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Employee Benefits Briefing

Participant Fee Disclosure
Fee Transparency—The Final Piece of the Puzzle

On October 20, the Department of Labor (DOL) published a final regulation requiring plan fiduciaries to make specific fee disclosures to participants in defined contribution plans that permit participant-directed investments. The regulation is generally effective for plan years beginning on or after November 1, 2011 (i.e., 2012 for calendar year plans); however, plan fiduciaries should begin working with service providers and investment managers in early 2011 to secure and arrange the necessary information to be disclosed.

These rules are in response to concerns that plan participants need more detailed information regarding plan performance and the fees and expenses that are being paid from participants' accounts. Presumably, the regulation will avoid any perceived need for Congressional proposals designed to achieve the same goals.

Background

The DOL's first step towards fee transparency was the publication of the Form 5500 Schedule C requirements, which were effective for the 2009 plan year. The second step involved the service provider fee disclosure requirements, which were published as interim final regulations on July 16, 2010.[1] Now the DOL has taken the third step—specifying what information fiduciaries of participant-directed plans must disclose to their participants.

[1] *See,* Service Provider Fee Disclosure: Another Step Towards Fee Transparency, Employee Benefits Briefing, July 29, 2010.

Summary

The following summary looks at the regulation from the responsible plan fiduciary's perspective.

Which Plans are Covered?

The regulation covers "participant directed individual account plans" (ERISA 3(34)), i.e., generally 401(k) and 403(b) plans that permit participants to make investment decisions for their own accounts. The regulation does not cover IRAs, governmental plans, simplified employee pensions (IRC 408(k)) or simple retirement accounts (IRC 408(p)).

What is the Effective Date?

The rules are applicable to plan years beginning on or after November 1, 2011. Thus, for most plans the rules apply to the plan year beginning January 1, 2012. The required disclosures (as discussed below) must be made by the 60th day of the applicable plan year.

What Disclosures Must Plan Fiduciaries Make?

Two types of disclosures are required.

A. Plan-Related Information

1. Required Disclosures to Participants
   - circumstances under which participants and beneficiaries can direct investments
   - limitations applicable to any investment instructions (e.g., transfer restrictions)

- circumstances relating to voting, tender and similar instructions as well as restrictions applicable to them
- identification of plan investment alternatives and investment managers
- description of any "brokerage windows" or "self-directed brokerage accounts" or similar arrangements
- general plan administrative expenses (e.g., legal, accounting, recordkeeping) not directly reflected in the investment alternatives themselves and their allocation to individual accounts
- individual expenses (e.g., loans, QDROs, brokerage window commissions, etc.) not reflected in the investment alternatives themselves

2. Timing for the Disclosures—the disclosures must be made on or before the date a participant or beneficiary can first direct investments, then annually thereafter. Changes in the information must be described at least 30 (but not more than 90) days before their effective date (in the case of unforeseeable or uncontrollable circumstances, the description must be furnished as soon as practicable). Actual general and individual expenses must be shown on a statement provided at least quarterly.

3. Method Used to Disclose—the summary plan description or a participant benefit statement can be used to provide the initial information, except that the actual general and individual expenses must be disclosed on quarterly statements. Electronic delivery is permitted for participants with regular access to e-mail.

B. Investment-Related Information

1. Required Disclosures to Participants
   - name of each designated investment alternative (not including "brokerage windows" or similar accounts)
   - investment category (e.g., stocks, bonds, employer securities, etc.)
   - performance data for 1, 5 and 10 (or shorter life) years, and fixed-return information
   - benchmarks for the investment where returns are not fixed
   - fee and expense information and related statements
   - internet web site address for the investment alternatives
   - materials received by the plan relating to available voting, tender and similar rights
   - information available upon request (e.g., prospectuses, financial statements, share value, portfolio list)

   The fee information must be expressed as an annual percentage and dollar amount for a $1,000 investment. This information must be in a comparative format, and special rules apply to investments in qualifying employer securities, annuities and fixed-rate investments.

2. Timing for the Disclosures—the disclosures must be made on or before the date the participant or beneficiary can first direct investments and annually thereafter. For new participants, this information should be part of the new participant materials that are provided to employees.

3. Method Used to Disclose—the investment-related information can be

provided in a disclosure statement. Electronic delivery is available for participants with regular access to e-mail. The DOL has attached to the regulation a four-page template for the disclosure of performance and fee information. This template is likely to serve as the basis for most plans in meeting the disclosure requirements.

What Steps Should Plan Fiduciaries Be Prepared to Take?

The responsible plan fiduciary needs to be prepared to implement a disclosure process which consists essentially of three steps:

A. *Step One—Obtain Service Provider Information*

Early in 2011, plan fiduciaries need to secure commitments from their service providers to provide the applicable performance and fee information in a timely manner. Plan fiduciaries will be protected from any incomplete and inaccurate information if they rely reasonably and in good faith on what the service provider has communicated.

B. *Step Two—Prepare and Timely Distribute the Information*

Once all the information is received, the plan fiduciary needs to decide what information each disclosure vehicle—summary plan description, participant benefit statement, disclosure statement, etc.—will contain. Then, those documents need to be prepared for distribution. For calendar year plans, the initial disclosures will need to be made by February 29, 2012.

C. *Step Three—Anticipate Participant Response*

Plan participants are likely to focus on the fee and performance data. Plan fiduciaries need to be prepared to respond to participant questions. Many factors have combined to lead employees to question the value of their retirement savings. Ideally, these new disclosures will serve to assure plan participants that their retirement investment alternatives are subject to careful and knowledgeable oversight.

Conclusion

These disclosure obligations present a significant challenge as well as a significant opportunity for plan fiduciaries. A well-devised plan implemented beginning early next year will be a critical factor in surmounting the challenge and making the most of the opportunity.

If you have any questions regarding the fee disclosure regulation, please contact **John J. Jacobsen, Jr.** (312-609-7680), **Philip L. Mowery** (312-609-7642) or **Paul F. Russell** (312-609-7740).

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