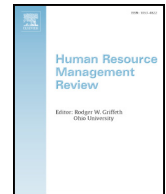




Contents lists available at ScienceDirect

Human Resource Management Review

journal homepage: www.elsevier.com/locate/humres

Understanding pension communications at the organizational level: Insights from bounded rationality theory & implications for HRM

Maureen Maloney*, Alma McCarthy

Discipline of Management, Cairnes School of Business and Economics, National University of Ireland, Galway, Ireland

ARTICLE INFO

Article history:

Received 8 January 2016
Received in revised form 25 July 2016
Accepted 1 August 2016
Available online xxxx

Keywords:

Occupational pensions
Defined contribution
Pension policy and practice
Compensation and benefits
Bounded rationality

ABSTRACT

This paper applies concepts from bounded rationality theory to develop an integrative model to understand how pension scheme structure and pension scheme communication impact pension participation and contribution rates at organizational level. Organizational pension policies create framing effects that can have intended and unintended consequences depending on how they impact on employees' cognitive processes. Organizational pension communication policy impacts employee pension outcomes through the interaction between fast-acting, automatic System 1 and deliberative, calculating System 2 that typically endorses and occasionally overrides System 1 judgments. System 1 exhibits mental short-cuts (heuristics) and systematic biases. The likelihood of a System 2 challenge to System 1 depends on the personal, socio-demographic and economic characteristics of the individuals within the workforce. We propose that those within the HR function, who understand framing effects, can develop pension policies that positively affect pension plan outcomes at the organization level, specifically the pension participation and average contribution rates, using a combination of policies that in some cases promote System 2 endorsement and in other cases, System 2 engagement.

© 2016 Elsevier Inc. All rights reserved.

1. Introduction

Employers offer pensions as a benefit to their employees, often to attract, motivate and retain the caliber of employees required for success in their industry. According to McGill et al. (2005, p. 355), “the prevalence of [pension] plans being offered by large employers makes it virtually imperative for all employers ... to offer some form of retirement program.” Pensions and retirement plans have, therefore, become an important dimension of employee compensation and benefits. One of the key debates in occupational pension research and policy literature is how to ensure employees participate in pension plans and invest sufficient funds over their working lives to provide for income during retirement. However, research indicates that there are serious shortfalls in both pension participation rates (i.e. the proportion of employees investing in occupational pension plans) and in the adequacy of those investments to meet future income needs in retirement (Munnell & Bleckman, 2014; OECD, 2013; Sass, 2014). Employers and their HR function play a critical role in pension savings behavior through the pension plans that they offer to their employees.

Weiner and Doescher (2008) discussed two general approaches to promoting occupational pension savings: structure and communications. Structural approaches emphasize the financial conditions surrounding the retirement savings decision that can

* Corresponding author.

E-mail addresses: maureen.maloney@nuigalway.ie (M. Maloney), alma.mccarthy@nuigalway.ie (A. McCarthy).

be altered by both governments and employers, including tax relief, defaults (e.g. automatic enrollment into an occupational pension plan) and employer matching arrangements. They describe communication approaches as focusing “... on changing both workers' knowledge and their perceptions” of pensions (Weiner & Doescher, 2008, p. 137). They suggest that communications can be used to educate and persuade employees to invest in their pensions. However, most pension research focuses exclusively on pension structure. Studies of note analyzing the impact of pension structure include research conducted by Madrian and Shea (2001) and Choi, Laibson, Madrian, and Metrick (2002, 2004a) which investigated the impact of changes to occupational pension plan structure, specifically automatic enrollment, on pension participation and contribution rates at the firm level. Other research has considered the impact of other structural features such as employer matching (Benartzi & Thaler, 2007; Choi, Laibson, & Madrian, 2004b), the number of investment funds available (Benartzi & Thaler, 2007; Cronqvist & Thaler, 2004; Huberman & Jiang, 2006; Papke & Porterba, 1995), and automatic contribution rate escalation (Benartzi & Thaler, 2007; Choi et al., 2004b; Thaler & Benartzi, 2004; VanDerhei, 2007).

Because the organizations where empirical research was conducted concerning structural pension policies were large, it is likely that there was significant communication with employees about their compensation, pay and benefits, and in particular about their occupational pension plan. However, in pension research examined to date, there is limited insight about pension communication policies that accompanied the structural change within organizations. While the evidence suggests that changes to pension plan structure significantly impact individual pension savings behavior, the contribution of pension communications is an important but largely ignored variable in understanding pension savings behavior within the organization. We argue that pension communication policies can be developed by the HR function to both support pension structural policies and to challenge pension plan members to evaluate their choices; the combination of both approaches should improve both employee and organizational pension outcomes.

It is well established that pension saving decisions for members of defined contribution (DC) pension plans are among the most complex decisions undertaken by individuals during their lifetime for many reasons (Choi, Laibson, Madrian, & Metrick, 2005; Choi, Laibson, & Madrian, 2009; Lusardi & Mitchell, 2007; Madrian & Shea, 2001). Retirement decisions are taken over decades under different personal and employment conditions. The total amount required depends on length of life and health at retirement, circumstances unknown during periods of employment. Economic conditions including fluctuating equity markets and price instability impact on the rate of return on investments. These factors test the knowledge and computational competence of DC pension plan members resulting in pension decision-making complexity that makes it difficult for individuals to estimate how much to save in order to accumulate sufficient resources to provide adequate income between retirement and death.

Bounded rationality is used to “... designate rational choice that takes into account the cognitive limitations of the decision-maker—limitations of both knowledge and computational capacity” (Simon, 2008, p. 893). We suggest that it provides a useful theoretical lens to understand pension decision-making as it provides insights on decision-making where rationality is limited by incomplete information and cognitive limitations for decisions that involve both risk and uncertainty.

This paper contributes to the literature in a number of important ways. First, much of the pension research examined to date, focused on pension structure resulting in a lack of attention to pension communication at the organizational level, an important dimension that may influence occupational pension savings behavior. This paper significantly adds to the literature by using a bounded rationality model to conceptualize the impact of both structure and communication policies on pension organizational outcomes enabling the evaluation of these two major pension policy levers using a single integrated framework. Second, drawing on bounded rationality theory to examine the limitations of individuals' cognitive processes, we explain how structural policies, particularly defaults, promote intuitive or passive decisions while communication policies may either support those decisions or promote reasoned decisions. Third, we discuss within the bounded rationality model a number of personal, socio-demographic and employment characteristics identified through research, that appear to impact on the ability of individuals to make reasoned or active pension decisions. We suggest that HR professionals who understand the characteristics of their workforce can develop structure and communication policies suited to the needs of the employees within their workforce. Fourth, the model will allow those in the HR function to predict the outcomes of changes to pension policies, based on the impact of policies on employees' cognitive processes and to evaluate if policies work as intended. Finally, the paper proposes research questions generated from bounded rationality theory and pension research which provide an agenda for future empirical studies in the field.

Following this introduction, Section 2 of the paper discusses the most common forms of occupational pensions, describes structure and communication policies used by organizations offering occupational pension plans as inputs to the pension decision-making process and defines the organizational pension outcomes, namely the participation and average contribution rates, that can be used to evaluate pension policy effectiveness. Section 3 draws from bounded rationality theory to explain the cognitive processes that intervene between pension policies and pension outcomes, proposing a model (Fig. 1 below) that can be used by practitioners to develop and evaluate pension policy changes. We conclude with a discussion of the theoretical contributions of this paper and the implications for practice.

2. Pension definitions, organizational pension policy approaches, & organizational pension outcomes

2.1. Pension definitions and pension plan types

A pension plan “is an arrangement that provides for payments to be made to a worker on retirement from paid work, or his/her dependents in the event of death” (Kenny, 2004, p. 1). Defined benefit (DB) and defined contribution (DC) are the two main types of occupational pension plans in use. DB plans are relatively simple from the perspective of the pension plan member/

Download English Version:

<https://daneshyari.com/en/article/5033668>

Download Persian Version:

<https://daneshyari.com/article/5033668>

[Daneshyari.com](https://daneshyari.com)