

GAO

Report to the Chairman, Committee on  
Ways and Means, House of  
Representatives

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September 2009

# RETIREMENT SAVINGS

Better Information  
and Sponsor Guidance  
Could Improve  
Oversight and Reduce  
Fees for Participants



GAO

Accountability \* Integrity \* Reliability



Highlights of [GAO-09-641](#), a report to the Chairman, Committee on Ways and Means, House of Representatives

## Why GAO Did This Study

American workers increasingly rely on defined contribution (DC) plans like 401(k) plans and individual retirement accounts (IRA) for retirement income. Together with other DC plans—401(a), 403(b), and 457 plans—these accounts hold about \$7.1 trillion. As workers accrue earnings on their investments, they also pay a number of fees that may significantly decrease retirement savings over the course of a career.

GAO examined: (1) the types of fees charged to participants and investments of various DC plans; (2) how DC plan sponsor actions affect participant fees; (3) how fee disclosure requirements vary; and (4) the effectiveness of DC plan oversight. GAO reviewed laws and regulations and consulted with experts, federal officials, service providers, and six plan sponsors.

## What GAO Recommends

Congress should consider (1) amending ERISA to require sponsors to disclose fee information to facilitate comparisons, and (2) giving the Department of Labor (Labor) specific authority over certain plans. Also, GAO recommends that the Internal Revenue Service (IRS) develop guidance on sponsor involvement, collect additional data on 457(b) plans, and share more information with financial regulators. Labor and IRS agreed with our recommendations, although IRS stated that it will continue sharing information with regulators using its current methods.

View [GAO-09-641](#) or [key components](#). For more information, contact Barbara Bovbjerg at (202) 512-7215 or [bovbjergb@gao.gov](mailto:bovbjergb@gao.gov).

## RETIREMENT SAVINGS

### Better Information and Sponsor Guidance Could Improve Oversight and Reduce Fees for Participants

#### What GAO Found

Participants in DC plans and IRAs generally pay the same types of fees, regardless of the plan in which they are enrolled, such as investment management fees. However, participants in some plans are more likely to invest in products that may have higher fees. For example, we found that participants in 403(b) plans and individual IRAs are more likely to invest in products like individual variable annuities or retail mutual funds, which frequently charge more than other investments. According to experts, one reason for the different investments is that many 403(b) plan sponsors do not make group products available to participants.

DC plan sponsors generally take certain actions that decrease participants' fees. Sponsors can help reduce participants' fees by, for example, offering cheaper investment products in which participants may choose to invest, like low-cost mutual funds. Sponsors may also pool assets to obtain pricing advantages. 401(k) and 401(a) plan sponsors frequently pool participants' assets to realize lower fees in mutual funds, but sponsors of 403(b) plans often do not. Instead, many 403(b) plan sponsors keep sponsor involvement to a minimum, which limits the opportunities to pool assets and decrease fees.

Fee disclosure requirements vary depending on plan regulations and investment regulations. Sponsors of plans subject to Title I of the Employee Retirement Income Security Act of 1974 (ERISA)—which was enacted in part to protect the interests of employee benefit plan participants—are required to disclose certain documents to participants, which may or may not describe fees. For plans not subject to these laws, such as state and local government plans, some states impose disclosure requirements, and some do not. Fee disclosure requirements also vary based on the type of investment product in which participants invest. The Securities and Exchange Commission regulates some investment products, like mutual funds, while others are regulated by states' insurance agencies. Because different regulators require different disclosures, participants in DC plans and IRAs can invest in similar products but receive different information on fees.

Labor oversees disclosure for participants of certain DC plans, while IRS oversees tax laws that underlie all DC plans, but both lack information that could strengthen oversight. Labor is responsible for enforcing requirements for disclosure—which may include fees—and the requirement that fiduciaries for some plans must ensure reasonable fees, and has proposed regulations to improve fee disclosure. However, Labor does not have the specific authority to collect information to help ensure that sponsors of certain 403(b) plans continue to protect participants' interests. While IRS does not oversee fees or fee disclosure, IRS oversees DC plans' compliance with the tax code. IRS does not collect information to easily enforce 457(b) plans' contribution limits and detect violations that may reduce federal tax revenue. In addition, IRS and other regulators do not routinely share information with one another to use resources effectively and help enforce a rule requiring reasonable fees.

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# Contents

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<b>Letter</b>		<b>1</b>
	Background	3
	Participants in Different Plans and IRAs Pay the Same Types of Fees, but Investment Choices Can Affect Fee Amounts	14
	Certain Sponsor Actions Decrease Participants' Fees, but Some Sponsors Take Fewer Actions than Others	18
	Participants Receive Different Fee Information Depending on ERISA Coverage and Regulator, Limiting Participants' Ability to Compare Investment Options	24
	Oversight of Fees and DC Plans Will Likely Improve with Recent Regulations, but IRS and Labor Still Lack Information That Could Strengthen Oversight	30
	Conclusions	37
	Matters for Congressional Consideration	38
	Recommendations	39
	Agency Comments and Our Evaluation	39
<b>Appendix I</b>	<b>Objectives, Scope, and Methodology</b>	<b>41</b>
<b>Appendix II</b>	<b>Comments from the Internal Revenue Service</b>	<b>44</b>
<b>Appendix III</b>	<b>Comments from the Department of Labor</b>	<b>48</b>
<b>Appendix IV</b>	<b>Characteristics of DC Plans and IRAs</b>	<b>50</b>
<b>Appendix V</b>	<b>GAO Contact and Staff Acknowledgments</b>	<b>52</b>
<b>Tables</b>		
	Table 1: Employers Eligible to Establish DC Plans and IRAs	6
	Table 2: Estimated Number of DC Plans and Participants, 2007	7
	Table 3: Tax-Deferred Contribution Limits for DC Plans, 2009	7
	Table 4: Opportunities for Rollovers and Transfers of Assets among Plans and IRAs	9

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Table 5: Regulators That Oversee DC Plans by Type of Employer	11
Table 6: Fees Associated with Three Common Investment Products	14
Table 7: Administrative Fees Associated with Plans	16
Table 8: Required Disclosure Documents to All Participants in Plans Subject to Title I of ERISA	24
Table 9: Required Fee Disclosure Information, by Regulator	28
Table 10: Estimated Total Assets for DC Plans and IRAs, 2008	50
Table 11: Estimated Contributions to DC Plans, 2007	50
Table 12: Estimated Contributions to Individual IRA Accounts, SEP, and SIMPLE Accounts, 2006	51
Table 13: Estimated Number of Individual IRA Account Owners and Individuals Contributing to Employer-Sponsored IRAs, 2006	51

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## Figures

Figure 1: Effect of a 1-Percentage Point in Higher Annual Fees on a \$20,000 DC Plan Balance Invested over 20 Years	21
Figure 2: Oversight of Fee Information Disclosed to Retirement Plan Participants	29
Figure 3: IRS Form W-2, Wage and Tax Statement, with Emphasis on Box 12, for Retirement Plan Contributions	35
Figure 4: Form W-2 Instructions	35

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## Abbreviations

CIF	collective investment funds
DB	defined benefit
DC	defined contribution
ERISA	Employee Retirement Income Security Act
ESOP	employee stock ownership plan
IRA	individual retirement account
I.R.C.	Internal Revenue Code
IRS	Internal Revenue Service
Labor	Department of Labor
MOU	memorandum of understanding
NAIC	National Association of Insurance Commissioners
OCC	Office of the Comptroller of the Currency
RFP	request for proposal
SEC	Securities and Exchange Commission
SIMPLE	Savings Incentive Match Plan

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United States Government Accountability Office  
Washington, DC 20548

September 4, 2009

The Honorable Charles B. Rangel  
Chairman  
Committee on Ways and Means  
House of Representatives

Dear Mr. Chairman:

American workers increasingly rely on 401(k) plans and individual retirement accounts (IRA) for retirement income. Besides 401(k) plans, lesser-known defined contribution (DC) plans—plans in which retirement savings are based on contributions and the performance of the investments in individual accounts—can provide opportunities for employers and employees to make tax-deferred contributions to retirement savings accounts. These other DC plans include 401(a),<sup>1</sup> 403(b), 457(b), and 457(f) plans. More than 49 million U.S. workers participate in employer-sponsored DC retirement plans, and 50 million have IRAs. Together, these retirement savings accounts hold about \$7.1 trillion in assets.

In recent years, policymakers have focused on the oversight of 401(k) plans and the fees charged to 401(k) plan participants. Fees are one of many factors—such as the historical performance and investment risk for each plan option—participants should consider when investing in a retirement plan because fees can significantly decrease retirement savings over the course of a career. In 2006, we reported that even a small fee deducted from a worker's assets annually could represent a large amount of money years later had it remained in the account to be reinvested and that 401(k) plan participants do not always receive information on the fees they are being charged.<sup>2</sup> Given the current economic environment, regulators, plan sponsors, and workers have reason to be increasingly worried about the performance of their retirement accounts.

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<sup>1</sup>In this report, we refer to DC plans, besides 401(k) plans, that qualify for a tax deferral under Internal Revenue Code section 401(a) as “401(a) plans.”

<sup>2</sup>GAO, *Private Pensions: Changes Needed to Provide 401(k) Plan Participants and the Department of Labor Better Information on Fees*, [GAO-07-21](#) (Washington, D.C.: Nov. 16, 2006).

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The types of fees charged to participants of 401(k) plans have led to questions about what types of fees are charged to participants in other types of DC plans and IRAs and whether participants across DC plans are getting the same information disclosed about fees to them. Similarly, questions have also been raised about how other types of DC plans are overseen. In light of the uncertainty about fees, disclosure to participants, and oversight of these plans and IRAs, the Chairman of the House Committee on Ways and Means asked GAO to examine other 401(a) plans, 403(b) plans, 457 plans, and IRAs to address the following questions: (1) How do the types of fees charged to participants and investments of various DC plans differ? (2) How do DC plan sponsor actions affect participants' fees? (3) How do fee disclosure requirements vary? and (4) How effective is the oversight of DC plans?

To explain how the types of fees charged to participants and investments in various DC plans differ, we consulted with a number of academic, industry, and association experts and obtained fee information from selected service providers. To determine how DC plan sponsor actions affect participant fees, we consulted with industry experts, as well as 11 service providers and 6 plan sponsors. To outline how fee disclosure varies by plan, we interviewed staff from relevant federal agencies, state insurance regulators, and national experts. We also conducted structured interviews with 11 service providers. To describe the effectiveness of DC plan oversight, we interviewed regulators and reviewed documentation, laws, and regulations.

We conducted this performance audit from June 2008 through September 2009 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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## Background

Pension plans are classified either as defined benefit (DB) or as defined contribution (DC) plans.<sup>3</sup> The benefits participants receive from DC plans are based on the amount of money in their individual accounts. The funds in these accounts can fluctuate over time as participants and employers make contributions and as the value of the investments rises and falls.

### Role of Employer and Participants in DC Plans

Employers and participants both play roles in a DC plan. Employers generally establish a plan, becoming the plan's "sponsor." Sponsors' roles vary depending on how the sponsor chooses to operate the plan or the type of plan. Some sponsors activities include:

- Contributing to participants' accounts;
- Deciding upon the investment options from which participants may choose;
- Processing participants' contributions to send to investment service providers;
- Keeping track of participants' investment choices, contributions, and other record-keeping; and
- Paying for the costs associated with maintaining the plan.

Participants' role in DC plans can also vary significantly depending on how the sponsor operates the plan, and the type of plan. Some participant activities include:

- Contributing to individual accounts;
- Choosing among investment options;
- Transferring assets to a different plan; and
- Paying for costs associated with participating in the plan.

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<sup>3</sup>Generally, DB plans promise to provide a fixed level of monthly retirement income that is based on salary, years of service, and age at retirement regardless of how the plan's investments perform.



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## Different types of DC plans

There are several types of DC plans, each one named for a section of the Internal Revenue Code (I.R.C.):

- In “401(a) plans,” participants qualify for an income tax deferral under section 401(a) of the I.R.C. One type of 401(a) plan is a money purchase plan. Sponsors of these plans are required to make specified contributions to participants’ accounts. Profit sharing plans can also be created under section 401(a). These plans are similar to money purchase plans, but sponsors can decide each year whether or not to make a contribution.<sup>4</sup>
- 401(k) plans are a type of 401(a) plan, typically a profit-sharing plan. Both sponsors and participants are permitted pre-tax contributions in 401(k) plans.
- 403(b) plans are similar to 401(k) plans, in that they typically permit both sponsors and participants to make pre-tax contributions, but are designed for public education entities and tax-exempt organizations that operate under I.R.C. §501(c)(3). Participants in these plans are generally limited to investing in annuity contracts issued by insurance companies and custodial accounts invested in mutual funds.<sup>5</sup>
- 457(b) plans are also like 401(k) and 403(b) plans in that they typically permit both sponsors and participants to make pre-tax contributions. 457(b) plans can be one of two types. 457(b) governmental plans are usually open to all employees at a state or local government, and are similar to some other DC plans in that contributions are set aside for the participants in a trust. In contrast, 457(b) tax-exempt plans usually limit participation to a group of managerial or highly compensated employees, and are unfunded. That is, the amounts deferred must remain the sole property of the tax-exempt sponsor, subject only to the claims of general creditors, until the amounts are made available to the participant or beneficiary.
- 457(f) plans are typically designed for highly compensated employees. 457(f) plans are generally “unfunded;” that is, sponsors do not have to set

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<sup>4</sup>Stock bonus plans, which are similar to profit sharing plans except that sponsors’ contributions generally take the form of stock in the sponsors’ company, also qualify under I.R.C. section 401(a). Employee stock ownership plans (ESOP) can be a type of stock bonus plan.

<sup>5</sup>Churches may also establish 403(b) plans. Participants in church plans have additional investment options.

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aside assets for participants. Instead, sponsors make a promise to pay participants some amount at a later date.<sup>6</sup>

In addition to DC plans, individuals can save for retirement in traditional IRAs, and employer-sponsored IRAs—Savings Incentive Match Plans for Employees (SIMPLE) and Simplified Employee Pension (SEP). Traditional IRAs allow eligible individuals to make tax-deductible contributions and accumulate tax-deferred investment earnings. Distributions from these accounts are generally subject to tax.<sup>7</sup> Another type of individual IRA, the Roth IRA, allows eligible individuals to make after-tax contributions; distributions are then generally tax-free. SIMPLE IRAs allow small employers to either match participating employee contributions or to contribute a fixed percentage of all eligible employees' pay.<sup>8</sup> SEP IRAs allow employers of any size to make voluntary tax deductible contributions into traditional IRAs for themselves and their employees. Contributions to all IRAs may not exceed certain limits.

As shown in table 1, different types of employers are eligible to establish various types of DC plans and IRAs. For example, all types of employers can establish a 401(a) plan or an employer-sponsored IRA, but only state and local governments can establish a 457(b) governmental plan.

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<sup>6</sup>Both 457(f) and 457(b) plans of tax-exempt organizations are sometimes referred to as "top hat" plans.

<sup>7</sup>Taxpayers ineligible for the deduction can make nondeductible contributions to take advantage of the deferral on investment earnings. Distributions are partially taxable. Distributions received before age 59½ are subject to an additional 10-percent income tax unless they meet certain requirements or are used for specific purposes, including the purchase of a first home or for higher education expenses.

<sup>8</sup>Employers must have 100 or fewer employees who earned \$5,000 or more during the preceding calendar year.

**Table 1: Employers Eligible to Establish DC Plans and IRAs**

	Private company	Tax-exempt organization	Church	Public education entity (school district)	State and local governments
401(a)	Yes	Yes	Yes	Yes	Yes
401(k)	Yes	Yes	Yes	No	No <sup>b</sup>
403(b)	No	Yes <sup>a</sup>	Yes	Yes	No, except public education entities
457(b) governmental	No	No	No	Yes	Yes
457(b) Tax-exempt	No	Yes	No <sup>c</sup>	No	No
457(f)	No	Yes	No	Yes	Yes
Employer-sponsored IRA	Yes	Yes	Yes	Yes	Yes
Traditional IRA	N/A	N/A	N/A	N/A	N/A

Source: IRS, GAO analysis.

<sup>a</sup>Only tax-exempt organizations that operate under I.R.C. §501(c)(3) are eligible to establish a 403(b) plan.

<sup>b</sup>The Tax Reform Act of 1986 prohibited state and local governments from establishing new 401(k) plans. However, 401(k) plans established by state and local governments before May 6, 1986, were “grandfathered,” and therefore permitted to maintain their plan as a 401(k) plan and are not subject to Title I of ERISA.

<sup>c</sup>Church plans that include employees may have 457(b) tax-exempt plans.

DC plans and IRAs are important vehicles for Americans’ retirement savings. As shown in table 2, DC plans have about 47 million participants. Among DC plans, 401(k) plans have the most participants with approximately 37 million. Together, DC plans and IRAs held about \$6.7 trillion in assets at the end of 2008. Participation in plans has increased over time; in 2005, the most recent year for which data is available, about 33 percent of workers participated in a DC plan and about 23 percent had an IRA account, while 12 percent participated in both. For more information on contributions and assets in DC plans and IRAs, as well as information on IRA account holders, see appendix IV.

**Table 2: Estimated Number of DC Plans and Participants, 2007**

	Number of plans (thousands)	Number of participants (thousands)
401(k)	624	37,492
403(b)	88	6,521
457(b) governmental and tax-exempt	30	3,476

Source: IRS.

Note: Data on 401(a) plans and 457(f) plans are not available. The data in this table come from a database taken from annual Form W-2 filings. The data are estimated and should not be compared to the data in other tables. In addition, these estimates differ from estimates generated from annual filings compiled by Labor because the collection methods are different.

## Contribution Limits

DC plans that permit participants to defer income have varying limits on the amount participants can defer annually. For example, in 2009, the contributions on which participants can defer income taxes are limited to \$16,500 for 401(k) and 403(b) plans, as shown in table 3. Contributions from 401(k) plan and 403(b) plan participants and sponsors together may not exceed the lesser of 100 percent of compensation or \$49,000. For 457(b) plans, deferrals cannot exceed \$16,500 in 2009.<sup>9</sup>

**Table 3: Tax-Deferred Contribution Limits for DC Plans, 2009**

	Individual contribution limit	Sponsor contribution limit	Sponsor and participant together contribution limit
401(a)	N/A	N/A	The lesser of 100% of compensation or \$49,000
401(k)	Up to \$16,500	N/A	The lesser of 100% of compensation or \$49,000
403(b)	Up to \$16,500	N/A	The lesser of 100% of compensation or \$49,000
457(b) Governmental	N/A	N/A	The lesser 100% of compensation or \$16,500
457(b) Tax-exempt	N/A	N/A	The lesser 100% of compensation or of \$16,500

<sup>9</sup>457(f) plans are generally different from other plans in that they are unfunded and have no deferral limits. Unlike most plans, deferrals are generally not required to be set in a retirement account or a trust. Thus, the plan is “unfunded.” Instead, participants and sponsors can agree in advance how much individuals will receive from the sponsor pending the fulfillment of certain terms, such as 5 years of service. Until the terms are met, the assets must remain in the possession of the employer and must be subject to a “substantial risk of forfeiture.” Otherwise, the assets generally become taxable in the year in which there is no substantial risk of forfeiture.

	Individual contribution limit	Sponsor contribution limit	Sponsor and participant together contribution limit
457(f)	Unlimited	Unlimited	Unlimited
Employer-sponsored IRA	SIMPLE : Up to \$11,500 SEP: N/A	SIMPLE: Either 100 percent match of employee contributions up to 3 percent of employee compensation; or contribute 2 percent of each eligible employee's compensation <sup>a</sup>  SEP: Up to 25% of employee's annual compensation, not to exceed \$49,000	SIMPLE: N/A SEP: N/A
Traditional IRAs <sup>b</sup>	Up to \$5,000	NA	N/A

Source: IRS.

<sup>a</sup>SIMPLE sponsors must choose to meet either of the two contribution criteria. However, employers choosing the first option are permitted to reduce the match to as low as 1 percent of compensation in any 2 of 5 years.

<sup>b</sup>Yearly contribution amounts are subject to limits based on income, pension coverage, and filing status.

## Rollover and Transfer Options

Most DC plans permit participants to move their assets out of their current plan under certain circumstances without being subject to income tax. Participants in most plans may “roll over” their assets into an IRA or into another type of plan without being subject to income taxes if they follow certain rules. Rollovers can occur when participants experience certain specified events—such as leaving their job or death—when their assets would otherwise be distributed. As shown in table 4, participants in 401(a), 401(k), 403(b), and 457(b) governmental plans may roll over their assets to any of these same types of plans or to IRAs. In contrast, participants in 457(b) tax-exempt and 457(f) plans may not roll over their assets into other plans or IRAs.

Participants may also “transfer” their assets to other similar plans under certain conditions. Transferred assets are also not subject to income tax. For 403(b) and 457(b) governmental plans, participants may transfer their assets to another like plan, if the plan sponsor accepts such transfers, as shown in table 4. Participants in 457(b) tax-exempt and 457(f) plans generally have no assets.<sup>10</sup>

<sup>10</sup>The ability to transfer or rollover assets is not affected by the product in which assets are invested. For example, participants who are invested in annuities and participants who are invested in mutual funds will be subject to the same transfer and rollover rules and limitations.

**Table 4: Opportunities for Rollovers and Transfers of Assets among Plans and IRAs**

	<b>Rollovers</b>	<b>Plan-to-Plan Transfers</b>
401(a)	401(a), 403(b) annuities, 401(k), 457(b) governmental, and IRAs	Other 401(a) or 401(k) plans
401(k)	401(a), 403(b) annuities, 401(k), 457(b) governmental, and IRAs	Other 401(a) or 401(k) plans
403(b)	401(a), 403(b) annuities, 401(k), 457(b) governmental, and IRAs	Other 403(b) plans
457(b) governmental	401(a), 403(b) annuities, 401(k), 457(b) governmental, and IRAs	Other 457(b) governmental plans
457(b) tax-exempt	No	N/A <sup>a</sup>
457(f)	No	N/A
Traditional IRA	401(a), 403(b) annuities, 401(k), 457(b) governmental, and IRAs	Other IRAs

Source: IRS.

<sup>a</sup>Participants in 457(b) tax-exempt plans may transfer their assets to other 457(b) tax-exempt plans. However, these plans are generally unfunded; therefore, they have no assets to transfer.

## Oversight of DC plans and IRAs

All DC plans and IRAs are subject to various provisions of the Employee Retirement Income Security Act of 1974 (ERISA), which was generally enacted to protect the interests of employee benefit plan participants and their beneficiaries. ERISA sets minimum standards for most pension plans in private industry to protect participants.

Title I of ERISA, which is generally enforced by the Department of Labor (Labor), establishes guidelines that help protect participants. For example, Title I of ERISA requires sponsors to disclose to participants certain information concerning the plan. Title I also establishes standards of conduct for plan fiduciaries, which are usually plan sponsors but can also include other service providers.<sup>11</sup> Fiduciaries must act for the exclusive benefit of plan participants and beneficiaries, rather than for their own or another party's gain. This means that fiduciaries must avoid conflicts of interest and act prudently.

<sup>11</sup>Under ERISA, a person is generally a fiduciary with respect to a plan, to the extent they exercise any discretionary authority or control over plan management or any authority or control over the management or disposition of plan assets, render investment advice respecting plan money or property for a fee or other compensation (or has the authority or responsibility to do so), or have discretionary authority or responsibility for plan administration. 29 U.S.C. § 1002(21)(A).

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Some DC plans are not subject to Title I of ERISA and thus are not overseen by Labor.

- Plans that are sponsored by state and local governments are not subject to Title I of ERISA.
- Labor defined a “safe harbor” for 403(b) plans sponsored by tax-exempt organizations. Sponsors that follow the safe harbor guidelines are not considered subject to Title I of ERISA because the plan is considered not to have been “established or maintained by an employer.” Sponsors of these plans must restrict their involvement in the plan to certain actions, or they will become subject to Title I of ERISA.
- Plans that are designed for highly compensated executives are generally excluded from certain parts of Title I of ERISA.
- Certain religious organizations may establish different kinds of retirement plans, but they are generally exempt from Title I of ERISA.<sup>12</sup>

Regardless of whether or not plans are subject to Title I of ERISA, all DC plans are subject to the I.R.C. and are overseen by IRS. The I.R.C. contains rules to qualify plans for tax deferrals and deductions, such as generally requiring plans to cover rank-and-file workers, not only highly-compensated employees.<sup>13</sup> The IRS enforces these provisions.

State and local governments can also play a role in overseeing DC plans. State and local governments may establish ERISA-like laws for state and local government plans. For example, some state governments require that certain plan sponsors adhere to standards of conduct for fiduciaries. Table 5 outlines how different DC plans are overseen by Labor, IRS, and state and local governments.

IRS and Labor share responsibility for overseeing IRAs. IRS has primary responsibility for tax rules governing how to establish and maintain any IRA. Labor has sole responsibility for overseeing ERISA’s fiduciary standards for employer-sponsored IRAs. Unlike employer-sponsored IRAs,

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<sup>12</sup>These “church plans” can be 401(a), 401(k), or 403(b) plans.

<sup>13</sup>State and local government plans are exempt from some of these requirements.

individual IRAs are not subject to Title I of ERISA and are generally not overseen by Labor.<sup>14</sup>

Table 5: Regulators That Oversee DC Plans by Type of Employer

	Subject to Title I of ERISA		Not subject to Title I of ERISA		
	Private companies	Tax-exempt organizations	State and local governments	Churches	Tax-exempt organizations under Labor’s 403(b) safe harbor
IRS	Yes	Yes	Yes	Yes	Yes
Labor	Yes	Yes <sup>a</sup>	No	No	No
State and local governments	No	No	Yes	No <sup>b</sup>	No <sup>b</sup>

Source: GAO analysis.

<sup>a</sup>Tax-exempt sponsors of 457(b) plans and 457(f) plans designed for highly-compensated employees are exempt from most of ERISA’s requirements such as participation and fiduciary responsibility. These plans are subject to a few provisions of Title I of ERISA relating to reporting, disclosure, administration, and enforcement.

<sup>b</sup>Some states may have laws that affect aspects of these plans, such as contract remedies.

Different regulators oversee different investment options available to DC plans and IRAs

- DC plans and IRAs hold assets in a range of investments, which, in turn, are regulated by different entities.
- *Mutual Funds.* A mutual fund is a pooled investment in a portfolio of securities, managed by a professional investment advisor. Investors buy shares in the fund, which represents an indirect ownership interest in the fund’s securities. Types of mutual funds include: stock or equity, bond or fixed-income, and money market. Mutual funds are sold in different “share classes” that each offer the same gross returns, but with different fee structures that result in different net returns. For example, in one share class, mutual fund shareholders may pay a “sales charge” when they purchase shares, while in another share class, they may pay a recurring charge deducted from fund assets to cover marketing costs. Mutual funds are generally regulated by the Securities and Exchange Commission (SEC), which requires funds to disclose fees and to inform investors of products’ potential risks.

<sup>14</sup>Labor and IRS also work together to oversee rules regarding IRA prohibited transactions; generally, Labor has interpretive jurisdiction and IRS has certain enforcement authority.



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- *Annuities.* An annuity is a contract between a plan participant or sponsor and an insurance company, under which the participant makes a lump-sum payment or a series of payments and the insurance company provides a payout for an agreed-upon span of time. Annuities may be purchased for groups or for individuals and can be fixed or variable. Fixed annuities guarantee a minimum interest rate on assets while the account is growing and also guarantee periodic payments after the annuity is claimed. Variable annuities are also insurance products and also guarantee periodic payments to participants. However, the amount of those payments depends in part on the value of the investments that underlie the account, which are typically mutual funds. States regulate insurance companies that provide fixed annuities. State regulators generally supervise insurance sales and marketing practices and policy terms and conditions to ensure that consumers are treated fairly when they purchase insurance products and file claims. For variable annuities, state agencies generally regulate the insurance contract that “wraps” around the investment options. If the underlying investment options are registered securities, the investments are regulated by SEC. Also, if variable annuities are sold to participants within certain retirement plans, the contracts are also regulated by SEC.<sup>15</sup>
  - *Collective investment funds (CIF).* CIFs are trusts managed by a bank or trust company that pool investments of retirement plans or other large institutional investors. These products are typically not available to individual investors. The federal agencies charged with oversight of banks regulate CIFs and other bank investment products, primarily the Federal Reserve Board, Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation.

Fees charged to participants in DC plans and IRAs

As participants in DC plans and IRAs accrue earnings on their investments, they also pay a number of fees, including expenses, commissions, or other charges associated with investments and plan operation. Fees are one of many factors participants should consider when choosing among the investment options a plan offers because fees can significantly decrease retirement savings over the course of a career. Even a small fee deducted from a participant’s assets annually could represent a large amount of money years later had it remained in the account to be reinvested.

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<sup>15</sup>This report does not discuss annuities that are purchased to pay benefits when a pension plan is terminated or when an annuity is purchased for a terminating participant as a distribution from the plan.

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Participants and sponsors pay investment fees charged by companies that manage mutual funds or other investment products for all services related to operating the fund. For example, a management fee covers the cost of selecting a mutual fund's portfolio of securities and managing the fund. After investment fees, administrative fees generally account for the next largest portion of plan fees. These fees cover the cost of operating the plan, such as keeping records of all participants' contributions and transactions.

The amount of fees charged to participants for investments may depend on whether the plan invests in products that are "institutional" or "retail." Generally, "institutional" investments are only sold to investors with large pools of assets and charge lower fees than retail products sold by the same service provider. "Retail" investments are available to any individual, and typically have higher fees. For example, individual investors typically purchase retail mutual funds, whereas large groups of investors, like certain DC plans, can pool their assets to purchase the same mutual funds with a volume discount depending on the size of the asset pool.

Service providers charge fees for administering investment and administrative services to plans in two ways. Under a "bundled" arrangement, the sponsor hires one company that provides the full range of services directly or through subcontracts. A bundled service provider may, for example, provide all record-keeping and investment services, as well as communications with participants. Under an "unbundled" arrangement, the sponsor uses a combination of service providers. Sponsors can also provide some of the administrative services themselves, such as record-keeping, but can only charge fees for charges the sponsor incurred directly.

Participants in Different Plans and IRAs Pay the Same Types of Fees, but Investment Choices Can Affect Fee Amounts

Participants Generally Pay the Same Types of Fees, Regardless of the DC Plan

Service providers told us that plan participants generally pay the same types of fees regardless of the DC plan in which they are enrolled. Several of the service providers we interviewed, who serve all types of DC plans, reported that they charge the same types of fees to participants of all different DC plans. For example, representatives of a company that services both 401(a) plans and 403(b) plans told us that participants in both plans pay investment management and record-keeping fees, as shown in table 6 and table 7.<sup>16</sup>

Table 6: Fees Associated with Three Common Investment Products

Fee description	Fixed annuity	Variable annuity	Mutual fund
All-inclusive annual fee imposed on the value of total assets in an account.	N/A	Wrap fee	N/A
Fee charged upon investing that reduces the initial investment.	N/A	Sales load	Sales charge or sales load
Fee charged upon redemption or when the product is sold, or when the contract is ended.	Surrender or withdrawal charges	Deferred sales load or surrender fee	Deferred sales charge or deferred sales load or redemption fee
Fee charged for any exchange or transfer of interest from the fund to another fund or to another investment company.	N/A	Exchange fee	Exchange fee

<sup>16</sup> 401(a), 401(k), and 457(b) governmental plans generally require that contributions to participants' accounts be set aside in a trust or held in an insurance contract. Service providers establishing and maintaining a trust to hold plan assets sometimes charge a trustee fee, usually a relatively small fee to maintain the trust. Sponsors of 403(b) plans are not required to hold assets in a trust, but participants investing in mutual funds must have custodial accounts. Sponsors or participants are sometimes charged for these custodial services, which are similar to charges for trustee services.

<b>Fee description</b>	<b>Fixed annuity</b>	<b>Variable annuity</b>	<b>Mutual fund</b>
Flat dollar amount that includes any contract, account, or similar fee imposed on contract-owner accounts on any recurring basis.	Contract fee	Contract fee	Account fee
Fee to compensate the insurance company for various risks it assumes under the annuity contract.	N/A	Mortality and expense risk fee	N/A
A fee that is charged by an advisor, often a pension consultant, hired to help the plan sponsor select funds for the plan and to monitor investments.	N/A	Investment consulting fee	Investment consulting fee
A fee to cover the cost of selecting a mutual fund's portfolio of securities and managing the fund.	N/A	Management fee	Management fee
Fee for servicing of the accounts, such as providing statements, reports, dispersing dividends, as well as custodial services.	N/A	Administrative fee	Administrative fee
Fee related to marketing and compensating brokers to sell the fund.	N/A	Distribution (12b-1 fee)	Distribution (12b-1 fee)
A charge deducted from each premium paid.	Percentage of premium charge	N/A	N/A

Source: GAO analysis.

Arrangements between DC plan sponsors and service providers may affect the types of fees charged. Sponsors can choose different service arrangements that may carry different types of fees, particularly bundled or unbundled services. Sponsors that choose a bundled arrangement may pay a smaller number of separate fees because service providers charge a consolidated fee for all services. For example, sponsors that hire a single service provider for all administrative services may pay a single fee for record-keeping, legal services, and accounting, while sponsors that have unbundled arrangements may be charged separate fees for each service. As shown in table 7, a range of administrative fees can be charged in unbundled arrangements.

**Table 7: Administrative Fees Associated with Plans**

Fee type	Fee description
Record-keeping fee	A fee that is usually charged by a service provider to set up and maintain the plan. This fee can cover a variety of activities such as enrolling plan participants, processing participant fund selections, preparing and mailing account statements, and other related administration activities.
Communication fee	A fee to cover the cost of educating participants about the plan such as providing participants with access to toll-free phone services, Internet service, and ongoing educational seminars.
Custodial or trustee fee	A fee that is charged by an individual, bank, or trust company to securely maintain plan assets.
Audit fee	A fee that is imposed by a service provider in connection with the annual audit that is required of ERISA-covered plans with more than 100 participants.
Legal fee	A fee that is charged by an attorney or law firm to provide legal support for administrative activities, such as ensuring the plan is in compliance with ERISA (by preparing forms like the Form 5500 or nondiscrimination testing) or representing the plan in a divorce settlement.
Transactional fees	Fees charged on an individual basis such as loan origination, loan maintenance, and distribution fees.

Source: GAO analysis.

Service providers also told us that traditional IRA account owners generally pay the same types of investment fees as DC plan participants. IRA account owners pay the same fees for investment products that any individual investor would pay, like sales loads or surrender charges. Investment service providers can charge IRA account owners a trustee fee to cover the administrative costs of managing the account, similar to a record-keeping fee or a custodial fee. Individual IRA account owners are not generally charged fees associated with plan compliance, like fees to cover the costs of ERISA-required annual reports.

## Participants in 403(b) Plans and IRAs More Often Invest in Products That Can Have Higher Fees Than Participants in Other DC Plans

403(b) plan participants and IRA account owners are more likely than participants in other DC plans to invest in products that can have higher fees than other products, such as variable annuities. Experts we interviewed said that variable annuities generally have higher fees than other products such as mutual funds because variable annuities charge investment fees as well as fees associated with the insurance portion of the product to cover the risk associated with providing certain guarantees, such as annuity rights or death benefits. As shown in table 6, variable annuity service providers typically charge fees for the underlying mutual funds, and they also often charge “mortality and expense” fees to cover the risk associated with providing guaranteed payments and minimum death benefits. In contrast, equities, and mutual funds have no such insurance guarantees; therefore, investing in these products can result in lower fees.

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In addition, 403(b) plan participants invest in individual investment products and mutual funds more often than participants in other plans, according to industry experts; these individual products generally have higher fees than group products. Employers may choose to have their 403(b) plans invest in group or individual annuities. Individual annuities represent a contract between a single participant and the service provider. The terms, fees, and record-keeping for each contract are established separately for each participant. In contrast, when participants enter the group annuity, they enter into the prearranged contract established by the plan sponsor. The sponsor can negotiate with the annuity service provider for lower fees and choose the options to be made available to participants. Similarly, retail mutual funds are available to investors with relatively low assets and usually have higher fees, whereas institutional mutual funds under the same service provider often have lower fees because investors with large pools of assets can obtain pricing advantages.

Experts told us that 403(b) plan participants may invest in individual annuities and mutual funds more often than participants in other plans for several reasons. First, according to Labor, 403(b) plans are different from other types of DC plans because individuals often have a more central role in choosing investment options. Like IRAs, many 403(b) plans operate with a one-to-one relationship between each participant and service provider. For example, the sponsors of some 403(b) plans simply send participants' contributions to the designated financial service provider.

Participants in 403(b) plans also tend to invest in individual variable annuities because more annuity providers market directly to 403(b) plan participants than mutual fund providers. Experts we interviewed told us that annuity sales staff commonly visit school districts and market directly to participants, while mutual fund sales staff rarely do so.

Furthermore, 403(b) plan participants may choose annuities more often than other investment options because some states have laws in place that facilitate the marketing of annuity products. According to experts, states with certain laws generally require sponsors of public school 403(b) plans to permit any service provider that meets certain criteria the opportunity to receive contributions. According to one expert, there are at least a handful of such states, including California and Texas. Sponsors of public school 403(b) plans in California and Texas generally cannot limit the number of options available to participants, but instead must permit qualified service providers to be included as an option to participants. According to experts we interviewed, annuity service providers tend to be the most frequently listed among the plan options.

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Like 403(b) plan participants, individual IRA account owners are more likely to invest in “retail” products than participants in other DC plans. IRA account assets are usually too low to be eligible for products typically reserved for high-volume clients, like collective investment funds, which generally have lower fees. In fact, one expert explained that it is common for individuals rolling over their assets from a DC plan into an IRA to see an increase in investment fees. This change occurs because individuals no longer have the group’s bargaining power to obtain lower-cost investment products.

In contrast to participants in 403(b) plans and IRAs, participants in 401(a), 401(k), and 457(b) governmental plans are more likely to invest in institutional mutual funds or group annuity products than retail mutual funds or individual annuities. Sponsors of 401(a), 401(k), and 457(b) governmental plans often pool assets and are able to purchase institutional products. Sponsors of 457(b) governmental plans also more frequently pool assets to invest in group annuity products, which can have lower fees than individual annuity products.<sup>17</sup>

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## Certain Sponsor Actions Decrease Participants’ Fees, but Some Sponsors Take Fewer Actions than Others

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### Certain Sponsors’ Actions Decrease DC Plan Participants’ Fees

A plan sponsor can take several actions to decrease DC plan participants’ fees. One way sponsors can help reduce participants’ fees is by offering relatively low-cost investment products in which to invest. For example, sponsors can offer low-cost mutual funds in addition to offering other products. Sponsors can also decrease participants’ fees by offering them the mutual fund share class that gives participants an opportunity to pay

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<sup>17</sup>Assets in 457(b) tax-exempt and 457(f) plans for highly compensated executives do not have to be invested. These plans are “unfunded,” that is, they are not set aside in an account for the participant, so in some cases, assets may not be invested at all.

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lower fees. Because each share class has the same gross return but different fee structures, sponsors of certain plans can evaluate the options to offer the share class most likely to reduce participants' fees. For example, owners of A class shares may pay fees when participants purchase shares, whereas owners of B class shares may pay fees when participants sell shares. Unlike owners of A and B class shares, owners of institutional class shares may pay very low or no fees when participants buy or sell shares.<sup>18</sup>

Sponsors may also decrease fees charged to participants by combining or pooling assets to access certain investment products, reduce fees, or negotiate with service providers. For example:

- Some investment products are available only to large-size investors, like collective investment funds. These “institutional” products often have lower fees than other “retail” investments.
- Other investment products are available to all types of investors, but offer lower fees for higher volume investments. For example, mutual funds often provide “breakpoints”—the designated dollar amounts at which management fees are reduced—for investors with higher volume.
- For annuity products, sponsors with pooled assets can negotiate terms and fees for group variable annuities that individuals typically cannot.
- Record-keeping service providers are likely to charge less per participant for a group of participants than for individual participants because pooling assets results in “economies of scale,” or efficiencies gained through higher volume.

Sponsors can also issue a request for proposal (RFP) to lower costs and decrease fees charged to participants. In response to an RFP, vendors submit bids describing their services and fees to the sponsor. Sponsors may then choose vendors who meet their participants' needs and may choose vendors with lower fees. For example, one expert told us that a statewide plan reduced total participant fees significantly because they issued an RFP and chose service providers with lower fees.

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<sup>18</sup>Institutional shares are only sold to larger investors, including 401(k) plans.

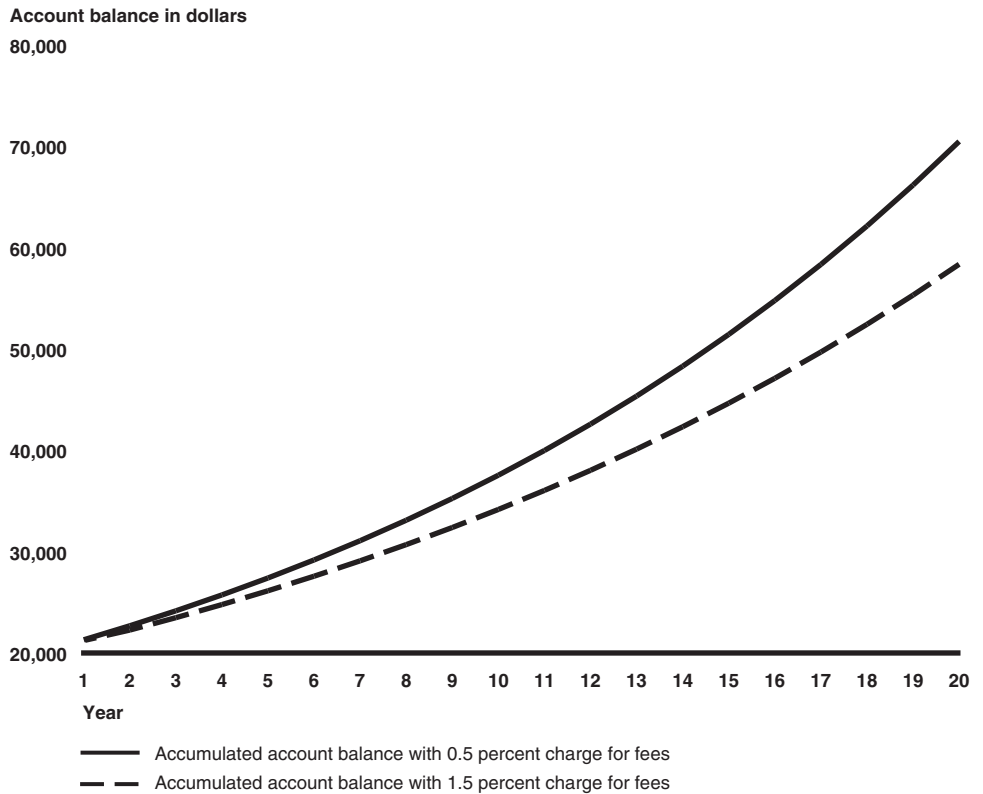


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Some sponsors may take actions that increase fees, such as offering optional features. For example, to provide participants with the option of taking out a loan against plan assets, sponsors may incur compliance and administrative costs associated with making sure loan amounts do not exceed limits set by IRS. These costs can be passed on to participants. Sponsors may also pass on higher investment costs to participants if an investment option has additional features. For example, service providers may charge an additional fee to give participants the option to convert a 401(k) plan account balance into a retirement annuity.

Lower fees benefit plan participants because they can significantly increase long-term retirement savings. As shown in figure 1, even a relatively small annual fee taken from a worker's assets represents a large amount of money had it been reinvested over time. Fees are one of many factors—such as the historical performance and risk for each investment option—participants should consider in making their investment decisions.

**Figure 1: Effect of a 1-Percentage Point in Higher Annual Fees on a \$20,000 DC Plan Balance Invested over 20 Years**



Source: GAO analysis.

## Some Plan Sponsors Take Fewer Actions to Decrease Fees Than Sponsors of Other DC Plans

DC plan experts told us that compared to 401(a), 401(k), and 457(b) governmental plans, sponsors of 403(b) plans generally take fewer actions to decrease fees for participants. The 403(b) plan sponsors often establish a direct one-on-one relationship between the service provider and the participant, which means sponsors' main responsibility is to send contributions from employees' paychecks to investment service providers. This one-on-one relationship between participant and service provider keeps sponsors' involvement to a minimum, limiting the ability to reduce fees.

Sponsors of some 403(b) plans often take fewer actions to decrease participants' fees for at least two reasons, according to experts we interviewed. First, many sponsors of 403(b) plans are public schools and tax-exempt organizations, and experts told us they may not have the

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resources to hire plan administrators who are retirement plan specialists. Instead, the staff who administer these plans are often responsible for payroll or other administration and may lack guidance on ways sponsors can reduce participants' fees. Second, for many state and local governments, 403(b) plans are a secondary retirement benefit to a DB plan. Experts told us that sponsors may not feel as motivated to play an active role in these plans since the 403(b) plan is supplemental.

For some governmental 403(b) plans, sponsors' ability to decrease fees for participants is limited by certain state laws. As we noted earlier, one expert told us that a handful of states, including California and Texas, have laws that limit state and local government 403(b) plan sponsors' ability to narrow the list of service providers offered to participants. Instead, sponsors must generally give any qualified service provider a "payroll slot," or an opportunity for participants to choose that service provider to receive contributions withdrawn from their paycheck. These requirements limit sponsors' ability to pool assets, negotiate with service providers, or conduct RFPs.

In contrast to 403(b) plans, other plans are often structured to require more sponsor actions. First, with some exceptions, sponsors of 401(a), 401(k), and 457(b) governmental plans are generally required by law to set participants' assets aside in a trust or other type of entity established to hold participants assets. As a result, sponsors are generally responsible for seeing to it that participants' funds are accounted for, and the trust provides a pool of assets that facilitates negotiating with service providers. Second, plans subject to Title I of ERISA (including some 403(b) plans) are required to name fiduciaries for their plans, and this role is often filled by plan sponsors or service providers. The law requires fiduciaries to act in the sole interest of participants and beneficiaries. In addition, Labor has interpreted the law as requiring fiduciaries to assess the reasonableness of fees charged to participants. Sponsors of plans not subject to Title I of ERISA—like plans sponsored by state and local governments—are not required to do so, unless state laws impose such duties.

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### IRS's New 403(b) Regulations May Encourage Sponsor Action, but Its Effect on Fees Is Unclear

Some 403(b) plan sponsors may take more action as a result of the IRS's 403(b) regulations that generally became applicable in January 2009, but the effect of this regulation on fees is unclear. Before these regulations, many sponsors established a one-on-one relationship between participants and service providers. IRS held participants responsible for qualification requirements such as certifying that they had not exceeded loan limitations. According to IRS officials, sponsors often did not track all

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participants' assets. Instead, experts told us that sponsors' main responsibility was sending contributions from participants' paychecks to investment service providers. However, under the new regulations, when participants want to exchange one 403(b) contract for another 403(b) contract under the same plan, sponsors must agree to share information about the participants with the service provider of the new 403(b) contract.<sup>19</sup> Plan sponsors have other duties under the new regulations as well, such as maintaining a plan document that outlines all the material provisions of the plan.

Given these changes, 403(b) plan experts disagree about the new regulations' effect on fees charged to participants. Some experts believe fees will increase because of additional compliance costs to cover the expense of services like creating a plan document. To create a plan document, sponsors may need more administrative and legal assistance, the costs of which could be passed on to participants. Other experts said the new requirements will lead to lower fees for participants because they give sponsors an incentive to narrow the range of investment options. One expert noted that the administrative burdens of keeping track of all of participants' funds has induced sponsors to reduce the number of investment service providers available to participants to limit record-keeping activities.<sup>20</sup> To limit the number of service providers, sponsors are likely to conduct RFPs and to consider costs in their decisions. Also, limiting service providers may reduce the number of times participants transfer their funds, reducing sales loads, surrender charges, or other fees associated with buying and selling investment options.

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<sup>19</sup>This includes information necessary for the contract to satisfy various legal provisions, such as whether participant loans from plan assets exceed certain limits.

<sup>20</sup>States with "any willing provider" laws are generally unable to reduce the number of service providers available to participants.

Participants Receive  
Different Fee  
Information  
Depending on ERISA  
Coverage and  
Regulator, Limiting  
Participants’ Ability to  
Compare Investment  
Options

Participants Receive  
Different Fee Information  
Depending on ERISA  
Coverage

Participants in DC plans subject to Title I of ERISA receive different fee disclosure documents than participants in non-Title I plans. ERISA requires sponsors, including employers who sponsor SEP or SIMPLE IRAs, to disclose certain documents to participants that may contain fee information. Sponsors must provide all participants with a summary plan description, account statements, and the summary annual report. As we previously reported, these documents may, but are not required to, disclose information on fees borne by individual participants, as shown in table 8.<sup>21</sup>

Table 8: Required Disclosure Documents to All Participants in Plans Subject to Title I of ERISA

Disclosure document	Document purpose	Information on fees
Summary plan description	To explain to participants how the plan operates.	May contain information on how various fees such as investment, record-keeping, and loan fees are charged to participants, but not required by ERISA to do so.
Account statement	To show the account balance due to a participant.	Typically identifies fees, such as for loans, which are directly attributable to an account during a specific period. Also, may show investment and record-keeping fees, but not required by ERISA to do so.
Summary annual report	To disclose the financial condition of the plan to participants.	Contains total plan costs incurred by plan participants during the year.

Source: GAO analysis.

<sup>21</sup>[GAO-07-21](#).

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As we found in our report on 401(k) plan fees, the fee information that ERISA requires sponsors to disclose is limited and does not provide participants with an easy comparison of fees for different investment options.<sup>22</sup> Disclosure documents may contain information on the total fees charged to participants, but may not clearly list all types of fees in a manner that facilitates comparison of investment options. As a result, participants may pay more than they would if they had clearer information.

For those plans not subject to Title I of ERISA, sponsors are not federally required to disclose fee information at all, although state laws may require them to do so. Experts told us that some, but not all, states established ERISA-like laws that include fee disclosure requirements. For example, Florida does not require all local government sponsors to disclose fee information to participants. Also, a retirement official in Minnesota told us that state law requires the sponsor of a state 457(b) governmental plan to make participants aware of fees that they pay, but statutes do not require similar fee disclosure for school districts' 403(b) plans. Similarly, Florida requires fee disclosure for state and local government 401(a) plans but not for 403(b) plans. As a result, participants in different state and local government plans within Florida may receive different information about the fees they pay.

Experts and sponsors also told us that sponsors of plans not subject to Title I of ERISA sometimes provide participants with information on fees, even though they are not required to do so. For example, sponsors may distribute prospectuses or fund profiles when employees become eligible for the plan even though they are not required by ERISA or state law to do so. DC plan experts told us that state and local government sponsors do this because they are accustomed to transparency, and because they feel responsible for helping their participants understand fees.

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### Participants also Receive Different Fee Information Depending on the Regulator

Participants receive different fee information based on the regulator of the product in which they invest. SEC regulates fee disclosure for some retirement plan investment options, such as mutual funds, and variable annuity products, and requires investment service providers to disclose fees in a prospectus, a document that details investment strategy and

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<sup>22</sup> [GAO-07-21](#).

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fees.<sup>23</sup> SEC requires require that a prospectus be provided to the purchaser of a security, such as a mutual fund. When the sponsor of a DC plan purchases shares of a mutual fund for participant accounts, the sponsor receives the prospectus. SEC regulations do not govern plan sponsors and, therefore, do not require sponsors to provide a prospectus to retirement plan participants.

We found that some service providers that are regulated by SEC give the prospectus to both the sponsor and the participant when the purchaser is the sponsor. Service providers also said they disclose fees in various other documents because they feel it is the right thing to do. For example, several service providers told us that their company makes fee information available to participants on their Web site and on fact sheets because they felt that transparency was constructive.

State insurance agencies also regulate fee disclosure for insurance products and may require disclosures that list the fees that participants pay. The National Association of Insurance Commissioners (NAIC) developed model disclosure regulations, which each state can choose to adopt. The regulations require that fixed annuity providers list the specific dollar amounts or percentage charges with explanations, as well as total amounts charged. According to NAIC, 27 states have adopted the NAIC Annuity Disclosure Model Regulation or have related state activity.<sup>24</sup> For example, one state specifically requires insurers to give prospective purchasers a buyer's guide to annuities and a contract summary as provided in the NAIC model regulation.<sup>25</sup>

However, other states have different fee disclosure requirements; therefore participants in different states may receive different information on fees. For example, while service providers must be licensed by each

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<sup>23</sup>The prospectus also contains fund information such as the investment objectives or goals, strategies for achieving those goals, risks of investing in the fund, expenses, and past performance.

<sup>24</sup>According to NAIC, states can adopt the model in its entirety in a uniform and substantially similar manner with minor variations in style and format. Examples of related state activity include: an older version of the NAIC model, portions of the NAIC model, legislation or regulation derived from other sources, bulletins, and administrative rulings.

<sup>25</sup>The buyers' guide describes fees that purchasers may or may not pay and the disclosure document must list products' specific charges and fees with an explanation of how they apply.

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state where it sells insurance products, at least one state does not require specific fee disclosures to some participants.<sup>26</sup>

California and Texas have more stringent disclosure requirements than the federal government. These states require specific disclosure of all fees for service providers licensed to sell products to participants in public 403(b) plans. California and Texas established online registries with fees disclosed in a consistent format to facilitate comparison of 403(b) service providers' fees. Licensed service providers must submit fees and other information to the registry to sell investment products to participants in the states' school systems. Both states organize the information from service providers to provide fee information in a standardized format.

Service providers listed in California's registry must disclose all direct and indirect fees charged to participants such as surrender fees, management fees, and annual fees. For example, in California, participants may compare fees of up to three similar investment products at one time. California's Web site, [www.403bcompare.com](http://www.403bcompare.com), allows any user to view and compare fees of selected products from multiple vendors side by side. Similarly, licensed service providers in Texas must disclose all fees they charge in the online registry, including both investment and administrative fees. These registries help sponsors and participants of 403(b) plans compare service providers' fees and other characteristics, which may facilitate choosing products with lower fees.

As shown in table 9, different regulators require different information to be disclosed. As a result, DC plan participants and IRA account owners may receive different information because of the entity that regulates the plan or the investment product.<sup>27</sup>

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<sup>26</sup>Participants in some plans may invest in products not registered with SEC or state insurance regulators, such as collective investment funds (CIF), which are overseen by bank regulators. The Office of the Comptroller of the Currency (OCC), for example, requires banks administering a CIF to disclose fees and expenses in a written plan and an annual financial report, in addition to other applicable state requirements.

<sup>27</sup>For individual IRA account owners who invest in products for which an amount is not guaranteed over a period of time, and the growth rate cannot be reasonably projected, IRS generally requires the trustee of an individual IRA to disclose each type of fee, and the amount of each fee (based on hypothetical assumptions) to the account owner—including trustee fees and other administrative fees—before the account is opened.



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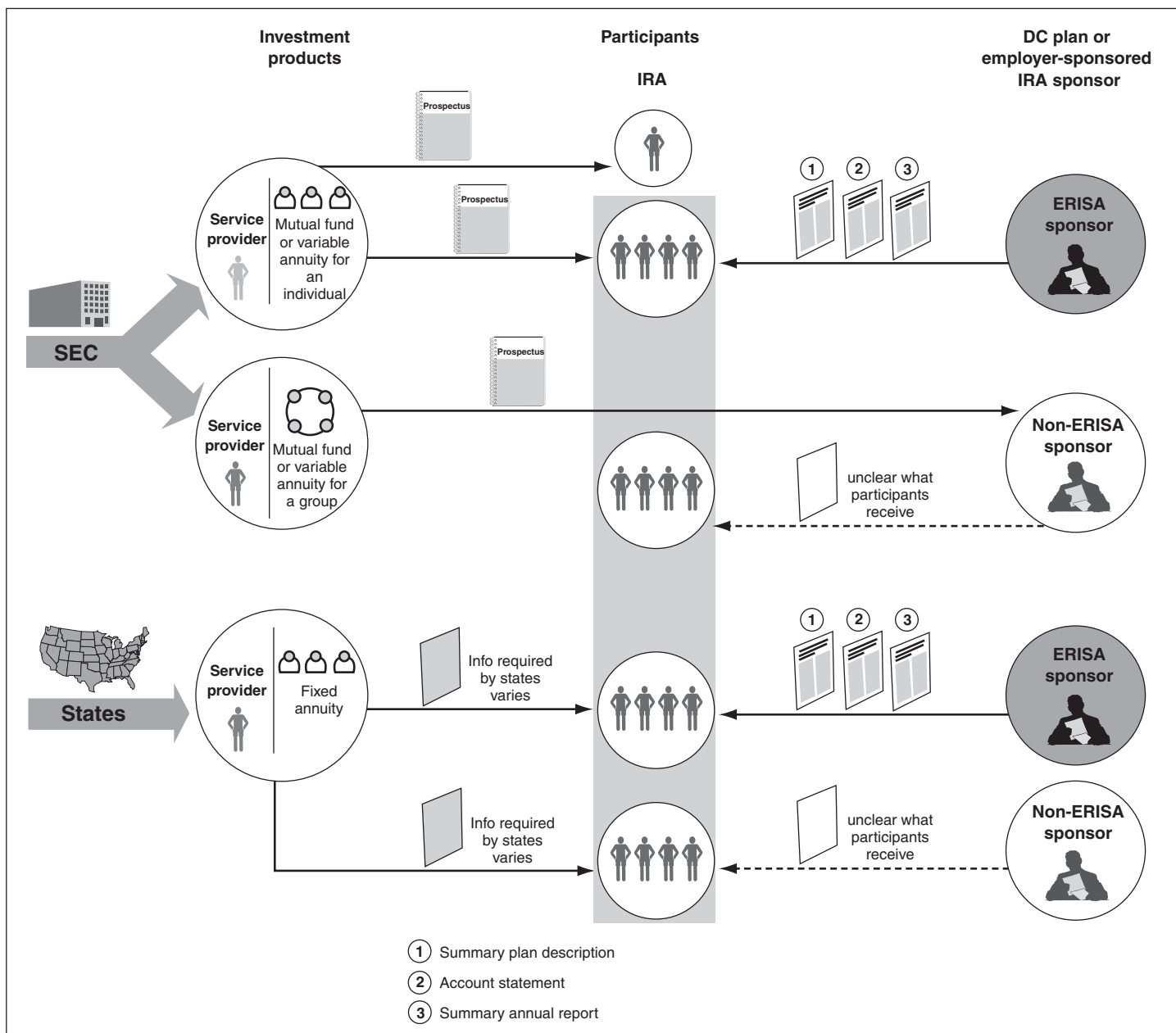
**Table 9: Required Fee Disclosure Information, by Regulator**

Regulator	Required fee disclosure information
ERISA	ERISA requires sponsors to provide participants with summary plan description, account statement, summary annual report, which may include information about fees such as investment fees, record-keeping fees, and total plan costs.
State and local governments	For sponsors of public DC plans, state and local government requirements vary. For example, one state requires certain sponsors to provide a quarterly statement that lists out all fees, while another state requires no fee disclosures for certain plans.
SEC	The prospectus contains a fee table with general fee information associated with the product, such as the expense ratio, which explains total fees reported as a percentage of the fund's assets. The prospectus does not contain certain fees charged by the plan such as transactional fees.
State insurance regulators	States' insurance department requirements vary. According to NAIC, some states have adopted NAIC's model disclosure regulations, which requires specific dollar amounts or percentage charges and fees listed with an explanation of how they apply. States who have not adopted NAIC's model regulations may have different disclosure requirements.

Source: GAO analysis.

Moreover, because of the different disclosure requirements, participants in DC plans and IRAs can invest in similar products but receive different information on fees. This may be confusing to participants who want to compare fees of different investment products to make an investment choice. For example, as shown in figure 2, under ERISA, participants must receive a summary plan description, an account statement, and a summary annual report, regardless of the product in which they are invested. But a participant who is invested in the same type of product in a plan not subject to Title I of ERISA may not receive any information from either the service provider or the sponsor. On the other hand, the participant may receive information from both the service provider and the sponsor, but the fee information may be in different formats, making it difficult for the participant to compare investment products.

**Figure 2: Oversight of Fee Information Disclosed to Retirement Plan Participants**



Sources: GAO; images, Art Explosion.

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## Oversight of Fees and DC Plans Will Likely Improve with Recent Regulations, but IRS and Labor Still Lack Information That Could Strengthen Oversight

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### Labor and IRS Oversee Fee Disclosure and DC Plans, and Recent Regulations on Fee Disclosure and 403(b) Plans Are Likely to Improve Oversight

Labor is charged with overseeing the statutorily required disclosures—which may include fee information—to participants of certain DC plans, while IRS oversees tax laws that apply to all DC plans. Both have recently issued or proposed regulations that are likely to improve oversight. Under ERISA, Labor is responsible for enforcing the requirements that plan fiduciaries ensure that fees paid with plan assets are reasonable and for necessary services. Labor does this in a number of ways, including collecting information on fees from plan sponsors, investigating participants' complaints or referrals from other agencies on questionable plan practices, and conducting outreach to educate plan sponsors about their responsibilities. In addition, Labor makes available a checklist with its annual filing instructions to help plan sponsors follow ERISA requirements, such as providing participants with certain documents like the summary plan description. While the checklist is not submitted to Labor, agency officials stated that it selects plans for investigation because of some indication that an ERISA violation may have occurred or may be about to occur, a process Labor calls "targeting." For example, we reported that Labor targeted 3,400 cases for review in 2005 as a result of various source leads, such as participant complaints, computer targeting, and other agency referrals.<sup>28</sup>

Labor proposed regulations in July 2008 to improve oversight of DC plans subject to Title I of ERISA. These regulations are designed to improve fee

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<sup>28</sup>GAO, *Employee Benefits Security Administration: Enforcement Improvements Made but Additional Actions Could Further Enhance Pension Plan Oversight*, [GAO-07-22](#) (Washington, D.C.: Jan. 18, 2007).

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disclosure to participants by requiring sponsors to provide participants with the actual amounts individuals were charged for administrative services, on a quarterly basis.<sup>29</sup> Sponsors would be required to disclose investment fees at least annually to participants in a chart or similar format to facilitate comparison of fees among investment options. These regulations apply only to plans subject to Title I of ERISA disclosure provisions, such as many 401(a), 401(k), some 403(b) plans, and some employer-sponsored IRAs. We have previously suggested that Congress amend ERISA to require all sponsors to disclose fees in a way that facilitates comparison among investment options.<sup>30</sup>

While IRS generally does not have responsibility for enforcing laws regarding fees and fee disclosure for DC plans, IRS oversees DC plans' compliance with the tax code. All DC plans allow a tax deduction or deferral for plan sponsors or participants. IRS makes sure that contributions are eligible for a tax deferral or deduction by analyzing features of retirement plans. IRS issued final regulations in 2007 that made significant changes to improve IRS oversight of all 403(b) plans. The regulations require sponsors to maintain a plan document that outlines the provisions of the plan, and manage the plan in accordance with the document. While previously sponsors had to provide certain information in writing, they were not generally required to maintain a formal plan document.

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**Labor Lacks Specific Authority to Collect Information to Help Ensure That Safe Harbor 403(b) Plans Protect Participants' Interests**

Labor lacks the specific authority to require sponsors of safe harbor 403(b) plans to submit information that would help ensure that participants' interests are protected. Labor oversees many DC plans sponsored by tax-exempt organizations that are subject to Title I of ERISA. However, Labor has defined a safe harbor for certain 403(b) plans that may operate outside of Title I. Under Labor's safe harbor regulations, 403(b) plans are defined as not having been "established or maintained by an employer" under ERISA if certain conditions are met. For example, in order to remain under the safe harbor, sponsors must generally limit their

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<sup>29</sup>These regulations are currently being reviewed by the new administration.

<sup>30</sup>[GAO-07-21](#), p. 29.

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involvement in the plan.<sup>31</sup> Plan sponsors make the decision to operate their 403(b) plans under the safe harbor, independent of Labor.

We found that Labor cannot identify safe harbor plans and therefore has no assurance that it is able to systematically enforce laws for 403(b) plans that may be operating outside of the safe harbor. Under ERISA, DC plans are required to file an annual report with Labor.<sup>32</sup> However, Labor currently does not have the authority to require that safe harbor plans provide similar information. Labor does have the authority to investigate any 403(b) plan of a tax-exempt employer to determine if the plan is covered by Title I of ERISA and may have reason to target safe harbor 403(b) plans for enforcement actions because sponsors may engage in activities that take them out from under the safe harbor and make them subject to Title I. For example, sponsors that act as fiduciaries are required to follow requirements that protect participants' interests, such as seeking reasonable fees for plan participants and avoiding conflicts of interest. However, Labor has no way to systematically assess whether or not sponsors of 403(b) safe harbor plans are acting as plan fiduciaries. As a result, Labor cannot ensure that participants' interests are protected. Because Labor is unable to identify safe harbor plans, it has no assurance that it is able to include all 403(b) plans subject to Title I of ERISA in its enforcement efforts.

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<sup>31</sup>Sponsor involvement must be limited to certain activities that facilitate the operation of the plan. Other safe harbor conditions are: plan participation must be "completely voluntary" for employees; rights under the plan are enforceable solely by employees (or a beneficiary of an employee); and the sponsor must not receive compensation or consideration for offering the plan, other than reasonable compensation to cover certain expenses.

<sup>32</sup>On this form—Form 5500 Annual Return/Report of Employee Benefit Plan—most sponsors report information like the number of participants, as well as details on the plan's financial condition and investments.

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## Lack of Information Sharing between IRS and Financial Regulators Limits Oversight of Service Providers

IRS and financial regulators have not always shared information with one another to use resources effectively and help enforce a rule requiring reasonable fees. In our discussions with IRS officials, they said that IRS agents who find evidence of legal violations are not obligated to share information with financial regulators.<sup>33</sup> However, providing such information would help in overseeing service providers of DC plans. Various service providers such as investment companies and record-keepers work with DC plans and participants and IRS agents are in a position to potentially find that some service providers have violated financial regulations.

Currently, IRS is under no obligation to report service providers' conduct to the proper financial regulators. No formal agreement is in place—such as a memorandum of understanding (MOU)—to guide coordination efforts, a practice we have identified as effective in prior work.<sup>34</sup> Financial regulators, such as the Federal Reserve Board and SEC, have established an MOU to facilitate their oversight of financial services firms. Without MOUs, IRS agents have no obligation to report violations, and without such reporting the potential for service providers withholding information from plan participants increases. An MOU—and corresponding changes to agents' guidance—could provide a means for agents to report violations, and such reporting could reduce the likelihood of service providers withholding information from plan participants. Such reporting could also provide an additional means by which to enforce a rule requiring reasonable fees.

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## IRS Does Not Collect Enough Information to Easily Enforce 457(b) Plans' Contribution Limits

IRS's does not collect enough information to easily enforce certain limits on participants' contributions to 457(b) plans, which could lead to excessive income tax deferrals. Some, but not all, DC plans have “catch-up” provisions that allow older participants to defer additional income.

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<sup>33</sup>I.R.C. § 6103 prohibits IRS from disclosing returns and return information unless a specific exception applies. However, there may be instances in which information, not considered a “return or return information” under §6103, could be disclosed without violating that statute.

<sup>34</sup>We have reported that agencies can strengthen their commitment to work collaboratively by articulating their agreements in formal documents, such as a memorandum of understanding, interagency guidance, or an interagency planning document, signed by senior officials in the respective agencies. See GAO, *Results-Oriented Government: Practices That Can Help Enhance and Sustain Collaboration among Federal Agencies*, [GAO-06-15](#) (Washington, D.C.: Oct. 21, 2005), p. 11.

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Older participants may wish to set aside more money than younger participants as they near retirement. In 2009, participants age 50 and over in 401(k), 403(b), and 457(b) governmental plans are permitted to contribute an additional \$5,500 over the normal contribution limit of \$16,500. Participants age 50 and over in 457(b) tax-exempt plans are not permitted to make additional catch-up contributions.<sup>35</sup>

Although there are two distinct types of 457(b) plans—governmental plans and tax-exempt plans—IRS cannot easily differentiate between participants in these plans to evaluate whether or not they are appropriately complying with catch-up contribution limits. IRS identifies plan participants in various retirement plans from information provided on the W-2 form that reports income tax deferrals. To identify a participant's contributions to a specific plan:

- Employers submit a Form W-2 for each participant in the plan, reporting annual contributions to the retirement plan, among other things.
- Form W-2 asks employers to identify the type of plan in which the participant is enrolled by listing the code representing the plan in box 12, along with the amount deferred, as shown in Figure 3.

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<sup>35</sup>In addition to these age 50 catch-up provisions, “special” catch-up provisions apply to both 457(b) tax-exempt and 457(b) governmental plans. For both governmental and tax-exempt 457(b) plans, for participants who are 3 years or less away from the year of normal retirement age, the plan ceiling is limited to the lesser of \$33,000 or \$16,500 plus the sum of any amounts in which the participant did not contribute up to the annual limit in prior years.

**Figure 3: IRS Form W-2, Wage and Tax Statement, with Emphasis on Box 12, for Retirement Plan Contributions**

22222 Void ☐ a Employee's social security number For Official Use Only ▶  
OMB No. 1545-0008

b Employer identification number (EIN) 1 Wages, tips, other compensation 2 Federal income tax withheld

c Employer's name, address, and ZIP code 3 Social security wages 4 Social security tax withheld

5 Medicare wages and tips 6 Medicare tax withheld

7 Social security tips 8 Allocated tips

d Control number 9 Advance EIC payment 10 Dependent care benefits

e Employee's first name and initial Last name Suffix 11 Nonqualified plans 12a See instructions for box 12

13 Statutory employees Retirement plan Third-party sick pay 12b

14 Other 12c

12d

f Employee's address and ZIP code

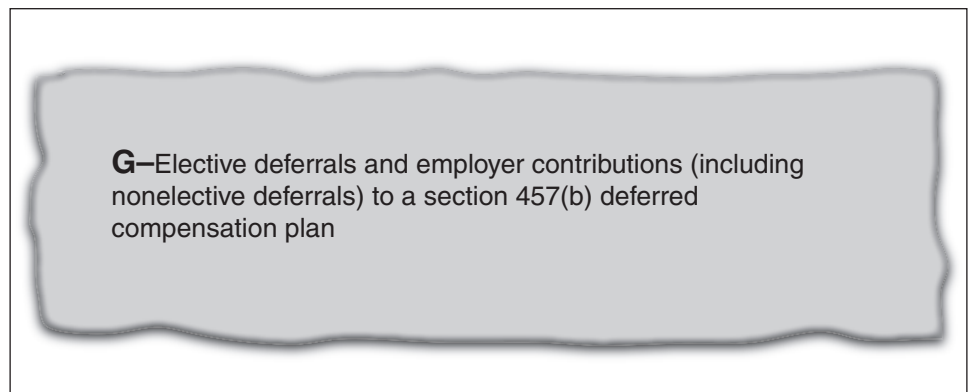
15 State Employer's state ID number 16 State wages, tips, etc. 17 State income tax 18 Local wages, tips, etc. 19 Local income tax 20 Locality name

Form **W-2** Wage and Tax Statement **2008** Department of the Treasury—Internal Revenue Service  
Copy A For Social Security Administration — Send this entire page with Form W-3 to the Social Security Administration; photocopies are **not** acceptable. For Privacy Act and Paperwork Reduction Act Notice, see back of Copy D. Cat. No. 10134D

Source: IRS.

- The instructions for the W-2 form list a single letter code (“G”), to represent deferrals to a 457(b) plan, as shown in figure 4.

**Figure 4: Form W-2 Instructions**



Source: IRS.



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We found that the W-2 code identifying 457(b) plans has not been changed for several years, and therefore the IRS does not have enough information to easily determine whether catch-up contributions are made appropriately. In 2002, section 457 was amended, allowing 457(b) governmental plan participants age 50 and over the opportunity to contribute \$5,500 in catch-up contributions. These contributions are not permitted for participants of 457(b) tax-exempt plans. However, the code on the W-2 form for these two plans remained the same.

Instead of relying on the W-2 form to systematically differentiate between participants in the two types of 457(b) plans, IRS agents rely on experience gained on the job to make distinctions. IRS agents seeking to enforce the different 457(b) catch-up contributions rules have to make a judgment to decide if the catch-up contributions are permitted. IRS officials explained that efforts to link the participant information to the type of sponsor is burdensome. IRS agents have to confirm the type of organization that sponsored the plan and then determine if the participant could make the extra contribution. For example, one IRS agent told us that the agent could contact the plan sponsor and ask for documentation of its tax-exempt or government status.<sup>36</sup>

As a result of IRS's inability to easily differentiate between 457(b) plan participants, the federal government may be losing tax revenue. For example, a 457(b) tax-exempt plan participant could erroneously make a catch-up contribution. Normally, the participant's contributions over the normal limit (\$16,500) would be subject to income tax, for which the highest income tax bracket was 35 percent in 2008. However, if a participant made the maximum catch-up contribution of \$5,500 and did not pay income taxes, he or she would avoid paying 35 percent of \$5,500. The federal government would lose \$1,925 in tax revenue for that year.

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<sup>36</sup>We have reported that IRS can efficiently resolve errors of this sort on taxpayer submissions using math error authority (MEA). Where possible, IRS uses MEA to correct certain errors before interest is owed by the taxpayer. IRS is granted MEA in 26 U.S.C. § 6213(b). It can only be used for certain purposes specified by Congress in 26 U.S.C. § 6213(g)(2). For more information, see GAO, *Tax Administration: IRS's 2008 Filing Season Generally Successful Despite Challenges, although IRS Could Expand Enforcement during Returns Processing*, [GAO-09-146](#) (Washington, D.C.: Dec. 12, 2008).

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## Conclusions

American workers participating in DC plans may not receive clear information on the fees that they pay, even though relatively small fees imposed annually can significantly affect retirement savings over the course of a career. In our previous work, we suggested that Congress consider amending the law to require fees to be disclosed to participants in 401(k) plans in a way that facilitates comparison of investment options, and our current work suggests that participants in all types of plans could benefit from enhanced disclosure. Labor has proposed regulations that address this concern, but we continue to believe that a change in the law is necessary to ensure that improved fee disclosure will be broadly available to all participants.

Although ERISA requires sponsors to disclose some fee information to participants, disclosure requirements for plans not subject to Title I of ERISA are less consistent. Depending on the service provider, the sponsor, and the state, participants in these plans may receive fee information from different entities, in different formats, or may receive no fee information at all. Some states have taken approaches to fee disclosures that are already helping participants to compare fees across investments. These approaches may provide a model not only for federal oversight, but also for other states as both works to enhance disclosure of DC plan fees.

While sponsors of some plans often take actions such as pooling assets to obtain pricing advantages, sponsors of 403(b) plans often do not. As a result, participants in 403(b) plans can end up paying higher fees than participants in other DC plans. If guidance were provided to all sponsors of DC plans about what role they can have in reducing fees, sponsors would be more likely to understand the actions they can take to help participants ensure they have adequate retirement savings. Given its responsibility to oversee plan fiduciaries, Labor has the expertise to develop such guidance, but it does not have authority over plans not subject to Title I of ERISA. IRS is in a better position to reach out to all sponsors. Collaboration between IRS and Labor can ensure that DC plans subject to Title I of ERISA and other plans are reached.

Both Labor and IRS have particular responsibilities for overseeing DC plans, and in Labor's case, making sure that plan sponsors ensure the reasonableness of fees charged is an especially important responsibility. However, steps must be taken to improve each agency's oversight of DC plans to ensure that not only are DC plan participants' retirement savings adequately safeguarded, but also that there is no absence of oversight for entities involved in the DC plan market. Therefore, while Labor is responsible for administering the statutory provisions that safeguard the

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interests of participants, these interests may be vulnerable if Labor does not have the specific authority to require that all 403(b) plan sponsors that fall outside of safe harbor rules systematically identify themselves. Without such authority, Labor cannot easily identify sponsors who may be covered by Title I of ERISA, which is designed in part to protect workers' retirement savings. In addition, IRS has a role to play in ensuring that the government receives the appropriate tax revenue. However, if IRS cannot easily determine whether participants in certain plans are improperly deferring income, then the federal government could be missing tax revenue if participants exceed deferral limits. Finally, encouraging regulators to share information on service providers' violations they have found in the normal course of reviewing plans with other regulators is likely to help ensure that all DC plan participants' retirement savings are protected. With a formal mechanism, such as an MOU, to share information with other regulators when potential violations are found, regulators are less likely to miss opportunities to enforce financial regulations designed to protect investors. Such an MOU would be appropriate for limited occasions when information on service providers can be shared without revealing protected taxpayer information.

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## Matters for Congressional Consideration

Congress should consider amending ERISA to require sponsors to disclose fee information on each investment option in the plan to participants in a consistent way that facilitates comparisons among the options not only for 401(k) plans, as we have previously suggested, but for all DC plans subject to Title I of ERISA. In addition, to help ensure participants in all DC plans receive consistent fee disclosure, Congress may wish to consider state approaches for fee disclosure to participants in non-Title I plans as models for federal requirements for ERISA plans.

Given the absence of direct oversight of safe harbor 403(b) plans, Congress may wish to consider giving Labor the specific authority to collect information to systematically monitor safe harbor plans, which will allow Labor to determine whether any safe harbor 403(b) plans are operating outside the safe harbor guidelines and are subject to Title I of ERISA.

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## Recommendations

To encourage plan sponsors to take actions that result in participants paying lower fees, we recommend that the Commissioner of Internal Revenue, together with the Secretary of Labor, provide guidance designed for sponsors of all types of DC plans to suggest ways sponsors can cost-effectively decrease participants' fees.

To be able to provide improved oversight and ensure participants are not violating tax deferral limits, the Commissioner of the Internal Revenue Service should collect information to allow them to easily differentiate between types of 457 plans.

To help ensure that information about service providers' violations is shared with financial regulators, we recommend that the Commissioner of the Internal Revenue Service work with financial regulators to establish a formal memorandum of understanding. Such a memorandum would help instruct agents and would be appropriate for limited occasions when information on service providers can be shared without revealing protected taxpayer information. In addition, the agencies should periodically review and update the memorandum, as appropriate.

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## Agency Comments and Our Evaluation

We provided a draft of this report to the Secretary of Labor, the Secretary of the Treasury, and the Chairman of the Securities and Exchange Commission. We obtained written comments from the Assistant Secretary of Labor and from the Deputy Commissioner of the Internal Revenue Service, which are reproduced in appendixes II and III. Treasury, IRS, SEC, and Labor also provided technical comments, which were incorporated in the report where appropriate.

Labor agreed with our recommendations. They noted that excessive fees can undermine long-term retirement savings for plan participants and described how two proposed regulations would give plan fiduciaries more responsibility for understanding plan fees and improve fee disclosure for participants. We agree that Labor's proposed regulations will assist plans sponsors in understanding their responsibilities for plan fees, but note that neither regulation has been made final. Labor also noted that it has produced guidance for plan sponsors on a variety of issues to help them understand their responsibilities under ERISA. However, this guidance is often focused on 401(k) plans, whereas all plans are likely to benefit from it.

IRS agreed with our recommendations to work with Labor to provide guidance to sponsors of all types of plans to help reduce participants' fees, as well as to collect enough information to distinguish between different

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types of 457 plans. With regard to establishing an MOU to facilitate information-sharing with financial regulators, IRS said that it will cooperate in situations we described. However, IRS also said that its method of doing so is sufficient. IRS described sharing information with another federal regulator without the use of an MOU, while complying with rules that protect the confidentiality of taxpayer and tax return information. As noted, IRS has been diligent in observing regulations protecting taxpayer information, and we agree that carefully structured cooperation is important. However, we continue to believe that an MOU is the best means for formally articulating such cooperation especially given the variety of entities involved in DC plan administration that cross regulatory boundaries. Just as IRS has established MOUs with other federal agencies such as Labor to share information, we believe that an MOU would be useful to guide coordination efforts with financial regulators to ensure that IRS agents know what is expected of them.

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Unless you publicly announce its contents earlier, we plan no further distribution until 30 days after the date of this report. At that time, we will send copies of this report to the Secretary of the Treasury, Commissioner of Internal Revenue, the Secretary of Labor, the Chairman of the Securities and Exchange Commission; appropriate congressional committees; and other interested parties. In addition, the report will be available at no charge on GAO's Web site at <http://www.gao.gov>.

If you have any questions concerning this report, please contact me at (202) 512-7215 or [bovbjergb@gao.gov](mailto:bovbjergb@gao.gov). Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made significant contributions to this report are listed in appendix V.

Sincerely yours,

A handwritten signature in black ink, reading "Barbara D. Bovbjerg". The signature is fluid and cursive, with the first name "Barbara" and last name "Bovbjerg" clearly legible.

Barbara D. Bovbjerg  
Director, Education, Workforce, and  
Income Security Issues

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# Appendix I: Objectives, Scope, and Methodology

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The objectives of this report were to examine: (1) how the types of fees charged to participants and investments of various defined contribution (DC) plans differ; (2) how DC plan sponsor actions affect participant fees; (3) how fee disclosure requirements vary; and (4) how effective is the oversight of DC plans.

To identify total assets for DC plans and IRAs, we reviewed a report that analyzed data from federal and private sources. We reviewed “The U.S. Retirement Market, 2008,” *Research Fundamentals*, vol. 18, no. 5 (Washington, D.C.: Investment Company Institute, June 2009). Total IRA market assets are derived from tabulations of total IRA assets provided by the IRS Statistics of Income (SOI) Division for tax years 1989, 1993, 1996–2002, and 2004. These tabulations are based on a sample of IRS returns. Total assets for 401(k) plans, 403(b) plans, and 457 plans are based on data from the Federal Reserve Board, the National Association of Government Defined Contribution Administrators, and American Council of Life Insurers. The Investment Company Institute (ICI) is a national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-trade funds, and unit investment trusts. Its research department collects and disseminates industry statistics, and conducts research studies relating to issues of public policy, economic and market developments, and shareholder demographics.

We obtained different sets of data from the Internal Revenue Service (IRS) on the general characteristics of DC plans, such as number of plans.

- First, we obtained one set of data from IRS’s Tax Exempt and Government Entities Division (TEGE). The 401(k), 403(b), and 457(b) plan and participant information was taken from a database that compiles information from all W-2 documents submitted to IRS. The data have some limitations. For 2007, this database collected W-2 forms from 92 percent all taxpayers who filed a W-2 that year. The other 8 percent represent taxpayers who file their forms late or amend returns. IRS also explained that some plans in which no individual made a contribution in a single year may not be represented in the count, but it is likely that few such plans exist. In addition, no data was available for 401(a) plans, or 457(f) plans. Because we used the data to illustrate the relative assets and contributions of DC plans, we found it reliable for our purposes.
- We reviewed the IRS’s Compliance Data Warehouse (CDW) Information Returns Master File (IRMF) for tax year 2006. CDW is a widely used database consisting of sensitive but unclassified taxpayer data from various data sources. The IRMF we received was extracted on May 15,

2009. We assessed these data and determined that they were sufficiently reliable for the purposes of this report.

- We also reviewed data from IRS's Statistics of Income (SOI) individual files for tax year 2006. SOI is also a widely used database consisting of a sample selected before audit of the income tax returns. Since the estimates we provide using these data sources are based on samples, they involve margins of error. Unless otherwise noted, population estimates' margins of error do not exceed 3.54 percentage points; contributions estimates' margins of error are a maximum of plus or minus 4.1 percent. We assessed these data and determined that they were sufficiently reliable for the purposes of this report.

To explain how the types of fees charged to participants and investments of various DC plans differ, we interviewed 6 plan sponsors and 11 investment service providers who interact with different DC plans to understand how fees may vary among plans. We also consulted with four legal experts on the differences among plans, as well as associations representing different types of plan sponsors, and service providers, and one union representing participants and sponsors. We obtained guidance from IRS and Department of Labor (Labor) explaining the features of each type of plan. We conducted a search of the literature, including academic and industry sources. We compared plan differences and similarities, and reviewed tax law and regulations on deferred compensation plans.

To determine how DC plan sponsor actions affect participant fees, we conducted a search of the literature, including GAO's prior work, and consulted with several industry experts on retirement plans, as well as associations representing different types of plan sponsors, and service providers, and experts on investment products, such as regulators, and researchers. We also consulted with representatives from 11 different investment service providers and 6 plan sponsors.

To outline how fee disclosure requirements vary by plan, we conducted a search of the literature, and reviewed the Employee Retirement Income Security Act of 1974 (ERISA), other laws, and the Internal Revenue Code. We reviewed disclosure laws in Florida and Minnesota to examine if state laws outlined disclosure requirements for plans not subject to ERISA. We also reviewed the requirements for California and Texas's Web sites that provide fee disclosure information to certain participants. We reviewed disclosure regulations related to retirement plans as well as investment products to compare information required to be disclosed across various DC plans and investment products.

We interviewed officials from the Securities and Exchange Commission (SEC), Financial Industry Regulatory Authority, National Association of Insurance Commissioners and state insurance regulators. We reviewed model disclosure for annuity products and SEC requirements for product disclosure. In addition, we interviewed and sought information from investment services providers, such as insurance companies and mutual funds providers, who interact with retirement plans to describe plan fees and disclosure practices. We analyzed 11 service providers' responses to structured questions on fees and disclosure. We consulted with national experts, such as industry associations and experts.

To describe the effectiveness of DC plan oversight, we interviewed officials from IRS and Labor to discuss plan oversight and topics related to reporting and compliance. We reviewed Title I and II of ERISA and reporting requirements associated with various DC plans. We examined Form 5500 with selected schedules and reviewed secondary legal documents such as W-2 forms, instructions, as well as guidance provided by Labor on 403(b) plans and 457 plans.

We conducted this performance audit from June 2008 through September 2009 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.



# Appendix II: Comments from the Internal Revenue Service



DEPUTY COMMISSIONER

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

August 19, 2009

Ms. Barbara D. Bovbjerg  
Director, Education, Workforce and  
Income Security Issues  
U.S. Government Accountability Office  
441 G Street, N.W.  
Washington, D.C. 20548

Dear Ms. Bovbjerg:

I reviewed your draft Government Accountability Office (GAO) report titled "Better Information and Sponsor Guidance Could Improve Oversight and Reduce Fees for Participants" (GAO-09-641).

The report makes an important contribution to the retirement community's understanding of the types of fees charged to defined contribution retirement plans and how those fees may vary depending on factors such as plan size. As you have pointed out in earlier reports, and reiterate in this one, fees have a direct impact on the account balances of participants in defined contribution plans, and a resulting impact on these individuals' retirement income. We agree that plan sponsors, administrators, and advisors can benefit from clear information about fees.

As you point out, the Department of Labor (DOL) has primary responsibility for issues relating to fees charged by firms that provide services to defined contribution plans. The DOL, in its response to this report, has outlined a program of regulation that it has undertaken to address this issue.

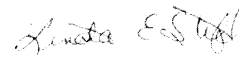
The Employee Plans function of our Tax Exempt and Government Entities Division has a wide-ranging customer education and outreach program which communicates with plan participants, sponsors, administrators and professional practitioners on matters of importance to the retirement community. As part of this program, Employee Plans publishes two quarterly electronic newsletters. "Employee Plan News" goes to 68,000 attorneys, accountants and actuaries who practice in the employee plans area. "Retirement News for Employers," aimed at small businesses (that tend to sponsor smaller-size defined contribution plans), goes to 50,000 subscribers. In each of these publications we feature a "DOL Corner" which contains news and direct communications from the DOL. Readers of our newsletters may link directly to DOL sources. These resources are available to provide our retirement community audiences with current information not only on tax-related matters, but also on important DOL issues such as fees.

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We look forward to working with the DOL on initiatives that will advance the goal of educating the retirement community about fees, and finding effective ways to reduce fees in order to boost retirees' income.

Responses to your specific recommendations are enclosed. We appreciate the continued and valuable support from you and your staff on this issue. If you have any questions or would like to discuss this response in more detail, please contact Sarah H. Ingram, Commissioner, Tax Exempt and Government Entities Division, at (202) 283-2500.

Sincerely,



Linda E. Stiff

Enclosure

Enclosure

**Recommendation for the Commissioner**

Together with the Secretary of Labor, provide guidance designed for sponsors of all types of defined contribution plans to suggest ways sponsors can cost-effectively decrease participants' fees.

**Response**

We would be pleased to consult with the Department of Labor (DOL) on ways plan sponsors can reduce participants' fee. As the DOL notes in its letter to Government Accountability Office in response to this report, it has undertaken the development of several regulatory projects intended to provide "useful and straightforward fee disclosure guidance in the near future." As the Secretary of Labor releases such guidance, we will use our customer education and outreach tools to help disseminate it, including posting the guidance or advice, or links to it, on the Internal Revenue Service's Employee Plans page.

**Recommendation for the Commissioner**

To provide improved oversight and ensure participants are not violating tax-deferral limits, the Commissioner of Internal Revenue should collect information to allow the Internal Revenue Service to easily differentiate between 457 plans sponsored by governments and 457 plans sponsored by tax-exempt entities.

**Response**

The concern underlying this recommendation arises because participants age 50 and above in 457(b) plans sponsored by a governmental unit may make annual "catch-up" contributions in addition to the standard annual contribution. However, participants in 457(b) plans sponsored by tax-exempt organizations may not make such "catch-up" contributions.

The Tax Exempt and Government Entities Division will explore ways to effectively differentiate between the two kinds of section 457(b) plans, including the possibility and the effect of amending the instructions for the Form W-2 to add a letter code or codes that will distinguish between governmental and tax-exempt section 457(b) plans.

**Recommendation for the Commissioner**

To help ensure that information about service providers' violations is shared with financial regulators, we recommend that the Commissioner of Internal Revenue work with financial regulators to establish a formal MOU. Such a MOU would help instruct agents and would be appropriate for limited occasions when information on service providers can be shared without revealing protected taxpayer information. In addition, the agencies should periodically review and update the MOU, as appropriate.

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**Response**

In our work with other federal agencies, we comply with section 6103 of the Internal Revenue Code. This is an important provision that addresses both the confidentiality and the disclosure of tax returns and return information. Acting carefully, we have been able to cooperate with federal agencies in highly effective enforcement efforts while fully respecting section 6103. A recent example is our partnership with the Department of Justice and the Federal Trade Commission. In that instance, we collectively moved against entities posing as tax-exempt credit counseling organizations without using a memorandum of understanding. We believe that the recommendation for a memorandum of understanding with financial regulators is not a substitute for carefully structured cooperation with these agencies, tailored to the characteristics of the situation. We have found that such cooperation is both effective and consistent with section 6103, and will engage in that cooperation in the situations you described.

# Appendix III: Comments from the Department of Labor

U.S. Department of Labor

Employee Benefits Security Administration  
Washington, D.C. 20210



August 13, 2009

Ms. Barbara D. Bovbjerg  
Director, Education, Workforce, and  
Income Security Issues  
United States Government Accountability Office  
Washington, DC 20548

Dear Ms. Bovbjerg:

We have reviewed the Government Accountability Office's (GAO) draft report entitled "Retirement Savings - Better Information and Sponsor Guidance Could Improve Oversight and Reduce Fees for Participants" (GAO-09-641) and the recommendation contained therein as it relates to the Secretary of Labor.

Specifically, the GAO is recommending that the Secretary, together with the Commissioner of the Internal Revenue Service, provide guidance designed for sponsors of all types of defined contribution plans to suggest ways sponsors can cost-effectively decrease participant fees.

The Department agrees with the GAO that excessive fees can undermine the retirement security of plan participants. ERISA requires plan fiduciaries, when selecting or monitoring service providers, to act prudently and solely in the interest of the plan's participants and beneficiaries. Fundamental to a plan fiduciary's ability to discharge these obligations is the availability of information sufficient to enable the plan fiduciary to make informed decisions about the services and the reasonableness of the costs for those services. Similarly, understanding what and how expenses affect participant accounts is of critical importance to plan participants and beneficiaries in choosing among investment choices.

While these principles may appear straight forward, the Department recognizes that understanding and obtaining the information necessary to make informed decisions about plan service providers, including their compensation arrangements, may be challenging for many plan sponsors. In recognition of this challenge, and consistent with the recommendations of the GAO, the Department has undertaken the development of a regulation that will not only assist plan sponsors in understanding what information they need to make informed decisions about their service providers, but will help assure that plan fiduciaries are provided the needed information by their service providers. Specifically, the Department proposed a regulation amending the rule under section 408(b)(2) of ERISA to establish an affirmative obligation on plan fiduciaries to obtain enumerated disclosures from service providers and on plan service providers to furnish such disclosures to plan fiduciaries. This information will enable plan fiduciaries to understand the nature and scope of the services to be provided, the cost of those

services, taking into account revenue sharing and other arrangements that may affect the cost of such services, and potential conflicts of interest on the part of service providers that may affect the quality of the services to be furnished to the plan. This regulation was published in proposed form on December 13, 2007 (72 FR 70988) and a public hearing was held regarding the proposal on March 31 and April 1, 2008. The Department currently is in the process of reviewing the regulatory record, including public comments, and plans to move forward in providing useful and straightforward fee disclosure guidance in the near future.

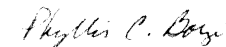
We also wish to note that, independent of the regulation under section 408(b)(2) of ERISA focusing on fiduciary-level disclosures, the Department is taking steps to improve the disclosure of fee and related plan information to pension plan participants and beneficiaries. A proposed rule was published in the Federal Register on July 23, 2008 (73 FR 43014). A component of the Department's proposal was a requirement that participants and beneficiaries be furnished a chart or similar document that would facilitate informed investment decisions by the plan's participants and beneficiaries. The Department currently is reviewing this regulation for purposes of adopting a final rule and model disclosure chart.

In addition, and also consistent with the GAO's recommendation, the Department maintains both educational materials and outreach events designed to assist plan sponsors in understanding their responsibilities under ERISA, including the selection and monitoring of service providers. Examples of materials available on our website include: "Meeting Your Fiduciary Responsibilities", "Understanding Retirement Plan Fees And Expenses" and guides for selecting and monitoring pension consultants, service providers and plan auditors. Information concerning our educational programs also is available on our website. The Department conducts numerous education and outreach events each year. Both our educational materials and our educational programs will be updated to reflect the new requirements of the section 408(b)(2) regulation, following its publication in the Federal Register.

Finally, we note that the Department coordinates with the Department of Treasury and the Internal Revenue Service on a wide variety of issues of mutual interest, including the formulation of regulatory standards and the delivery of public education programs. We believe plan sponsors and other members of the regulated community benefit significantly from such cooperative efforts.

As evidenced by the foregoing, the Department has been sensitive to plan cost and related issues for some time. EBSA is committed to protecting the employer-sponsored benefits of American workers, retirees, and their families. We appreciate having had the opportunity to review and comment on the draft report. Please do not hesitate to contact us if you have questions concerning this response or if we can be of further assistance.

Sincerely,



Phyllis C. Borzi  
Assistant Secretary

# Appendix IV: Characteristics of DC Plans and IRAs

DC plans together have about the same amount of estimated assets as all types of IRA accounts, as shown in table 10. At the end of 2008, assets for DC plans were estimated at \$3 billion, while for IRAs, total estimated assets were about \$3.6 billion. 401(k) plans have significantly more assets than 403(b) plans or 457 plans.

**Table 10: Estimated Total Assets for DC Plans and IRAs, 2008**

(Dollars in billions)	
	Total assets
401(k)	\$2,350
403(b)	572
457(b) governmental and tax-exempt	140
Traditional IRAs	3,221
Roth IRAs	165
SEP <sup>a</sup>	180
SIMPLE	44

Source: ICI.

Note: Data on 401(a) and 457(f) plans are not available. Data in this table are estimated and should not be compared to the data in other tables.

<sup>a</sup>Asset estimates for SEP plans include figures for Salary Reduction-SEP (SAR-SEP) plans. The Small Business Job Protection Act of 1996 prohibited the formation of new SAR-SEP IRAs after December 31, 1996.

Table 11 shows estimated contributions to different types of DC plans in 2007. Participants and sponsors made significantly more contributions to 401(k) plans than other types of DC plans.

**Table 11: Estimated Contributions to DC Plans, 2007**

(Dollars in billions)	
	Contributions
401(k)	\$165
403(b)	28
457(b) governmental and tax-exempt	13

Source: IRS.

Note: Data on 401(a) and 457(f) plans are not available. The data in this table were provided by IRS and come from a database that contains data taken from annual Form W-2 filings. The data are estimated and should not be compared to the data in other tables. See appendix I for further discussion of this issue.

Although table 10 shows that total assets for traditional IRAs are significantly greater than assets for other types of IRAs, estimated contributions for 2006 are less disparate, as shown in table 12. Traditional IRAs often receive rollovers from DC plans; therefore their assets are greater.

**Table 12: Estimated Contributions to Individual IRA Accounts, SEP, and SIMPLE Accounts, 2006**

(Dollars in billions)	
	Contributions
Traditional IRA	\$18
Roth IRA	19
SEP	15
SIMPLE	9

Source: IRS.  
Note: This data came from IRS’s Compliance Data Warehouse and IRS’s Statistics of Income. The data are estimated, and should not be compared to the data in other tables. See appendix I for further discussion of this issue.

Table 13 shows the estimated number of individuals who own IRA accounts and contribute to employer-sponsored IRAs. Individual traditional and Roth IRAs have significantly more account owners than participants in employer-sponsored IRAs.

**Table 13: Estimated Number of Individual IRA Account Owners and Individuals Contributing to Employer-Sponsored IRAs, 2006**

	Number of account owners (thousands)
Traditional IRA	5,414
Roth IRA	6,843
SEP	1,559
SIMPLE	2,088

Source: IRS.  
Note: This data came from IRS’s Compliance Data Warehouse and IRS’s Statistics of Income. The data are estimated and should not be compared to the data in other tables. See appendix I for further discussion of this issue.



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# Appendix V: GAO Contact and Staff Acknowledgments

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## GAO Contact

Barbara D. Bovbjerg (202) 512-7215 or [bovbjergb@gao.gov](mailto:bovbjergb@gao.gov)

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## Staff Acknowledgments

In addition to the contact named above, Tamara Cross, Assistant Director; Anna Bonelli; Kenrick Isaac; William King; Jillena Roberts; John W. Wheeler, Jr.; Jaime Allentuck; Susan Baker; Alex Galuten; Mimi Nguyen; Jessica Orr; Walter Vance; and Najeema Washington made important contributions to this report.

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