



Retirement Plan Fees: Comparison Shopping the Costs of Investment

Saving for retirement is an important goal. Making choices around where one chooses to invest is part of this process. Of equal importance is understanding and effectively managing the cost of investing.

When you retire you can leave assets with your employer, self-manage through an Individual Retirement Account (IRA), or seek professional investment management services.

Regardless of your preference, it's important to understand how retirement investing costs can affect the growth of your investments. This brochure provides information about those costs so you can make informed choices regarding where and with whom to invest.

Retirement plan fees and expenses can be thought of in many ways, but let's break them down into three broad categories:

Investment Management Costs

Paying an expert to make investment decisions on your behalf.

Administrative Costs

Miscellaneous costs not directly related to investment management—for example, the cost of issuing statements, operating a telephone service center/website, etc.

Sales Costs

Fees paid to an investment provider or third party (an investment advisor) to purchase, or exit, an investment. This cost can be avoided if you purchase your investment directly from an investment provider.

A useful analogy for thinking about these costs is comparing them to the costs of purchasing airplane tickets:

Airfare

Paying an airline to transport you to your destination.

Administrative Costs

Miscellaneous costs not directly related to operating a plane—for example, the cost of issuing tickets, operating a telephone service center/website, etc.

Sales Costs

Fees paid to a third party (a travel or ticket agent) to help you find your fare. This cost can be avoided if you purchase the ticket directly from the airline.

When you purchase an airplane ticket, you have a few considerations. For most people they fall in the following order of importance:

1. A reasonable fare
2. The best seat and travel times they can find for what they're willing to pay
3. An airline that they trust

However, when it comes to investing, many of us reverse these priorities:

1. An investment manager they trust
2. The best return they can find for the risk they're willing to take
3. A reasonable fee

Why do we tend to rank cost lower when it comes to investing? One explanation: investment costs aren't charged to a credit card as they are with plane tickets, they're absorbed out of the investment. We tend to not pay attention to those costs because we assume "the investment," not us, will pay for them by growing in value. However, "the investment" is still your money.

To illustrate, let's compare the hypothetical costs of an airplane ticket purchased through a third-party vs. doing it yourself, and the



Table 1

	Broker-Assisted Airplane Ticket	Self-Purchased Airplane Ticket	\$ 100k Broker- Assisted Investment Management ¹	Self-Purchased Investment ²
Service Cost	\$500	\$375	\$2,000	\$250
Administrative Cost	\$0	\$25	\$0	\$500
Sales Cost	\$25	\$0	\$3,000	\$0
Total	\$525	\$400	\$5,000	\$750

1. 1% to investment manager + 1% to fund company; 3% sales cost

2. index fund purchase through employer-sponsored retirement with 0.5% administrative fee, no sales fees

costs of a hypothetical \$100,000 investment (using a third-party broker in an IRA) vs. self-directed investing (through an employer-sponsored retirement plan). (See Table 1)

Word to the Wise

The lowest cost retirement investments typically involve (1) indexed or passively managed investments; (2) large employer sponsored retirement plans where administrative costs can be spread out over a large number of participants; and (3) the absence of sales costs to third parties to gain access to, or exit, investments.

The previous illustration reveals how much costs can potentially vary, but the only way to understand the costs of your potential investment is to ask questions of the investment providers. Here are some tips on how to do this effectively:

1. Request that the provider disclose all fees to you, direct or indirect, explicit or implicit, on your investment and investment earnings on an annual basis. Ask for an illustration based on a hypothetical dollar investment of \$100,000. Have the provider verify in writing that it has represented all direct or indirect fees to be assessed out of your investment or investment earnings. If the information you're given doesn't make sense, don't be shy about telling the

provider: "You need to make this more clear."

2. Don't avoid researching the costs of investment based simply on what you hope to achieve in performance returns. Remember that in the investing world, you don't always "get what you pay for"—it's very easy to pay a higher fee and also receive a lower return.
3. Always remember these three basic keys to successful investing: (a) identifying the level of risk you are willing to take; (b) diversifying your investment in a manner consistent with your risk tolerance; and (c) managing the cost of investment so it doesn't eat too deeply into your returns.

Look for Value

Value matters in retirement investing as much as in other purchases you make in life. Many individuals will spend weeks or months debating the purchase of a \$500 plane ticket, but only a few minutes deciding how to invest \$100,000. Be bold in looking out for this significant asset you've accumulated. As always, you are your best advocate.

Are you interested in more information about investments and fees?

Listed below are some organizations that provide publications and tools that can help in your research.

U.S. Department of Labor–Employee Benefits Security Administration

<http://www.dol.gov/ebsa/publications/main.html> is a publications section of the website with retirement brochures such as Understanding Retirement Plan Fees and Expenses and What You Should Know About Your Retirement Plan

Securities and Exchange Commission

<http://www.sec.gov/investor/pubs.shtml> links to the publications section of the Office of Investor Education and Assistance website which has several brochures regarding investments such as Invest Wisely: An Introduction to Mutual Funds and Mutual Fund Fees and Expenses

National Association of Securities Dealers

<http://www.nasd.com/InvestorInformation/index.htm> is an Investor Information section of the website with several publications and resources in categories such as “Smart Investing”, “Investor Protection”, and “Tools and Calculators”

About NAGDCA

The National Association of Government Defined Contribution Plan Administrators is composed of deferred compensation and defined contribution plan administrators from the 50 states and over 100 local governments and entities, as well as the private industry plan providers. NAGDCA is an organization in which the members work together to improve government 457 plans through a sharing of information on investments, marketing, administration and laws relating to public sector deferred compensation/defined contribution plans.

For more information visit www.nagdca.org.

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