



The Future of Fee Disclosure (and What Small Businesses Need to Know About It)

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It's about time! That's the sentiment from investor advocates to the proceedings in Washington that have brought 401(k) plan fee disclosure into legislative crosshairs. Proceedings in the House of Representatives and at the U.S. Department of Labor have helped bring this long neglected issue to light among lawmakers and securities industry regulators.

Today, legislators, retirement plan industry companies and the other financial professionals involved in the implementation of 401(k) plans are all waiting to hear the guidance set to be delivered from the U.S. Department of Labor on this issue to determine their next steps. On the plan management and delivery side, fee transparency almost certainly will be financially painful for the companies that have not already committed to fully transparent fee disclosure.

On the flip side of this issue, it is certain that small businesses and their employees stand to derive the most benefit from legislation requiring more transparent fee disclosure information outlined clearly in layman's terms. The future of 401(k) plan fee disclosure will deliver a rebalanced playing field between small businesses and their plan providers.

Excessive and undisclosed 401(k) fees currently undermine the ability of the 50 million American workers covered by 401(k) plans to save for retirement, especially those who work in the underserved market of small employer plans. These fees are one of the most obvious hurdles to a secure retirement for all workers.

Why all the recent fuss about hidden fees?

Ethics has become a hot topic over the past six years, as regulators and lawyers have gone after corruption in corporate America and in the financial services industry, and it only makes sense that the issue of 401(k) fee disclosure is now being addressed.

Many 401(k) providers, including insurance companies, mutual fund complexes, brokers and banks, structure plans to include layers of fees and fail to educate employees on how those fees are paid and how they may impact retirement savings. Almost no employees who participate in 401(k) plans understand or know how to account for such things as "soft dollar" fees, 12b-1 fees, variable annuity wrap fees, sub-transfer agency fees, sales loads or other expenses that might come out of the assets that they have set aside for retirement.

These fees can be devastating to a retirement nest egg. An asset-based fee of as little as 1 percent can quickly eat into an account's value.

Unscrambling the opaque, multi-level fee structure within 401(k) plans has been a task that Congress has neglected for years. Now, thanks to a push from Rep. George Miller (D-CA), the issue of 401(k) fee

disclosure has made its way in front of Congress. Recently, the Department of Labor sought comments on the subject in preparation for proposing new regulations and Rep. Miller introduced a bill in late July that would require full disclosure of 401(k) fees and require disclosure of consultant conflicts of interest.

What's the future of 401(k) fees?

So, what's the future for hidden fees? Can we solve this problem without the addition of unnecessary regulations?

Plain and simple, 401(k) plan participants and plan sponsors have the right to basic information about their 401(k) plans. Specifically, those committing their retirement savings to a plan deserve simple and jargon-free disclosure of fees associated with plan management, distribution and investments.

A mandate for better disclosure of hidden fees, including universal guidelines for all providers to provide both business owners and employees with a plain-English explanation of the fees that affect the business and individual balances would be a great first step.

Beyond legislation that would outline what constitutes fee disclosure transparency, the implications of such a law are a big part of the future for 401(k) fees. This discussion, while not about managing costs, must include a discussion of the impact of fee disclosure requirements and the future outlook for total costs that a participant and a plan sponsor can expect.

To date, the role of technology and the internet in this issue has gone unaddressed. As fee transparency becomes a reality, it should become apparent that the costs attributed to plan administration, enrollment and education can be trimmed significantly with better utilization of the technology and internet-based tools that can make retirement plans largely more affordable to the small and mid-sized business that is most impacted by the current murky nature of fee disclosure.

By using current technology and providing simple and straightforward Web-based tools for plan sponsors and participants, 401(k) providers can manage costs to offer better retirement plans to small employers — and disclosure of hidden fees is just the beginning.

Ultimately, those in favor of fee transparency within 401(k) plans are subject to the might of the lobbyists representing the interests of mutual fund and insurance companies with a large amount of money at stake. Should fee transparency guidelines be enacted, we can expect to see small businesses confused by the cost structure of plans get into the game when the fee discussion is simplified.

If Fee Disclosure Transparency is the Future...

If we solve the hidden fee problem, there's still the larger issue, which is summed up succinctly by the Investment Company Institute's response to the Department of Labor's recent call for responses to the fee issue:

"The biggest challenge in ensuring adequate retirement security for all Americans lies in encouraging more small employers to offer a workplace plan."

Many 401(k) providers will tell you that their biggest competition in closing deals with small businesses is inaction. Rather than contend with the complexity and financial commitment that sponsoring a plan might entail, business owners often choose to avoid setting up a 401(k) plan.

Presuming that the fee disclosure issue is addressed, providers can set about educating business owners and employees about the importance of saving for retirement and finding ways to enable them to take action without putting them in a position where they can see and understand the costs associated with such a plan.

Small businesses pay the price – but they don't have to

Up to 85% of small businesses don't have a plan – and yet a 401(k) is one of the most important benefits that small business employees look for – second only to health care.

How did we get here?

As the 401(k) industry is primarily compensated by asset-based revenues, it is a generally accepted industry maxim that small plans cannot be profitable and that those plans can only be sold by hiding fees from the small employers that sponsor plans and their employees.

The irony is, small plans DO make business sense. In fact, the opportunity in the 401(k) market is in small plans. The number of small plans (plans with less than 100 participants) grew by nearly 200,000 from 1996 to 2005 and it is expected to grow by another 100,000 from 2005 to 2011.

Where do we go from here?

The retirement plan industry will continue to face scrutiny and pressure to cut fees as long as the market for their services (potential plan sponsors and participants) do not understand where their fees go. Mutual fund and insurance companies can expect their revenue to shrink if participants and sponsors get a good look under the covers of 401(k) plan fees.

For small businesses, fee disclosure transparency will remove one of the obstacles in understanding and appreciating how retirement savings plans can benefit companies, owners and employees.

Finally, if the 401(k) industry wants to justify its existence, we need to openly level the playing field so all of the players – plan sponsors, participants, administrators, managers – understand what the true costs and benefits of implementing a retirement plan. Here's to hoping that our Congress will send us in the right direction on this issue.