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ERISA Participant Fee Disclosures for 401(k) and Other Individual Account Plans

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DOL's Three-Pronged Approach to Increasing Fee Transparency

- ★ **Disclosure to the Government** – First step was new Schedule C disclosure requirements
- ★ **Disclosure to Plan Fiduciaries** – Second step was enhanced disclosure to plan fiduciaries by service providers otherwise known as the 408(b)(2) Regs
- ★ **Disclosure to Plan Participants** – The final piece is new Disclosure Rules for Participant-Directed Retirement Plans

Background on Participant Fee Disclosure

- ✦ In April of 2007, the DOL requested information from participants, service providers and plan sponsors as to what kind of rules should be adopted so that participants and beneficiaries have the necessary information to make informed investment decisions
- ✦ Based on those comments, the DOL published proposed regulations on July 23, 2008
- ✦ The final rule was published on October 14, 2010 and generally follows the proposed rules
 - > There were, however, some additional rules for annuities, nonregistered investments and employer securities

The Basics

★ When do the rules go into effect?

- > The regulations go into effect for plan years beginning on or after November 1, 2011
 - January 1, 2012 for calendar year plans
- > Generally, anyone who is a participant or beneficiary with the right to direct investment of their individual account must receive the appropriate notices on or before the date they can first direct their investments (and annually thereafter)
 - Special 60-day rule for participants and beneficiaries in the plan on the effective date

The Basics

★ What plans are covered?

- > A “covered individual account plan” is any participant-directed individual account plan as defined in section 3(34) of ERISA, except that such term shall not include any plan involving individual retirement accounts or individual retirement annuities described in sections 408(k) or 408(p) of the Internal Revenue Code

Types of Information That Must be Disclosed

- ✦ Plan-related information
 - > General plan information
 - > Administrative expenses information
 - > Individual expenses information
- ✦ Investment-related information
 - > Performance data
 - > Benchmark information
 - > Fee and expense information
 - > Internet Web site address
 - > Glossary

Disclosure of Plan-Related Information

★ Disclosure requirement

- > A plan administrator or person designated by the plan administrator to act on its behalf shall provide to each participant or beneficiary the following information, based upon the latest information available to the plan

Disclosure of Plan-Related Information

★ General Plan Information

- > An explanation of the circumstances under which participants and beneficiaries may give investment instructions
- > An explanation of any specified limitations on such instructions under the terms of the plan, including any restrictions on transfer to or from a designated investment alternative
- > A description of or reference to plan provisions relating to the exercise of voting, tender and similar rights appurtenant to an investment in a designated investment alternative as well as any restrictions on such rights

Disclosure of Plan-Related Information

- > An identification of any designated investment alternatives offered under the plan
- > An identification of any designated investment managers; and
- > A description of any “brokerage windows,” “self-directed brokerage accounts,” or similar plan arrangements that enable participants and beneficiaries to select investments beyond those designated by the plan

Disclosure of Plan-Related Information

- ♦ If there is a change to the information described above, each participant and beneficiary must be furnished a description of such change at least 30 days, but not more than 90 days, in advance of the effective date of the change, unless the inability to provide such advance notice is due to events that were unforeseeable or circumstances beyond the control of the plan administrator, in which case notice must be furnished as soon as reasonably practicable

Disclosure of Plan-Related Information

★ Administrative Expenses

- > An explanation of any fees and expenses for general plan administrative services, which
 - may be charged against the individual accounts of participants and beneficiaries and
 - are not reflected in the total annual operating expenses of any designated investment alternative, as well as the basis on which such charges will be allocated (e.g., pro rata, per capita) to, or affect the balance of, each individual account

Disclosure of Plan-Related Information

- ♦ If there is a change to the information described above, each participant and beneficiary must be furnished a description of such change at least 30 days, but not more than 90 days, in advance of the effective date of the change, unless the inability to provide such advance notice is due to events that were unforeseeable or circumstances beyond the control of the plan administrator, in which case notice must be furnished as soon as reasonably practicable

Disclosure of Plan-Related Information

- ✦ At least quarterly, participants and beneficiaries must receive a statement that includes
 - > The dollar amount of the fees and expenses described above under “Administrative Expenses” that are actually charged (whether by liquidating shares or deducting dollars) during the preceding quarter to the participant’s or beneficiary’s account for such services
 - > A description of the services to which the charges relate (e.g., plan administration, legal, accounting services); and

Disclosure of Plan-Related Information

- > If applicable, an explanation that, in addition to the fees and expenses disclosed, some of the plan's administrative expenses for the preceding quarter were paid from the total annual operating expenses of one or more of the plan's designated investment alternatives (e.g., through revenue sharing arrangements)

Disclosure of Plan-Related Information

★ Individual Expenses

- > An explanation of any fees and expenses
 - that may be charged against the individual account of a participant or beneficiary on an individual, rather than on a plan-wide, basis (e.g., fees attendant to processing plan loans or QDROs) and
 - which are not reflected in the total annual operating expenses of any designated investment alternative

Disclosure of Plan-Related Information

- ♦ If there is a change to the information described above, each participant and beneficiary must be furnished a description of such change at least 30 days, but not more than 90 days, in advance of the effective date of the change, unless the inability to provide such advance notice is due to events that were unforeseeable or circumstances beyond the control of the plan administrator in which case notice must be furnished as soon as reasonably practicable

Disclosure of Plan-Related Information

- ✦ At least quarterly a statement that includes
 - > The dollar amount of the fees and expenses that are actually charged (whether by liquidating shares or deducting dollars) during the preceding quarter to the participant's or beneficiary's account for individual services; and
 - > A description of the services to which the charges relate (e.g., loan processing fee)

Disclosure of Investment-Related Information

- ★ Most recent annual disclosure
 - > The requirement to furnish information on or before the date on which a participant or beneficiary can first direct his or her investments may be satisfied by furnishing to the participant or beneficiary the most recent annual disclosure including any updates to the information provided to the participants and beneficiaries

Disclosure of Investment-Related Information

♦ General Rule

- > The plan administrator or person designated by the plan administrator to act on its behalf, based on the latest information available to the plan shall furnish to each participant or beneficiary on or before the date on which he or she can first direct his or her investments and at least annually thereafter, the following information with respect to each designated investment alternative offered under the plan

Disclosure of Investment-Related Information

♦ Identifying Information

- > The name of each designated investment alternative; and
- > The type or category of the investment (e.g., money market fund, balanced fund (stocks and bonds), large-cap stock fund, employer stock fund, employer securities)

Disclosure of Investment-Related Information

★ Performance Data

- > For designated investment alternatives with respect to which the return is not fixed
 - The average annual total return of an investment for 1-, 5-, and 10- calendar year periods (or for the life of the alternative, if shorter) ending on the date of the most recently completed calendar year (as well as a statement indicating that an investment's past performance is not necessarily an indication of how the investment will perform in the future)

Disclosure of Investment-Related Information

- > For designated investment alternatives with respect to which the return is fixed or stated for the term of the investment
 - Both the fixed or stated annual rate of return and the term of the investment

Disclosure of Investment-Related Information

- > If, with respect to such a designated investment alternative, the issuer reserves the right to adjust the fixed or stated rate of return prospectively during the term of the contract or agreement, the current rate of return, the minimum rate guaranteed under the contract, if any, and a statement advising participants and beneficiaries that the issuer may adjust the rate of return prospectively and how to obtain (e.g., telephone or Web site) the most recent rate of return

Disclosure of Investment-Related Information

★ Benchmarks

- > For designated investment alternatives with respect to which the return is not fixed
 - The name and returns of an appropriate broad-based securities market index over the 1-, 5-, and 10-calendar year periods (or for the life of the alternative, if shorter) comparable to the performance data periods provided above, and which is not administered by an affiliate of the investment issuer, its investment adviser, or a principal underwriter, unless the index is widely recognized and used

Disclosure of Investment-Related Information

- ◆ Fee and Expense Information for designated investment alternatives with respect to which the return is not fixed
 - > The amount and a description of each shareholder-type fee (fees charged directly against a participant's or beneficiary's investment, such as commissions, sales loads, sales charges, deferred sales charges, redemption fees, surrender charges, exchange fees, account fees, and purchase fees, which are not included in the total annual operating expenses of any designated investment alternative) and a description of any restriction or limitation that may be applicable to a purchase, transfer, or withdrawal of the investment in whole or in part (such as round trip, equity wash, or other restrictions)

Disclosure of Investment-Related Information

- > The total annual operating expenses of the investment expressed as a percentage (i.e., expense ratio), calculated in accordance with the rules in the regulations
- > The total annual operating expenses of the investment for a one-year period expressed as a dollar amount for a \$1,000 investment (assuming no returns and based on the percentage described in the regulations)
- > A statement indicating that fees and expenses are only one of several factors that participants and beneficiaries should consider when making investment decisions; and

Disclosure of Investment-Related Information

- > A statement that the cumulative effect of fees and expenses can substantially reduce the growth of a participant's or beneficiary's retirement account and that participants and beneficiaries can visit the Employee Benefit Security Administration's Web site for an example demonstrating the long-term effect of fees and expenses

Disclosure of Investment-Related Information

- ★ Fee and Expense Information for designated investment alternatives with respect to which the return is fixed for the term of the investment
 - > The amount and a description of any shareholder-type fees and a description of any restriction or limitation that may be applicable to a purchase, transfer or withdrawal of the investment in whole or in part

Disclosure of Investment-Related Information

★ Website Information

- > An Internet Web site address that is sufficiently specific to provide participants and beneficiaries access to the following information regarding the designated investment alternative
 - The name of the alternative's issuer
 - The alternative's objectives or goals in a manner consistent with Securities and Exchange Commission Form N-1A or N-3, as appropriate
 - The alternative's principal strategies (including a general description of the types of assets held by the investment) and principal risks in a manner consistent with Securities and Exchange Commission Form N-1A or N-3, as appropriate

Disclosure of Investment-Related Information

- The alternative's portfolio turnover rate in a manner consistent with Securities and Exchange Commission Form N-1A or N-3, as appropriate
- The alternative's performance data updated on at least a quarterly basis, or more frequently if required by other applicable law; and
- The alternative's fee and expense information described above

Disclosure of Investment-Related Information

♦ Glossary

- > A general glossary of terms to assist participants and beneficiaries in understanding the designated investment alternatives, or an Internet Web site address that is sufficiently specific to provide access to such a glossary along with a general explanation of the purpose of the address

Disclosure of Investment-Related Information

♦ Annuity Options

- > If a designated investment alternative is part of a contract, fund or product that permits participants or beneficiaries to allocate contributions toward the future purchase of a stream of retirement income payments guaranteed by an insurance company, the information set forth above with respect to the annuity option, to the extent such information is not otherwise included in investment-related fees and expenses described above

Disclosure of Investment-Related Information

- ✦ The investment-related information above shall be provided in a comparative format that is designed to facilitate a comparison of such information for each designated investment alternative available under the plan and prominently displays the date
 - > It must include
 - A statement indicating the name, address, and telephone number of the plan administrator (or a person or persons designated by the plan administrator to act on its behalf) to contact for the provision of the information described above

Disclosure of Investment-Related Information

- A statement that additional investment-related information (including more current performance information) is available at the listed Internet Web site addresses; and
 - A statement explaining how to request and obtain, free of charge, paper copies of the information required to be made available on an Internet Web site
- > Nothing shall preclude a plan administrator from including additional information that the plan administrator determines appropriate for such comparisons, provided such information is not inaccurate or misleading

Disclosure of Investment-Related Information

- ✦ Information to be provided subsequent to investment
 - > The plan administrator shall furnish to each investing participant or beneficiary, subsequent to an investment in a designated investment alternative, any materials provided to the plan relating to the exercise of voting, tender and similar rights appurtenant to the investment, to the extent that such rights are passed through to such participant or beneficiary under the terms of the plan

Disclosure of Investment-Related Information

- ◆ Information relating to designated investment alternatives to be provided upon request
 - > Copies of prospectuses (or, alternatively, any short-form or summary prospectus, the form of which has been approved by the Securities and Exchange Commission) for the disclosure of information to investors by entities registered under either the Securities Act of 1933 or the Investment Company Act of 1940, or similar documents relating to designated investment alternatives that are provided by entities that are not registered under either of these Acts;

Disclosure of Investment-Related Information

- > Copies of any financial statements or reports, such as statements of additional information and shareholder reports, and of any other similar materials relating to the plan's designated investment alternatives, to the extent such materials are provided to the plan;
- > A statement of the value of a share or unit of each designated investment alternative as well as the date of the valuation; and
- > A list of the assets comprising the portfolio of each designated investment alternative which constitute plan assets and the value of each such asset (or the proportion of the investment which it comprises)

Form of Disclosure

- ★ The information required to be disclosed may be provided as part of the plan's summary plan description or as part of a pension benefit statement if such summary plan description or pension benefit statement is furnished at a frequency that complies with the requirements of the regulation

Protection for Good Faith Efforts at Compliance

- ✦ The regulations clarify that, to the extent a plan administrator reasonably and in good faith relies on information from an investment or other service provider in making the required disclosures, the plan administrator will not be held liable for any inaccuracy or lack of completeness
- ✦ Plan administrators should proactively address these rules with their service providers (TPAs, recordkeepers, fund managers) and amend their plan, trust, and provider agreements as necessary to allocate responsibility for satisfying the various disclosure requirements
- ✦ Plan committees may need to amend their charters to address the new disclosure duties

Coordination With Other ERISA Provisions

- ✦ The information to be furnished under the new rules is subject to the same standards of delivery that apply to other ERISA required disclosures, including provision of required plan information via the internet or the employer's intranet or e-mail system
- ✦ Some – but not all – of this information is already being disclosed by plan administrators who take advantage of the limited exemption from fiduciary liability under ERISA section 404(c)
- ✦ For the first time, the new regulations make disclosure of detailed plan and investment information an affirmative fiduciary duty of the plan administrator

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