TOWERS WATSON

A Look at Defined Contribution Match Reinstatements

By Vishal Apte and Brendan McFarland

During the recent financial crisis, many employers took cost-cutting measures to preserve their cash. These included layoffs, hiring freezes, furloughs, salary freezes and, in a few cases, salary reductions. Some employers also scaled back retirement benefits, although the cutbacks were often temporary. This analysis looks at 260 companies that either reduced or suspended their 401(k) plan matching contribution after 2008 to see what happened next.

A 2009 Towers Watson study chronicled the effects of the recession on defined contribution (DC) plans — specifically suspended or reduced employer matching contributions.[1] Suspending contributions during tough financial times is not unheard of — there were several such suspensions in 2003. The 2009 analysis found that a surprisingly high number of organizations were temporarily suspending their DC matching contributions to get through the recent crisis.

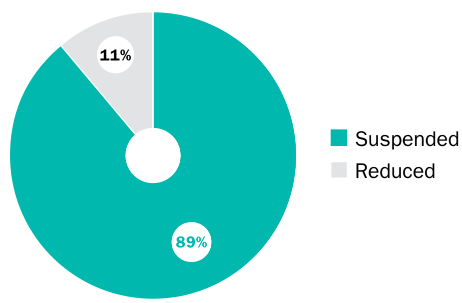
Matching contributions encourage workers to contribute to their retirement savings and help them build a nest egg. With DC plans becoming nearly universal among employers and, in some cases, now the primary vehicle for building up retirement savings, cutbacks to these contributions can derail employees' retirement preparations.

While the number of employers taking such actions increased during the crisis, overall they represent a minority of 401(k) plan sponsors.[2] And beginning in 2010, many employers reinstated their matching contributions, probably due to economic growth in the interim.

Of the 260 companies in our sample, 231 originally suspended their matches, whereas 29 chose a different path to cost savings, reducing such benefits instead of suspending them outright (as shown in *Figure 1*).

Most of the suspensions and reductions to DC matches were initiated during the first two quarters of 2009, but some continued through May 2010. The timing of the cutbacks is shown in *Figure 2*.

Figure 1. Initial form of cutback to DC matching contributions

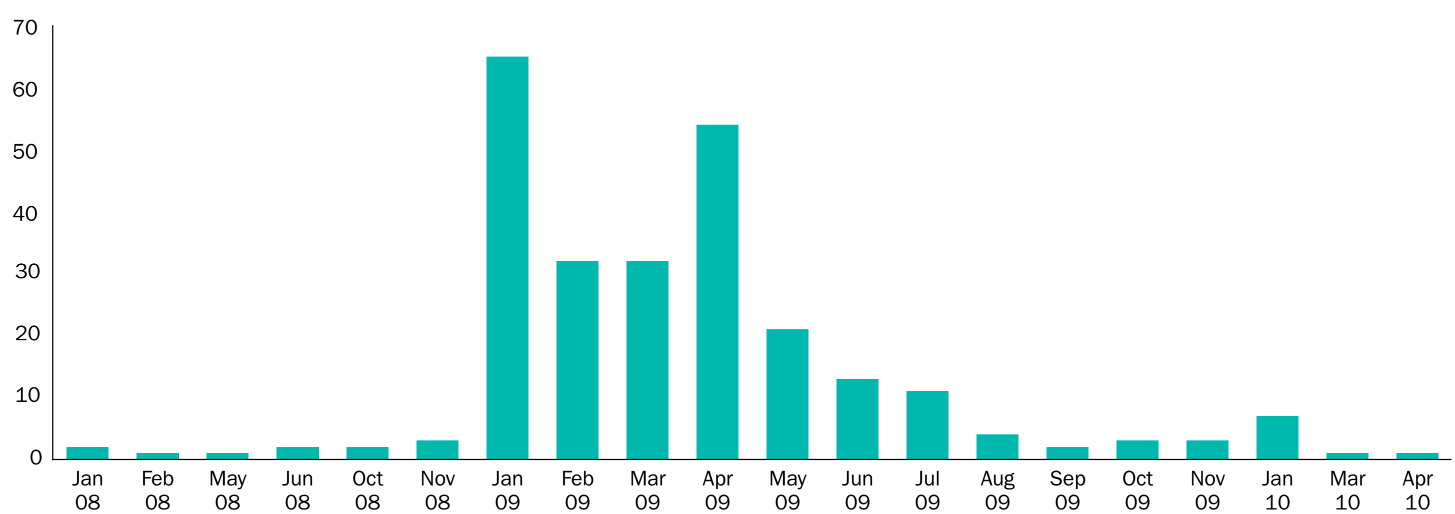


N=260
Source: Towers Watson.

[1] "Economic Crisis Prompts Many Companies to Suspend Contributions to Employee Savings Plans," *Watson Wyatt Insider,* May 2009, available at www.watsonwyatt.com/us/pubs/insider/showarticle.asp?articleid=21034.

[2] According to Towers Watson's *New Strategies in Defined Contribution Plan Design: Results and Analysis From the 2010 Survey of Defined Contribution Plan Sponsors*, only 13% of respondents reported the suspension of their 401(k) match during the crisis.

Figure 2. Timing of match suspensions and reductions by number of companies

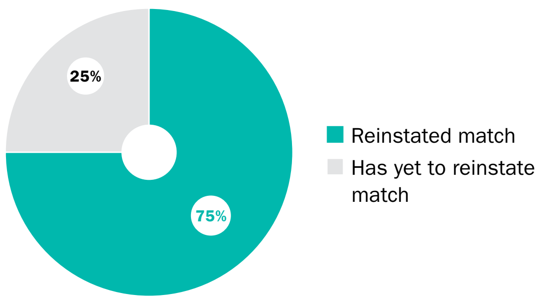


N=260
Source: Towers Watson.

> "Of those that reinstated their match, 105 companies (74%) reintroduced the original match amount."

Approximately 83% of the suspensions/reductions occurred during the first half of 2009, with roughly 46% of the changes taking place in either January or April. Many companies implemented their cutbacks in January 2009, which might have triggered a domino effect that rippled through the first half of 2009. The increase in April is possibly from companies timing their changes to coincide with the start of a new fiscal quarter.

Figure 3. Follow-up actions after match was suspended



N=205
Source: Towers Watson.

Figure 4. Levels of reinstatements for matching contributions

	N	Prior contribution percentage	Current contribution percentage	Difference
Lower	**32**	**4.50%**	**2.36%**	**–2.14%**
Same	**105**	**3.39%**	**3.39%**	**0.00%**
Higher	**5**	**2.90%**	**4.30%**	**1.40%**

Note: The data assume employees make the contributions necessary to receive the maximum matching contribution.
Source: Towers Watson.

Companies that suspended matching contributions

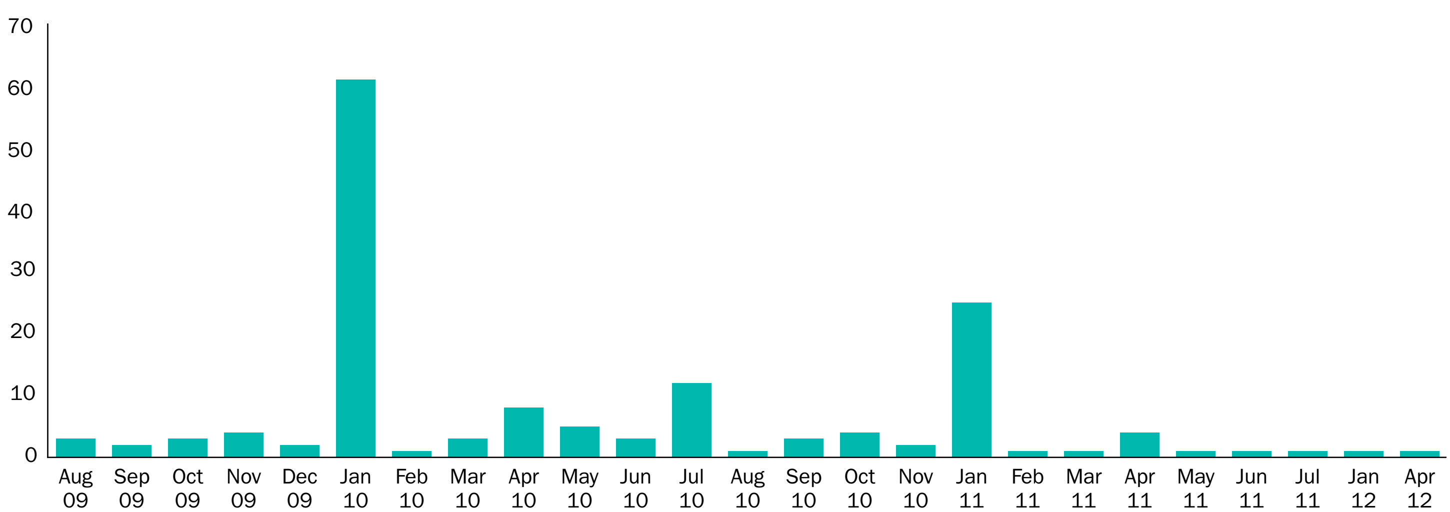
As the economy began picking up a little steam and company balance sheets stabilized, employers began reinstating their matching contributions — usually at the same level, but sometimes higher or lower than the original match. An overview of the reinstatements is illustrated in *Figure 3*.

Reinstatement data were unavailable for 26 of the 231 companies that originally suspended their match. While the majority of the analyzed companies chose to reinstate their match (75%), a good number of them still do not offer a matching contribution to their employees.

Of those that reinstated their match, 105 companies (74%) reintroduced the original match amount (as shown in *Figure 4*). Among these plan sponsors, the most frequent match formula before and after the crisis was 50% of up to 6% of salary.

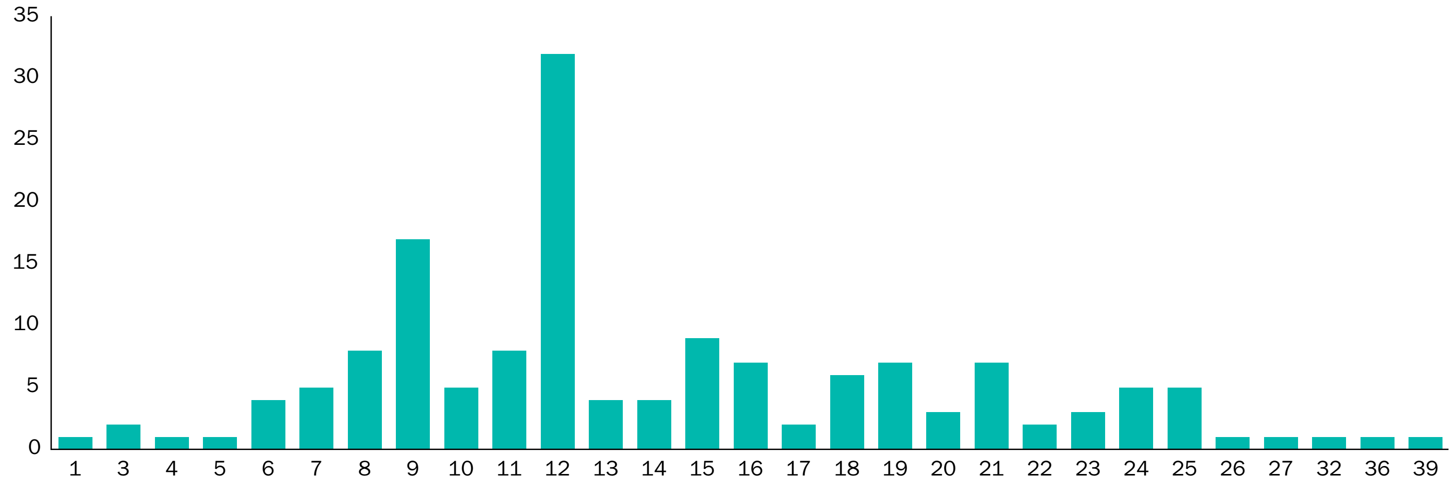
About 23% of companies that suspended and then reinstated their match reduced the match. Among these companies, the reinstated match was slightly more than half of their original contribution. A small minority (3%) reinstated a higher match, increasing the formula by an average 1.4 percentage points. In all but one of these cases, the increase was associated with a pension close or freeze, and the higher match was intended to make up for some of the lost DB plan benefits. The effective dates of the match reinstatements for these companies are shown in *Figure 5*.

Figure 5. Effective dates of match reinstatements by number of companies



N=153
Source: Towers Watson.

Figure 6. Duration of match suspensions in months by number of companies



N=153
Source: Towers Watson.

Forty percent of companies in this analysis reinstated their matching contribution by the beginning of 2010. The second-largest wave of reinstatements was in early 2011.

The median duration for match suspensions was 12 months, as shown in *Figure 6* for companies with quantifiable dates. As the figure illustrates, most companies reinstated their match after nine or 12 months.

The relationship between reinstatement rates and industry sector is also compelling. *Figure 7* shows reinstatement rates by industry. Manufacturing and health care had the highest reinstatement rate, at 88%, and entertainment had the lowest reinstatement rate, at 50%. With the exception of the entertainment, financial and publishing industries, reinstatement rates exceeded 70% for all sectors.

Figure 7. Match reinstatements by industry

	N	Yes	No
Automotive	14	79%	21%
Electronic	8	75%	25%
Entertainment	8	50%	50%
Financial	15	53%	47%
Health care	8	88%	12%
Manufacturing	49	88%	12%
Publishing	26	62%	38%
Retail	16	82%	18%
Technology	30	73%	27%
Transportation	8	75%	25%
Other	23	78%	22%

Source: Towers Watson.

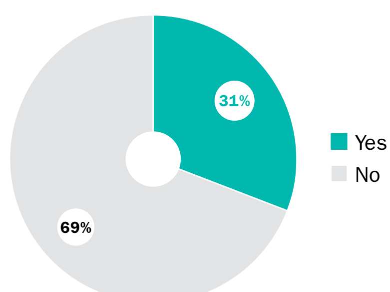
"Manufacturing and health care had the highest reinstatement rate and entertainment had the lowest."

Companies that reduced matching contributions

As stated earlier, 29 organizations reduced their DC match during and after the recession rather than suspending it outright. Thirty-one percent of these companies have since reinstated their pre-reduction match formula (see *Figure 8*). Of these companies, the median duration of the temporary lower match rate was 12 months.

Figure 9 (next page) distinguishes employers whose match reduction remains ongoing from those whose reduction was temporary. Where the reduced formula remains in effect, the match was reduced by an average of 2.19 percentage points.

Figure 8. Was the match reduction reinstated to prior levels?



N=29
Source: Towers Watson.

"Roughly 75% of employers have reinstated their match."

Conclusion

Perhaps reflecting the slow recovery of the U.S. economy, some employers are taking their time in reinstating their suspended 401(k) match contributions. Roughly 75% of them have reinstated their match. Of that group, 74% restored the match to its pre-crisis level, and most others now contribute slightly more than half of the pre-crisis contribution rate.

A smaller group of employers took a different approach during the crisis, reducing their match rather than suspending it. About 31% of these companies have reinstated the full pre-crisis match.

With so many reinstatements having already occurred through 2011, at first it appeared the "wave of reinstatements" would continue through the year. But given recent economic turmoil and the possibility of a double-dip recession, the wave could go in either direction. It could recede, with companies suspending their contributions yet again.

A scenario that left employees to finance their savings plans entirely on their own — as their main retirement vehicle — would be problematic for companies, employees and society. Matching contributions are a major tool in enticing employees to participate in DC savings plans — as well as in helping them build adequate retirement savings — and plan participation would likely decline without them. Historically, DC plans without a match have much lower participation rates than those with a match. Lower participation and savings rates could cause problems for employers down the road, as employees might not save enough to retire in a timely and efficient manner.

Figure 9. Temporary versus ongoing match reduction

	N	Prior contribution percentage	Temporary contribution percentage	Current contribution percentage	Difference
Ongoing reduction	**20***	**4.58%**	**N/A**	**2.42%**	**–2.19%**
Temporary reduction	**9**	**3.81%**	**2.56%**	**3.81%**	**0.00%**

*One company increased its match over the original reduction but not to the pre-crisis benefit level.
Note: The data assume employees make the contributions necessary to receive the maximum matching contribution.
Source: Towers Watson.

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