

Forbes

Jumping Out The 401(k) Brokerage Window

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September 6, 2012

...These days more and more 401(k)s run on dual tracks. On the main track employers offer a streamlined menu of mutual fund choices to keep average workers from feeling overwhelmed. If a participant can't decide, his retirement money is put in a single "target date" fund, in which the stock allocation is reduced as he ages and nears his retirement date.

But on an auxiliary (and sometimes hidden) track employees can use a brokerage window to buy thousands of different mutual funds and usually exchange-traded funds and individual stocks, too.

In 2011, 29% of large and midsize employers offered windows, up from 18% in 2007, according to benefits consulting firm Aon Hewitt. While only 6% of workers with access to windows use them, the escapees tend to have high incomes and big balances—an average of \$207,000, three times the average for all 401(k) participants, Aon reports.

Medical practices and legal, accounting and other firms with lots of highly paid professionals are the most likely to offer windows. But big companies have been adding windows as they reduce the regular mutual fund choices in their plans, leaving some sophisticated investors clamoring for more freedom and particularly for ETFs.

This past April, for example, automotive parts supplier Delphi added a window as it cut the funds offered in its 401(k) from 38 (including 11 target date funds) to just 22 (including 11 target funds). "The Delphi plan was essentially dumbed down to the extent that you really can't build a solid portfolio," complains David Kudla, an investment advisor in Grand Blanc, Mich. So he used the window to move his Delphi clients into a mix of individual stocks, funds and ETFs. ...

...That said, sticking to your in-plan funds is usually cheaper and more convenient than investing through a window. Kudla notes that his clients at Visteon, another auto parts supplier, neither have nor need a brokerage window because they have enough good choices within the plan.

There may be an annual fee, of, say, \$100, for using a window. And while there are normally no transaction fees for buying and selling funds within your plan's regular lineup, each purchase and sale through a window might cost you. Moreover, your plan may offer institutional bond or stock index funds with extremely low annual expenses. (So you might, for example, make those index funds your core holdings and use a window to bet on a handful of managed funds, sector funds or stocks.) ...