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The Economics of Providing 401(k) Plans, 2009

Average Expense Ratios Edged Up for Stock and Bond Funds in 401(k) Plans in 2009

Study Shows 401(k) Investors Continue to Gravitate to Lower-Cost Mutual Funds

Washington, DC, September 16, 2010 - 401(k) plan participants invested in mutual funds on average paid slightly higher expense ratios in 2009, according to an annual report by the Investment Company Institute that examines the economics of providing 401(k) plans. At year-end 2009, more than half of the $2.8 trillion in 401(k) assets was invested in mutual funds, primarily in stock funds.

Expense Ratios Edge Up

*The Economics of Providing 401(k) Plans, Services, Fees and Expenses, 2009*finds that the expense ratios of stock and bond funds averaged slightly higher in 2009, compared with 2008. The asset-weighted average expense ratios paid by 401(k) investors on their stock funds rose 3 basis points to 0.74 percent. The asset-weighted average expense ratio paid by 401(k) investors on their bond funds increased 2 basis points to 0.55 percent. Meanwhile, for money market funds, the asset-weighted average expense ratios paid by 401(k) investors fell 2 basis points to 0.36 percent.

The expense ratio increases were attributable in significant part to the effects of the stock and bond market downturn in 2008 and early 2009, because certain fixed costs were spread over proportionally fewer assets. The average stock and bond fund expense ratios paid by 401(k) investors had declined in the previous five years. The drop in money market fund expense ratios in 2009 is largely attributed to ongoing fee waivers by firms during a continuing low interest rate environment.

Investors Choose Lower-Cost Funds

Despite the slight increase in expense ratios, the report also found that 401(k) mutual fund investors continue to gravitate towards lower-cost mutual funds with below-average turnover. Eighty percent of 401(k) assets held in mutual funds were in "no-load" funds—funds that do not have a sales charge. The remainder of mutual fund assets held in 401(k) plans was invested in load funds, but such funds typically waive their loads for retirement plan participants. Thus, for most 401(k) investors, the total expense ratio is the only investment charge they pay in the mutual funds held in their plans.

The bulk of 401(k) assets invested in mutual funds were invested in stock mutual funds. More than three-quarters of stock mutual fund assets held in 401(k) plans were in stock mutual funds with expense ratios less than 1 percent.

"The 401(k) plan investment market is highly competitive," said Sarah Holden, Senior Director, Retirement and Investor Research. "Although there are many measures to consider when investing—such as investment objective and risks and historical performance—the data suggest that plan sponsors research their plan options carefully and participants concentrate their assets in lower-cost mutual funds."

"Because mutual funds fully disclose their operating expenses in a standardized form—the expense ratio—the fees incurred by 401(k) investors are readily available" said Michael Hadley, Associate Counsel for Pension Regulation and a co-author of the study. "This transparency helps 401(k) plan sponsors and participants make informed decisions, and the data suggest they consider fees together with other key investment criteria."

The study details the many services that 401(k) plan sponsors receive, along with the complexities, regulations and related costs of offering a plan, and notes that plan fiduciaries who oversee the plan must ensure that costs for plan services are reasonable. Related research includes ICI's *Trends in the Fees and Expenses of Mutual Funds, 2009*, which reports industry trends, and a Deloitte/ICI study, *Defined Contribution/401(k) Fee Study*.