An Interview with David Wray

By Editor Test *Wed, Feb 8, 2012*

Don't expect participants to revolt when they see how high their 401k fees are, and don't expect 12b-1 fees to disappear, said the president of the PSCA. But the problem of 'fee bracket creep' should be fixed by new federal rules.

As the president of the Profit Sharing Council of America, an association of retirement plan sponsors of all sizes, David Wray is in a good position to evaluate the potential impact of the Obama administration's efforts to change the way Americans save for retirement.

We spoke recently with Wray and asked for his views on the February 2 announcement by the Departments of Labor and Treasury regarding the creation of new requirements for fee disclosure in retirement plans and the removal of certain technical roadblocks to turning qualified savings into retirement income.

RIJ: What are your takeaways from last week's announcement?

Wray: They've clarified that you can take partial annuitization, they clarified the spousal consent issue, and they clarified that if you buy longevity insurance, it will be coordinated with required minimum distributions. All of those things are intended to expand the choices for participants. We'll have to see what the next step is.

RIJ: On fee disclosure, this doesn't necessarily mean that a plan can have only the least expensive index funds, right?

Wray: This isn't about being cheaper. It's about ensuring value. If someone has a high-service plan, it will cost more. But it is clear that employers will have to rigorously review the fee structure in light of the benefits provided. There is no single right answer to questions about 'reasonableness' of fees. The largest fees are for investment management, and people wonder if fee disclosure will impact the philosophic approach to investing, in terms of active versus passive. One the one hand, fiduciaries in large foundations use active management. On the other hand, obviously there are arguments for passive management. The question is, will this [action by Treasury and Labor] change that? I don't know.

RIJ: How do you think participants might react to fee disclosure?

Wray: You'll have a period of time when people are surprised, because they didn't realize the fees are paid out of their assets. There will be a lot of questions, but once the questions are answered, it will go back to normal. The 401(k) plan participants aren't retail investors. They're in plans because employers entice them into them. So once you explain the fees they will go back to normal behavior. No one's going to be storming the corner offices.

RIJ: How do you think plan sponsors are reacting?

Wray: For the large companies this is just another typical government regulation. They have lawyers.

They'll convert this to a routine. The real challenge is how is this delivered to small plans, and how they will digest this.

In the past, plan sponsors knew they had to supervise the investments, but this is a new and highly specific directive. The government is saying, 'You must get this information in this way at this time.' It's the sponsor's obligation to ensure that providers deliver it. If the data arrives in the form of 5,000 pages in a box, the small plan sponsor won't have a clue. So they hire consultants, and hand them the box. But the Department of Labor recognizes this and has provided a roadmap for plan sponsors for dealing with it.

RIJ: How will fee disclosure change the way business has been done?

Wray: The big change in all of this will be for small plans sponsors whose plans have been subject to 'fee bracket creep.' Small plan sponsors are typically very busy people. They forget that when they signed the original contract the fee structure was based on very few assets in the plan. The fees were naturally very high at that time, because you had to pay to get it running.

The plan is like an individual account in the sense that, as the account balance grows, you should get lower fees, especially as you walk through thresholds—and there are definite thresholds. But if the plan sponsor hasn't looked at the fee structure for 10 or 20 years, there's likely to be a problem with bracket creep. The fees may still be at the same high level as when there were no assets. That's where you'll see an adjustment. With appropriate supervision, there should be a discussion every four or five years about the fees.

RIJ: How will plan advisors be affected?

Wray: There's another place where there will be an adjustment. The fee issue is all about getting value for the fees, so what will be exposed is that if people are getting paid and not providing service to plan, there will be pressure to end that relationship. If the broker [who sold the plan] is still getting a trail fee, and that broker hasn't shown up for six years and isn't providing services, that arrangement is going to be addressed.

RIJ: What about revenue sharing? Will 12b-1 fees disappear?

Wray: This won't eliminate 12b-1 fees from plans. Consider the 12b-1 fee as a kind of wrap fee. If they went away they'd come back as a wrap fee. For instance, Form 5500 is a bear to fill out. Somebody has to pay for completing it. If the plan pays for it you have to assess the account holders. The 12b-1 can be used to pay for that; it fits a certain kind of model for advisors. Some people say we'll go all to passive investments and there will be no 12b-1 fees. In that case, you'll have a wrap fee. The 12b-1 fee was originally used to help pay for marketing for individual mutual funds. In the 401(k) world it became a sort-of wrap fee replacement.

RIJ: Realistically, fee disclosure isn't going to solve the really big retirement issues, like the overall lack of saving, right?

Wray: Fee disclosure is not about getting people to save more. Yes, we want the system to be as efficient as possible. But getting people to save in their plans is a whole different issue. As I said before, participants aren't retail investors. You coax them into the plans through techniques and alternatives, but the problem is still about saving enough.

The reality is, Americans don't save a lot. We don't think of saving first. Overcoming that is difficult. People can always find excuses not to save, especially if they haven't gotten a raise. Reducing fees merely addresses the question, 'How do we accumulate more faster?' But the challenge to get people to save remains. We've been making progress, but when you read that 'the economy will go well in 2012 if people spend more and save less,' you realize how we talk about spending and saving. It's almost a cultural issue.