and enrollment instructions detailing how the participant can opt out of the automatic contribution if desired along with any specific timing requirements for payroll processing.

Help is on the way

Despite best efforts, auto enrollment can be difficult to administer, and mistakes can still happen. Two of the most common errors with auto enrollment is failure to automatically enroll a plan participant or failure to properly apply the automatic escalation feature. Both errors can be self corrected utilizing the principles in the Employees Plans Compliance Resolution System (EPCRS). To encourage employers to offer automatic enrollment, the IRS has a initiated a safe harbor correction for some of these most common errors many of which can be corrected at a reduced cost to the Employer. If you suspect an error was made, early detection is also one of the best defenses so please contact your relationship manager who can guide you through the correction process.