MAXIMIZING YOUR RECORDKEEPER RELATIONSHIPS
A Brief Guide to Getting the Most Out of Your Defined Contribution Plan Vendor
By Michael Kopec, CRPS, Director of Investment Consulting, and Gary Pallatta, Senior Consultant

For plan sponsors, maintaining a successful relationship with your defined contribution (DC) plan recordkeeper can provide many benefits. Better pricing, additional features and improved servicing may be available to organizations that remain actively involved with their providers after the initial engagement. However, it is not unusual for plan committees to place the review of an existing vendor at the bottom of their priority list.

Mid to large-sized DC plans are increasingly threatened by excessive fee litigation. While plan expenses are an important component of any vendor review, fees alone should not be the focus. The Department of Labor (DOL) explicitly states that employers must “ensure that fees paid...are reasonable in light of the level and quality of services provided.” Hence, the DOL makes it clear that fees are to be reviewed in the context of service and overall value.

Based on this DOL guideline, it is essential to periodically assess if all contractual obligations are being met (not just fees). In this regard, we will focus on five core components to consider in order to both meet your fiduciary duties and get the most value from your retirement plan recordkeeper: Fees, Hidden Expenses, Plan Demographics, Service Quality and Technology.

Executive Summary

- Plan Sponsors have a duty to act in the best interests of their participants, and understanding the capabilities and resources within their vendor plays an important role in helping their employees reach retirement readiness.

- While the DOL has provided guidance on the overall responsibilities of plan sponsors, these guidelines fall short of speaking to best practices when dealing with recordkeepers. This paper aims to help plan fiduciaries maximize their recordkeeper relationships with the end goal of better retirement outcomes.

- As the retirement industry continues to evolve, it is imperative for plan sponsors to stay abreast of trends in the marketplace in order to have a prudent decision-making process regarding those products and services being offered.

1 “A Look at 401(k) Plan Fees,” U.S. Department of Labor. August 2013. (Italics have been added for emphasis and are not included in the original report.)
Fees

Most plan sponsors are well-aware of the need to formally monitor their retirement plan fees, but a surprising number fail to realize this responsibility extends to reviewing all fees: administrative, investment and ad hoc. As plan fiduciaries, committee members can be held personally liable for a plan’s (mis)management. If they are not reviewing pricing on a routine basis (ideally, once every three years), what was once considered “reasonable” could evolve into being deemed excessive. In a December 2016 study by BrightScope and ICI, in a period of five years, all-in recordkeeping fees for 401(k) plans fell by 15% (from 0.65% to 0.55%, as shown in Exhibit I). If during this same period, your plan’s fees remained stagnant, that could lead to participant complaints and potential legal scrutiny.

Exhibit I: Total Plan Cost by 401(k) Plan Assets

Total plan cost as a percentage of assets among plans with audited 401(k) filings in the BrightScope database (by plan assets, 2009 and 2014).

![Participant Weighted Fees (%)](chart)

<table>
<thead>
<tr>
<th>Plan Size</th>
<th>2009</th>
<th>2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>$1M to $10M</td>
<td>1.38</td>
<td>1.24</td>
</tr>
<tr>
<td>&gt;$10M to $50M</td>
<td>1.00</td>
<td>0.98</td>
</tr>
<tr>
<td>&gt;$50M to $100M</td>
<td>0.79</td>
<td>0.74</td>
</tr>
<tr>
<td>&gt;$100M to $250M</td>
<td>0.61</td>
<td>0.57</td>
</tr>
<tr>
<td>&gt;$250M to $500M</td>
<td>0.63</td>
<td>0.50</td>
</tr>
<tr>
<td>&gt;$500M to $1B</td>
<td>0.51</td>
<td>0.44</td>
</tr>
<tr>
<td>&gt;$1B</td>
<td>0.34</td>
<td>0.27</td>
</tr>
<tr>
<td>More than $1B</td>
<td>0.65</td>
<td>0.55</td>
</tr>
<tr>
<td>All Plans</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: BrightScope; Investment Company Institute; Lipper.

Both for-profit and not-for-profit DC plans are increasingly becoming subject to this fee litigation, including corporate 401(k) plans and the recently targeted health system and university 403(b) plans. In order to combat such allegations, plan sponsors need to illustrate that expenses are being regularly reviewed by having proper monitoring procedures in place and documenting those practices.

Because no two plans are the same, the most accurate method for executing a fee study is to collect current pricing bids that are specific to your plan’s unique characteristics from alternate vendors in your plan’s market segment. (These should be actual fee quotes based on what each provider would charge to take on your plan’s administration.)

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By reviewing competing vendor quotes against those of the incumbent, an organization can help prudently compare how their plan’s provider fares against the marketplace. This information can then be used to determine if your current pricing structure is justified. If not, you should ask your recordkeeper to consider repricing the plan. If you find they are either unwilling or unable to do so, moving forward with a vendor search should be seriously considered.

**HIDDEN EXPENSES**

Looking solely at the base recordkeeping cost of a DC plan excludes certain revenue, which understates the plan’s total cost (potentially in the thousands of dollars). When conducting a fee benchmarking, you should ensure that all sources of revenue paid to the provider are included in order to gain an accurate assessment of a plan’s true cost.

**Exhibit II: Upfront versus Optional Service Fee Examples**

<table>
<thead>
<tr>
<th>Upfront Fee</th>
<th>Potential Hidden Expense Example</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Base Cost</strong></td>
<td><strong>Optional Services for Plan Sponsor</strong></td>
</tr>
<tr>
<td>• Basis Point</td>
<td>• Document Preparation</td>
</tr>
<tr>
<td>• Per-Head Charge</td>
<td>• Document Amendments</td>
</tr>
<tr>
<td>• Revenue Share</td>
<td>• Participant Mailings</td>
</tr>
<tr>
<td>• Bundled Model</td>
<td>• Audit / Testing Support</td>
</tr>
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<td></td>
<td></td>
</tr>
</tbody>
</table>

As depicted in Exhibit II, there are number of ancillary services that can drive up costs, both to the employer and employees; for example, consider participant distributions. If a vendor charges $50 per distribution, and you have 100 participants taking distributions each year, then there is $5,000 in additional fees being collected by the recordkeeper (the ‘hidden’ expense). This same exercise can be conducted for loans, installments, withdrawals, refunds, corrections and other transactions which add revenue to a vendor’s bottom line. Similarly, for plan sponsors, there can be costs associated with preparing/amending plan documents or for work related to audit and testing support—again, all of which will increase a plan’s total cost and should be included in your assessment.

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3 Keep in mind, though, that in order to have an impartial comparison, potential vendors must provide pricing based on the current investment lineup. Similarly, you must provide potential vendors with all relevant plan characteristics, such as the number of participants, total account balances, investment options and other basic features.

4 Remember, according to ERISA, it is not necessary to have the lowest fee possible, only the lowest fee that’s been prudently determined to meet the needs of your plan participants. If your plan is administratively complex, for example it has multiple payroll feeds or a custom plan document, it may necessitate a more hands-on approach and therefore dictate higher fees. So long as this information is reviewed regularly, and your committee comes to an agreement that a vendor provides a superior value, a higher cost can be justified. Just be sure to document that a prudent and thought-out decision-making process was conducted when arriving at that conclusion.
Finally, ongoing participant services, such as managed accounts, need to be considered. Service providers are increasingly encouraging clients to move away from target date funds into potentially more expensive managed account products. Since managed accounts can provide participants with more customized advice, this may be an appropriate value-added expense. However, plan committees need to assess if this level of service, and the associated costs, are right for their participants.

These are just a few of the hidden expenses that can increase your plan’s total cost. Therefore expenses, in their entirety, should be monitored and reviewed for reasonableness.

**PLAN DEMOGRAPHICS**

Defined contribution plans will grow and change over time in terms of assets, employees, complexity and participant needs. During periods of growth, changing plan demographics are generally viewed positively due to the associated economies of scale. However, should plan pricing go unchanged after a period of significant growth, this could be viewed more negatively from a fiduciary standpoint (if those same economies of scale go unleveraged).

Recall the all-in fee graphic from page #1 (with the more recent data redrawn here as Exhibit III). Note the direct correlation between cost and size. As plans grow, the savings could be significant, provided you renegotiate fees along the way.

**Exhibit III: Plan Cost by 401(k) Plan Assets in 2014**

*Total plan cost as a percentage of assets among plans with audited 401(k) filings in the BrightScope database (by plan assets, 2014).*

![Exhibit III: Plan Cost by 401(k) Plan Assets in 2014](image)

Similarly, participant demographic changes need to be monitored, as they will help determine the service model best suited for your organization. If the number of participants grows meaningfully—either organically or through a merger/acquisition (M&A)—the current service offering should be reassessed.

From this standpoint, some companies may need to evaluate their plan more frequently than others. Consider the technology industry where growth objectives may drive M&A activity. This could result in accelerated participant growth in a company’s plan, which may play a key role in the services required. Perhaps the new participant base has led to a larger percentage of baby boomers compared to prior years. This might increase the need for individualized communications around retirement readiness. It could also create a need for more personalized advice, since this generation is nearing retirement. Conversely, should millennials now comprise the majority, the addition of a financial wellness solution may have a higher priority.

These participant demographic changes can come at any time and in many forms, so it’s important to review them with your recordkeeper as they arise in order to ensure that the current plan pricing/service structure remains optimal for your organization.

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SERVICE QUALITY

It is the incumbent vendor’s responsibility to approach their client with issues, and likewise, a plan sponsor has a duty to monitor that vendor. Over the course of a healthy relationship, a natural dialogue should develop regarding ongoing service quality. Unfortunately, this is often not the case.

We have found that in many situations full recordkeeper searches are not primarily driven by fees, but rather, by a dissatisfaction with service. These issues often start as trivial matters that can escalate into larger headaches.

To avoid these situations, or if you’ve already found yourself in one, here are two options to help rectify a damaged vendor relationship.

- **Provide Feedback:** Many vendors conduct surveys, host events or solicit feedback periodically as a way to better understand their clients’ needs. When given the opportunity, be honest and share your opinion. These forums serve as a catalyst for internal change, so it’s important to participate, as this feedback may allow your vendor to address minor issues before they escalate into major problems.

- **Incorporate a Service-Level Agreement:** Once lingering issues have been brought to your vendor’s attention, outlining specific goals and deadlines can provide a tangible means of measuring service quality going forward. These agreements should specify criteria that can be used to hold your provider accountable. Such criteria should be realistic so that a clear measure of success or failure can be assessed. Any inability to uphold these standards would then result in the forfeiture of a portion of fees charged. It is important to remember that these conversations are not meant to be punitive, but rather, to help maintain consistent overall service levels. Ideally, service level agreements can be seen as strengthening the relationship between client and vendor as they provide clear definitions of the behaviors expected.

While it can be uncomfortable at times, acknowledging and addressing issues early on is the best, and sometimes the only, way to move forward.

TECHNOLOGY

Technological advancements have improved a number of industries, and the financial sector is no exception. Online accessibility, reporting and cyber security are all evolving to meet the growing demands of the retirement industry. Plan sponsors need to understand their vendor’s capabilities in this capacity, in order to confirm whether their tools are competitive compared to the marketplace. Once this technology is reviewed versus peers (e.g., better, equal or worse for a particular participant population), then a committee can assess if the associated costs are ‘reasonable’ in light of what’s offered.

Some of the more common differentiators in this area revolve around the employee experience, including a provider’s website, applications (‘apps’) and phone services.

- **Website:** Most vendor websites offer a basic overview of a participant’s current financial situation, while including functionality to easily update their accounts. Higher-quality sites may also provide retirement benchmarks and milestone goals, while suggesting steps toward improving retirement readiness outcomes.
- **Apps:** Most tablet and mobile applications also include account information and the ability to make changes, however, the higher-end apps will include the same features that are available through a service provider’s website.

- **Phone:** Given the importance of providing a positive employee experience, call center hours, wait times, training for call center representatives and overall service quality all need to be reviewed. Employers should also consider including these items in a vendor service-level agreement to ensure ongoing consistency and monitoring.

Again, each of these services should be evaluated in the context of a plan’s current participant population. To do so, try keeping in mind these key questions: 1) will employees use this technology? 2) if so, to what extent? 3) in doing so, will this technology meet their needs? and 4) ultimately, will this assist participants in reaching retirement readiness? A plan sponsor with a higher percentage of millennial employees, for example, may find website tools of greater value than those with a higher population of baby boomers (who may be more likely to use phone services). Each of these services can be measured based on those answers versus the quality of the provider’s technology compared to peers (see Exhibit IV for a sample illustration). This assessment can then be used to determine if a higher cost can be justified as ‘reasonable.’

**CONCLUSION**

If you are unsure if your recordkeeper is performing as promised (or are concerned they may not be), think back to what’s important to your plan and its participants. Understanding how your employees’ needs may change over time and then regularly relaying that information back to your provider is key to a successful relationship. Having this honest and open communication will help to mitigate conflicts and avoid potential service disruptions down the road.

As the retirement industry continues to evolve, vendors will continue to expand their offerings. For plan fiduciaries, it’s imperative to stay abreast of what’s available in the marketplace in order to have a prudent decision-making process regarding those products. Whether you already have a great relationship, or are starting to have concerns, it never hurts to ask: are you getting the most out of your retirement plan recordkeeper?

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