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Comment Jonathan Skinner

There is nothing like a powerful empirical randomized study to help clean old theories out of the attic and replace them with fresher and empirically more compelling ones. With this randomized study of the Quick Enrollment plan, the team of Choi, Laibson, and Madrian have added to their remarkable series of experiments on how 401(k) plan structures affect saving behavior. The experiment provides insights for two theoretical areas: the economics of savings and the economics of choice. I'll consider each in turn.

In the conventional model of lifecycle saving, individual agents maximize utility over their lifespan by smoothing consumption—or more precisely, by ensuring that all appropriate Euler-equation conditions are satisfied. Thus saving is simply a residual between earnings and optimally chosen consumption. In a series of papers, Madrian and colleagues have forced us to think quite differently about savings in optimizing models. First, in Madrian and Shea (2001), we found that the default matters; when new employees must opt out of a 401(k) saving plan, rather than having to opt into a 401(k) plan, they are far more likely to save more, at least within the 401(k). The result does not provide very strong support for our conventional models of saving: if something as trivial as a default rule could have a long-term impact on saving and hence on consumption, then we must conclude that these marginal savers aren't doing a very good job of

optimizing. In Choi, Laibson, and Madrian (2004), they find more than just the default option matters; employee saving decisions are quite sensitive not just to default rules, but to a variety of other dimensions in the 401(k) plan.

And in this chapter, Choi, Laibson, and Madrian study an experiment in which workers are offered a quick enrollment option for the 401(k). Strictly speaking, it is not a default plan, because it requires an active choice to check the “yes” box, but it does constrain the worker into choosing a very conservative contribution rate (2 or 3 percent) and asset allocation (in one case, just money market accounts). Does this experiment by itself shed new light on saving behavior that we didn’t know before? Yes, but not much. If workers were willing to be pushed into default saving plans, then it’s not too surprising that the ease of checking a box on a form should have similarly long-term saving effects in perhaps a suboptimal long-term saving plan.¹

Does this experiment tell us a great deal more about models of economic choice? Here the answer is yes. Economists have generally assumed that more choice is better in an almost tautological sense. But the burgeoning empirical evidence seems to suggest that too many options can actually discourage consumers from making choices even when those choices are probably beneficial. And this chapter provides another important piece of evidence against the notion that more choice is better. Indeed, too many 401(k) choices can result in no 401(k) at all.

While this is news to economists, sociologists and marketing experts have known this for years. One book by Steven Cristol and Peter Sealey gives away the punch line in the title: *Simplicity Marketing: End Brand Complexity, Clutter, and Confusion*. And in the famous 1970 book *Future Shock*, Alvin Toffler wrote:

Today in the techno-societies there is an almost ironclad consensus about the future of freedom. Maximum individual choice is regarded as the democratic ideal. Yet most writers . . . conjure up a dark vision of the future, in which people appear as mindless consumer-creatures, surrounded by standardized goods, educated in standardized schools, fed a diet of standardized mass culture, and forced to adopt standardized styles of life. (p. 263)

Ironically, the people of the future may suffer not from an absence of choice, but from a paralyzing surfeit of it. They may turn out to be victims of that peculiarly super-industrial dilemma: overchoice. (p. 264)

A more scientific test of this “paralyzing surfeit” is provided in Gourville and Soman (2006), who adopted Toffler’s label of “overchoice” in their

1. This also presumes that workers are not offsetting 401(k) contributions by reducing saving in non-401(k) forms. Madrian and Shea (2001) found no evidence of substitution with perhaps their closest substitute: non-401(k) employee saving plans.

study of consumer choice behavior. They conducted several experiments on consumers at shopping malls. In one experiment, consumers were told: “Imagine that you are planning to buy a microwave oven. At the store, you will find the following alternatives.” They would then provide subjects with a description of different microwaves as options, always with a “lone” brand (sometimes Panasonic, sometimes Sharp) matched with from one to five microwaves produced by the “alternative” brand (again either Sharp or Panasonic). The outcome variable was the percentage of times that one of the alternative brand choices was chosen.

There were two different classes of options, alignable and nonalignable. Alignable choices corresponded to different values along a given dimension, for example the size of the microwave. For the alignable choice, the power output, warranty, and features were held constant for both the target microwave and up to five alternatives. The alternatives varied only on the basis of capacity and price; ranging from 1.1 cubic feet (at a price of \$140) to 1.9 cubic feet (at a price of \$220), depending on the number of choices.

Nonalignable choices were options that were more difficult to compare. For these hypothetical microwaves, the options provided identical capacity (1.1 cubic feet) and power output, but the features differ across prices and the five alternative choices: on-line help, adjustable speed turntable, moisture sensor, hold warm features, and programmable menus.

The results were striking. When there were more alignable options, consumers were more likely to choose one of the offered options (rather than the lone brand). With one option, they chose the target brand slightly more than 50 percent; with four or five options they chose the target brand slightly less than 80 percent of the time. By contrast, offering more than two nonalignable options led to a decline in the likelihood that one of the alternative options would be chosen. When there were four to five nonalignable options, the choice of one of these target options dropped to just 40 percent.

These results make perfect intuitive sense. I can easily judge whether I want a bigger or smaller microwave based on past experiences of trying to fit plates or trays into them. But comparing adjustable speed with on-line help—I wouldn’t have a clue. It’s easiest to make no choice at all.

The analogy applies as well to the case of Quick Enrollment. With so many complex options, it’s just easier to choose just one option, even if that option may not be perfectly suited to one’s long-term saving plans. (The model is a little more complex here, because of the option to not contribute at all.) And the lessons from this research apply as well to the design of 401(k) programs. First, expanding the choice set along an alignable dimension, like the percentage of income to contribute, could actually increase the percentage of workers who sign up. Thus one could imagine three different subgroups for saving: Quick Enrollment Basic (2 percent of

earnings) Quick Enrollment Saver (4 percent) and Quick Enrollment Supersaver (6 percent).

Second, there are inherent nonalignable choices that need to be made in making investments. How can one really compare Japanese stock funds, inflation-indexed bonds, or high-yield corporate bonds? Choosing a default of money market accounts may protect firms from legal suits in the event that the (say) Japanese stock market implodes, but it's not really the best approach to saving for retirement. Perhaps collapsing these nonalignable choices to something that sounds alignable—like “low growth/low risk,” “middle growth/middle risk,” and “high growth/high risk” would be one approach to strike a middle ground between a paralyzing surfeit of choice and the absence of any choice at all.

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