Financing Your 401(k) Plan

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Introduction & Background

Participants in 401(k) plans will soon have access to increased fee disclosure regarding plan administration (also referred to as recordkeeping). Set to become effective November 1, 2011 with a 120-day transition period, the Department of Labor's (DOL) new policy includes a requirement to disclose to participants when plan investments, through a component of their expense ratio, are being utilized to pay for plan administration and/or other qualified plan expenses. Also known as revenue sharing, this convenient and often default plan financing practice has been commonplace for years, yet has largely gone unnoticed by participants due to insufficient transparency.

While using revenue sharing to pay for plan administration services is routine, the fact that it is collected as a percent (also referred to as basis points, or "bps") of assets creates issues of participant subsidization -- whereby some participants pay higher recordkeeping fees than other participants in the same plan, despite having access to the same suite of services. This occurs by virtue of their account balance and/or investment allocation rather than the quality or level of services received. In a plan utilizing this financing practice, participants with higher account balances and/or invested in higher revenue sharing options (both relative to others in the plan) are subsidizing the recordkeeping cost of the participants with lower account balances and/or invested in lower revenue sharing options. This has a direct impact on participant account balances and can be considered an inequitable way to allocate plan costs across the participant base, as there is a wide disparity between the services rendered and the costs of those services at the individual level.

As participants continue to gain access to greater fee transparency, many of them in plans that use revenue sharing to cover plan expenses will likely be alarmed to learn how their administration fees are collected, especially when tied to their investment allocation. Furthermore, once participants understand that they may additionally be paying for services for the benefit of their colleagues and realize that this practice has been in place for an extended time period, the level of concern will likely increase greatly -- in turn increasing a fiduciary's liability exposure. In an effort to potentially lower their liability, plan sponsors should take this opportunity, if they have not yet done so, to review plan financing options with their recordkeeper and ensure that they utilize the method most appropriate for their specific plan.

Recent Trends

Over the past few years, a growing number of plan sponsors have transitioned their plan financing strategy from a revenue sharing model to direct per participant fees. In this model, the plan administration fees are directly charged to participant account balances, usually in an evenly allocated manner. Since revenue sharing is not required in this approach, the plan can therefore use the lowest cost investment vehicle and/or share class, for which the plan qualifies, for each of their investment managers.

At Gosselin Consulting Group, we believe an evenly distributed direct per participant fee is the appropriate financing strategy for most plans. This strategy fairly allocates the recordkeeping costs across the participant base, minimizes or eliminates participant subsidization, provides participants with full plan administration fee transparency, mitigates certain fiduciary liabilities, and allows for more effective performance monitoring. While often perceived to lead to participant confusion or dissatisfaction, our experience shows that these issues can be overcome by proper communication and education. When done in conjunction with a transition to a fixed fee pricing model, this approach can oftentimes lead to lower overall plan administration costs and investment fees, both of which ultimately benefit plan participants.

In this paper, we will explore:

- Fiduciary Implications of Plan Financing Strategies
- New Plan-Related Participant Fee Regulations
- Plan Financing Strategies & The Subsequent Impact on Participant Account Balances
- The Long-Term Impact of Participant Subsidization
- Additional Thoughts and Considerations

Fiduciary Implications

While the DOL does not mandate or recommend a particular plan financing strategy, portions of Rule 408(b)(2) and ERISA fiduciary standards in general would suggest that direct per participant fees would comply with industry best practices if applied at the participant level.

According to DOL Rule 408(b)(2), plan sponsors, as fiduciaries, can enter into a service arrangement only if:

- fee arrangements or contracts with plan service providers are reasonable
- only reasonable compensation is paid for services provided
- certain disclosures are made by the service provider, including conflicts of interest that may compromise the delivery of the services provided

According to ERISA fiduciary standards, plan sponsors are required to act prudently and solely in the interest of the plan's participants and beneficiaries. As part of their responsibilities as a fiduciary, they must:

- act with a duty of loyalty and manage all decisions for the exclusive benefit of plan participants and their beneficiaries
- implement policies and procedures to manage and avoid conflicts of interest
- assess the reasonableness of all service provider fees

Considering participants in a plan generally have access to the same set of services, those paying administration fees higher than the plan's average participant (total plan administration costs divided by number of participants) could consider their fees unreasonable and therefore not in their own best interest. Conceivably, it could also suggest that the plan sponsor is favoring those participants who are paying less than the plan's average participant. Additionally, the fact that a participant account balance or the choice of a particular investment can impact a participant's administration fees creates an inherent conflict of interest.

In light of new fee disclosure regulations, inadequate participant account balances, and ongoing market volatility, emphasis on participant fee awareness will continue to be an area of interest for public policy makers, plan sponsors, and participants. Plan sponsors need to ensure that their financing strategy is the most appropriate and effective option for their plan and should be prepared to field participant questions and/or concerns regarding the utilization of the particular strategy.

In conjunction with choosing a plan financing strategy, plan sponsors must also choose the pricing strategy (asset vs. fixed fees) most appropriate for their plan. The pricing strategy usually precedes the financing discussion. Similar to the plan financing strategy, we encourage plan sponsors to clearly understand the available pricing models, including their impact to fees over the duration of the service provider contract period, and request or choose the model they believe to be most appropriate for their plan. Otherwise, the plan may end up paying excessive compensation/unreasonable fees to the recordkeeper as plan assets grow, thus potentially leading to a fiduciary breach. For more information on this subject, please refer to the Gosselin Consulting Group position paper titled **"The Cost of Free Recordkeeping."**

New Regulations

Plans that finance all or a portion of their general plan administration services through a direct per participant charge will be required to illustrate the specific participant fee in dollar terms on a quarterly basis, and also provide an explanation of the services provided for that fee. Although the regulation is new, most plans that utilize this financing strategy already disclose this information. Participants in plans using this model can continue to invest knowing that their account balance, in most cases, and their investment choices will not impact their administration fees.

Plans that finance all or a portion of their general plan administration services through revenue sharing will not be required to illustrate the specific amount that directly offsets recordkeeping expenses in any form (bps or hard dollar). These plans will only be required to indicate that a portion of one or more funds' stated total expense ratio is used to offset plan administration costs on a quarterly basis. For example, the statement may indicate the following:

> *"in addition to the expenses reported on the statement, some of the plan's administrative expenses for the preceding quarter were paid from the annual operating expenses of one or more of the plan's designated investment alternatives (e.g., through revenue sharing arrangements, Rule 12b–1 fees, sub-transfer agent fees)"*
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> Source: Federal Register l Part IV l Department of Labor l Employee Benefits Security Administration l 29 CFR Part 2550 l Fiduciary Requirements for Disclosure in Participant-Directed Individual Account Plans; Final Rule (October 20, 2010)

The obvious drawback to this statement is that it does not indicate which of the investments contributed to administrative expenses or how much they each contributed. As a result, participants in plans using revenue share will remain unable to determine their administration fees, yet those paying close attention will now be aware that their account balance and most likely their investment choices will determine their administration fees -- thus leading to broader plan sponsor fiduciary exposure.

Regardless of the plan administration financing strategy, all plans that charge fees for actions specific to a particular participant will be required to disclose and provide a description of the assessed fee. Examples of direct charges include loan fees and qualified domestic relations order (QDRO) processing fees. At Gosselin Consulting Group, we are proponents of participants directly bearing the costs associated with any additional services received and/or transactions performed whenever possible.

For further information regarding this new regulation, please refer to the following DOL web addresses:

- Summary Fact Sheet: http://www.dol.gov/ebsa/newsroom/fsparticipantfeerule.html
- Federal Register Rules and Regulations: http://webapps.dol.gov/FederalRegister/PdfDisplay.aspx?DocId=24323

Plan Financing Strategies

"Plan financing" refers to the methodology by which a 401(k) plan pays for its non-investment-manager-related expenses. These expenses may include general plan administration fees, other service provider fees (i.e. third party investment consultant, accounting, legal, etc.), and participant-initiated transaction fees. For the purposes of our discussion, we will focus on the payment of general plan administration fees, though it is important to note that other service provider fees can be financed utilizing the same approaches presented below. Additionally, we will assume that individual transaction fees (i.e. loans, QDRO's, etc.) are charged directly to the participant performing the transaction.

The table below illustrates three separate strategies that can be used to pay for general plan administration costs. The strategies include:

1) charging fees directly to participant accounts (Models A or B)
2) assessing fees through plan investments (Models C or D)
3) directly charging fees to the corporate entity sponsoring the plan (Model E)

In some instances, a plan sponsor may utilize a combination of two or more models, either consciously or unknowingly. While most recordkeepers have their own preferred strategy, many will now allow for flexibility if requested by the plan sponsor and/or their consultant. In light of fiduciary responsibilities and liabilities, we encourage plan sponsors to inquire about their financing options and request the approach that best meets their plan's unique objectives.

	Direct Per Participant Fee ($)		**Through Plan Investments - Revenue Sharing (bps)**		**Direct Plan Sponsor Fee ($)**
	(A)	**(B)**	**(C)**	**(D)**	**(E)**
Sub-Type (if any)	Evenly distributed (each participant pays same dollar amount for recordkeeping)	Pro-rata distributed (individual participant recordkeeping fee based on asset balance)	Revenue share (bps) is equal across investments	Revenue share (bps) varies between investments	-
			Proprietary recordkept investments will create additional investment management fee revenue for recordkeeper		
Plan Administration Cost Distribution	All participants pay the same dollar amount (no subsidization)	Pro-Rated: Participants with higher account balances pay more than those with lower account balances	Participants with higher account balances pay more than those with lower account balances	Participants in higher revenue share investments and/or with higher account balances pay more than those in lower revenue sharing investments and/or with lower account balances	Plan sponsor pays all service provider expenses
Investment Vehicles / Share Classes Utilized [1,2]	Lowest cost available	Lowest cost available	Higher cost (includes revenue sharing component)	Higher cost (includes revenue sharing revenue component)	Lowest cost available
Participant Plan Administration Fee Transparency	Full fee transparency	Full fee transparency	Lacking transparency [3]	Lacking transparency [3]	Full fee transparency
Additional Costs Required	-	-	• Unitization costs • Custom reporting and communication costs • Implicit costs	Implicit costs	-
Considerations	• Fee as % of account balance can be significant for participants with very small account balances	• Participant subsidization	• Participant subsidization • Transparency • Additional plan costs • Potential for error • Implicit costs	• Participant subsidization • Transparency • Implicit costs	• Corporate earnings and financial stability • Non-participating employee technically share costs

[1] For desired investment managers (unless recordkeeper restrictions apply - i.e. proprietary requirement, etc.)
[2] Based on plan meeting any specific investment manager requirements (i.e. asset minimum, etc.)
[3] Unless plan sponsor requests transparency and plan administrator has functionality to comply

Choosing the Appropriate Plan Financing Strategy

Choosing an appropriate plan financing strategy is an important decision that carries fiduciary implications for the plan sponsor. At Gosselin Consulting Group, we are advocates of the equitably distributed direct per participant fee model. However, we understand that each 401(k) plan has unique features and characteristics that may necessitate the use of an alternate financing strategy.

In order to initiate the financing discussion, we look to assess a committee's viewpoint on the three specific topics outlined below. Each topic is accompanied by a series of questions meant to facilitate the discussion. While there is an extensive list of additional considerations, we believe these three simple questions best assist the committee in developing a policy that is fair, justified, and transparent -- ultimately minimizing plan sponsor fiduciary liability and maximizing participant satisfaction.

1) Distribution of the Cost of Plan Administration Services (The implications of participant subsidization)

A) Should all participants pay the same fee (in dollar terms) for plan administration services?
B) Should participants pay for plan administration services based on their account balance?
C) Should participants pay for plan administration services based on their account balance and investment allocation?

Based on our experience, *most* plan sponsors would answer Yes to statement "A". *Some* plan sponsors would answer Yes to statement "B". Very few plan sponsors would answer Yes to statement "C". Yet despite these results, most plan sponsors continue to subscribe to statement "C" and pay for their plan administration via revenue sharing derived from the plan's investment options. If your plan utilizes one or more investment options that have varying amounts of revenue share (bps), your plan subscribes to "C". Both plan B & C create issues of participant subsidization and lack participant transparency.

2) Investment Vehicles / Share Classes Utilized

A) Should investment manager performance be judged net of investment management and operations fees?
B) Should investment manager performance be judged net of investment management fees, operational fees, and revenue share?

Based on our experience, *most* plan sponsors would answer Yes to statement "A" and *most* plan sponsors would answer No to statement "B". Plans that pay for plan administration costs through a direct per participant charge subscribe to Statement A. Plans that pay for plan administration costs through revenue sharing subscribe to Statement B. The revenue sharing component increases the total expense ratio, and thereby reduces the investment manager return. For plans that choose to use revenue sharing, it may be beneficial for the committee to additionally analyze the manager's lowest cost vehicle and/or share class performance, in addition to the higher priced vehicle and/or share class in the plan, in order to minimize the potential of making an imprudent investment decision due to revenue sharing embedded in the fund's expense ratio.

3) Participant Fee Transparency

A) Should participants be provided with full transparency with respect to the recordkeeping fees they are paying?
B) Should participants be provided with partial transparency with respect to the recordkeeping fees they are paying?
C) Should participants be provided with no transparency with respect to the recordkeeping fees they are paying?

While an answer of Yes to "A" and No to "B" and "C" would seem obvious, the practical application of full fee transparency is rare. This is largely a result of many plan sponsors using revenue sharing investment options to pay for their plan's administration. Based on our experience, reaching a consensus viewpoint on how to finance the plan's administration costs can be difficult and even controversial for the plan's committee and recordkeeper. As such, the DOL received a multitude of comments as they were developing new participant fee transparency regulations. An excerpt of these comments are provided below:

- *Some commenters expressed concern that participants and beneficiaries may be misled into believing that there is little or no administrative expense associated with their participation in the plan when a significant portion of the cost of administrative services is actually paid out of investment-related charges.*
- *Other commenters disagreed and believed that, because any such administrative services would be paid for from the total annual operating expenses of the designated investment alternatives in which participants invest and because such annual operating expenses are required to be separately disclosed, participants and beneficiaries will receive comprehensive information about the total charges, for administration and investment, that will be assessed against their accounts. These commenters also argue that the burden associated with attempting to attribute some portion of total annual operating expenses to plan administrative services would be significant and vastly outweigh any potential benefit to participants and beneficiaries of such attribution.*
- *Most commenters, however, agreed that it is appropriate to inform participants, when applicable, that administrative expenses are paid from investment- related fees and are not reflected in the reported administrative expense amount. The Department was persuaded that some information, even if general, would help participants to better understand the fees and expenses attendant to operating their plan and of the fact that some fees and expenses might be underwritten by the investment alternatives offered by their plans.*

Source: Federal Register I Part IV I Department of Labor I Employee Benefits Security Administration I 29 CFR Part 2550 I Fiduciary Requirements for Disclosure in Participant-Directed Individual Account Plans; Final Rule (October 20, 2010)

Based on new regulations, participants will be provided with limited fee transparency if the plan utilizes revenue sharing to pay for plan administration costs. Participants will be granted full fee transparency only if the plan charges a direct per participant fee for plan administration services. In our view, whenever the plan sponsor can provide its participants with greater transparency, whether with regard to investment costs or service provider fees, it serves to benefit both parties in making better and more informed decisions. As such, we are proponents of the direct per participant fee approach and the resulting full fee transparency to participants.

A Closer Look at Plan Financing Strategies and The Impact on Actual Participant Administration Fees

In this section, we have created a sample 401(k) plan to illustrate the participant impact, in dollar terms, of using plan financing Models A-D *(as described in the table on page 3).* We have not included an illustration for Model "E" in this section since the "Direct Plan Sponsor Fee" model does not directly impact participants and is rarely utilized. The plan statistics and investments for our sample 401(k) plan are outlined in the table below. Stated fees are shown on an annual basis. For the purpose of simplicity, the plan utilizes only four investments (in line with ERISA's diversification guidelines), of which all available share classes are listed within the table. Unless otherwise noted in the examples, all other plan and investment related statistics remain constant.

Sample Investment Manager Line Up (utilized in tables below, for Models A-D)

Plan Statistics					
Plan Assets = $200 million	# of Participants = 5,000	Fixed Annual Per Participant Fees = $60 per participant (Total Plan Administration Fees: 5,000 x $60 = $300,000)			
Investment Name [1,2]	**Asset Class**	**"Rev Share" Class Expense Ratio (%)**	**Revenue Sharing (%)**	**"Instl" Class Expense Ratio (%)**	**Revenue Sharing (%)**
Investment W	Pre-Diversified	0.85%	0.40%	0.45%	0.00%
Investment X	Stable Value	0.40%	0.25%	0.15%	0.00%
Investment Y	Domestic Equity	-	-	0.05%	0.00%
Investment Z	International Equity	1.20%	0.15%	1.05%	0.00%

[1] Investment managers A - D are included as samples and are not meant to represent any particular investment managers
[2] The asset classes provided are included as samples and not meant to represent any recommended asset class structure

Direct Per Participant Fee Collection (Models A & B) *as illustrated in the Plan Financing Strategy table on page 3*

General plan administration fees are collected via a direct charge against the participant's account balance -- fully independent from the participant's investments. Most often, these fees are evenly allocated across the participant base, although some plans choose to pro-rate the fees based on account balance. Fees are typically posted and collected on a quarterly or annual basis. Since administration fees are collected via participant account charges, the plan can utilize their investment managers' lowest cost investment vehicle and/or share class, assuming the plan meets any specific investment requirements. Plan administration fees are fully transparent to the participants and the issue of participant subsidization is significantly reduced or, ideally, eliminated.

Model A: Evenly Distributed Across Participant Base

In this model, each participant pays the same fee (in dollar terms) for recordkeeping services. There is clearly a case for this methodology if one assumes that participants within a particular plan generally have access to and receive the same suite of services, as is typically the case with retirement plans.

The table below illustrates this methodology. The plan administration fee *(in gray)* remains the same for all participants despite differences in account balances and investment holdings (*in orange*). Revenue sharing *(in green)* is eliminated, as the plan can utilize their investment managers' lowest cost vehicle and/or share class.

MODEL A Participant Name	Account Balance ($)	Investment Option	Prospectus Net Expense Ratio (%)	Revenue Sharing Component (%)	Plan Admin Fee ($) [1]
Participant 1	$10,000	Investment W	0.45%	0.00%	$60
Participant 2	$50,000	Investment X	0.15%	0.00%	$60
Participant 3	$100,000	Investment Y	0.05%	0.00%	$60
Participant 4	$500,000	Investment Z	1.05%	0.00%	$60

[1] Fee represents actual per participant fee quote ($60 per participant) from plan administrator.

At Gosselin Consulting Group, we believe this is the most equitable plan financing strategy, as participants generally have access to and receive the same suite of services. Utilizing the lowest cost investment vehicle and/or share class for each desired investment manager maximizes investment performance and provides for the most representative manager performance evaluation. Ultimately, we believe this allows the plan sponsor to best position themselves as a fiduciary.

Please note that select circumstances may impact a plan sponsor's ability or desire to structure a portion or their entire plan with this approach. For example, a start-up plan with minimal assets may not have the scale to qualify for their investment managers' lowest cost vehicles/share classes. Additionally, plans of all sizes may not have the appetite to charge a fee directly to new participants until they reach an established account balance threshold, so that the fee isn't excessive relative to their balance (on a percentage basis). For example, consider a participant who is new to the plan and has an average year one account balance of $1,000. The $60 plan administration fee utilized in this example would constitute 6% of their account balance. In these cases, the corporate entity may want to consider financing these plan administration costs on behalf of those participants until a minimum acceptable balance is reached.

As noted earlier, direct per participant fees are often perceived to lead to participant confusion or dissatisfaction, yet our experience shows this not being the case when the transition to this model is properly communicated. Often, when done in conjunction with a transition to a fixed fee pricing model, this approach improves the quality of investment choices and lowers overall participant costs, both of which ultimately benefit plan participants through higher account balances.

Model B: Pro-Rated Across Participant Base by Account Balance

In this model, each participant pays a pro-rated recordkeeping fee (in dollar terms) based on their account balance. Therefore, participants with larger account balances pay higher recordkeeping fees than those with lower balances -- thus creating an issue of subsidization if all participants are receiving the same level and type of services. Since participants generally have access to the same suite of services, we find this methodology more challenging to justify from a fiduciary standpoint vs. Model A, the evenly distributed model.

Though we are not proponents of this model, this methodology of subsidization is one that many Americans are quite familiar with. The US tax system is one where citizens with a larger taxable income pay higher taxes, in dollar terms, than those with a lower taxable income, despite generally receiving the same services. In fact, the US tax code takes this concept one step further, as the tax rate (in bps or tax rate percentage terms) additionally increases as one's taxable income base expands (often referred to as a progressive tax/fee).

A plan can arrive at a pro-rated by account balance structure through two models. The first model, B, is illustrated below, while the second model, C, is illustrated in the **Through Plan Investments (Revenue Sharing) Fee Collection** section on the following page.

Like Model A, the fee in Model B is directly charged against the participant account balance, but is now based on the size of the account balance. The table below illustrates this methodology. The plan administration fee *(in gray)* increases based on account balance despite the fact that participants generally receive the same suite of services and invest in different options. Revenue sharing *(in green)* is eliminated, as the plan can utilize their investment managers' lowest cost vehicle and share class.

MODEL B Participant Name	Account Balance ($)	Investment Option	Prospectus Net Expense Ratio (%)	Revenue Sharing Component (%)	Plan Admin Fee ($) [1]
Participant 1	$10,000	Investment W	0.45%	0.00%	$15
Participant 2	$50,000	Investment X	0.15%	0.00%	$75
Participant 3	$100,000	Investment Y	0.05%	0.00%	$150
Participant 4	$500,000	Investment Z	1.05%	0.00%	$750

[1] Plan Admin Fee = Participant Account Balance / Plan Assets * Total Plan Administration Fees

Through Plan Investments (Revenue Sharing) Fee Collection (Models C & D) *as illustrated in the Plan Financing Strategy table on page 3*

Under this model, general plan administration fees are collected via revenue sharing. In some cases, plan administration fees may be further subsidized through proprietary investment management fees. Since plan administration costs are paid from revenue sharing and management fees, both components of the fund's total expense ratio, it forces the plan sponsor to make key investment decisions with plan administration fees in mind. Under this model, plan administration fees are not transparent to participants.

For the purposes of our discussion, we will focus on the revenue sharing component of the expense ratio. While some plan sponsors choose to pro-rate the fees based on account balance (similar to Model B), the task can be complex and administratively burdensome, resulting in increased overall plan fees. More often, the plan's investments have varying levels of revenue share. As a result, a participant's investment mix, not the quality, amount, or type of services received, determines that participant's administration fees. Administration fees are typically processed daily through the funds' NAVs and collected from the investment manager or other custodian by the plan administrator on a quarterly basis. Since administration fees are collected via the investment expense ratios, the plan will either have to unitize their investment managers lowest cost vehicle and/or share class to create "revenue sharing" or utilize a more expensive share class that already includes revenue sharing.

Model C: Pro-Rated Across Participant Base by Account Balance

As previously mentioned, this strategy mimics Model B in terms of its account balance subsidization, yet its implementation is quite different and actually increases overall plan fees. In order to achieve this type of cost allocation through investments, the plan investments must each generate the same amount of revenue sharing (in bps or percentage terms). Using our sample 401(k) plan statistics, each investment option must generate 15 bps (or 0.15%) of revenue sharing:

Revenue Sharing (15 bps or 0.15%) = Total Plan Administration Fees ($300,000) / Total Plan Assets ($200,000,000)

This structure, while simple in theory, is often complicated to implement for two major reasons: 1) revenue sharing levels often vary between asset classes and firms, and 2) plan assets are constantly fluctuating. As a result, most plans have to incur additional costs related to unitizing plan investments (re-striking the NAV with a wrap fee to create equal levels of revenue sharing) and developing custom communication materials. Below we take a closer look at these factors and their impact to our sample plan:

1. Revenue Share Variation: Amongst the plan's four investment options, only one investment manager (Z), has an existing share class with 15 bps revenue sharing *(as referenced on page 5 "Rev Share" class)*. As a result, each of the remaining three funds' lowest cost share class will need to be unitized with a 15 bps wrapper to create the proper level of revenue sharing. As an example, we list the calculation below for Investment Manager W, one of the three managers required to be unitized.

"Unitized" Total Expense Ratio (0.62%) = Base Total Expense Ratio (0.45%) + Wrapper (0.15%) + Hypothetical Unitization Costs (0.02%)

2. Plan Asset Fluctuation: Constant asset fluctuation necessitates occasional wrap fee adjustments. As noted above, it initially appeared as if only three investment options required unitization. However, as plan assets rise or fall, the percentage (or bps) of plan assets required to cover the $300,000 annual plan administration fee fluctuates. In this example, a 6.5% decrease in assets requires a 16 bps wrap fee, just as a 7% increase in assets only requires a 14 bps wrap fee. As an example, we've provided the calculation for a 6.5% decrease in assets.

New Plan Assets ($187,000,000) = Base Plan Assets ($200,000,000) - [Base Plan Assets ($200,000,000) x Plan Return (6.5%)]
New Revenue Share Requirement (16 bps or 0.16%) = Total Plan Administration Fees ($300,000) / New Plan Assets ($187,000,000)

As a result, all four investment's lowest cost share class would eventually have to be unitized to properly account for these ongoing changes.

Like Model B, which creates issues of participant subsidization, we find this model challenging to justify considering all participants generally have access to the same suite of services. This model also increases overall plan costs (unitization fees, custom communication materials), necessitates additional work (increasing chance of error), creates constant expense ratio fluctuations, and adds to participant confusion -- all factors which lead to increased fiduciary liability.

The table below illustrates this methodology in more detail. As with Model B, the plan administration fee *(in gray)* increases based on account balance, despite the fact that participants generally receive the same suite of services and invest in different investment options. In contrast however, participants incur the unitization fees *(in orange)* in addition to the plan administration fees. These unitization fees are usually embedded as a component of the fund's unitized expense ratio. Revenue sharing *(in green)*, created by the wrap fee component, now exists. As a result, the total expense ratio increases by 17 bps for each investment option (15 bps wrap fee + 2 bps unitization fee), thus negatively impacting performance.

MODEL C Participant Name	Account Balance $	Investment Option	Prospectus Net Expense Ratio (%)	Revenue Share Component (%)	Unitization Component (%)	Plan Admin Fee ($) [1]	Unitization Fee ($)
Participant 1	$10,000	Investment W	0.62%	0.15%	0.02%	$15	$2
Participant 2	$50,000	Investment X	0.32%	0.15%	0.02%	$75	$10
Participant 3	$100,000	Investment Y	0.22%	0.15%	0.02%	$150	$20
Participant 4	$500,000	Investment Z	1.22%	0.15%	0.02%	$750	$100

[1] Plan Admin Fee = Participant Account Balance / Plan Assets * Total Plan Administration Fees

Model D: Determined by Investment Allocation

In this model, each participant pays a recordkeeping fee (in dollar terms) based on both their investment allocation and their account balance. Since we have already discussed the account balance subsidization issue, we will now focus on the investment allocation component. Investment allocation subsidization occurs when one or more funds within the plan have variation in their revenue sharing level (bps or percentage terms). In this example, we utilize each investment manager's share class with the higher revenue sharing component. Participants in the investments with the higher revenue sharing component pay higher recordkeeping fees than those invested in funds with the lower revenue sharing component, assuming all else is held equal.

The table below illustrates this methodology. Here we have purposely set each participant's account balance at $60,000 to avoid account balance subsidization and more specifically, illustrate investment allocation subsidization. Therefore, the participant's plan administration fee *(in gray)* is entirely based on their investment choice. At the extremes, Participant 1, invested in the fund with 40 bps revenue sharing, incurs $240 in annual recordkeeping fees while Participant 3, invested in the fund with 0 bps revenue sharing, incurs no annual recordkeeping fees.

MODEL D Participant Name	Account Balance $	Investment Option	Prospectus Net Expense Ratio (%)	Revenue Share Component (%)	Plan Admin Fee ($) [1]
Participant 1	$60,000	Investment W	0.85%	0.40%	$240
Participant 2	$60,000	Investment X	0.40%	0.25%	$150
Participant 3	$60,000	Investment Y	0.05%	0.00%	$0
Participant 4	$60,000	Investment Z	1.20%	0.15%	$90

[1] Plan Admin Fee = Participant Account Balance * Revenue Share Component

Additional Considerations Regarding Account Balance Subsidization & Revenue Sharing

As discussed, revenue sharing and direct per participant charges based on individual balances can dramatically alter administration fees at the participant level within a particular plan, as they are impacted by account balances and/or investment choices.

- When considering the impact of account balance, it is important to remember that a participant's investment performance and contribution / withdrawal rates will alter their administration fee. Essentially those participants whose performance is better than the plan's average and who contribute more than the plan average will increasingly be paying for a higher percentage of the plan's administration costs potentially creating an issue when considering education materials encourage higher contribution percentages.

- When considering the impact of investment choice, it is important to remember that those participants choosing investment managers with higher revenue sharing will unknowingly pay higher administration fees. While this in itself is a conflict, consider the risks for a plan that is set up for auto-enrollment into a default option, where that option has the highest revenue share amongst all plan options. Similarly, consider a plan where the stable value fund, usually the lowest returning investment in the plan (especially considering today's rates), has the highest revenue share component.

Additional Considerations Regarding Equitably Distributed Direct Per Participant Fees

As much as a plan sponsor may want to achieve zero revenue sharing for all their investment options, it may not be possible based on the investment managers offered in the plan or those being considered. Still today, many investment firms do not offer a non-revenue sharing mutual fund share class or collective trust and some investment firms that do offer them may have minimum qualifications that some plans may not meet. Additionally, the net investment cost (total net expense ratio less revenue sharing) for a share class with revenue sharing may actually be more beneficial to the plan than the lowest cost share class. In both instances, plan sponsors need to consider the severity of the situation to determine their best approach and ensure that a prudent process is followed to arrive at a decision, while ensuring all criteria followed are properly documented.

The Long Term Impact of Participant Subsidization

The concept of revenue sharing is often discussed on an annual basis and is typically presented in a basis points format. For some, this format mistakenly de-emphasizes the impact of subsidization on relative participant account balances within a plan. We have presented the dollar impact of subsidization in annual terms, but now consider the long-term impact that subsidization can have on a participant's account balance over the duration of their working life (while keeping in mind that the average 401(k) participant balance is only $75,000).

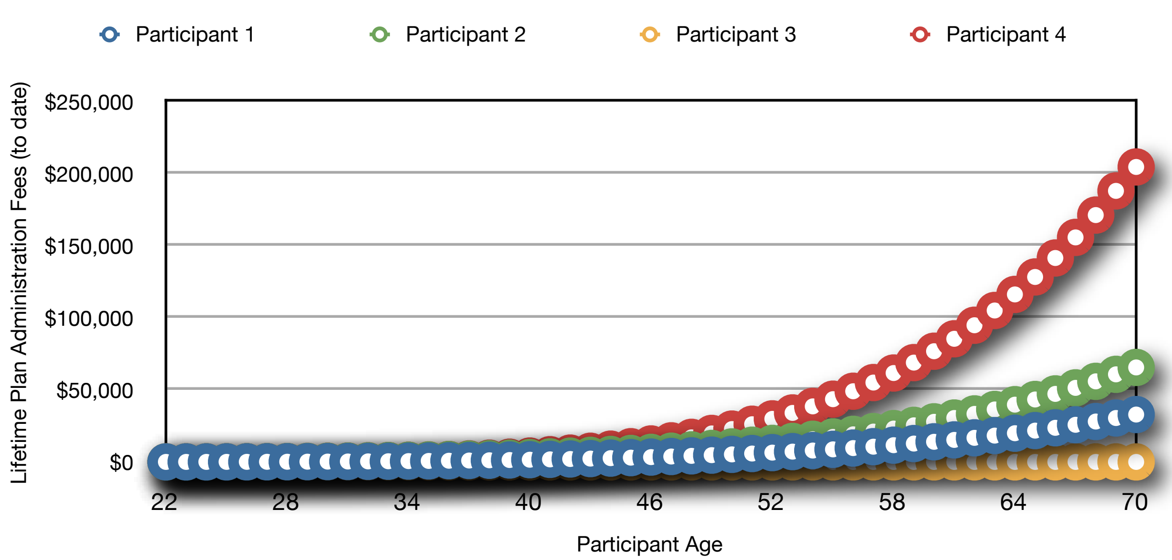
The table below illustrates four participants, all assumed to be in the same plan. For this example, we will illustrate the long-term impact of participant subsidization on account balances using various contribution rates and investment choices. These are just two of many variables (e.g. salary, investment return, etc.) that determine participant plan administration fees and ultimately ending account balances. In this example, all four participants earn a salary of $30,000 when they enter the workforce (age 22) and start contributing to the plan immediately upon hire. Each receives a 2% raise annually and earns an annualized return of 7%, both over their entire career. General observations:

- Participant 2 pays $65,547 in plan administration fees over their lifetime, double what Participant 1 has paid, simply because their contribution rate was 10% rather than 5%
- Participant 3 pays no plan administration fees over their lifetime, simply because their investment choice does not have revenue share
- Participant 4 pays $204,648 in plan administration fees over their lifetime, over six times what Participant 1 has paid, over three times what Participant 2 has paid, vs. the $0 Participant 3 paid, simply because they maximized their contribution rate starting at age 35
- Those participants paying above the plan's average lifetime fee will incur additional lost earnings (not illustrated) from not being able to invest the dollars they paid above the plan's average

	Participant 1	Participant 2	Participant 3	Participant 4
Starting Salary (age 22)	$30,000	$30,000	$30,000	$30,000
Annual Salary Increase	2%	2%	2%	2%
Annualized Return	7%	7%	7%	7%
Annual Contribution Rate	5% (Age 22 - 69)	10% (Age 22-69)	10% (Age 22-69)	10% (Age 22-34) Max Allowable (Age 35-69) [1]
Investment Revenue Sharing	0.35%	0.35%	0.00%	0.35%
Ending Account Balance by Age 70	$772,421	$1,541,280	$1,541,280	$5,346,427
Total Plan Admin Fees by Age 65	$21,559	$42,999	$0	$127,270
Total Plan Admin Fees by Age 70	$32,860	$65,547	$0	$204,648

[1] Maximum allowable rate is based on current 2011 limit of $16,500 adjusted annually ongoing by an assumed 2.49% inflation rate. Assumed inflation rate of 2.49% is simple annual average of US Consumer Price Index from 2000 - 2011.

Lifetime Participant Administration Fees (to date)



Summary

This paper is meant to illustrate the impact that a plan's financing strategy can have on a plan's individual participant's administration fees. As outlined, these fees can vary dramatically between participants in a plan when they are directly charged based on a participant's account balance or whenever revenue sharing is utilized. The individual participant fees in most plans that utilize revenue sharing are significantly impacted by an individual participant's investment allocation, creating a clear conflict of interest. Plan sponsors could face additional fiduciary liability as a result of non-equitably distributed participant administration fees if one applies the concepts embedded in Regulation 408(b)(2) and ERISA's fiduciary standards to the individual participant level.

Participants in plans utilizing revenue sharing to pay for plan administration costs have largely been unaware that they are paying recordkeeping fees through their expense ratios, let alone the amount they are paying, due to insufficient transparency industry-wide. As new regulations are put in place and fees continue to be a newsworthy topic, participants will become more aware of their administration fees. This is likely to lead to significant participant concern, especially for those who are subsidizing the cost of other participants in their particular plan, and ultimately lead to increased plan sponsor fiduciary liability.

At Gosselin Consulting Group, we believe an equitably distributed direct per participant fee is the most appropriate plan financing strategy for most plan sponsors. This approach fairly allocates the recordkeeping costs across the participant base, minimizes or eliminates participant subsidization, provides participants with full plan administration fee transparency, mitigates certain fiduciary liabilities, and allows for more effective performance monitoring. All plan sponsors should evaluate their plan financing strategy as part of their standard and ongoing fiduciary responsibilities to confirm that it's the most appropriate given their unique plan circumstances and objectives.