



New DOL Service Provider Fee Disclosure Regulation: What Plan Fiduciaries Need to Know

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financial goals of fiduciaries
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MODERATED BY

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Agenda

- Background
- Overview of DOL Interim Final Regulation
- Plans Covered by New Rules
- Covered Service Providers
- Required Disclosure
- Timing of Required Disclosure
- Exception for Inadvertent Disclosure Errors
- Class Exemption for Plan Fiduciaries
- Next Steps for Plan Sponsors/Fiduciaries
- Addendum



Background – Service Provider Prohibited Transaction Rules

- ERISA's prohibited transaction rules prohibit:
 - Furnishing of services between party in interest and plan (ERISA § 406(a)(1)(C))
 - Use of plan assets by or for the benefit of a party in interest (ERISA § 406 (a)(1)(D))
- Plan service providers are parties in interest
- One bite rule
- Section 406(b) self-dealing/conflict of interest rules
- Corresponding Internal Revenue Code provisions



Background – Service Provider Exemption

- ERISA Section 408(b)(2) exempts transactions between plan and service provider if:
 - Service provider provides necessary services to plan
 - Plan pays no more than reasonable compensation for the services
 - Plan can terminate services on reasonably short notice without penalty
- Does not provide an exemption from Section 406(b) self-dealing/conflict of interest rules



Background – Consequences of Prohibited Transactions

- If transaction between plan and service provider fails to satisfy Section 408(b)(2):
 - Service provider subject to excise tax liability
 - Unwinding of transaction
 - Possible breach of fiduciary duty by plan fiduciary



Overview of DOL Interim Final Regulation

- Service provider must satisfy new rules in order for service provider exemption to apply
- Rules are effective July 16, 2011
- DOL soliciting comments
- New rules are part of DOL 3-pronged approach to fee disclosure for retirement plans:
 - Form 5500, Schedule C service provider fee disclosure effective beginning with 2009 plan year
 - DOL interim final regulations on service provider fee disclosure
 - DOL final regulations on disclosure to participants



Plans Covered by New Rules

- Covered:
 - Retirement plans subject to Title I of ERISA
 - 401(k) and other individual account plans
 - Defined benefit plans
 - 403(b) plans
- Not Covered:
 - Church and government plans
 - IRAs, Simplified Employee Pensions (SEP IRAs) and Simple Retirement Accounts (Simple IRAs)
 - Welfare plans



Covered Service Providers – General Requirements

- Gateway requirements:
 - Service provider has contract or arrangement with a covered plan to provide services
 - Expects to receive \$1,000 or more in compensation from plan (including compensation payable to affiliates and subcontractors)
- Services fall into one or more of three categories



Covered Service Providers – Fiduciaries and Registered Investment Advisers (First Category)

- Fiduciary provides services directly to a covered plan
- Fiduciary provides services to investment fund/product that holds plan assets (“Plan Asset Fund”) and in which a covered plan has a direct equity investment, including:
 - Insurance company separate accounts
 - 81-100 collective investment trusts
 - Hedge funds that hold plan assets
- Services provided directly to covered plan as registered investment adviser



Covered Service Providers – Certain Recordkeeper and Brokerage Services (Second Category)

- Recordkeeping or brokerage services if:
 - Provided to covered individual account plan
 - Includes 403(b), 401(k)
 - Plan permits participants to direct investment of their accounts
 - One or more investment options will be made available in connection with the recordkeeping or brokerage services



Covered Service Providers – Other Service Providers Receiving Indirect Compensation (Third Category)

- Other specified services provided to covered plan for which service provider (or an affiliate or subcontractor) expects to receive indirect compensation or compensation from related parties
- Services covered: accounting, auditing, actuarial, appraisal, banking, consulting, custodial, insurance, investment advisory, recordkeeping, brokerage, third-party administration, valuation services



Required Disclosure – Core Requirements

- Disclosure must be provided in writing to responsible plan fiduciary (fiduciary with authority to enter into or renew arrangement with service provider)
- Must include description of services to be provided to covered plan
 - Not required to describe non-fiduciary services to be provided to a Plan Asset Fund
- If applicable, must include statement that service provider will provide services as a fiduciary or registered investment adviser



Required Disclosure – Core Requirements (cont'd)

- Must disclose compensation service provider (and affiliates or subcontractors) expects to receive
 - Compensation means anything of monetary value (e.g., money, gifts, awards, trips), except for de minimus nonmonetary compensation (\$250 or less during term of arrangement)
 - Disclosure must contain sufficient information to permit evaluation of reasonableness




Required Disclosure – Direct and Indirect Compensation

- Must disclose direct and indirect compensation service provider (and affiliates or subcontractors) expects to receive in connection with services
 - Direct compensation is compensation received directly from covered plan
 - May be disclosed in the aggregate or by service
 - Indirect compensation is compensation received from any source other than covered plan, plan sponsor or the service provider or its affiliates or subcontractors
 - Must identify payer of indirect compensation and services for which indirect compensation is received




Required Disclosure – Compensation Among Related Parties

- Must disclose any compensation paid among service provider and its affiliates and subcontractors in connection with services
 - Applies only if compensation is transaction-based (e.g., commissions, soft dollars, finder's fees) or charged directly against plan assets and reflected in net value of investments (e.g., 12(b)-1 fees)
 - Must include identification of payers and recipients of compensation and services for which compensation will be paid



Required Disclosure – Termination Compensation; How Compensation Paid

- Must disclose any compensation service provider expects to receive on termination of arrangement, including how any prepaid amounts will be calculated and refunded
- How compensation will be paid to service provider, e.g., direct billing, charge against participant accounts, charge against plan investments



Required Disclosure – Additional Requirements for Recordkeepers

- In the case of recordkeeping services:
 - Must include a description of all direct and indirect compensation that service provider (and affiliates or subcontractors) expects to receive in connection with providing recordkeeping services
 - If recordkeeping services are bundled with other services or if compensation for recordkeeping services is offset or rebated based on other compensation received by recordkeeper, a separate estimate of the cost of the recordkeeping services

- If in connection with recordkeeping or brokerage services investment options (excluding brokerage windows) under covered participant-directed individual account plan are made available, the recordkeeper or broker must disclose the following with respect to each investment option:
 - Sales loads, redemption fees and other fees charged against plan investments in connection with purchase/sale of interest in the investment option
 - Annual operating expenses of the investment option if the return is not fixed
 - Any other ongoing expenses associated with the investment option



Required Disclosure – Additional Requirements for Recordkeepers and Brokers that Provide Investment Platforms and Fiduciaries of Plan Asset Funds (cont'd)

- If service provider is a fiduciary of a Plan Asset Fund in which covered plan has a direct equity investment, service provider must provide the disclosures described above, unless provided by recordkeeper or broker



Timing of Required Disclosure

- Initial Disclosure
 - Existing arrangements
 - Disclosure required by July 16, 2011
 - Arrangements entered into, extended or renewed on and after July 16, 2011
 - Disclosure reasonably in advance of date arrangement entered into, extended or renewed
 - Special Rules
 - Investment vehicle that becomes a Plan Asset Fund – disclosure required within 30 days after service provider knows
 - New investment options – disclosure must be provided as soon as practicable but not later than date responsible plan fiduciary designates as investment option



Timing Of Required Disclosure (cont'd)

- Disclosure Changes
 - Any change in prior disclosure must be disclosed as soon as practicable after change, but no later than 60 days after service provider is informed of change
- Information to Comply with Reporting and Disclosure Requirements
 - Upon request of responsible plan fiduciary, covered service provider must provide any other compensation information required for Form 5500 disclosure or other reporting and disclosure requirements
 - Must be provided generally within 30 days after request



Exception for Inadvertent Disclosure Errors

- Covered plan will still qualify for the Section 408(b)(2) service provider exemption if service provider:
 - Acted in good faith and with reasonable diligence
 - Disclosed correct information as soon as practicable, but not more than 30 days, after it knows of error or omission



Class Exemption for Plan Fiduciaries

- Plan fiduciary not treated as engaging in prohibited transaction resulting from disclosure errors by service provider if certain conditions satisfied, including:
 - Fiduciary did not know service provider failed to make required disclosures, and reasonably believed service provider complied with disclosure rules
 - Upon discovering failure, fiduciary requests in writing that service provider furnish the required information
 - If service provider fails to provide required information within 90 days of written request, fiduciary notifies DOL of service provider's failure
 - Upon discovering failure, fiduciary determines whether to continue or terminate the arrangement with the service provider



Next Steps For Plan Sponsors/Fiduciaries

- Identify covered plans
- Identify covered service providers
- Contact covered service providers
- Develop procedures to monitor and ensure compliance with class exemption



ADDENDUM – DOL Final Regulations on Disclosure to Participants

- On October 14, 2010, DOL issued final regulations on disclosure of plan and investment related information to participants in participant-directed individual account plans
- Applies to covered individual account plan for plan years beginning on or after November 1, 2011
- Required Plan-Related Disclosures:
 - Plan administrator must provide the following plan-related information on or before the date participants can direct the investment of their accounts, and then annually thereafter
 - General plan information, including investment options and how to give investment directions





ADDENDUM – DOL Final Regulations on Disclosure to Participants (cont'd)

- Explanation of administrative fees and expenses charged to or deducted from participant accounts, e.g., recordkeeping, accounting, legal fees
- Explanation of any fees and expenses charged to or deducted from participant accounts based on participant action, e.g., loan, wire transfer fees
- Plan administrator must provide quarterly statements of actual charges to and deductions from participant accounts
- Required Investment-Related Disclosures:
 - Plan administrator must provide certain investment-related information on or before the date participants can direct the investment of their accounts, and then annually thereafter, including



ADDENDUM – DOL Final Regulations on Disclosure to Participants (cont'd)

- Performance data
 - Benchmark information
 - Fee and expense information
 - Internet website address
 - Glossary of investment terms
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- Investment-related information must be furnished in a comparative chart or similar format
 - DOL provides a model chart to be used by plan administrators



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