The New York Times | http://nyti.ms/2cRMTxs

ENTREPRENEURSHIP

Think a 401(k) Is Not a Sexy Benefit? Competition May Change That

By JOHN F. WASIK SEPT. 21, 2016

When a company starts up, a retirement plan is usually the last item on the laundry list.

Many employers want to offer one, but uncertainty over costs and a time-consuming setup process deter many.

That could explain why only about 14 percent of small businesses have employer-provided plans, according to data from the Government Accountability Office.

But changes in technology, an expense war in the mutual fund industry and innovative plan offerings have made smaller companies take a second look. In a tight labor market, benefits like retirement plans are increasingly being viewed as necessities to attract quality, long-term employees.

Michael Nemeroff started Printfly, which runs RushOrderTees.com, a custom T-shirt printing business, with his brother and sister in 2002 in Philadelphia. He began offering a 401(k) retirement plan within the last year for his 180 employees, 80 percent of whom are millennials. It was a great tool for recruiting and retaining employees, he said.

“I know that investing can be daunting at first,” Mr. Nemeroff said. “This gave them an extremely easy method of investing into their future.”

The company offers a 50 percent employer match on the first 3 percent of employee contributions. The company hired 1847 Financial, a division of Penn Mutual, to set up and administer the plan, and employees can invest in several funds offered by American Funds.

"We made sure it was right for our employees," Mr. Nemeroff said. It cost about $50,000 to set up the plan, administer it and educate his work force, he said. "We wanted to make sure our employees understood it."

Although such costs can be prohibitive for some companies in their early stages, Printfly reported $23 million in sales last year and is projecting growth of 40 to 60 percent this year.

Yet for most start-ups, seeding a retirement plan doesn't seem as enticing to would-be employees as ownership or recreational benefits. Many typically offer a stake in the company, or nonmonetary benefits like eclectic cafeterias or pool tables.

"Very few start-ups offer retirement plans on Day 1," said Jamie Hopkins, a professor at the American College of Financial Services in Bryn Mawr, Pa., which trains financial professionals, and a co-director of its New York Life Center for Retirement Income. "Less than 10 percent of start-ups offer a plan."

In recent years, the needle has barely moved when it comes to small companies offering 401(k)s.

According to employer data analyzed for The New York Times by BrightScope, a financial information company based in San Diego, in 2006, about 36,000 401(k) plans at companies with fewer than 250 employees were "new," or started that calendar year.

Eight years later, slightly more than 34,000 401(k) plans were started by similar-size companies, said Brooks Herman, head of data and research for BrightScope, noting that there was a dip in new plans after the 2008 financial crisis. The company's snapshot does not include individual or small-employer individual retirement accounts, so the actual numbers are probably higher.

"Economic and market conditions have a greater effect on new benefits — like a 401(k) plan being offered — than the availability of cheap services," Mr. Herman said.

Although they are subject to various rules and contribution limits, tax deductions are also available to employers for 401(k) plans. Businesses that start such plans can qualify for a tax credit of up to $500 for each of the first three years of their plans.

To qualify, a business must have at least one employee, other than the owner, who earns less than $120,000 a year. Employers can also deduct any matching contributions.

Still, costs matter for businesses. Entrepreneurs understandably watch every dollar, so the often-steep administrative expenses of a retirement plan can be discouraging. Most conventional 401(k)'s involve a lot of paperwork, filing requirements and continuing administrative expenses.

And small businesses often have higher 401(k) costs than larger corporations. According to a recent report by Employee Fiduciary, a provider of low-cost plans for small businesses, the average "all-in" expense — covering everything — was 2 percent of assets under management for a sampling of small-business plans with total assets under $2 million. The report looked at about 120 plans and included plans offered by insurance companies, which tend to be more expensive.

Small employers are often saddled with higher costs because, the argument goes, they do not offer economies of scale. However, the mutual fund and exchange-traded-fund industry is increasingly competing on expenses and has pursued smaller companies.

For example, Vanguard's Target Retirement 2050 Fund, a "target-date" bundle of four of the company's funds for participants who plan to retire around 2050, costs only 0.16 percent in expenses annually.

Small-business retirement planning is turning into a start-up industry in itself. For instance, Honest Dollar is selling such benefits for a monthly fee of $8 a month per employee, while ForUsAll has begun offering 401(k) plans for smaller companies.

Employees and employers alike have also had other retirement savings options.

The Simplified Employee Pension, or SEP I.R.A., for small-business owners and the self-employed, and the Simple I.R.A., which allows both employees and employers to contribute to an individual retirement account, have been available for decades and require minimal paperwork.

Employees can set up their own I.R.A. or retirement plans, but company-sponsored 401(k)'s have distinct benefits. Employees can contribute up to $18,000 tax free to 401(k)'s, and those 50 or older can contribute an additional $6,000.

I.R.A.s set up by individuals have contribution limits of $5,500 for employees under age 50. Simple I.R.A. contributions are limited to $12,500 in 2016, plus an additional $3,000 for those 50 or older.

More recently, states like California, Illinois and Maryland have moved toward creating their own low-cost programs for small businesses that do not offer retirement plans.

Another emerging inexpensive option is available through robo-advisers, mostly automated services that have streamlined retirement plan access and relatively low expenses.

One such robo-advisory firm, Betterment, introduced a 401(k) plan this year catering to businesses. It features Vanguard funds, record-keeping, and annual all-in expenses ranging from 0.1 percent to 0.6 percent, according to its website.

As with most retirement plan expenses, the more assets managed, the lower the total cost. The best price in the Betterment example is for plans with more than $1 billion in assets.

Betterment said it had more than 200 companies in its new small-business offering — 75 percent of which had fewer than 250 employees — although it would not disclose how many were start-ups.

The industrywide push to lower fund and plan costs will continue to make retirement plans more appealing to entrepreneurs.

Another incentive may be the relatively new Labor Department rule that will require anyone offering retirement plan advice to act in the best interests of employees.

“We’ll see more low-cost plans,” said Mr. Hopkins of the American College of Financial Services.

If the rule, scheduled to go into effect next year, survives multiple legislative and court challenges by business groups, it could pare small-plan expenses. High-cost programs would most likely not survive the “best interest” provision of the Labor Department rule.

The various changes and rules can be daunting, but advisers say the best first step for start-ups considering offering retirement plans is to gather information for themselves and for their employees.

“The best thing is to get educated by someone you trust,” said Mr. Nemeroff of Printfly. “Don’t do it by yourself. Ask yourself how it’s going to help your team. Education is the most important part. How can you help everyone plan for the future?”

A version of this article appears in print on September 22, 2016, on page B7 of the New York edition with the headline: The Next Hot Start-Up Benefit Could Be a 401(k).
