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SMALL FEES, BIG IMPACT

Seemingly insignificant charges in retirement plans can add up.

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So much fine print goes unread. Few people realize how significantly 401(k) account fees can impact their retirement savings efforts. AARP recently conducted a poll of 401(k) participants and the results were eye-opening: 71% incorrectly assumed that they paid no account fees at all, and another 6% said they were entirely clueless about the matter.¹

In 2012, 401(k) plan sponsors will have to inform plan participants about the fees they pay when enrolled in these programs. Some of these fees are also common to IRAs.¹

What kind of impact are we talking about? The Department of Labor offers a hypothetical example.

- An employee has a 401(k) account with \$25,000 in it and 35 years to go until his retirement date.
- Over time, he makes no further contributions to his account.
- Over the next 35 years, his 401(k) generates an average 7% annual return.
- If the plan's fees and expenses are just 0.5% annually, he winds up with \$227,000 in his account 35 years later.
- If the plan's fees and expenses take a 1.5% bite out of his return annually, he winds up with just \$163,000 after 35 years.
- All other factors aside, a 1% difference in annual fees would mean a 28% difference in his retirement savings over these 35 years.²

Financially, there is nothing trivial about these fees.

The common charges. Your three major 401(k)/IRA fees are account termination fees, account maintenance fees and account transfer charges. There aren't many ways around them. The admin fee may hit \$50 per year, and while that looks like chump change, consider that it amounts to 1% of a young IRA owner's initial maximum contribution in 2011. Fortunately, these annual admin fees are often waived when your account balance surpasses a certain level.³

The uncommon charges. Have you ever paid a Form 990-T fee? It can ding you for a few hundred bucks. So can a recordkeeping fee, if you have an individual 401(k) and use a third-party recordkeeper. Have you ever paid a loan processing charge? A

federal fund wire fee? An overnight delivery fee for checks? You would be surprised at the magnitude of some of these charges.

An interesting choice that is rarely explored. If your 401(k) or IRA custodian allows you to be billed directly, you may have the option to pay some of your account fees with money held outside the account. If you are in the accumulation phase (saving up for retirement), this can be a tax-efficient way to deal with some of these charges. If you are in the distribution phase, it may be better tax-wise to pay the fees with money from the IRA or 401(k) instead.¹

A little scrutiny can mean a big difference. According to BrightScope, a firm which gathers data about retirement plans, the average retirement plan offered through an investment company with a balance exceeding \$100 million imposes an annual fee of 1.08%. If the plan has between \$10 million and \$100 million under management, the annual fee for plan participants averages 1.36%; if the plan has a balance of below \$10 million, the annual fee for plan participants averages 1.36%. It is little wonder that financially savvy employees end up asking their companies to switch to 401(k) programs with lower annual fees.⁴



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Citations.

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