



ERISA Fee Transparency: New DOL Rules for Service Provider Disclosures

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Presented by
**Nell Hennessy
Priscilla Ryan
Erin Sweeney**

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DOL Fee Initiatives

- Disclosure of indirect fees on Schedule C of the Form 5500
- Disclosure to plan fiduciaries by service providers
 - Amendment to service provider exemption (regulation under ERISA §408(b)(2))
 - Proposed prohibited transaction exemption
- Consultant/Advisor Project (“CAP”) national enforcement initiative
- Participant disclosure
 - DOL Request for Information (RFI)

Form 5500 Schedule C

- Current Schedule C requires disclosure of direct compensation paid to top 40 service providers
- Effective for 2009 Plan Year, disclosure required of **direct and indirect** compensation of \$5,000 or more to any plan service provider
 - Direct Compensation - amounts paid by plan
 - Indirect compensation - amounts received by service providers from other sources
- Fees that reduce the investment's return, such as mutual fund investment management fees, must be separately reported

Indirect Compensation

- Indirect compensation includes:
 - Gifts or meals
 - No reporting of gifts of \$50 or less, if total gifts from same source below \$100 (gifts less than \$10 don't count against \$100 limit)
 - Awards
 - Trips for employees
 - Research
 - Finder's fees
 - Soft dollar payments
 - Float income
 - Commissions

Indirect Fees Not Reported on Schedule C

- Bundled service provider
 - No break down of amounts paid to affiliates, subcontractors
 - EXCEPT: transaction-based fees must be disclosed
- Insurance related fees
 - Compensation related to insurance products is reported on Schedule A, not Schedule C
 - Insurance commissions must be reported
 - Rules for indirect compensation parallel to Schedule C

Disclosure by service providers

- Plan payment to service providers is a prohibited transaction absent an exemption
- ERISA §408(b)(2) provides exemption for “reasonable arrangements” with service providers if no more than “reasonable compensation” is paid
- Current regulation defines “reasonable arrangement” as one that can be terminated on reasonably short notice without penalty
- DOL has proposed amendment to the prohibited transaction exemption for service providers would requiring service provider to:
 - Disclose indirect compensation to plan fiduciaries
 - Provider information necessary for plan fiduciaries to fill out Schedule C of Form 5500

What Happens If Fees Not Disclosed

- If service provider doesn't provide information on indirect compensation, box to check on Form 5500 Schedule C
- Service provider subject to 15% prohibited transaction excise tax (Code § 4975)
- Potential ERISA violation for plan fiduciary
- DOL has proposed class exemption for fiduciaries if contract requires disclosure but service provider fails to provide necessary information

Proposed Prohibited Transaction Class Exemption

- Applies to Fiduciaries when service providers fail to disclose information required by § 408(b)(2)
- Conditions:
 - Fiduciary did not have reason to know provider would not comply
 - Fiduciary must request in writing the disclosure
 - Fiduciary must notify the DOL
 - 30 days after refusal to provide compensation information
 - within 90 days after written request
 - Fiduciary must consider terminating the contract

National Enforcement Initiative

- Consultant/Advisor Project (“CAP”) - new DOL national enforcement program
- DOL field offices will place particular investigative emphasis on receipt of improper, undisclosed compensation by pension consultants and other investment advisers
 - Whether adviser/consultant used its position to generate additional fees for itself or its affiliates
 - Whether plan fiduciaries adhered to investment guidelines
 - Improper selection or monitoring of consultant or adviser
 - Potential criminal violations, such as kickbacks or fraud

Disclosure to Participants

- DOL issued a Request for Information (RFI) asking what type of disclosure should be required
- Responses to the RFI can be viewed at <http://www.dol.gov/ebsa/regs/cmt-feedisclosures.html>
- Policy issue for DOL: how to provide sufficient information to participants without overwhelming them
- DOL is likely to propose regulations in 2008

Other Fee Developments

- Legislation - “401(k) Fair Disclosure for Retirement Security Act of 2007” (H.R. 3185)
 - Detailed fee and rate of return disclosure to participants in participant-directed plans
 - Detailed disclosure of 12 categories of fees by service providers to plan
 - Plans would be required to offer a low cost index fund
- Securities and Exchange Commission
 - Reexamining 12b-1 fees, mutual fund fee disclosure
- Litigation
 - Class Actions against plan sponsors
 - Class Actions against service providers

What Fiduciaries Are Doing

- Reviewing plan fee arrangements
 - Identify direct/indirect compensation
 - Benchmark investment fees, admin costs
 - Explore lower cost investment alternatives
- Reviewing fiduciary process
 - Adequate due diligence
 - Documentation
- Reviewing disclosure to participants about how plan fees are paid, especially asset-based fees to pay plan administrative costs

MORE QUESTIONS????

For additional information, contact:

Nell Hennessy
President & CEO
Fiduciary Counselors Inc.

nell.hennessy@fiduciarycounselors.com
202-558-5141

Priscilla Ryan
Partner
Sidley Austin LLP

pryan@Sidley.com
312-853-7072

Erin Sweeney
Counsel
Dickstein Shapiro LLP

sweeneye@dicksteinshapiro.com
(202) 420-3477



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