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Unexplained fees pose danger for participants

By SHEILA LIVADAS

Because of a recent spate of class action lawsuits, experts say more employers should step up their efforts to examine inflated administrative and investment fees in 401(k) plans.

Still, companies that do so in good faith may encounter plan providers and administrators unwilling to disclose many meaningful details.

Technical language and omitted information in annual account statements, summary plan descriptions and mutual fund prospectuses also may stymie plan participants' efforts to learn more about the fees.

The problem is critical, experts say, because unchecked fees have the potential to wash away thousands of dollars for employees in charges and lost investment returns over time.

"It's very, very convoluted to figure out what the fees are if you're a plan participant," says Gary Mink, executive vice president of HR Benefit Advisors Ltd. in Rochester. "Most of these plan fees are being netted out of the investment returns.

"And that's the reason why most funds are underperforming the market because so much is being skimmed off of those investment returns to pay for those fees."

For protection, experts recommend employers work with plan vendors that disclose embedded fees in writing. Employers should then monitor whether the plans they select deliver market returns. Every three years firms should benchmark their plans against ones of similar size and renegotiate fees, experts maintain.

Small or occasional fees may seem like nothing to sweat, but hard numbers tell a different story.

According to congressional testimony delivered last March by national financial expert Stephen Foster, a couple investing \$10,000 annually over 30 years and earning 10 percent in a 401(k) can expect to have more than \$1.9 million at retirement. A couple earning only 9 percent because of a 1 percent fee would end up with roughly \$350,000 less.

Recent litigation also has illuminated the problem. The St. Louis, Mo., law firm Schlichter, Bogard & Denton LLP, for example, has brought several lawsuits against employers, alleging that they saddled work-



Photo by Kimberly McKinzie

"Most of these plan fees are being netted out of the investment returns," says Gary Mink, executive vice president of HR Benefit Advisors.

ers with excessive fees and failed to disclose information about the charges.

Targeting corporate giants such as Boeing Inc., Caterpillar Inc., International Paper Co. and others, the law firm's suits contend these employers—often called plan sponsors—violated the Employee Retirement Income Security Act of 1974.

Rules wrapped into the federal law spell out minimum protection standards for voluntarily established pension and health programs, including provisions stating that parties other than participants may not benefit from the plans.

Also at issue in the lawsuits is the practice of revenue sharing, defined as when investment companies share a portion of their earnings with record keepers or other service providers. Some of the harshest critics of the retirement industry liken revenue sharing to kickbacks.

Investment firms also have not gone unscathed. In December, Schlichter, Bogard & Denton brought suit against Fidelity

Investments on behalf of employees of Deere & Co., the farm equipment manufacturer. As in the other suits, the law firm alleges Fidelity fleeced staffers. Deere also was named in the action.

Though litigation has thrown several well-known corporations in hot water, HR Benefit Advisors' Mink says he still encounters many employers that seek his firm's plan benchmarking services in good faith.

"We have many plan sponsors that are very busy; they don't have the time (but) they know this is something that should be looked at," he says.

Mink adds that employers do have options to remedy problematic fees.

"If they're happy with their vendor, then we could move forward and negotiate with their current vendor to get the cost more in line," he says. "Of course, we would do that armed with the facts of what similar plans are doing.

"If costs are way high and their services are sub-par," Mink continues, "then they may want to consider a provider search. And then we would do a 401(k) provider search for them."

One firm that sought HR Benefit Advisors' services last year is Buffalo-based Sorrento Lactalis Inc., a nationwide producer of ricotta and other cheeses.

Concerned about having three 401(k) plans as a result of acquisitions, Sorrento worked with HR Benefit Advisors to search for a new provider to combine the plans—valued at \$50 million—and consequently lowered participants' fees by nearly 20 percent.

Mink notes that understanding the urgency of the fee problem hinges on the widespread disappearance of defined-benefit pension plans. Without that safety net, many workers now must be more watchful of their nest eggs.

"Pretty much what has happened is that employees are on their own for retirement," he says. "No longer can they be guaranteed that they're going to receive (that) benefit."

James D'Amico, president and CEO of Genesee Valley Trust Co. in Pittsford, contends the reasons for out-of-whack fees range from ignorance to inertia on the part of employers.

"There's a couple of reasons for it," explains D'Amico, whose firm is an independent discretionary plan trustee. "No. 1

is that I think a lot of the costs are invisible to the decision makers. They're in the form of soft charges, or charges that are being assessed against things that are not easy to decipher—rather than, 'Here's a bill; pay it.'"

The retirement industry's adept marketing strategies also play a role in the problem, D'Amico adds.

"So when you get a nice-looking package, and it's presented by a well-branded organization, the presumption is 'How bad can it be?'" he says. "If one took the time to pay attention to the national statistics, it's actually quite frightening as to the failure of 401(k) plans to do all they're supposed to do for the employee."

D'Amico says the time has come for mandatory full disclosure of fees.

"The other thing I think that would help is if they allowed higher contribution levels," he says. "I think you could get successful owners more interested because, in fact, they would have more money at risk and might take a more personal interest in the thing."

James Genthner, founder and executive vice president of Epic Advisors Inc. in Rochester, agrees that change needs to come soon.

"Knowledge is power in the financial services industry," says Genthner, whose firm operates as a full-service plan provider,

including offering record-keeping and administrative services. "We need to level the playing field between the seller and the buyer (employers and participants) of retirement plan services.

"We can do this by arming the buyers with meaningful information regarding total plan costs.

He also says fees need to be transparent.

"Just as an example, it would help tremendously to express total cost in terms of a dollar amount because people can't relate to 80 basis points," Genthner says. "But they can relate to \$10,000."

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