ETFs Slowly but Surely Replacing Mutual Funds in 401(k)s

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The exchange traded fund (ETF) industry has long lusted after the prospect of being a standard component of 401(k) plans. While it's making some serious headway, one provider in particular is leading the charge and having an impact.
BlackRock has been pushing hard to get Americans to ditch mutual funds in 401(k) plans in favor of ETFs, and it looks like it's having some effect.

BlackRock estimates that as much as $2 billion of its **iShares** funds are now held in 401(k) plans. Mutual funds make up $2 trillion of the $2.7 trillion 401(k) market, and naturally, the ETF industry is salivating at the prospect of chipping away at that market share.

ETFs have a lot of selling points, but the one that would be most appealing to 401(k) plan participants is is that of low fees. The average expense ratio for an iShares ETF is 0.41%, vs. the 1.50% average of a mutual fund. That difference can translate into savings in the tens of thousands over decades, says Joe Mont for TheStreet.

BlackRock isn't the only firm getting ETFs into plans, though; **ShareBuilder 401(k)** provides plans to small businesses and **Vanguard** uses index mutual funds in its own 401(k)s. **WisdomTree** created a business unit in 2007 that delivers 52 ETFs to the 401(k) marketplace. Small businesses like Invest n' Retire have been the early adopters of ETFs in retirement plans, but once larger companies and corporations join in, the growth may really take off.

ING's ShareBuilder 401(k) is a plan aimed at giving small business a low-cost retirement plan that uses only ETFs. Stuart Robertson, general manager and principal, says that after a recession-related slowdown, the company is expected to top its pre-market meltdown numbers. "There's a lot of confidence in the markets and the need to save is starting to resonate," he says.

One new thing at ShareBuilder is their automatic pricing discount plan, which rewards customers with lower costs as they hit certain milestones. For example, when they hit $1 million, the administrative costs and asset management fees are lowered; once they surpass $5 million, there are no administrative costs and the asset management fees are even lower. "That way, they always have a great price plan. We don't require a contract," says Robertson.

ShareBuilder sticks to the "Keep It Simple, Silly" philosophy of investing by offering 16 ETFs, plus five ETF-based model portfolios. That's by design because, as Robertson puts it, "most small businesses don't really have the resources to have an investment manager run the 401(k)."

The lineup of ETFs that covers all major asset classes and fixed income is reviewed every six to 12 months to ensure that those funds are still effective on expense ratio, market cap and other factors. The model portfolios are reviewed every two to three months based on economic and other factors.