

MEMO# 9412

November 13, 1997

INSTITUTE TESTIFIES BEFORE DEPARTMENT OF LABOR REGARDING 401(K) PLAN EXPENSES

[9412] November 13, 1997 TO: BOARD OF GOVERNORS No. 60-97 PENSION MEMBERS No. 53-97 RE: INSTITUTE TESTIFIES BEFORE DEPARTMENT OF LABOR REGARDING 401(k) PLAN EXPENSES

The Institute testified at a November 12 Department of Labor hearing regarding 401(k) plan expense disclosure. The Department called this hearing to obtain public comment on the following concerns: (1) the extent to which employers and employees are obtaining adequate information regarding 401(k) plan fees and expenses; (2) whether employers are shifting plan administrative expenses to plan participants, either directly via annual or quarterly charges against individual accounts or indirectly through investment management fees paid by participating employees, including whether such fees are adequately disclosed to employees; and (3) the reasonableness of the fees charged for 401(k) plan services and investment products. Copies of the statements of Secretary of Labor Alexis Herman and Assistant Secretary Olena Berg, the Institute's written testimony and a list of the individuals that testified at the hearing are attached. In oral testimony, the Institute emphasized the importance of disclosure and explained that the fee table in a mutual fund prospectus provides standardized disclosure of all fees and expenses associated with a mutual fund. Under ERISA section 404(c) regulations, employers are required to provide prospectuses to plan participants. The testimony made the following three points: (1) The growth of defined contribution plans generally, and 401(k) plans in particular, is a positive development providing employees with an easy-to-understand benefit, the advantages of tax-deferred salary reduction, investment control and benefit portability. (2) Employers, in their role as plan fiduciaries, are responsible for prudently selecting and monitoring both investment options and service providers and ascertaining which best fits the needs of their plans and employees at a reasonable price. In determining reasonableness of price, employers must consider all expenses, including expenses associated with particular investment products and expenses incurred in connection with plan administration. Fierce competition, ongoing monitoring of price and quality - 2 - by employers, and the ability of employers to change providers moderates prices and increases the level of and quality of services. (3) Most importantly, employees should be provided information about all fees and expenses related to the investment options in their plans and all plan administration fees that affect their account balances. In the case of mutual funds, the fee table in the prospectus provides detailed fee information, including annual operating expenses of the mutual fund. In the case of non-mutual fund investment vehicles that are not required to produce a prospectus, however, current regulations require disclosure of annual operating expenses only upon participant request. The lack of

an affirmative disclosure requirement for non-mutual fund products leaves many participants without appropriate expense information, as mutual funds constitute only about 39 percent of the 401(k) market. Additionally, the Institute stated that no provision of ERISA explicitly requires full disclosure of all plan administration fees that are charged against participant accounts. The Institute recommended that the Department of Labor require employers to deliver annual operating expense information of all investment alternatives to employees and also disclose to them all plan-level fees that affect participant accounts, at least in the case of plans that fall within ERISA section 404(c). Matthew P. Fink President Attachment (in .pdf format) Note: Not all recipients of this memo will receive an attachment. If you wish to obtain a copy of the attachment referred to in this memo, please call the Institute's Library Services Division at (202)326-8304, and ask for this memo's attachment number: 9412.

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.