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## WHAT'S INSIDE




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# The Economics of Providing 401(k) Plans: Services, Fees, and Expenses, 2013

## KEY FINDINGS

- **401(k) plan participants investing in mutual funds tend to hold lower-cost funds.** At year-end 2013, 401(k) plan assets totaled $4.2 trillion, with nearly 38 percent invested in equity mutual funds. In 2013, the average expense ratio for equity mutual funds offered in the United States was 1.37 percent. 401(k) plan participants who invested in equity mutual funds, however, paid an average of less than half that amount, 0.58 percent.

- **The expense ratios that 401(k) plan participants incur for investing in mutual funds have declined substantially since 2000.** In 2000, 401(k) plan participants incurred an average expense ratio of 0.77 percent for investing in equity funds. By 2013, that figure had fallen to 0.58 percent, a 25 percent decline. The expenses that 401(k) plan participants incurred for investing in hybrid and bond funds also fell from 2000 to 2013, by 19 percent and 21 percent, respectively.

- **The downward trend in the expense ratios that 401(k) plan participants incur for investing in mutual funds continued in 2013.** The average expense ratio that 401(k) plan participants incurred for investing in equity mutual funds fell from 0.63 percent in 2012 to 0.58 percent in 2013. The average expense ratio that 401(k) plan participants incurred for investing in hybrid funds fell from 0.60 percent in 2012 to 0.58 percent in 2013. And the average expense ratio that 401(k) plan participants incurred for investing in bond mutual funds fell from 0.50 percent in 2012 to 0.48 percent in 2013.

- **401(k) plans are a complex employee benefit to maintain and administer, and they are subject to an array of rules and regulations.** Employers offering 401(k) plans typically hire service providers to operate these plans, and these providers charge fees for their services.

- **Employers and employees generally share the costs of operating 401(k) plans.** As with any employee benefit, the employer typically determines how the costs will be shared.

## Why Employers Offer 401(k) Plans

During the past three decades, 401(k) plans have become a popular workplace benefit, valued for their role in providing employees a means to set aside a portion of their compensation on a tax-favored basis. Indeed, 401(k) plans have become the most common defined contribution (DC) plan, holding $4.2 trillion in assets at year-end 2013 (Figure 1).[1] Over the past two decades, mutual funds have become the primary vehicle for 401(k) plan investments, with the share of employer-sponsored 401(k) plan assets held in mutual funds jumping sevenfold—from 9 percent at year-end 1990 to 63 percent at year-end 2013.

Employers that offer 401(k) plans, an optional employee benefit, face conflicting economic pressures: the need to attract and retain qualified workers with competitive compensation packages, and the need to keep their products and services competitively priced. As a firm increases overall compensation to its employees, it increases its ability to hire and retain workers but also increases the costs of producing its products and services. To provide and maintain 401(k) plans, employers are required to retain a variety of administrative, participant-focused, regulatory, and compliance services. All these services involve costs; generally, the plan sponsor and the plan participants share these costs.

## Paying for 401(k) Plan Services

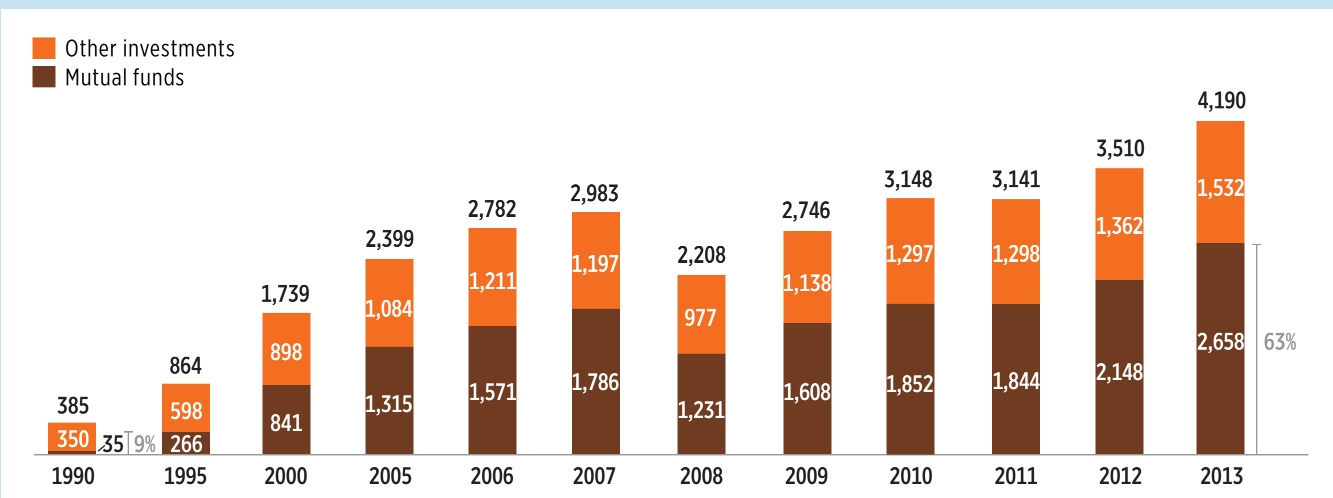
### 401(k) Plans Are Strictly Regulated

401(k) plans are complex to maintain and administer, and they are subject to an array of rules and regulations that govern their operation, including Section 401(k) of the Internal Revenue Code (IRC), the basis for their tax-favored treatment.[2] The Department of the Treasury and the Internal Revenue Service (IRS) enforce the tax code and impose numerous requirements that plans must satisfy to qualify for special tax treatment.[3] Further, the plans must meet many statutory and regulatory requirements under the Employee Retirement Income Security Act of 1974 (ERISA), enforced by the Department of Labor (DOL).

FIGURE 1

**401(k) Plan Assets**

*Billions of dollars, selected years*




Note: Components may not add to the total because of rounding.
Sources: Investment Company Institute, Federal Reserve Board, and U.S. Department of Labor

## 401(k) Plan Sponsors Provide a Variety of Services

When an employer offers a 401(k) plan to its employees, it selects an individual or group of individuals, known as plan fiduciaries,[4] to oversee the administration of the 401(k) plan for the exclusive benefit of plan participants, consistent with ERISA and the terms of the plan. The plan fiduciaries must arrange for the provision of the many services required to create and maintain a 401(k) plan.

*Administrative services* maintain the framework of a 401(k) plan and include recordkeeping functions, such as maintaining plan and participant records and creating and delivering participant account statements (Figure 2). DOL regulations generally require plans to allow participants to change their investment elections at least quarterly,[5] but most 401(k) plan participants are permitted to make daily transactions in their plans.[6] Administrative service providers process all participant transactions. In addition, plan fiduciaries must arrange for administrative services relating to setting up, converting, and terminating plans, as well as trustee services.[7]

*Participant-focused services* help employees fully achieve the benefits of their 401(k) plans. Plan sponsors provide a wide array of communications, educational resources, and advice services to help participants invest and plan for retirement (Figure 2).[8] Plan fiduciaries select a lineup of professionally managed investment options that typically covers a range of risk and return,[9] sometimes including a brokerage window through which participants may select securities not in the plan's lineup.[10] If a plan sponsor permits loans, the plan fiduciaries must arrange for loan processing services.[11] In addition, plans may opt to provide participants with access to annuity purchasing services at the time of retirement.

*Regulatory and compliance services* ensure that a plan fulfills legal requirements imposed by statute, DOL and IRS regulations, and other guidance (Figure 2). Plans are subject to complicated restrictions on contributions,[12] lengthy audited annual reports to the DOL,[13] and tax reporting to the IRS. Plans may have additional compliance burdens under federal securities or state laws.[14] Further, each investment option used in a plan has its own compliance requirements. For example, mutual funds must comply with the Investment Company Act of 1940 and other securities laws,[15] bank collective trusts with banking regulations, and group annuity contracts with state insurance rules.

## Plan Sponsors Must Ensure That Service Costs Are Reasonable

Federal law requires that plan sponsors "ensure that the services provided to their plan are necessary and the cost of those services is reasonable."[16] In February 2012, the DOL released regulations concerning the fee and compensation information that plan sponsors must collect—and that service providers must disclose—to ensure that a contract or arrangement for services is considered "reasonable" under ERISA.[17] With these regulations, which became effective in July 2012, the DOL aims to help ensure that plan sponsors can make informed decisions about plan services and their costs and to reveal any potential conflicts that a service provider might have.[18] Fees are only one factor that a plan sponsor must consider. Other factors include the extent and quality of service and the characteristics of the investment options chosen.[19]

The DOL also released a regulation in October 2010 that requires plans to give participants, when they become eligible for the plan and annually thereafter, key information about the plan's investments and fees.[20] The DOL's goal here is to ensure that 401(k) participants have the information they need to make plan-related decisions, such as whether to participate and how to allocate the assets in their accounts among the investments available.

## Plan Sponsors Select Service Providers and Investment Arrangements

Plan sponsors select the service providers for their 401(k) plans and choose the investment options offered in them.[21] The costs of running a 401(k) plan generally are shared by the plan sponsor and participants, and the arrangements vary across plans. The fees may be assessed at a plan level,

FIGURE 2

### Services Provided to 401(k) Plans

| |
|---|
| **Administrative services** |
| ***Recordkeeping***, including maintaining plan records; processing employee enrollment; processing participants' investment elections, contributions, and distributions; and issuing account statements to participants |
| ***Transaction processing***, including purchases and sales of participants' assets |
| ***Plan creation/conversion/termination***, including associated administrative services |
| ***Trustee services***, providing the safe holding of the plan's assets in a trust, as required by ERISA |
| **Participant-focused services** |
| ***Participant communication***, including employee meetings, call centers, voice-response systems, web access, and preparation of summary plan description and other participant materials |
| ***Participant education and advice***, including online calculators and face-to-face investment advice |
| ***Investment management***, typically offered through a variety of professionally managed investment options |
| ***Brokerage window***, if offered, allowing direct purchase of individual securities by plan participants |
| ***Maintenance of an employer stock fund***, if offered, to facilitate the purchase of employer securities within the plan |
| ***Loan processing***, if a loan feature is offered |
| ***Insurance and annuity services***, if offered, including offering annuities as distribution options |
| **Regulatory and compliance services** |
| ***Plan document services***, including off-the-rack "prototype" plans |
| ***Consulting***, including assistance in selecting the investments offered to participants |
| ***Accounting and audit services***, including preparation of annual report (Form 5500) |
| ***Legal advice***, including advice regarding interpretation of plan terms, compliance with legal requirements, plan amendments, and resolution of benefit claims |
| ***Plan testing***, to comply with Internal Revenue Code nondiscrimination rules |
| ***Processing of domestic relations orders***, ensuring that the split of accounts pursuant to divorce orders complies with ERISA |

Sources: Investment Company Institute, U.S. Department of Labor, and Internal Revenue Service a participant-account level, as a percentage of assets, or as a combination of arrangements.

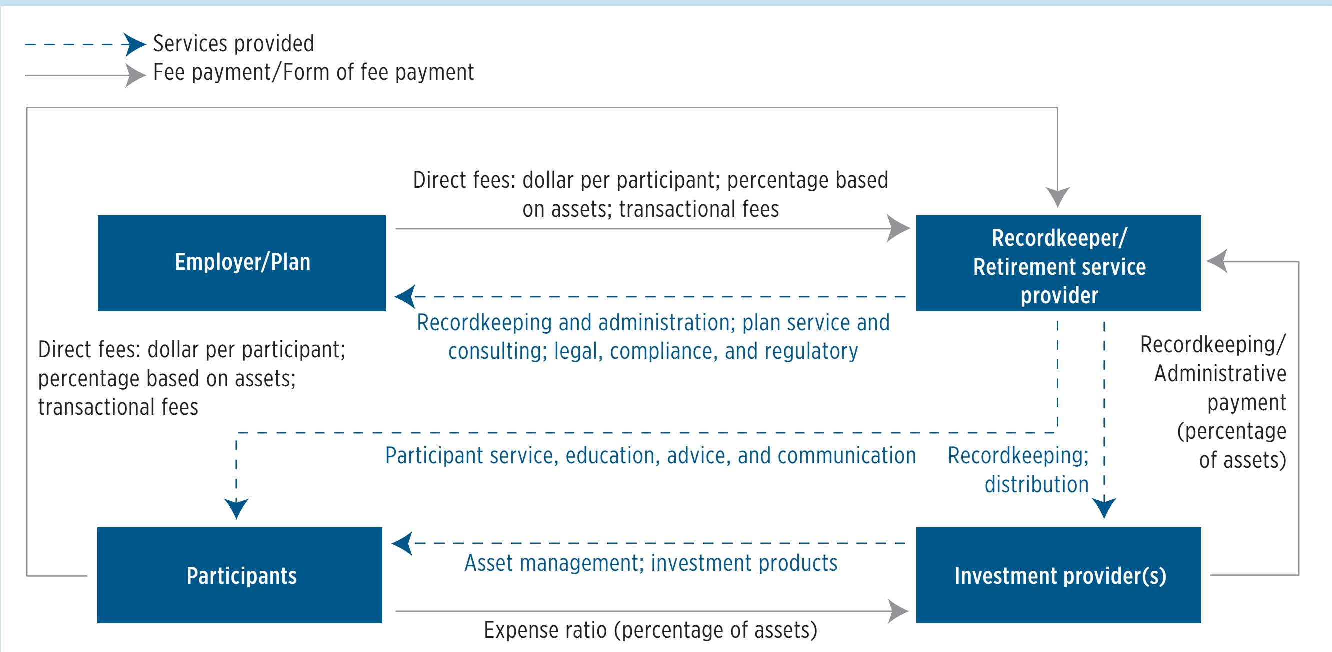
Figure 3 shows possible fee and service arrangements in 401(k) plans. The boxes on the left highlight employers, plans, and participants, which use services in 401(k) plans. The boxes on the right highlight recordkeepers, other retirement service providers, and investment providers that deliver investment products, investment management services, or both.

The dashed arrows illustrate the services provided. For example, the investment provider offers investment products and asset management to participants, while the recordkeeper provides services to the plan and the participants. The solid arrows illustrate the payment of fees for products and services. Participants—or the plan or employer—may pay directly for recordkeeping services. Participants may pay indirectly for recordkeeping services through fund expenses reflected in investment expense ratios (solid arrow from participants to investment providers) if the investment provider covers some recordkeeping/administrative expenses by paying the recordkeeper (solid arrow at the far right) for recordkeeping services (dashed arrow between recordkeeper and investment provider).

The DOL requires that the plan sponsor pay the costs associated with the initial design of the plan, as well as any design changes.[22] Beyond these design services, employers can share the costs of the plan services with their employees. However, many employers choose to cover some or all plan-related costs that legally could be shouldered by the plan participants. Any costs not paid by the employer, which may include administrative, investment, legal, and compliance costs, effectively are paid by plan participants.[23]

FIGURE 3

**A Variety of Arrangements May Be Used to Compensate 401(k) Service Providers**




Note: In selecting the service provider(s) and deciding the cost-sharing for the 401(k) plan, the employer/plan sponsor will determine which combinations of these fee arrangements will be used in the plan.

## A Means to Compare: The "All-In" 401(k) Plan Fee

As Figure 3 shows, 401(k) plan fees can be assessed per plan, per participant, or per dollar invested (asset-based fees). In addition, the fees may be paid by the plan sponsor (the employer), the plan participants (employees), or the plan itself. To compare fees across plans, this array of fee arrangements must be converted into an "all-in" fee—a single number for each plan constructed as a percentage of plan assets. An all-in fee is necessary to determine the key factors that influence plan fees.

Because fees are affected by many factors, a range of fees is found across 401(k) plans. For example, a Deloitte/ICI survey in late 2011 (see page 7) found that plan size was a key driver of the all-in fee.[24] Plans with more participants and larger average account balances tended to have lower all-in fees than plans with fewer participants and smaller average account balances. This effect likely resulted in part from fixed costs required to start up and run the plan, much of which are driven by legal and regulatory requirements. It appears that economies of scale are gained as a plan grows because these fixed costs can be spread across more participants, a larger asset base, or both. In addition, plans with lower allocations to equity investments tended to have lower fees than plans with higher equity allocations, reflecting the fact that fixed-income investments generally have lower expense ratios than equity investments.

## Looking at Fees and Expenses of Mutual Funds Held in 401(k) Accounts

Virtually all participant-directed 401(k) plans offer a variety of pooled investment options (such as a selection of mutual funds, collective trusts, and/or separately managed accounts), and some also include guaranteed investment contracts (GICs),[25] company stock,[26] or a brokerage window that gives participants access to direct investment in stocks, bonds, and other securities.[27] All told, 63 percent of the $4.2 trillion in 401(k) plan assets at year-end 2013 was invested in mutual funds (Figure 4).[28] Mutual funds are required by law to disclose their fees and expenses, and ICI studies trends in those fees and expenses.[29] In addition, ICI separately tracks 401(k) plan account holdings of mutual funds.[30] This report combines the results of these analyses in order to examine the fees and expenses that investors incur on mutual funds held in 401(k) accounts.[31] This analysis finds that:

» 401(k) plan participants tend to be invested in lower-cost mutual funds.

» At year-end 2013, 86 percent of mutual fund assets in 401(k) plans were held in no-load funds, while 14 percent were held in load funds, predominantly in fund share classes that do not charge retirement plan participants a front-end load.

### *The Deloitte/ICI Defined Contribution Plan/401(k) Fee Study*

As part of an ongoing comprehensive research program, ICI engaged Deloitte to survey DC plan sponsors on fee structures in the DC plan market. In late 2011, Deloitte conducted a web-based survey of DC plan sponsors to update a similar effort in 2009. Survey results for 2013 are being processed and will be released in late summer 2014. The research addressed:

- the mechanics of plan fee structures;
- components of plan fees; and
- primary and secondary factors that affect fees ("fee drivers").

Due to the variety of fee and service structures in the DC/401(k) market, the study created an analytical tool, the "all-in" fee. The all-in fee incorporates all administrative, recordkeeping, and investment fees, whether assessed at a plan level, a participant-account level, or as an asset-based fee, across all parties providing services to the plan—whether they are paid by the employer, the plan, or the participants. The all-in fee excludes fees that apply only to participants engaged in a particular activity (e.g., loan fees). In addition, the all-in fee does not evaluate the quality of the products and services provided.

The survey gathers detailed information on plan characteristics, design, demographics, products, services, and their associated fees. While the survey is not intended to be a statistical representation of the DC/401(k) marketplace, the demographics of the plans participating in the survey appear to be similar to those in the broader DC plan market (in average account balance, number of investment options, average participant contribution rate, asset allocation, and plan design). Because the distribution of plans in the sample differs from the distribution of all 401(k) plans, to estimate industrywide fees, the survey responses had to be weighted by plan size to align with the universe of 401(k) plans reported by the DOL.

The 2011 survey results are reported in *Inside the Structure of Defined Contribution/401(k) Plan Fees: A Study Assessing the Mechanics of the "All-In" Fee*, available at www.ici.org/pdf/rpt_11_dc_401k _fee_ study.pdf.

## Investors Pay Two Types of Mutual Fund Fees and Expenses

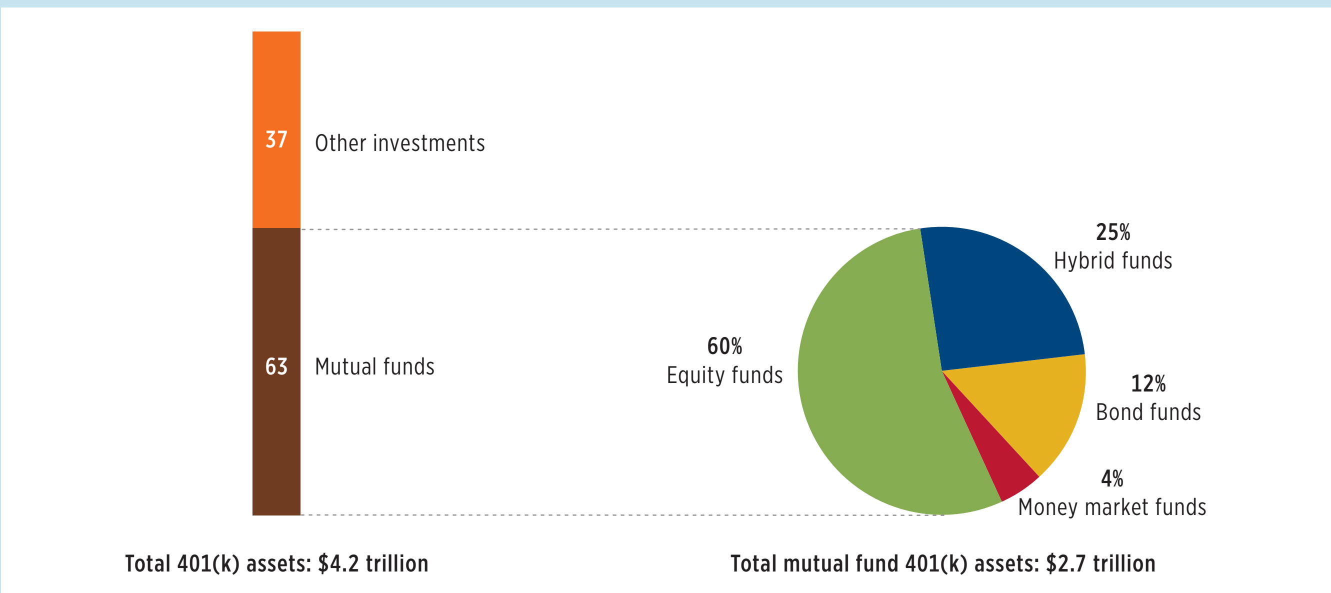
Investors in mutual funds can incur two primary types of fees and expenses when purchasing and holding mutual fund shares: sales loads and mutual fund expenses. Sales loads are one-time fees paid either at the time of purchase (front-end loads) or when shares held for less than a specified number of years are redeemed (back-end loads, also known as contingent deferred sales loads, or CDSLs). Mutual fund expenses include ongoing charges for portfolio management, fund administration, and shareholder services, as well as fund distribution charges (known as 12b-1 fees).[32]

Sales loads often are waived for mutual funds purchased through 401(k) plans, but 401(k) investors do incur the fund expenses of the mutual funds in their 401(k) accounts. Ongoing expenses are paid from fund assets, so investors pay these expenses indirectly. The total expense ratio, which reflects both the operating expense ratio—including portfolio management, fund administration and compliance, shareholder services, and other miscellaneous costs—and 12b-1 fees, is measured in this report as an asset-weighted average. Using the asset-weighted average to measure costs provides an aggregate estimate of what 401(k) participants actually pay to invest in mutual funds through their 401(k) plans. Mutual funds with larger shares of assets in 401(k) plans contribute proportionately more to the asset-weighted average than do less widely held funds.

FIGURE 4

**Nearly Two-Thirds of 401(k) Plan Assets Are Invested in Mutual Funds**

*Percentage of assets, 2013*




Note: Percentages may not add to 100 percent because of rounding.

Sources: Investment Company Institute, Federal Reserve Board, and U.S. Department of Labor

### *Understanding Fund and Share Class Categories*

Many mutual funds offer several different share classes, all of which invest in the same portfolio (fund) while offering different services tailored to the needs of different investors or, in the case of 401(k) plans, the group of participants in the plan. The combination of sales loads and 12b-1 fees that an individual investor might pay depends on the share class.

ICI categorizes funds or fund share classes as either *load funds* or *no-load funds*. Load funds have a commission or sales load and can be further classified as either *front-end load, back-end load, level load,* or *other load*. Front-end load funds carry an up-front sales charge and may have a 12b-1 fee, typically between 0.25 percent and 0.35 percent of the fund's net assets. Back-end load funds and other load funds are offered for sale at net asset value without a front-end load, but use combinations of 12b-1 fees and CDSLs. Level load funds typically have an annual 12b-1 fee of 1.0 percent to compensate financial professionals for assisting investors. The figures on load funds in this paper include load funds that waive sales loads for retirement plan investors (see Figure 5, as well as Figures A2 and A3 in the appendix).

No-load funds have no sales loads and have 12b-1 fees of 0.25 percent or less. The no-load funds are further classified as either *institutional* or *retail*. The figures in this paper classify a no-load fund as institutional if the fund's prospectus states that the fund or share class is designed to be sold primarily to institutional investors or institutional accounts. This classification includes investments by individuals in 401(k) accounts that are purchased by or through an institution such as an employer, trustee, or fiduciary on behalf of its employees, owners, or clients. The figures label the remaining no-load funds as retail (which includes no-load funds that are designed for the retirement plan market).

Similar designations have long been used in the mutual fund industry. But as the industry has evolved, their original connotations have become less meaningful, including when applied to 401(k) plans. Participant-directed 401(k) plans have characteristics associated with both retail investors (because plans often have many individual accounts that must be maintained and investors that must be served) and institutional investors (when the plan brings larger total investments). Nevertheless, these definitions are useful for research purposes such as illustrating trends in 401(k) plan assets held in mutual funds—for example, highlighting the fact that 401(k) plans may purchase shares through a range of funds and share classes.

## Trends in Funds and Share Classes Used in 401(k) Plans

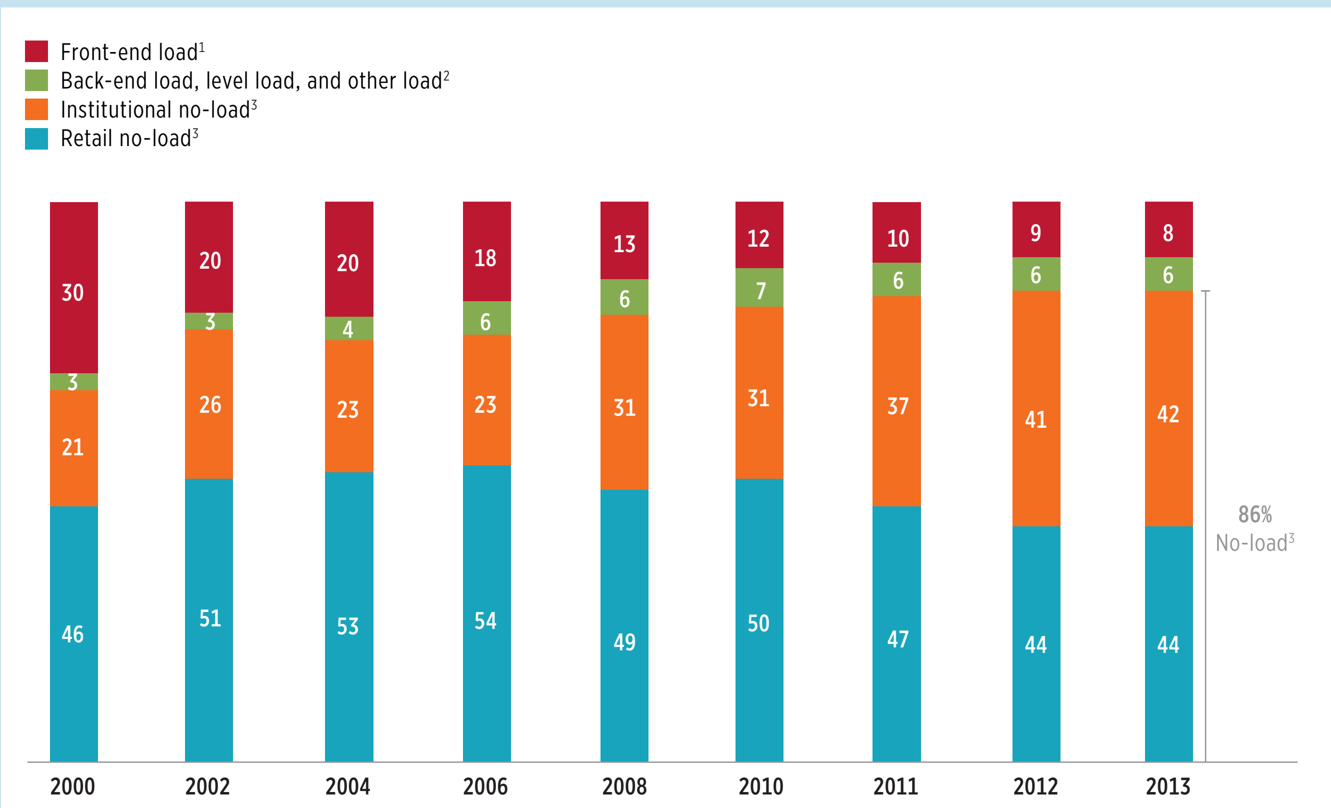
*No-load funds*. Altogether, 86 percent of 401(k) plan mutual fund assets were invested in no-load funds at year-end 2013, about evenly split between retail and institutional no-load funds (Figure 5).[33] Retail no-load funds held 44 percent of total 401(k) mutual fund assets, and institutional no-load funds held 42 percent. Over the past decade, institutional no-load funds have grown as a share of 401(k) mutual fund assets, while the shares of retail no-load funds and load funds have fallen.

*Load funds*. Load funds accounted for the other 14 percent of 401(k) mutual fund assets at year-end 2013 (Figure 5). Eight percent of 401(k) mutual fund investments were held through front-end load shares. Most funds waive front-end loads for retirement plans, so 401(k) plan participants generally are not charged a front-end load on shares purchased through their plans.[34] The remaining 6 percent of 401(k) mutual fund assets were invested in back-end load[35] share classes, level load[36] share classes, and other load share classes.[37]

FIGURE 5

### 401(k) Mutual Fund Assets by Share Class

*Percentage of assets, selected years*




[1] Front-end load > 1 percent. Primarily includes Class A shares; includes assets where front-end loads are waived.

[2] See Figure A2 in the appendix for more detail.

[3] No-load shares have front-end load = 0 percent, contingent deferred sales load = 0 percent, and 12b-1 fee ≤ 0.25 percent.

Note: Data exclude mutual funds available as investment choices in variable annuities and tax-exempt mutual funds. Components may not add to 100 percent because of rounding.

Sources: Investment Company Institute and Lipper

## 401(k) Participants Hold Lower-Cost Mutual Funds

*Equity funds.* Sixty percent of 401(k) plan assets invested in mutual funds were invested in equity funds at year-end 2013 (Figure 4).[38] Consistent with the general industry trend, average equity fund expense ratios incurred by 401(k) investors declined for the fourth straight year in 2013, falling to 0.58 percent (Figure 6).[39] In 2013, 401(k) investors continued to concentrate their equity fund assets in lower-cost funds. Indeed, the 0.58 percent asset-weighted average was less than half the 1.37 percent simple average for all equity funds—and lower than the industrywide asset-weighted average of 0.74 percent. 401(k) mutual fund investors incur lower average expense ratios not only for equity funds overall but also when disaggregated into domestic and world equity funds (Figure 7).

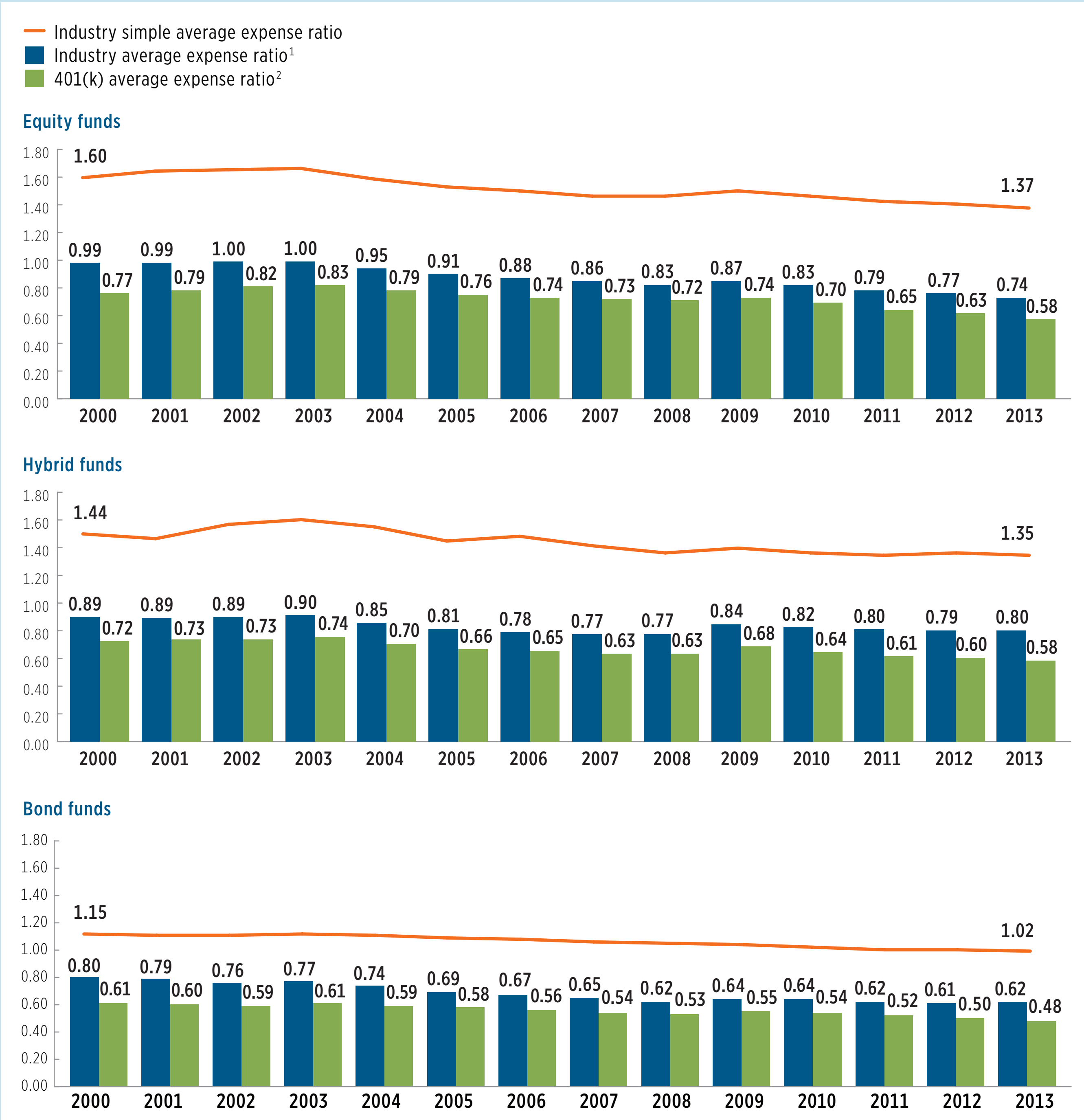
Several factors contribute to the relatively low average expense ratios incurred by 401(k) plan participants investing in mutual funds. Both inside and outside the 401(k) plan market, mutual funds compete among themselves and with other financial products to offer shareholders service and performance.[40] In addition, shareholders are sensitive to the fees and expenses that funds charge.[41] Indeed, new sales and assets tend to be concentrated in lower-cost funds, providing a market incentive for funds to offer their services at competitive prices.[42] In the 401(k) plan market, performance- and cost-conscious plan sponsors also impose market discipline. Plan sponsors regularly evaluate the performance of the plans' investments,[43] and performance reflects fees. In 2012, 47 percent of plan sponsors indicated that they had replaced a fund in the last year because of poor performance.[44]

The lower average expense ratios incurred by 401(k) participants also reflect other factors. Some plan sponsors choose to cover a portion of 401(k) plan costs, which allows them to select funds or share classes with lower built-in servicing costs. Further, many 401(k) plans have large average account balances, and economies of scale help reduce the fees and expenses of the funds offered in these plans.[45] Finally, unlike outside 401(k) plans, where shareholders typically pay for the assistance of a financial adviser when investing in mutual funds,[46] there is a more limited role for financial adviser services inside these plans.

FIGURE 6

## 401(k) Mutual Fund Investors Tend to Pay Lower-Than-Average Expenses

*Percent, 2000–2013*




[1] The industry average expense ratio is measured as an asset-weighted average.

[2] The 401(k) average expense ratio is measured as a 401(k) asset-weighted average.

Note: Data exclude mutual funds available as investment choices in variable annuities and tax-exempt mutual funds.

Sources: Investment Company Institute and Lipper

FIGURE 7

### Average Total Mutual Fund Expense Ratios

*Percent, 2011–2013*

| | 2011 | | 2012 | | 2013 | |
|---|---|---|---|---|---|---|
| | Industry[1] | 401(k)[2] | Industry[1] | 401(k)[2] | Industry[1] | 401(k)[2] |
| **Equity funds** | **0.79** | **0.65** | **0.77** | **0.63** | **0.74** | **0.58** |
| Domestic | 0.73 | 0.61 | 0.71 | 0.58 | 0.68 | 0.54 |
| World | 0.95 | 0.80 | 0.93 | 0.77 | 0.90 | 0.72 |
| **Hybrid funds** | **0.80** | **0.61** | **0.79** | **0.60** | **0.80** | **0.58** |
| **Bond funds** | **0.62** | **0.52** | **0.61** | **0.50** | **0.62** | **0.48** |
| High-yield and world | 0.86 | 0.82 | 0.85 | 0.81 | 0.83 | 0.78 |
| Other | 0.55 | 0.49 | 0.54 | 0.47 | 0.53 | 0.45 |
| **Money market funds** | **0.20** | **0.22** | **0.17** | **0.20** | **0.17** | **0.19** |

[1] The industry average expense ratio is measured as an asset-weighted average.

[2] The 401(k) average expense ratio is measured as a 401(k) asset-weighted average.

Note: Data exclude mutual funds available as investment choices in variable annuities and tax-exempt mutual funds.

Sources: Investment Company Institute and Lipper

Expense ratios vary among the mutual funds that 401(k) participants hold. At year-end 2013, 85 percent of 401(k) plan equity fund assets were invested in mutual funds with expense ratios of less than 1.00 percent, with 38 percent invested in mutual funds with expense ratios of less than 0.50 percent (Figure 8).[47]

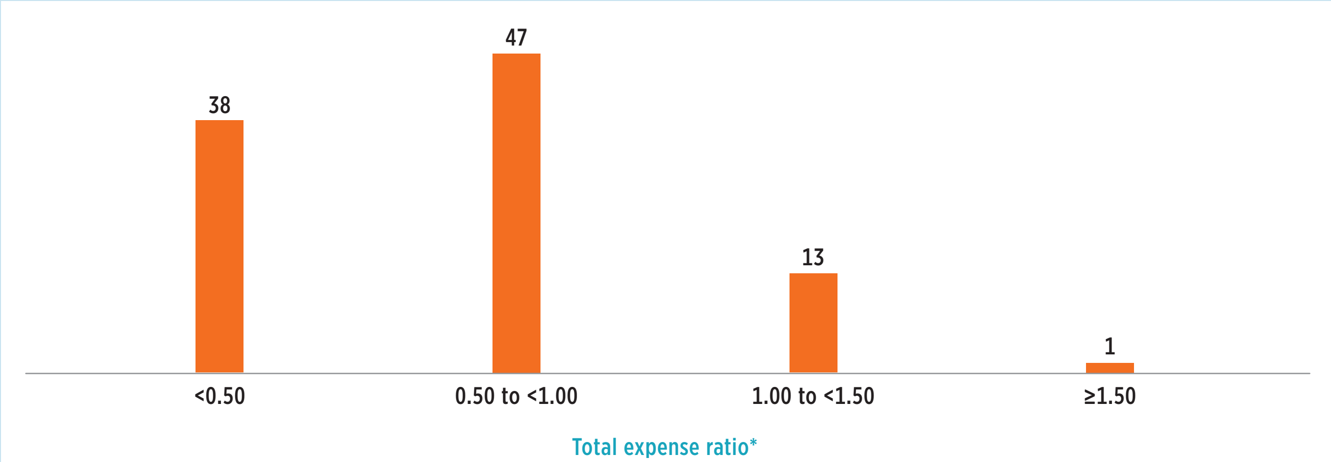
*Hybrid funds*. Twenty-five percent of 401(k) mutual fund assets were invested in hybrid funds, which invest in a mix of equities and bonds, at year-end 2013 (Figure 4). At year-end 2013, 401(k) hybrid fund investors paid an asset-weighted average expense ratio of 0.58 percent, less than half the industrywide simple average (1.35 percent) and more than 25 percent less than the industrywide asset-weighted average of 0.80 percent (Figure 6).[48]

*Bond funds*. Twelve percent of 401(k) mutual fund assets were invested in bond funds at year-end 2013 (Figure 4). The asset-weighted average expense ratio paid by 401(k) investors on bond funds fell slightly in 2013 (Figure 6). As with investors in equity funds and hybrid funds, 401(k) bond fund investors have concentrated their assets in lower-cost bond funds. At year-end 2013, 401(k) bond fund investors paid an asset-weighted average expense ratio of 0.48 percent, about half the industrywide simple average (1.02 percent) and 23 percent less than the industrywide asset-weighted average of 0.62 percent. As with investors in equity funds, the average expense ratio paid by 401(k) investors in bond funds also is lower when disaggregated into domestic and world bond funds (Figure 7).[49]

FIGURE 8

**401(k) Equity Mutual Fund Assets Are Concentrated in Lower-Cost Funds**

*Percentage of 401(k) equity mutual fund assets, 2013*




*The total expense ratio includes fund operating expenses and the 12b-1 fee.

Note: Data exclude mutual funds available as investment choices in variable annuities. Components do not add to 100 percent because of rounding.

Sources: Investment Company Institute and Lipper

*Money market funds*. Only 4 percent of 401(k) mutual fund assets were invested in money market funds at year-end 2013 (Figure 4), and 401(k) participants holding money market funds had an asset-weighted average expense ratio of 0.19 percent in 2013, down from 0.20 percent in 2012 (Figure 7). The decline in money market fund fees over the past few years has been due in large part to investment advisers waiving advisory fees in the current low interest rate environment.[50]

In addition to the impact of the range and quality of services provided, many factors affect the all-in fees of 401(k) plans. Further, as with any other employee benefit, the costs associated with 401(k) plans are typically shared between the employer and plan participants.

Participants who work for employers that do not heavily subsidize their plans will incur higher fees on average. Plans that charge account-level fees will tend to have lower-cost investment options than plans without direct account-level charges. Because of the relatively fixed costs that all plans incur, participants in plans with a small amount of assets tend to pay higher fees per dollar invested than plans with a larger amount. Participants in plans that have many small accounts typically pay higher fees per dollar invested than plans with larger accounts. Plans with more service features tend to be more costly than plans with fewer service features.

All of these factors affect the costs of the plan and the plan's investment options. They must all be considered when evaluating the reasonableness of a plan's costs.

## Other Costs Incurred by Mutual Fund Investors

Mutual funds also incur costs when buying and selling securities. These costs are not included in the fund's total expense ratio but are reflected in the calculation of net return to the investor. To help shareholders evaluate the trading activity of a mutual fund, the Securities and Exchange Commission (SEC) requires each mutual fund to report its "turnover rate" in its annual shareholder report and its prospectus.[51]

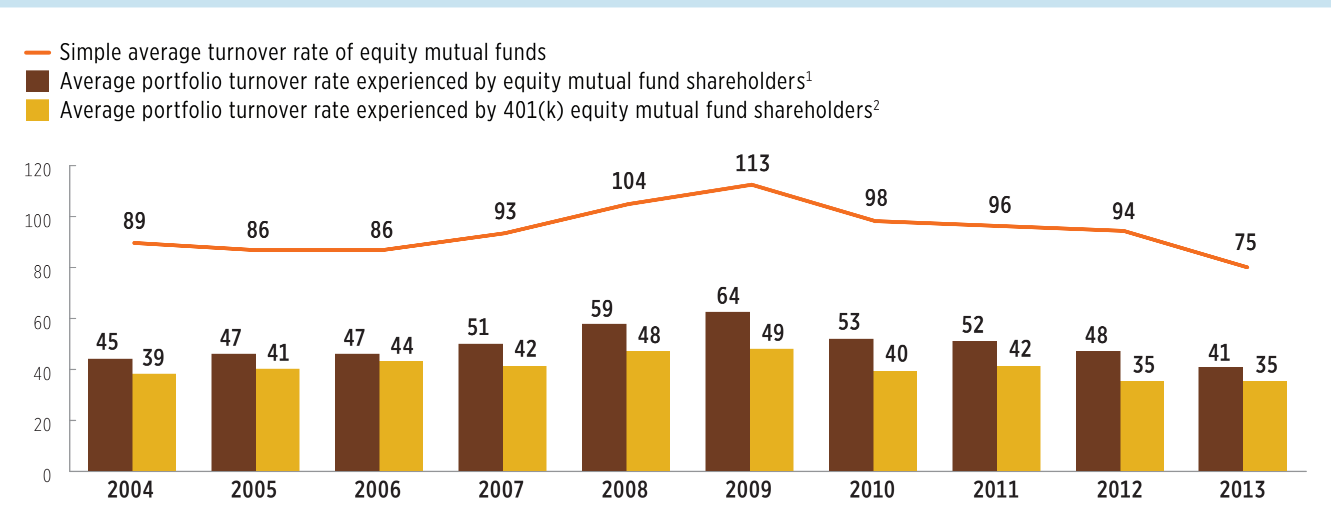
Broadly speaking, the turnover rate is a measure of how rapidly a fund is trading the securities in its portfolio relative to total fund assets.[52] All pooled investments incur trading costs while managing their portfolios.

*Equity fund turnover rates*. Participants in 401(k) plans tend to own equity funds with lower-than-average turnover rates. The industrywide simple average turnover rate in equity funds was 75 percent in 2013 (Figure 9).[53] However, mutual fund shareholders tend to invest in equity funds with much lower turnover rates, as reflected in the lower industrywide asset-weighted average turnover rate of 41 percent. The average turnover rate for equity funds selected by 401(k) plan participants in 2013 was lower still: 35 percent on an asset-weighted basis.

FIGURE 9

### Average Portfolio Turnover Rates for Equity Mutual Funds

*Percentage of assets, 2004–2013*




[1] Average portfolio turnover rate experienced by equity mutual fund shareholders is measured as an asset-weighted average (reported as a percentage of fund assets).

[2] Average portfolio turnover rate experienced by 401(k) equity mutual fund shareholders is measured as a 401(k) asset-weighted average (reported as a percentage of 401(k) fund assets).

Note: The turnover rate is the lesser of a fund's purchases or sales of portfolio securities for a reporting period divided by the monthly average value of the portfolio securities owned by the fund during the reporting period. Data exclude mutual funds available as investment choices in variable annuities.

Sources: Investment Company Institute and Strategic Insight Simfund

## Conclusion

401(k) plans are now the most common private-sector employer-sponsored retirement plan in the United States, holding $4.2 trillion in assets at year-end 2013. Employers choose whether to offer these plans to employees as part of their total compensation packages; if a plan is offered, employees choose whether to participate. Creating and maintaining a 401(k) plan both involve a variety of services, and the costs of these services are generally shared by the plan sponsor and the plan participants.

401(k) plans provide many American workers with the opportunity for cost-effective investment in mutual funds. Plan participants invest primarily in equity funds, and the bulk of these equity fund assets is held in lower-cost mutual funds with lower-than-average portfolio turnover.

Numerous factors contribute to the relatively low expense ratios incurred by 401(k) plan participants investing in mutual funds. Among them are: (1) competition among mutual funds and other investment products to offer shareholders service and performance; (2) plan sponsor decisions to cover a portion of 401(k) plan costs, which allow them to select lower-cost funds or share classes; (3) economies of scale, which large investors such as 401(k) plans can achieve; (4) cost- and performance-conscious decisionmaking by plan sponsors and plan participants; and (5) the limited role of professional financial advisers in these plans.

### *Additional Reading*

- **"Trends in the Expenses and Fees of Mutual Funds, 2013."** *ICI Research Perspective.* Available at www.ici.org/pdf/per20-02.pdf.
- ***Inside the Structure of Defined Contribution/401(k) Plan Fees.*** Deloitte Consulting LLP and Investment Company Institute. Available at www.ici.org/pdf/rpt_11_dc_401k_fee_study.pdf.
- **"The U.S. Retirement Market, First Quarter 2014."** Investment Company Institute. Available at www.ici.org/info/ret_14_q1_data.xls.
- **ICI Resources on 401(k) Plans.** Investment Company Institute. Available at www.ici.org/401k.
- **ICI Resources on 12b-1 Fees.** Investment Company Institute. Available at www.ici.org/rule12b1fees.

## Notes

1 See Investment Company Institute 2014b.

2 Congress added Section 401(k) of the IRC in 1978, to become effective in 1980 (see Revenue Act of 1978, P.L. 95-600). However, companies generally did not begin to adopt 401(k) plans until the Department of the Treasury and the IRS issued proposed regulations clarifying the scope of Section 401(k) on November 10, 1981 (see 46 Fed. Reg. 55544, November 10, 1981; Holden, Brady, and Hadley 2006).

3 The main advantages of a tax-qualified 401(k) plan are that employers can take an immediate deduction for their contributions, employees can defer taxation of contributions, and employees do not pay income tax on contributions or earnings until the monies are distributed. (For a detailed explanation of the tax benefits of deferral, see Brady 2012.) In exchange for this special tax treatment, the IRC imposes numerous conditions, many of them designed to ensure that participants in all income ranges attain the benefits of the plan. For further discussion, see, for example, Allen et al. 1997. Since 2006, employers have been able to offer a Roth 401(k) option, which, like a Roth IRA, allows employees to contribute on an after-tax basis but receive distributions tax-free. Also like a Roth IRA, earnings are subject to income tax if the employee distributes them within five years of the first contribution to the Roth 401(k) or before reaching age 59½.

4 ERISA requires that the plan sponsor appoint a "named" fiduciary or fiduciaries to administer the plan. See ERISA Section 402. A plan sponsor may, and often does, name itself as the plan administrator. In its role as plan administrator, the employer assumes fiduciary responsibility to select and monitor service providers and investment options for the plan. Most employers appoint a retirement committee consisting of senior human resource or other employees to oversee the administration of the plan. In their role acting for the employer as plan administrator, the members of the committee assume fiduciary responsibility to administer the plan solely in the interest of plan participants and beneficiaries. For convenience, this report often refers to "employer" and "plan sponsor" to mean the fiduciary or fiduciaries appointed to administer the plan.

5 Department of Labor Reg. Section 2550.404c-1. For an explanation of this regulation, see note 9.

6 Plan Sponsor Council of America 2013 reports that 96.1 percent of the 686 profit-sharing and 401(k) plans in its survey allow participants to initiate daily fund transfers.

7 To protect 401(k) plan assets, ERISA Section 403 requires that pension plan assets be held in a trust or invested in insurance contracts.

8 Plan sponsors use an array of educational resources, including enrollment kits, newsletters, fund performance sheets, intranet sites, webinars, seminars, workshops, paycheck stuffers, retirement gap calculators, posters, and individually targeted communication (see Plan Sponsor Council of America 2013). The most commonly cited primary purpose for plan education is increasing participation (33.0 percent of plans).

9 Where participants are given control of the investments in their accounts, which is common in 401(k) plans, the selection of investment options available is usually designed to meet the requirements of ERISA Section 404(c). This section provides liability relief for plan sponsors and other plan fiduciaries from losses resulting from employees' exercise of investment control. The DOL regulations under ERISA Section 404(c) are designed to ensure that participants have control over their assets and have adequate opportunity to diversify their holdings. Plans must offer at least three diversified investment options with materially different risk and return characteristics. (Although 401(k) plans can offer company stock or any individual stock, neither would qualify as one of the three core options.) Plans generally must allow transfers among the diversified investment options at least quarterly. Hewitt Associates 2007 reports that 90 percent of the 292 plans it surveyed in spring 2007 considered themselves compliant with ERISA Section 404(c). Aon Hewitt 2013 reports that 401(k) plans had an average of 20 investment options in 2012; Plan Sponsor Council of America 2013 reports that 401(k) plans had an average of 19 investment options available for participant contributions in 2012. Deloitte Consulting LLP, the International Foundation of Employee Benefit Plans, and the International Society of Certified Employee Benefit Specialists 2013 reports that the nearly 400 401(k) plan sponsors surveyed had an average of 19 investment options in 2012.

10 Plan Sponsor Council of America 2013 reports that 17.1 percent of plans in its survey offered a self-directed brokerage window and that 5.6 percent offered a self-directed mutual fund window. These windows hold a very small amount of assets: 1.1 percent of plan assets were invested through the brokerage window, and 0.2 percent were invested through the mutual fund window. The Vanguard Group 2014 similarly reports limited use of brokerage windows: in 2013, 13 percent of defined contribution plans recordkept by Vanguard offered brokerage windows, covering 25 percent of participants. In plans offering a self-directed brokerage window, only 1 percent of those plan participants used it, and about 1 percent of those plan assets were invested through the window.

[11] The EBRI/ICI 401(k) database indicates that 59 percent of plans offered a loan feature at year-end 2012, covering 87 percent of 401(k) plan participants. Also at year-end 2012, 18 percent of 401(k) plan participants had loans outstanding. See Holden et al. 2013.

[12] The IRC includes a number of flat annual dollar contribution limits. In addition, several sections of the IRC provide a framework for nondiscrimination testing, which limits contributions to 401(k) plans to ensure that employees in all income ranges benefit from the plan. For example, the actual deferral percentage (ADP) nondiscrimination test essentially requires that the before-tax contributions of highly compensated employees (as a percentage of their eligible compensation) do not exceed those of non–highly compensated employees (as a percentage of their eligible compensation) by more than a specified amount.

[13] Plans file their annual reports on Form 5500, a form issued jointly by the DOL, the IRS, and the Pension Benefit Guaranty Corporation (PBGC). The DOL publishes summary annual reports tabulating the Form 5500 data (see U.S. Department of Labor, Employee Benefits Security Administration 2013a and 2013b).

[14] For example, plans can incur costs responding to requests for information pursuant to SEC Rule 22c-2, under which mutual funds may obtain trading information necessary to ensure compliance with the fund's short-term trading policies. In addition, 401(k) plans that allow participants to invest in the employer's stock must register with the SEC on Form S-8. ERISA preempts most state laws that relate to employee benefit plans, but plans might still need to comply with state tax laws relating to withholding and information filing. The Consumer Financial Protection Bureau, created by the Wall Street Reform and Consumer Protection Act of 2010, potentially has the ability to regulate service providers to 401(k) plans, but only with respect to specific regulatory areas approved by the DOL and the Department of the Treasury.

[15] For discussion of regulations governing mutual funds, see Investment Company Institute 2014a.

[16] See U.S. Department of the Treasury and U.S. Department of Labor 2012. See also U.S. Department of Labor, Employee Benefits Security Administration, "A Look at 401(k) Plan Fees," "Understanding Retirement Plan Fees and Expenses," "Selecting and Monitoring Pension Consultants—Tips for Plan Fiduciaries," and "Tips for Selecting and Monitoring Service Providers for Your Employee Benefit Plan." Some commentators, however, have argued that the core standard under ERISA that governs plan fiduciaries—the duty of prudence—requires that fiduciaries engage in a prudent process in evaluating a plan's investments and services and does not require a particular result. See Vine 2010.

[17] See 77 Fed. Reg. 5632 (February 3, 2012).

[18] See U.S. Department of the Treasury and U.S. Department of Labor 2012.

[19] See U.S. Department of Labor, Employee Benefits Security Administration, "Understanding Retirement Plan Fees and Expenses" and "A Look at 401(k) Plan Fees." See also U.S. Securities and Exchange Commission, "Calculating Mutual Fund Fees and Expenses" and "Mutual Fund Fees and Expenses."

[20] See 75 Fed. Reg. 64910 (October 20, 2010). Under this regulation, participants must receive general plan information and investment-related information before making an initial investment decision, and annually thereafter. This includes information on how to give investment instructions and on what, if any, account fees or fees for individual services (e.g., loans, investment advice) participants pay. The regulation requires that participants be given a chart comparing each investment in the plan's investment lineup: the investment's name and type; sales charges and any restrictions on withdrawal; the expense ratio; the annual dollar cost of the expense ratio for each $1,000 invested (assuming no returns); 1-, 5-, and 10-year performance; and performance of a benchmark index over the same periods. Participants are referred to a website for more information on the investment's objectives, principal strategies and risks, portfolio turnover rate, and quarterly performance data. Although there are some differences, the information required under this regulation is similar to the information that mutual fund investors receive as part of a fund's prospectus. The initial disclosures under this regulation were due, in most cases, 60 days after the July 1, 2012, effective date for the service provider disclosure regulation, or August 30, 2012. The DOL provides information to help employees learn about fees associated with their 401(k) plans. See U.S. Department of Labor, Employee Benefits Security Administration, "A Look at 401(k) Plan Fees." The SEC also provides investor education at www.sec.gov/investor.shtml.

[21] Plan sponsors use a variety of arrangements to obtain services for their 401(k) plans. When multiple service providers are used (an "unbundled" arrangement), the expenses of each provider (e.g., trustee, recordkeeper, communications firm, investment manager) are charged separately to the plan. When one provider is used to perform a number of services (a "bundled" arrangement), the single provider interacts with the plan and then pays for the other bundled services out of the fees it collects from the plan. Some plans use a combination of these approaches—for example, by selecting a single provider for administrative participant services and one or more providers for investment options. In this case, the costs of administering the plan may be defrayed through fees paid by the investment product, which are reflected in the fund's expense ratio, rather than through a direct charge paid by plan participants or the plan sponsor. For mutual funds, service provider fees can be paid from fund assets. The new DOL regulations described in note 17 require service providers that provide recordkeeping as part of a bundle to give the plan a reasonable and good faith estimate of how much the recordkeeping services will cost the plan.

[22] U.S. Department of Labor Opinion Letters 97-03A (January 23, 1997) and 2001-01A (January 18, 2001).

[23] For the most part, 401(k) plan assets are held in individual accounts established for each participant. However, the costs of running a 401(k) plan also may be partly defrayed through employee "forfeitures." Employees who terminate employment without fully vesting (that is, earning full ownership of account assets) forfeit matching or other employer contributions. (Participants always are fully vested in their own contributions.) These forfeitures typically are used to offset fees or pay for additional employer contributions. Deloitte Consulting LLP, the International Foundation of Employee Benefit Plans, and the International Society of Certified Employee Benefit Specialists 2013 reports that 64 percent of plans that had matching contributions used matching contribution forfeitures to reduce employer contributions; 35 percent used the forfeitures to offset fees; 9 percent reallocated the forfeitures to participants; and 12 percent did something else. (Plans can indicate more than one use of these funds; data are for 2012.) Plan Sponsor Council of America 2013 reports that 66.4 percent of 401(k) plans with forfeitures allocate forfeitures to reduce company contributions; 13.7 percent allocate the forfeitures among participants (based on account balances, 4.4 percent; based on participant contributions, 1.3 percent; or based on the participant's share of company contributions, 8.0 percent); 39.4 percent used the forfeitures to reduce plan expenses; and 1.3 percent did something else (data are for 2012). The IRC and ERISA determine the maximum vesting schedule for 401(k) plans and require that employer contributions made to the 401(k) plan not be removed from the plan. In addition, plans may charge fees for some transactions, such as taking a loan or making a withdrawal, and participants typically pay those fees in full when making the transaction.

[24] See Deloitte Consulting LLP and Investment Company Institute 2011 for full results and regression analysis of the fee data from the survey.

[25] Guaranteed investment contracts (GICs) are insurance company products that promise a specific rate of return on invested capital over the life of a contract. A similar investment option is a synthetic GIC, which consists of a portfolio of fixed-income securities "wrapped" with a guarantee (typically by an insurance company or bank) to provide benefit payments according to the terms of the plan. For additional discussion of these investment options and 401(k) plan participants' asset allocations, see Holden et al. 2013.

[26] Company stock is the stock of the plan sponsor (employer). See Holden et al. 2013 for additional discussion of 401(k) participant investment in company stock in 401(k) plans.

[27] See discussion of availability and use of self-directed brokerage windows in note 10.

[28] For additional information on mutual funds and the U.S. retirement market, see Investment Company Institute 2014b.

[29] See Reid and Rea 2003; Investment Company Institute 2004, 2005, and 2014a; and Gallagher 2014.

[30] See Investment Company Institute 2014b.

[31] Additional servicing fees not reflected in mutual fund total expense ratios are not captured in this analysis, nor is the cost of holding other types of investments in 401(k) plans.

[32] Financial advisers, retirement plan recordkeepers, discount brokerages, and other financial intermediaries provide an array of important and valuable services to mutual fund shareholders. For 401(k) plans, these services can include recordkeeping, transaction processing, participant communication, education and advice, and regulatory and compliance services (see Figure 2). Mutual funds and their investment advisers use a variety of arrangements to compensate plan service providers for these services. Under one arrangement, a mutual fund's board of directors may adopt a plan pursuant to Rule 12b-1 under the Investment Company Act of 1940. As explained in U.S. Securities and Exchange Commission, "Mutual Fund Fees and Expenses," Rule 12b-1 allows mutual funds to use fund assets to cover distribution expenses and shareholder service expenses. "Distribution" fees include fees paid for marketing and selling fund shares, such as compensating brokers and others who sell fund shares as well as paying for advertising, printing and mailing prospectuses to new investors, and printing and mailing sales literature. Under Financial Industry Regulatory Authority (FINRA, formerly the National Association of Securities Dealers [NASD]) rules, 12b-1 fees used to pay marketing and distribution expenses (as opposed to shareholder services) cannot exceed 75 basis points (NASD Conduct Rule 2830(d)). "Shareholder service" fees are paid to respond to investor inquiries and provide investors with information on their investments. A mutual fund may pay shareholder service fees without adopting a 12b-1 plan. FINRA imposes an annual cap of 25 basis points on shareholder service fees (regardless of whether these fees are authorized as part of a 12b-1 plan). For further discussion of 12b-1 fees and how funds use them, see Investment Company Institute 2005 and "ICI Resources on 12b-1 Fees," available at www.ici.org/rule12b1fees. At year-end 2013, 81 percent of equity mutual fund assets held in 401(k) plans were invested in funds that had no 12b-1 fee, and another 12 percent were invested in funds with 12b-1 fees of 25 basis points or less (see Figure A6 in the appendix). Funds also may pay service providers for subtransfer agency services or administrative services out of fund assets. This is reflected in the fund's total expense ratio (in the "other expense" category). The fund's adviser (or a related entity) also may compensate the service provider(s) out of the profits earned from the advisory fee collected from the fund.

[33] See Figure A2 in the appendix for additional historical data. In addition, see Figure A3 in the appendix for mutual fund assets by share class and type of mutual fund (equity funds, hybrid funds, and bond funds).

[34] See Reid and Rea 2003.

[35] Back-end load shares, which are primarily Class B shares, typically have an annual 12b-1 fee of 100 basis points and a CDSL set at 5 percent in the first year the shares are held. Then, the CDSL falls 1 percentage point per year, reaching 0 percent in the sixth or seventh year that the shares are held. Back-end load shares that are transferred or exchanged within a fund family are not subject to the CDSL. Generally, after six to eight years, Class B shares convert to Class A shares, which lowers the 12b-1 fee from 100 basis points to that of Class A shares. For additional details, see Investment Company Institute 2014a and Reid and Rea 2003.

[36] Level load shares, which include Class C shares, typically have an annual 12b-1 fee of 100 basis points and a CDSL set at 1 percent in the first year that the shares are held. After the first year, no CDSL is charged on redemptions. These shares usually do not convert to Class A shares. For additional details, see Investment Company Institute 2014a and Reid and Rea 2003.

[37] See Figure A2 in the appendix for additional data.

[38] Expense information is not available for mutual funds held as investment choices in variable annuities (often referred to as VA mutual funds).

[39] For additional discussion of industrywide mutual fund fee trends, see Gallagher 2014.

[40] For a more-detailed discussion of competition in the mutual fund industry, see Coates and Hubbard 2006, Reid 2006, Stevens 2006, and Investment Company Institute 2014a.

[41] In February 2006, ICI conducted an in-home survey of 737 randomly selected fund owners who had purchased shares of stock, bond, or hybrid mutual funds outside workplace retirement plans in the preceding five years (see Investment Company Institute 2006). On average, these fund owners considered nine distinct items of information about a fund before purchasing shares, five of which they considered "very important" to making the final decision to invest. Seventy-four percent of these fund owners wanted to know about a fund's fees and expenses before purchasing shares; 69 percent reviewed or asked questions about the fund's past performance.

[42] For example, see Investment Company Institute 2014a and Collins 2005.

[43] Deloitte Consulting LLP, the International Foundation of Employee Benefit Plans, and the International Society of Certified Employee Benefit Specialists 2013 reports that 69 percent of the plans in its survey evaluated and benchmarked the performance of plan investments on a quarterly basis; 11 percent did so semiannually; 15 percent annually; and 5 percent at some other frequency (data are for 2012).

[44] Deloitte Consulting LLP, the International Foundation of Employee Benefit Plans, and the International Society of Certified Employee Benefit Specialists 2013 finds that 47 percent of plans had replaced a fund due to poor performance within the last year; 24 percent had replaced a fund one year to less than two years ago; 14 percent had replaced a fund two years to less than five years ago; 6 percent had last replaced a fund five or more years ago; and 9 percent had never replaced a fund (data are for 2012).

[45] The size of the plan—in terms of assets, participants, and average account balance—is key in pricing services. However, many factors influence plan fees, and they all must be considered when evaluating the reasonableness of a plan's cost. In addition, the reasonableness of fees paid by a plan is different from the question of whether a plan fiduciary engaged in a prudent process under ERISA in selecting and monitoring plan services and investments (see note 16).

[46] Investment Company Institute 2014a reports that among mutual fund shareholders owning funds outside employer-sponsored retirement plans in 2013, 81 percent owned fund shares through investment professionals. Schrass 2013 found that owning a DC account decreased the probability of a mutual fund–owning household having an ongoing advisory relationship and that owning an IRA increased the probability. In the regression analysis, these variables were highly significant, and their interaction with ongoing advisory relationships makes sense: financial advice is more readily available outside employer-sponsored retirement plans, and rollover activity, which is common throughout people's working lives, generates traditional IRAs, which are considered to be outside employer-sponsored plans. Financial advisers provide a range of services to investors: they help investors identify financial goals and recommend funds to meet those goals, conduct transactions, maintain financial records, and coordinate the distribution of prospectuses, financial reports, and proxy statements (see Leonard-Chambers and Bogdan 2007).

[47] For the distribution of expense ratios of mutual funds held in 401(k) plans disaggregated by more-detailed investment objectives, see Figure A4 in the appendix.

[48] One reason that the average expense ratio of hybrid funds industrywide has remained largely stable (at about 0.80 percent) since 2011, rather than falling as assets have risen, is that one-quarter of net flows into hybrid funds over the past three years has been directed to "alternative strategies" funds, which ICI includes in the hybrid category. The investment charters of these funds often allow them to engage in short-selling of securities or to invest in futures and commodities. These strategies offer the advantage of diversification across a wider range of asset classes but can cost more to undertake. See Gallagher 2014.

[49] For more information, see Gallagher 2014.

[50] The average expense ratio of money market funds industrywide decreased in 2013 as a result of fee waivers due primarily to the current low interest rate environment. See Gallagher 2014 for more detail.

[51] The SEC has modified its prospectus rules to make the turnover rate more prominent—by moving it to the summary section at the beginning of the prospectus. See 74 Fed. Reg. 4546 (January 26, 2009). The new DOL rules described in note 20 will require that participants have access to a website showing, among other information, the portfolio turnover rate for each investment in the plan's lineup.

[52] The SEC requires that a fund's turnover rate be calculated by dividing the lesser of its purchases or sales of portfolio securities for a reporting period by the monthly average of the value of its portfolio securities during the same reporting period.

[53] For a more-detailed discussion of portfolio turnover, see Reid and Millar 2004.

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## Appendix

This appendix contains additional detail on fees paid in 401(k) plans. Figure A1 focuses on who pays annual 401(k) recordkeeping/administrative fees. Figures A2 and A3 report 401(k) mutual fund assets by share class, first across all 401(k) mutual funds (Figure A2) and then within equity funds, hybrid funds, and bond funds separately (Figure A3). Figure A4 reports the distribution of 401(k) fund assets by investment objective and total expense ratio. Finally, Figures A5 through A7 show information on 12b-1 fees paid by 401(k) investors in mutual funds.

FIGURE A1

### Who Pays Annual 401(k) Recordkeeping/Administrative Fees?

*Percentage of plans surveyed, 2012*

| | Percent |
|---|---|
| **Plan sponsor** | **18** |
| **Participant** | **67** |
| Via investment product fees and expenses* | 51 |
| Via additional reduction to investment returns* | 5 |
| Via direct charge | 11 |
| Pro rata based on account balances | 3 |
| Equal dollar to all participants | 6 |
| Other | 2 |
| **Direct fees paid by both plan sponsor and participants** | **8** |
| **Other** | **7** |

* These fees are in the form of a wrap fee or added basis point charge.

Note: This figure reports tabulations based on the 294 401(k) plan sponsors that responded to a question on who pays 401(k) recordkeeping/administrative fees. (The survey covers nearly 400 401(k) plan sponsors.)

Source: Investment Company Institute tabulation of data from Deloitte Consulting LLP, International Foundation of Employee Benefit Plans, and International Society of Certified Employee Benefit Specialists 2013

FIGURE A2

## 401(k) Mutual Fund Assets by Share Class

*Percentage of assets, 2000–2013*

| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Load** | **33** | **32** | **22** | **24** | **25** | **24** | **23** | **22** | **20** | **19** | **18** | **16** | **15** | **14** |
| Front-end load[1] | 30 | 29 | 20 | 21 | 20 | 18 | 18 | 16 | 13 | 13 | 12 | 10 | 9 | 8 |
| Back-end load,[2] level load,[3] and other load[4] | 3 | 3 | 3 | 3 | 4 | 5 | 6 | 6 | 6 | 7 | 7 | 6 | 6 | 6 |
| **No-load[5]** | **67** | **68** | **78** | **76** | **75** | **76** | **77** | **78** | **80** | **81** | **82** | **84** | **85** | **86** |
| Institutional no-load | 21 | 24 | 26 | 25 | 23 | 23 | 23 | 25 | 31 | 30 | 31 | 37 | 41 | 42 |
| Retail no-load | 46 | 44 | 51 | 51 | 53 | 53 | 54 | 53 | 49 | 50 | 50 | 47 | 44 | 44 |
| **Total** | **100** | **100** | **100** | **100** | **100** | **100** | **100** | **100** | **100** | **100** | **100** | **100** | **100** | **100** |

[1] Front-end load > 1 percent. Primarily includes Class A shares; includes assets where front-end loads are waived.

[2] Front-end load = 0 percent and contingent deferred sales load (CDSL) > 2 percent. Primarily includes Class B shares.

[3] Front-end load ≤ 1 percent, CDSL ≤ 2 percent, and 12b-1 fee > 0.25 percent. Primarily includes Class C shares; excludes institutional share classes.

[4] All other load share classes not classified as front-end load, back-end load, or level load shares.

[5] Front-end load = 0 percent, CDSL = 0 percent, and 12b-1 fee ≤ 0.25 percent.

Note: Data exclude mutual funds available as investment choices in variable annuities and tax-exempt mutual funds. Components may not add to the total because of rounding.

Sources: Investment Company Institute and Lipper

FIGURE A3

## 401(k) Mutual Fund Assets by Share Class

*Percentage of assets, selected years*

| Equity funds | 2000 | 2006 | 2008 | 2010 | 2012 | 2013 |
|---|---|---|---|---|---|---|
| **Load** | **38** | **25** | **23** | **20** | **16** | **14** |
| Front-end load[1] | 36 | 20 | 16 | 13 | 10 | 9 |
| Back-end load,[2] level load,[3] and other load[4] | 3 | 6 | 7 | 7 | 6 | 6 |
| **No-load[5]** | **62** | **75** | **77** | **80** | **84** | **86** |
| Institutional no-load | 16 | 17 | 20 | 22 | 33 | 36 |
| Retail no-load | 45 | 58 | 56 | 58 | 51 | 49 |
| **Total** | **100** | **100** | **100** | **100** | **100** | **100** |
| **Hybrid funds** | **2000** | **2006** | **2008** | **2010** | **2012** | **2013** |
| **Load** | **25** | **26** | **24** | **23** | **20** | **21** |
| Front-end load[1] | 22 | 17 | 15 | 13 | 10 | 10 |
| Back-end load,[2] level load,[3] and other load[4] | 3 | 9 | 10 | 10 | 10 | 12 |
| **No-load[5]** | **75** | **74** | **76** | **77** | **80** | **79** |
| Institutional no-load | 10 | 10 | 14 | 21 | 25 | 22 |
| Retail no-load | 65 | 64 | 62 | 56 | 55 | 56 |
| **Total** | **100** | **100** | **100** | **100** | **100** | **100** |
| **Bond funds** | **2000** | **2006** | **2008** | **2010** | **2012** | **2013** |
| **Load** | **21** | **17** | **15** | **15** | **14** | **14** |
| Front-end load[1] | 17 | 13 | 11 | 11 | 10 | 9 |
| Back-end load,[2] level load,[3] and other load[4] | 4 | 4 | 4 | 4 | 4 | 4 |
| **No-load[5]** | **79** | **83** | **85** | **85** | **86** | **86** |
| Institutional no-load | 51 | 56 | 58 | 58 | 64 | 67 |
| Retail no-load | 28 | 27 | 27 | 27 | 22 | 19 |
| **Total** | **100** | **100** | **100** | **100** | **100** | **100** |

[1] Front-end load > 1 percent. Primarily includes Class A shares; includes assets where front-end loads are waived.

[2] Front-end load = 0 percent and contingent deferred sales load (CDSL) > 2 percent. Primarily includes Class B shares.

[3] Front-end load ≤ 1 percent, CDSL ≤ 2 percent, and 12b-1 fee > 0.25 percent. Primarily includes Class C shares; excludes institutional share classes.

[4] All other load share classes not classified as front-end load, back-end load, or level load shares.

[5] Front-end load = 0 percent, CDSL = 0 percent, and 12b-1 fee ≤ 0.25 percent.

Note: Data exclude mutual funds available as investment choices in variable annuities and tax-exempt mutual funds. Components may not add to the total because of rounding.

Sources: Investment Company Institute and Lipper

FIGURE A4

## 401(k) Mutual Fund Assets by Investment Objective and Total Expense Ratio

*Percentage of assets, 2013*

| | Expense ratio | | | |
|---|---|---|---|---|
| | <0.50 | 0.50 to <1.00 | 1.00 to <1.50 | ≥1.50 |
| **Total** | **46** | **43** | **10** | **1** |
| **Equity funds** | **38** | **47** | **13** | **1** |
| Domestic | 43 | 45 | 11 | 1 |
| World | 23 | 55 | 19 | 3 |
| **Hybrid** | **42** | **47** | **9** | **2** |
| **Bond funds** | **62** | **34** | **4** | **(*)** |
| High-yield and world | 6 | 77 | 14 | 2 |
| Other | 69 | 28 | 3 | (*) |
| **Money market funds** | **100** | **(*)** | **(*)** | **(*)** |

(*) = less than 0.5 percent

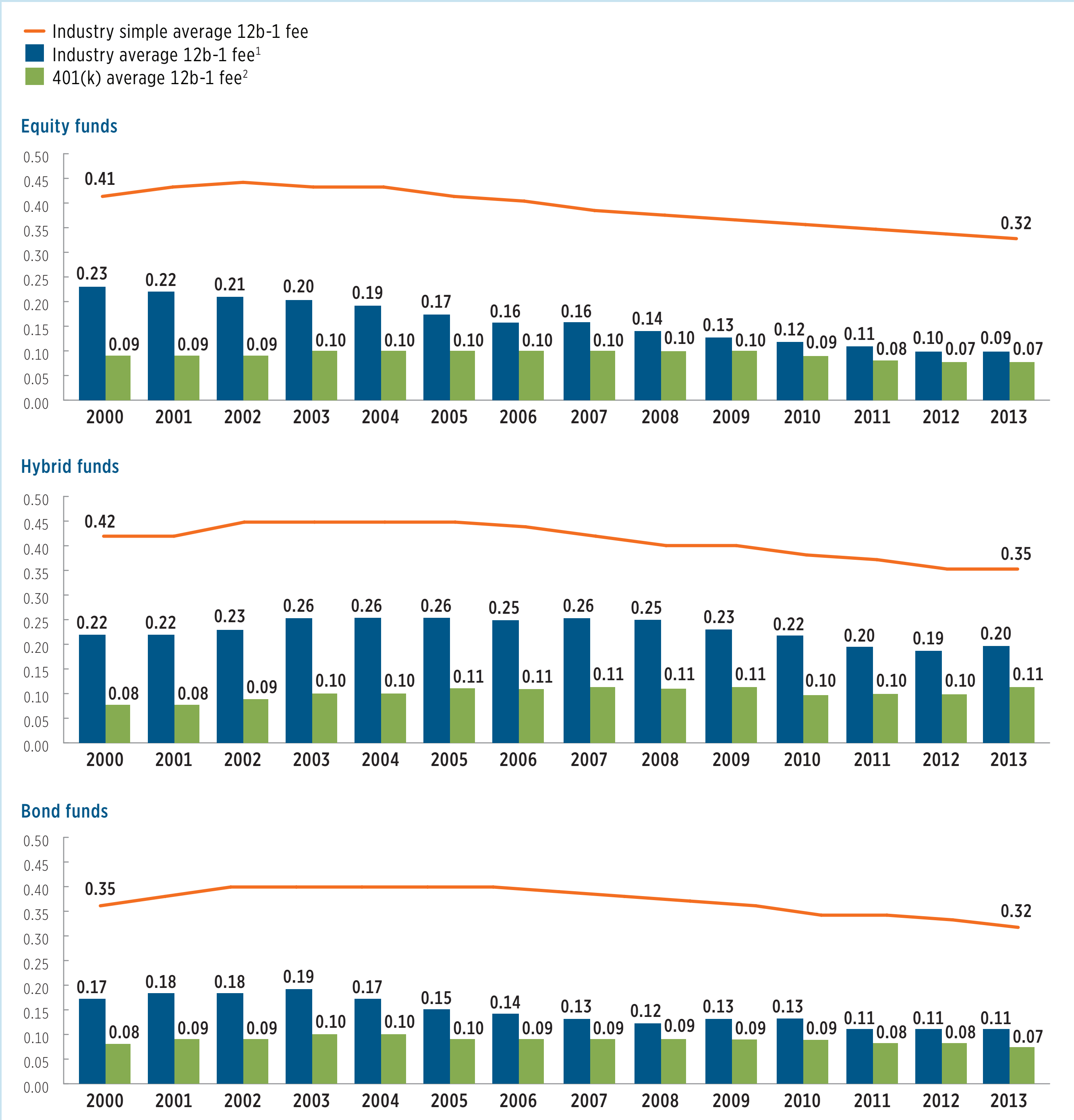
Note: The total expense ratio includes fund operating expenses and the 12b-1 fee. Data exclude mutual funds available as investment choices in variable annuities and tax-exempt mutual funds. Row percentages may not add to 100 percent because of rounding.

Sources: Investment Company Institute and Lipper

FIGURE A5

## 401(k) Mutual Fund Investors Tend to Pay Lower-Than-Average 12b-1 Fees

*Percent, 2000–2013*




[1] The industry average 12b-1 fee is measured as an asset-weighted average.

[2] The 401(k) average 12b-1 fee is measured as a 401(k) asset-weighted average.

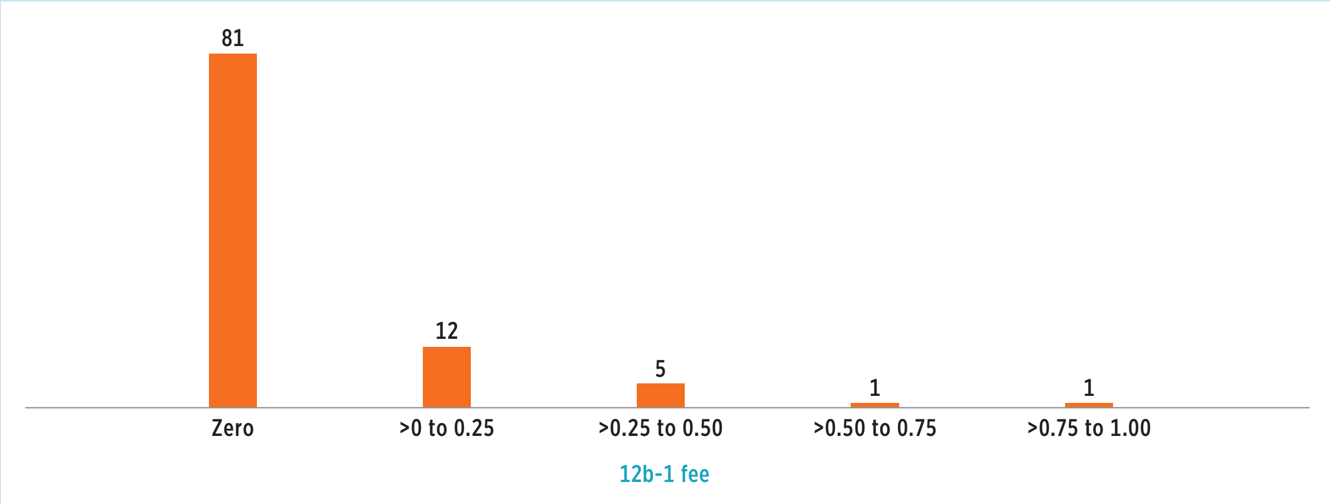
Note: Data exclude mutual funds available as investment choices in variable annuities and tax-exempt mutual funds. Data include mutual funds without 12b-1 fees.

Sources: Investment Company Institute and Lipper

FIGURE A6

## 401(k) Equity Mutual Fund Assets by 12b-1 Fee

*Percentage of 401(k) equity mutual fund assets, 2013*




Note: Data exclude mutual funds available as investment choices in variable annuities.

Sources: Investment Company Institute and Lipper

FIGURE A7

## 401(k) Mutual Fund Assets by Investment Objective and 12b-1 Fee

*Percentage of assets, 2013*

| | 12b-1 fee | | | | |
|---|---|---|---|---|---|
| | Zero | >0 to 0.25 | >0.25 to 0.50 | >0.50 to 0.75 | >0.75 to 1.00 |
| **Total** | **80** | **13** | **4** | **1** | **1** |
| **Equity funds** | **81** | **12** | **5** | **1** | **1** |
| Domestic | 83 | 11 | 4 | 1 | 1 |
| World | 74 | 18 | 6 | 2 | 1 |
| **Hybrid** | **76** | **12** | **6** | **4** | **2** |
| **Bond funds** | **76** | **20** | **3** | **1** | **1** |
| High-yield and world | 65 | 25 | 7 | 2 | 1 |
| Other | 77 | 19 | 3 | 1 | 1 |
| **Money market funds** | **97** | **3** | **1** | **(*)** | **(*)** |

(*) = less than 0.5 percent

Note: Data exclude mutual funds available as investment choices in variable annuities and tax-exempt mutual funds. Row percentages may not add to 100 percent because of rounding.

Sources: Investment Company Institute and Lipper

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