
One 401k provider girds for price pressure as disclosure kicks in

By Editor Test *Wed, Sep 5, 2012*

Simply pursuing the lowest cost is a real risk for small plan sponsors, who account for 90% of the nation's 401(k) plans, said Kevin Watt, senior vice president of Security Benefit's defined contribution group.

Along with the symbolic end of summer, the end of August—the 30th, to be exact—also marked the deadline for starting disclosure of 401(k) fees by plan sponsors to plan participants. As of last July 1, plan sponsors were to have received a rundown of fees from their plan providers.

At this early stage of the fee-transparency game, observers still don't know for sure whether a spike in cost-consciousness—among sponsors or participants—will follow the fee disclosure deadlines, or if a significant number of plan sponsors will want to switch plan advisors, providers or administrators in search of lower fees.

Providers are evidently concerned about a price war, and suggest that plan sponsors take care not to sacrifice quality for low price.

An executive at Security Benefit warned in a recent release that the Labor Department's fee disclosure rules could trigger a "fee race to the bottom" unless plan providers shift the focus to the "reasonableness" of service costs rather than the costs alone.

Simply pursuing the lowest cost is a risk for small plan providers, which account for 90% of the nation's 401(k) plans, said Kevin Watt, senior vice president of Security Benefit's defined contribution group.

"The ability to easily see costs will prove invaluable to plan participants," he said. "But reasonableness means a lot more than cheap." If service quality decays, plan participants could be hurt more than helped by the new rule, he said.

"It's absolutely critical that before the RFPs [requests for proposals] start going out, participants need to know what they give up for stripped-down, low-cost plans," Watts added.

The first round of the DOL's fee disclosure rules, which became effective on July, requires service providers to disclose the compensation they receive to plan sponsors. Sponsors will be able to compare service prices among providers more easily, stoking price competition among providers.

As of August 30, the new rules require plan sponsors to begin disclosing the fees of the investment options in their plans to participants. Watt said disclosures will give good advisors an opportunity to stress the link between the cost of advice and investment outcomes.

Security Benefit partners with licensed financial planners to provide advice to employer-sponsored retirement plans. The firm's recently-launched Security Benefit SecurePoint Retirement 401(k) product includes the services of Mesirow Financial as an ERISA 3(38) fiduciary.

Plan sponsors are not compelled by their fiduciary responsibility or by the new regulations to determine that fees are low, only that the fees are “reasonable.” Their perception of reasonableness may depend on whether they get complaints about fees—or perhaps legal action—from plan participants.

Fidelity Investments, the largest 401(k) provider, has released fee data to participants and not received much feedback, but that was no surprise because Fidelity’s fees already reflect vast economies of scale. It may take longer to see how participants at tens of thousands of small, higher-cost plans will react as they learn more about their fees.

“Participants will be surprised by the size of these fees,” predicts business and tax attorney Christopher Ezold, a Philadelphia-based attorney specializing in business, employment and health care law. (According to a research group, New York City-based Demos, the total fees paid on 401(k) plans reduce accumulation in retirement accounts by 30% on average over a lifetime of saving.)

“In fact, many will be startled to see that they are paying investment management fees at all. The new rules will likely strengthen a trend to reduce fees on all 401(k) plans as long as participants learn what action they should take,” Ezold said. But he warned that the mere availability of fee information will not necessarily lead to lower fees.

“Now that the proverbial curtain has been pulled away, the heightened focus on fees will empower the participants to demand a better return on their investment,” said Ezold. “However, participants need to do their homework and take action. These new quarterly reports need to be examined and compared if the plan participants expect to see change.”