

PENSION PARTICIPANT KNOWLEDGE ABOUT PLAN FEES

Introduction

Participants in defined contribution plans pay billions of dollars annually in fees to fund managers for the management of their investments and may pay other fees related to costs associated with their participation in the plans. This Data Digest presents results of a survey that provide insights into pension participants' knowledge of the fees they pay for their 401(k) plans.

Knowledge about investment fees is important to pension participants because of the wide range in fees that are charged and because of the negative effect of fees on net rates of return. In the United States, fees charged pension participants in actual plans vary from 0.07 percent of assets for an S & P 500 stock index fund available to 401(k) participants in one plan up to more than 3.0 percent for an actively managed international stock fund. On a pension portfolio of \$100,000, these fees would range from \$60 a year for a pension entirely invested in the low fee S& P 500 stock index fund to \$3,000 a year for a pension entirely invested in the high fee international stock fund.

Survey

In November and December 2003, a survey was fielded for AARP by Southeastern Institute of Research, Inc. of Richmond, VA.¹ The universe surveyed was residents of the United States age 25 or older, with oversampling of the population age 50 and older. The survey sample was selected by a random digit dialing process to all households with telephone service living in the United States. The total sample size was 1,207 persons.

Survey Results

All survey respondents who participated in a 401(k) or similar defined contribution plan and held stocks, either directly or indirectly through mutual funds, were asked about their knowledge of the fees they paid. They were asked, "Do you know how much in

fees you are paying for holding those stocks in that plan, either as a percent of assets or as a total dollar amount?" The results are displayed in Table 1. The questionnaire provides three possible answers—"yes," "no," and "don't know." The questionnaire does not indicate what the distinction is between the last two negative responses, and we combine them as indicating a lack of knowledge as to the amount paid in fees. For all age groups examined, at least 75 percent of those holding stock in a defined contribution plan indicated that they did not know how much they were paying in fees at the time of the interview.

While the main point of Table 1 is its indication of the low level of knowledge about fees paid by pension participants, the table also presents information on gender differences in knowledge about fees. Males were less likely to self-report lack of knowledge of fees they paid than females (74 percent versus 86 percent).

As a follow-up question, those respondents who answered that they knew how much they were paying in fees at the time of the interview were asked how much that was, either as a percentage of their pension assets or in dollars. More than one-third of those respondents who had answered "yes" to the previous question either answered "don't know" or refused to answer the follow-up question (Table 2). This follow-up suggests that the "yes" responses in the previous question overstated the extent of knowledge. Only major demographic groups by size are examined in Table 2 because of the small number of observations of people answering "yes" to the first question. No results for groups with an unweighted base of less than 30 are reported.

Adjusting the original responses for this follow-up by combining the negative responses from the first and second questions, more than 80 percent of defined contribution pension participants would be

Table 1. Do you know how much in fees you are paying for the stocks held in your 401(k) plan, either as a percent of assets or as a total dollar amount? (Percent, except for Unweighted base)					
Response	Yes	No	Don't know	Refused	Unweighted base
Age 25-49	17	58	24	1	139
Age 50+	20	59	21	0	342
Age 50-64	18	62	20	0	257
Age 65+	25	53	22	0	85
Male	26	53	21	0	138
Female	14	65	21	0	204

Source: AARP Aging Indicator Survey 2003, fielded for AARP by Southeastern Institute of Research, Inc. of Richmond, VA.

Table 2. Do you know how much you currently are paying in fees (specifying that you know either the dollar amount or the amount as a percentage of assets)? (Percent, except for Unweighted base)					
Response	Dollar amount	Percentage	Don't know	Refused	Unweighted base
Age 50+	29	33	25	13	66
Male	32	31	25	12	36
Female	23	38	25	14	30

Note: The age group 25-49 is not reported in this table because its unweighted base is less than 30 observations.
Source: AARP Aging Indicator Survey 2003, fielded for AARP by Southeastern Institute of Research, Inc. of Richmond, VA.

categorized as self-reporting that they did not know how much they were paying in fees. Categorizing participants by gender, more than 80 percent of males and more than 90 percent of females self-reported that they did not know how much they were paying in fees.

Conclusions

The growth of defined contribution plans places an increased responsibility on participants for making financial decisions. For this reason, financial information and financial education have

become important aspects of retirement income policy. To make informed decisions concerning investment choices, participants need to know what fees they are paying. An older worker with a substantial amount accumulated in a 401(k) plan may pay thousands of dollars a year in fees charged against his plan assets. The data presented here suggest that participants generally do not know how much they are paying in fees on their 401(k) plans.

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ⁱ Weighting, response rates, and the full annotated questionnaire are available upon request from Sarah Zapolsky, Senior Research Advisor, AARP, 601 E Street NW, Washington, DC 20049, szapolsky@aarp.org.