



AMERICAN BENEFITS COUNCIL

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MYTHS AND FACTS REGARDING 401(K) PLAN FEES

Recent media coverage and public opinion has mischaracterized the relationship between employer-sponsored defined contribution retirement programs, such as 401(k) plans, and the fees paid by employers and participants. The Council strongly supports efforts to improve fee disclosure, but in order to do so in a productive way it is important to distinguish the myths and facts about 401(k) plan fees.

Myth: *Employers oppose expanded disclosure of 401(k) fees.*

Fact: Employers support enhanced disclosure of 401(k) fees. Many Council's members have assisted the U.S. Department of Labor in its ongoing efforts to enhance plan fee disclosure and have testified before Congress on how to ensure useful disclosure among employers, service providers and plan participants.

Myth: *Fees participants pay for employer-provided 401(k) plans exceed what is typically paid for standard mutual funds.*

Fact: An Investment Company Institute report found that 401(k) participants have generally concentrated their assets in low-cost mutual funds. "The average total expense ratio incurred by 401(k) investors in stock funds was 0.74 percent in 2006, less than half of the 1.50 percent simple average for all stock funds and *lower* than the industry-wide asset-weighted average of 0.88 percent. 401(k) mutual fund investors not only incur low average expense ratios in stock mutual funds overall, but also in each broad type of stock fund: domestic stock funds, hybrid funds, and foreign stock funds." (ICI, "The Economics of Providing 401(k) Plans: Services, Fees, and Expenses, 2006" September 2007).

Myth: *Employers are insensitive to fees charged by 401(k) providers because they pass them on to participants.*

Fact: Employers are well-educated about their workforce's needs and conscientiously seek reasonable fees and services for their employees. The concentration of 401(k) assets in low-cost funds, as described above, is due in part to the close oversight of employers.

Myth: *401(k) fee legislation will lower plan fees for participants.*

Fact: The 401(k) market for services is very competitive, with providers competing fiercely not just on fees but also on quality of services. No disclosure legislation can eliminate the significant costs of operating a 401(k) plan and complying with numerous legal requirements. While transparency of fees is an aid to competition, that disclosure must be straightforward and provide employers and participants with useful information, or the costs of providing the disclosure will actually increase fees.

Myth: *Increased fee disclosure will lead to better returns for 401(k) plan participants.*

Fact: Participants need to think critically about their investment choices. Fees are only one aspect of retirement investing that participants must consider. Appropriateness of fees can only be judged in context, and must be weighed along with risk, diversification, historical and expected rate of return and investment objectives (i.e., short-term or long-term goals). For example, it would not be appropriate for participants to concentrate all their accounts in money market funds or employer stock, even though these options may have the lowest fees.

Myth: *Most 401(k) plan fees profit employers and plan administrators, and fees should not exceed one percent.*

Fact: Fees are not profit centers for employer plan sponsors. Under employee benefits law, the employer as fiduciary must ensure that fees paid for services are reasonable and the retirement plan is used solely for the participants and does not inure to the benefit the plan sponsor in any manner. The reasonableness of a plan's fee depends, in part, on the plan's size. Many compliance costs must be incurred whether the plan has 50,000 or five employees. In addition, high quality services and products may have greater fees to pay for valuable participant services such as: Internet access and voice response systems, online distribution and loan modeling, online calculators for comparing deferral options, investment advice and education services deferral options. With expanding choices and increased access to their plans, participants are coming to rely on these services, making investment changes to achieve their own objectives.

Myth: *Congress has forced companies to confront the issue of 401(k) fees.*

Fact: Employers' interest and expertise in this area have been increasing as the marketplace has evolved from a predominantly defined benefit pension plan environment to a defined contribution retirement savings plan environment. Employers have been actively contributing to the formal analysis by the U.S. Department of Labor that began in 2006 – before Congress or the courts took-up the issue.

Myth: *The courts have ruled that current 401(k) fees are illegitimate.*

Fact: Rulings on this issue have generally not found any problems. Most court cases have not yet been decided.

Myth: *More disclosure is better disclosure.*

Fact: To be useful, disclosure must be accessible and meaningful to plan participants. Voluminous information can unintentionally result in disclosures that are ignored or exacerbate the paralysis that often affects participation decisions, thereby discouraging saving for retirement. Anecdotal evidence widely suggests that benefit statements are already quite robust, and yet many summary documents are seldom read.

Myth: *Disclosure of 401(k) fees is the most pressing issue threatening retirement savings.*

Fact: Fees are just one part of the puzzle. Increased financial literacy and retirement plan coverage are vitally important to the nation's economic future. "Improving financial literacy" and "increasing the share of workers in workplace retirement plans" were the first two goals listed in the Council's long-term strategic plan document, *Safe and Sound: A Ten-Year Plan for Promoting Personal Financial Security*. Fees are important, but should not be focused upon to the exclusion of other critical aspects of retirement planning.