

*In everyone's best interest*

EMPLOYEE BENEFIT CONSULTANTS | RETIREMENT PLAN ADMINISTRATORS | REGISTERED INVESTMENT ADVISORS

EMPLOYEE RETIREMENT PLANS

Current Developments in Plan Administration and Participant Investment Choices

Retirement Plan Fees –

One man's bread and butter and another's expense. It all depends on whether you're a provider or user of plan services.

The Department of Labor and the Internal Revenue Service take this bulletin's opening statement seriously. We do as well, and as a plan sponsor a regular review of plan fees is part of your plan sponsor fiduciary responsibility.

Three Necessary Expenses

Establishing your plan, investing the plan's assets, and the ongoing administration are three expenses that are inescapable.

First, to establish your plan you'll need a plan and trust document, a booklet for participants (summary plan description) that explains the benefits and obligations of participating in the plan, and a variety of forms for enrolling, naming beneficiaries, directing account investment, etc.

Second, investment products for your plan are available from many providers.

Insurance companies are usually the most expensive as they are an added layer of cost while adding little value. They do provide an annuity option to terminating participants, but it is our experience that very few participants find an annuity more valuable than a lump-sum distribution. Buying mutual funds through an insurance company is bound to cost more than buying funds directly from the mutual fund company.

Mutual funds are the most common choice for smaller plan sponsors. However, they often come with a hefty expense ratio. There is the compensation to the manager, usually a percentage of the assets under management, who the fund company hires on an annual contract. The fund company has the job of administering the fund, distributing reports, keeping score of who owns how many shares, and earning a profit.

The last group in the mutual fund food chain is the distribution system, usually investment brokerage firms who receive a commission for as long as the buyer holds the shares.

The average expense ratio for a no-load, mutual fund, i.e., one that pays no direct commission to a broker for selling it, is 1.4%; those with commissions are about .35% higher.

Most mutual funds, because of the fee structure, distribution system and tax status are really designed for individuals, not qualified retirement plans.

BENEFITWORKS usually recommends that plan trustees consider exchange-traded unit trusts or model portfolios designed by independent security analysts, such as Standard & Poor's or Value-Line. Using these typically saves .8% to 1.2% of plan assets each year.

With an investment earning 8% for 25 years a difference of .8% makes a difference of 20% in the value of an account!

Interestingly (and the SEC is considering more disclosure by mutual fund companies) mutual fund expense ratios

do NOT include transaction costs of buying and selling securities. MorningStar (a mutual fund research and reporting firm) estimated that many actively traded mutual funds will be required to show more than .5% of additional expenses.

In managing portfolios, our firm uses TD Ameritrade Institutional Services to buy and sell securities, paying a fee of \$9.95 for up to 5,000 shares of stock. Example: a purchase of 2,000 shares at a price of \$37.50 per share would cost \$75,000 plus a transaction cost of \$9.95, a miniscule expense of .000133 for the transaction.

The final expense is for ongoing plan administration. This includes maintaining accounts for all plan participants. Separate accounts are established for each participant's contributions, employer contributions and rollover contributions, for each investment choice – easily 7,500 accounts for a 100-participant plan. Also, participant account values must be determined daily and reported quarterly. We use a web site to make values available at any time to participants.

Annual reporting to the IRS, including plan testing for compliance with the IRS Code, as well as tax notification to terminated participants is required.

We are committed to charging only fees that are fully disclosed and to be a high quality/low-cost provider. In most cases, our annual administrative fee is .85% or less, making our total charge less than what most plans pay for investment products alone.

Who Should Pay Plan Expenses?

The IRS gives employers considerable breathing room in this regard. The basic rule is that the cost of setting

up the plan and any amendments to keep it qualified by the IRS are to be paid by the employer/sponsor. The ongoing costs of investing assets, allocating contributions, reporting to participants and reporting to the IRS may be paid either by the employer, the participants, or shared by both.

In practice, the larger the plan the more likely the participants will pay all administrative costs. Very few S&P500 companies pay ongoing expenses.

The expenses of administering the plan are tax deductible to the employer. Any matching or profit contributions made by the employer are also fully tax deductible.

Our experience is that if an employer is paying plan expenses, it is better to use those dollars as an additional matching contribution.

Participants are aware of and appreciate an employer matching contribution. It encourages employee participation. If the employer uses funds to pay plan expenses, the employees are simply not aware of the benefit or amount of such a contribution.

The answer to “who pays for what” is finally one the employer makes based on his overall human resource policy and other benefit programs.

If you would like assistance in determining your present total plan costs (the IRS thinks all trustees have a fiduciary responsibility to understand total costs), or would like an evaluation of cost-sharing ideas, don't hesitate to give us a call, (717) 273-8441 or email us at info@benefitworks.com.