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Second Edition

# The Burdens of Knowledge

## Plan Sponsor Duties and Responsibilities After New Fee Disclosure Regulations

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# Introduction

## The Burdens of Knowledge

The Burdens of Knowledge refers to the increased obligations that responsible fiduciaries have as they become more informed (fiduciaries referenced here are those responsible for ERISA plans). This knowledge improves the fiduciaries' ability to act in the interest of beneficial owners, who in this case are plan participants and beneficiaries.

The increased knowledge also obligates the fiduciary to use that knowledge. The ability to make better decisions with the increased knowledge means that fiduciaries must incorporate the added knowledge and the complexity that this adds into decision making. Fiduciaries may ultimately have to explain how the new knowledge was used to protect the interests of beneficial owners, and if not, why not.

As a prudent person, a fiduciary also has the responsibility to assess the reliability of new information. Such an assessment is an integral part of decision making. The assessment of new information, especially from new sources can be time consuming and burdensome.

Fiduciaries also have the burden of responsibility to inform beneficial owners when material facts are learned so that the beneficial owner may also use the new knowledge to enhance his/her decision making.

This paper is written for fiduciaries that are responsible for retirement plans subject to New Fee Disclosure regulations. Included are specific requirements of these regulations as well as those created by the additional knowledge gained from the disclosures.

## Familiar Terminology

This paper uses familiar terminology to avoid unwieldy language that would be required if precise language was used. The following terms are used throughout this work and when used have the specific meanings given here:

- **Participant** refers to the beneficial owner of an interest in a retirement plan that is subject to one or more of three new disclosure regulations. In this paper, the term Participant includes plan participants and beneficiaries.
- **Plan Sponsor** refers only to the responsible plan fiduciary for ERISA plans subject to any or all three new disclosure regulations. The term Plan Sponsor, as used here, includes responsible plan fiduciaries that are technically not plan sponsors but excludes those who are technically plan sponsors and are not responsible plan fiduciaries.
- **New Fee Disclosures** refer to three regulatory changes affecting ERISA plans that require additional disclosures commencing some time before July 1, 2012. New Fee Disclosures consist of a report issued to the government on form 5500 ("Schedule C"), reports received from covered service providers ("408(b)(2)") and reports issued to Participants ("404(a)(5)").
- **Plan Investments** refer to those investments that are selected and monitored by the Plan Sponsor for use by Participants. Plan Investments exclude investments made available through brokerage windows or other such facilities.

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## Who is Disclosing What to Whom and Why

The New Fee Disclosure regulations explicitly expands the fiduciary responsibilities of Plan Sponsors and increases the responsibilities by virtue of the knowledge gained. Plan Sponsors should not lose sight of these duties and responsibilities in the urgency to meet the deadlines for compliance. Failure of Plan Sponsors to carry out these new duties and responsibilities can have more severe consequences than simply missing a deadline for compliance. While a late disclosure is undesirable and can result in a reprimand, such failures are easily corrected if not severe. On the other hand, failure to carry out fiduciary duties can disqualify an entire plan, punish Plan Sponsors with fines and penalties, and open the door to litigation.

It is essential that these new duties and responsibilities are understood and given the high priority they deserve.

## The New Disclosures

The three New Fee Disclosures are:

- **Schedule C** of form 5500: Certain Plan Sponsors were required to file a revised Schedule C, which reports *actual* fees and expenses to the Department of Labor ("DoL"), Internal Revenue Service ("IRS") and the Pension Benefit Guaranty Corporation ("PBGC").

  The stated purpose for changing Schedule C is that the DoL has concluded that more information should be disclosed on the Form 5500 Annual Return/Report regarding plan fees and expenses.

  The revised Schedule C is applicable to all plans required to file From 5500 (not required for 5500-SF) and went into effect for plan years beginning on or after January 1, 2009.

- **408(b)(2)**: All Plan Sponsors must receive *estimated* fee and expense disclosures from "covered" service providers which include record keepers, broker/dealers, RIAs, advisors and investment managers.

  According to the DoL, the changes to 408(b)(2) are a significant step toward ensuring that pension plan fiduciaries are provided the information they need to assess both the reasonableness of the compensation paid for plan services and potential conflicts of interest that may affect the performance of those services.

The new 408(b)(2) disclosures apply only to defined contribution and defined benefit pension plans[1] and must be made by July 1, 2012. The Website www.ERISAFeeDisclosure.com contains the tool *CSP Determinator* that provides guidance on what service arrangements require a 408(b)(2) disclosure.

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[1] 408(b)(2) regulations apply to employee pension benefit plans or pension plans within the meaning of ERISA section 3(2)(A) (and not described in section 4(b)) of the Act. Regulations do not apply to "simplified employee pension plans" described in section 408(k) of the Internal Revenue Code of 1986 (the Code), "simple retirement accounts" described in section 408(p) of the Code, individual retirement account described in section 408(a) of the Code, or an individual retirement annuity described in section 408(b) of the Code.

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- **404(a)(5)**: All Plan Sponsors of participant directed plans are required to make two types of disclosures of fees and expenses to Participants and eligible employees. The two disclosures are *estimated* investment fees and expenses and Participant rights that are reported annually and *actual* administrative costs that are reported quarterly.

  The estimate stated by the DoL is that over the ten-year period 2012-2021, the present value of the benefits provided by the changes to 404(a)(5) will be approximately $14.9 billion and the present value of the costs will be approximately $2.7 billion.

  The 404(a)(5) regulations apply to any participant-directed individual account plan as defined in section 3(34) of ERISA, for plan years beginning on or after November 1, 2011.

## Covered Service Provider

The New Fee Disclosure regulations introduced the term "Covered Service Provider" to define which firms are required to make disclosures to Plan Sponsors. The three categories of Covered Service Providers are 1) fiduciaries, 2) providers of record keeping and brokerage services or 3) any service providers that receive compensation indirectly from the plan.  See *CSP Determinator* on www.ERISAFeeDisclosure.com for complete details.

# In Summary

The Department of Labor has introduced a new set of regulations aimed at reducing the costs in 401(k) and similar retirement plans. Regulations also seek to ensure that Participants' interests are well served.

The New Fee Disclosure regulations place the major responsibility on the Plan Sponsor and Participants to select appropriate lower cost options and lower fees in that way. The New Fee Disclosures consist of new information, new formats and new sources.

Under the new regulations Plan Sponsors must:

- Receive required disclosures from all Covered Service Providers;
- Use the disclosures to identify unreasonable services and costs then take action to change them;
- Report cost and service information to Participants and respond to their inquiries.

The New Fee Disclosure regulations impose an obligation on Plan Sponsors to perform certain checks and balances in order to identify unreasonable fees charged by service providers. (See *APPENDIX E* for a Fee Disclosure Assessment Example).

## Plan Sponsor Q&A

The following questions and answers provide a brief overview of the major issues that Plan Sponsors face by the introduction of the New Fee Disclosure regulations.

Q: Do Plan Sponsors have additional duties and responsibilities under New Fee Disclosure regulations?

A: Yes, Plan Sponsors must

- Assess the quality and completeness of disclosures
- Evaluate and take appropriate action on the arrangement with each service provider
- Report new information to Participants in prescribed format
- Comply with the specific New Fee Disclosure regulations

Q: Who will carry out these duties? Can they all be passed on to a third party?

A: Many can be delegated but Plan Sponsor must answer to completeness, accuracy and reasonableness of the arrangement with each Covered Service Provider.

Q: What happens if Plan Sponsors don't carry out these duties?

A: Plan Sponsors suffer consequences of a fiduciary breach unless an exemption is obtained by filing a complaint.

Q: How does the exemption work?

A: File a complaint about a failing provider to DoL/IRS within specified time frame.

Q: How does a Plan Sponsor find out who is not complying?

A: The Website www.ERISAFeeDisclosure.com contains the tool *CSP Determinator* that provides guidance on what service arrangements require a 408(b)(2) disclosure.

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Q: What happens if the plan auditor finds there is non compliance?

A: A plan auditor is certain to uncover failure… but discovery may be after the opportunity to file for an exemption.

Q: How does a Plan Sponsor determine if disclosure is complete and accurate?

A: Plan Sponsor must reconcile multiple disclosures, ask Covered Service Providers for additional information such as dollars amounts instead of just rates or percentages, get totals and verify them as well as compare actual costs to estimates provided under 408(b)(2).

Q: How does a Plan Sponsor know if costs are reasonable?

A: Assess whether the plan is successful in meeting its goals and then determine what features are essential to Participants and ask for benchmark costs for those features from service providers or use independent benchmark service to compare the cost of essential features.

Q: Can Participant reports really show zero cost or a cost that is lower than actual?

A: Regulations permit this… but that would be deceptive. Do not accept this discrepancy. On the other hand, costs paid directly by employers are not reported since such costs are not borne by Participants.

Q: How do Plan Sponsors prepare for Participant questions?

A: Become knowledgeable and pre-determine how to respond… use Websites and phone centers offered by service providers. Plan Sponsors should be prepared to answer the most likely questions from Participants:

- Can't you find a plan with lower costs?
- How long have I been paying these costs?
- Is there an alternative to paying these costs?
- Will the costs change in the future?
- What happens if I drop out of the plan?

Q: What should Plan Sponsors do today?

A: All service providers may not be fully aware of the New Fee Disclosure regulations or may be unable to prepare accurate data to meet the deadlines. If you don't know whether your service providers can or will comply… you have to ask today and get an answer in writing. Seek an exemption if no answer is received or if it is unsatisfactory.

Q: How will New Fee Disclosure regulations affect the relationship with your 401(k) providers?

A: Providers who are open and provide meaningful and clear disclosures build trust… providers who burden Plan Sponsors or Participants with complex and confusing disclosures will lose their trust.

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Q: What is the greatest risk for Plan Sponsors from New Fee Disclosures?

A: While a fiduciary breach represents the highest dollar exposure theoretically, the more likely issue is the potential for disgruntled employees to use the information disruptively.

Q: What is the biggest challenge for Plan Sponsors with these new regulations?

A: Plan Sponsors will be responsible for a number of new documents coming from different sources and in different formats. Understanding, evaluating and taking the required action is a daunting task, particularly for small employers.

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# Goals & Objectives of New Fee Disclosure

The expressed view of federal legislators that wrote the requirement for enhanced fee disclosure into the Pension Protection Act of 2006 ("PPA") was simply that Participants' retirements were being eroded by fees that they considered to be excessive. The PPA addressed this erosion by requiring disclosures that would make costs a major factor in vendor selection and choice of Plan Investments.

The disclosures add the Burden of Knowledge to Plan Sponsors, who are therefore pressured to seek lower costs in their retirement plan arrangements. The three New Fee Disclosure regulations combine to create an incentive for Plan Sponsors to act. There is regulatory pressure from the government agencies in the Schedule C reporting. The pressure of fiduciary liability is introduced by 408(b)(2) and the threat of a Participant discord arises from 404(a)(5).

The PPA assigned the DoL the responsibility of writing the regulations that would disclose costs in such a way that competitive pressure would ultimately lower the cost to Participants.

## DoL Goals

In response to the PPA, the DoL has finalized the New Fee Disclosure regulations with the following expressed goals.

### *Schedule C*

Schedule C revisions are intended to *clarify the reporting requirements and improve the information plan officials receive regarding amounts being received by plan service providers*.

### *408(b)(2)*

408(b)(2) intends for Plan Sponsors to ensure …*that arrangements with their service providers are "reasonable" and that only "reasonable" compensation is paid for services*.

### *404(a)(5)*

404(a)(5) is designed so *that workers in this type of plan are given, or have access to, the information they need to make informed decisions.*

## New Standard: No Relief for Existing Arrangements

New regulations often include some form of amnesty or "grandfathering" in which existing practices and agreements are permitted to continue. The New Fee Disclosure regulations have no such provision.

Plan Sponsors must comply and make new arrangements where necessary, regardless of how long old arrangements have been in effect.

This approach causes the effect of the New Fee Disclosures to occur immediately and not spread out over several years or decades.

## Reasonable Compliance

Reliance on a reasonable belief or good faith is sufficient to meet the requirements in several aspects of the New Fee Disclosure regulations. This language raises the question of what constitutes reasonable belief.

Reasonable belief can be substantiated by demonstrating that steps were taken, that would be expected in the normal course of business, to confirm the completeness and accuracy of information.

Examples of the use of reasonableness as a basis for compliance are:

### 408(b)(2)

*(ix) Exemption for responsible plan fiduciary. Pursuant to section 408(a) of the Act, the restrictions of section 406(a)(1)(C) and (D) of the Act shall not apply to a responsible plan fiduciary, notwithstanding any failure by a covered service provider to disclose information required by paragraph (c)(1)(iv) or (vi) of this section, if the following conditions are met:*

> *(A) The responsible plan fiduciary did not know that the covered service provider failed or would fail to make required disclosures and reasonably believed that the covered service provider disclosed the information required by paragraph (c)(1)(iv) or (vi) of this section;*

### 404(a)(5)

*A plan administrator will not be liable for the completeness and accuracy of information used to satisfy these disclosure requirements when the plan administrator reasonably and in good faith relies on information received from or provided by a plan service provider or the issuer of a designated investment alternative.*

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# Enforcement, Penalties & Threats

The New Fee Disclosure regulations contain new mechanisms that are designed to persuade Plan Sponsors and Covered Service Providers to comply and therefore cause a reduction in Participant costs. These internal mechanisms are presented as a group to provide a perspective of the combined effect.

## 408(b)(2) Enforcement

Unless acting in a fiduciary capacity, service providers to ERISA plans are outside the authority of the DoL. The DoL can only regulate the plans themselves, but it is the service providers that are believed to be eroding Participant assets through high fees. In order to achieve the goal of reducing plan costs, the New Fee Disclosure regulations have deputized Plan Sponsors to act as fee regulators, under threat of penalties to the Plan Sponsors themselves.

Plan Sponsors' face the penalties of a fiduciary breach if they fail to carry out the mission of lowering costs. The New Fee Disclosure regulations give Plan Sponsors three ways to avoid the penalties:

- Make the determination that services and costs are successful, necessary and reasonable
- Make improvements by changing service arrangements
- Use an exemption that is obtained by filing a complaint against a service provider

When the Plan Sponsor files a complaint, the IRS, which does have the authority to regulate service providers is brought into the loop.

In this way, the DoL can exert regulatory pressure on entities over which it has no direct jurisdiction. On the other hand, Plan Sponsors can face penalties and other threats if they fail to take advantage of the information that is made available through the New Fee Disclosures.

## Schedule C Penalties

Plan Sponsors must provide complete and accurate information and must otherwise comply fully with the filing requirements of ERISA and the Internal Revenue Code. The DoL and IRS are able to impose penalties on Plan Sponsors for not giving complete and accurate information and for not filing complete and accurate statements and returns/reports.

Examples of penalties are:

1. $1,100 a day for each day a Plan Sponsor fails or refuses to file a complete report.
2. Any individual who willfully violates any provision of Part 1 of Title I of ERISA shall on conviction be fined not more than $100,000 or imprisoned not more than 10 years, or both.
3. A penalty up to $10,000, five (5) years imprisonment, or both, may be imposed for making any false statement or representation of fact, knowing it to be false, or for knowingly concealing or not disclosing any fact required by ERISA.

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## 404(a)(5) Duty

Plan Sponsors have the duty to make disclosures to Participants on a regular and periodic basis, including:

- Participant's rights and responsibilities with respect to the investment of assets held in, or contributed to, their accounts
- Sufficient information regarding the plan, including fees and expenses, and regarding Plan Investments and investment related fees and expenses, in order for Participants to make informed decisions with regard to the management of their individual accounts.

Compliance with 404(a)(5) disclosure regulations is necessary to satisfy this duty, provided that the information contained in such disclosures is complete and accurate.

## Threat of Litigation

In addition to the potential action by regulators, non-compliance also exposes Plan Sponsors to litigation. Several class action lawsuits by Participants against Plan Sponsors are currently pending. The New Fee Disclosure regulations create the opportunity for many more such actions.

Litigants seek ways to reimburse Participants for losses suffered as a result of various breaches of fiduciary duties. To date, litigation has not been very successful for plaintiffs but the efforts continue to recover lost assets from Plan Sponsors and other fiduciaries.

This active threat makes it prudent for Plan Sponsors to protect corporate and personal assets from awards by juries.

# The Responsibility of Knowing

Compliance with the New Fee Disclosure regulation presents extensive new information to Plan Sponsors that adds to the responsibility of being a plan fiduciary. The New Fee Disclosures enable many Plan Sponsors to discover[2]:

### *What Costs Are*

- The total cost of operating the plan
- The cost of record keeping services
- Indirect payments that are routed from the plan to various service providers

### *Services Being Provided*

- The services performed by each service provider
- Services that were thought to be provided but are not and/or are not available

### *The Nature of Relationships*

- Which service providers act in a fiduciary capacity and which do not
- Incentives and other conflicts that are in opposition to the interests of Participants

### *Cost Burdens on Participants*

- The difference in costs for large balance Participants and those with low balances
- Differences between what Participants believe and the actual facts

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[2] The DoL reports in its 408(b)(2) preamble, *"Plan sponsors need comprehensive information on service provider compensation in order to discharge their fiduciary duty and secure good value for their plans and participants. However, only 57 percent of sponsors report that their service provider discloses revenue sharing agreements and investment offsets with both alliances and their own proprietary funds. (See e.g., Deloitte, 401(k) Benchmarking Survey 2008 Edition.)*

*About one-quarter of sponsors are not familiar with revenue sharing arrangements between their investment managers and retirement plan providers (26 percent) and compensation arrangements between retirement plan providers and the intermediary involved in the plan (25 percent) (familiarity was lower among sponsors of smaller plans). (See e.g., Chatham Partners, Looking Beneath the Surface: Plan Sponsor Perspectives on Fee Disclosure (2008).)*

*These findings suggest that gaps in critical information are large and widespread. Some sponsors who lack critical information are aware of the problem and poised to use the information effectively once it is more accessible. Others are less aware, but proactive disclosure will raise awareness for some of these sponsors."*

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## Legal Responsibility versus Participant Expectation

Regulatory compliance can protect Plan Sponsors from enforcement action by regulators but it is insufficient to meet expectations of Participants. The expectation is that the acquired knowledge is used to benefit Participants and does more than improve employee satisfaction. Most significant is that it enhances the relationship with employees by increasing trust and increasing Participant's engagement with the employer.

Meeting Participant expectations also provide an intuitive compass that avoids litigation and enhances the chances of success if litigation does occur.

## Risk of Misinformation

Whether driven by regulatory requirements, or Participant expectation or by workplace efficiency, disclosures must above all not misinform. Misinformed Plan Sponsors or Participants[3] make poor decisions that can affect an entire plan or simply inconvenience a participant.

The concern about misinformation is particularly acute when disclosing new types and new sources of information and when the users are unfamiliar with the data. The New Fee Disclosures and the process to prepare and disseminate them have not had the benefit of several years of experience and refinement. There is therefore every reason to be particularly vigilant.

Plan Sponsors must ensure that the information received and that which is disseminated to the government and to Participants does not misinform and therefore must be complete, accurate, clear, not misleading and in an appropriate context.

## Protection of New Fee Disclosure Regulations

New Fee Disclosure regulations redefine what Plan Sponsors must do to avoid the penalties and consequences of violating ERISA prohibitions. In essence, Plan Sponsors are guilty of ERISA violations unless they comply with the New Fee Disclosure regulations.

**As noted elsewhere in this paper, New Fee Disclosure protections are independent of and do not relieve Plan Sponsors from other ERISA responsibilities[4] or from the requirements of other statutes.**

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[3] As reported in the AARP report, *401(k) Participants' Awareness and Understanding of Fees*, referenced by Congress and the DoL, *"More than eight in ten (83%) participants acknowledged that they actually do not know how much they pay in fees and expenses associated with their own plan."*

[4] See DoL publication, "*Meeting Your Fiduciary Responsibilities*".

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### *408(b)(2)*

Plan Sponsors that comply with 408(b)(2) regulations are considered to have met the obligation to ensure that any contracts or arrangements with service providers are reasonable. Under 408(b)(2), Plan Sponsors have reasonable contracts or arrangements only if:

- Plan Sponsors receive the prescribed disclosures from all Covered Service Providers;
- Receipt is timely, as described in the regulation;
- Disclosures contain the prescribed information;
- Disclosures are considered to be complete and accurate;
- Services are necessary for the establishment or operation of the plan;
- Services produce a successful result for Participants;
- The information is usable in determining if services and costs are reasonable;
- Failing any of the above, Plan Sponsors receive an exemption by filing a complaint with the DoL;
- Plan Sponsors evaluate disclosures and take action to correct any unreasonable services or costs.

### *404(a)(5)*

By complying with 404(a)(5) Plan Sponsors are considered to have taken steps to ensure that Participants are made aware of their rights and responsibilities on a regular and periodic basis with respect to the investment of assets held in, or contributed to, their accounts and are provided sufficient information regarding the plan, including fees and expenses, and regarding designated investment alternatives, including fees and expenses attendant thereto, to make informed decisions with regard to the management of their individual accounts. Plan Sponsors comply with 404(a)(5) only if:

- Participants and eligible employees receive prescribed disclosures;
- Receipt is timely, as described in the regulation;
- Disclosures contain the prescribed information;
- Disclosures are considered to be complete and accurate;
- Disclosures are written in a manner calculated to be understood by the average plan participant;
- Providers of services to the plan and Plan Investments are prudently selected and monitored.

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## Prescribed Responsibilities

Plan Sponsors have a number of responsibilities to fulfill in order to comply with New Fee Disclosure and to receive the protection from the associated penalties. Certain of these responsibilities can be outsourced to an appropriate service provider but others remain with the Plan Sponsor.

Also implied in the regulation is the requirement that an outsourced service provider does not have potential conflicts of interest, such as assessing the reasonableness of its own services or compensation.

Responsibilities that can be outsourced include:

- Preparation and distribution of disclosures.
- Determination if disclosures comply with regulations.
- Obtaining comparative costs and service data to assess reasonableness.
- Assessment of completeness and accuracy of disclosures.
- Determination if services are necessary.
- Determination if disclosures are usable and understandable.
- Responding to Participant inquiries.

Responsibilities that remain with the Plan Sponsor include:

- Determination if services and costs are reasonable
- Renegotiating contracts or arrangements or replacement of service provider.
- Selection and monitoring of service providers.
- Filing complaints and obtaining exemption from DoL.

## Other Applicable Plan Sponsor Responsibilities

As noted elsewhere, the New Fee Disclosure protections are not general releases from responsibilities but apply only to specified duties. The potential for Plan Sponsors and/or service providers to run afoul of other regulations are greatest in the following:

- False and Misleading Statements: The potential for such violations are inherent in the receipt of similar information from multiple sources and then disclosing to Participants and the government.
- Omission of Material Facts: Material costs and services that are disclosed to Plan Sponsors under 408(b)(2) should be conveyed to Participants, in addition to the specific requirements of 404(a)(5).
- Advertising Rules: Broker/dealers and investment advisers must make securities related disclosures and are prohibited from making certain claims. Such violations can occur in the preparation and delivery of New Fee Disclosures.
- Other Prohibited Transactions: Service providers who become fiduciaries by virtue of the services they describe in New Fee Disclosures may engage in activities or receive compensation that represent a fiduciary breach.

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## What Will a Jury Say?

The New Fee Disclosure regulations enable Participants (and their attorneys) to make a compelling case against Plan Sponsors of high cost plans. Litigation against Plan Sponsors is a very likely course to recover unreasonable fees paid by Participants. The judgment as to whether Participants are injured by high cost plans would therefore be made by juries and not by regulators.

Full compliance with regulations do not necessarily indemnify Plan Sponsors from a jury of average citizens if they consider the Plan Sponsors actions to be unfair or unreasonable.

The question that Plan Sponsors should ask is how would each action or failure to act on available information appear to a jury.

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# Balancing Reasonable Cost and Participants Interests

There can be little doubt that the New Fee Disclosures focus attention on costs while making only incidental reference to the total value proposition that those costs represent. Plan Sponsors, however, must take a broader view than the new role of fee regulators.

As fiduciaries, acting in the interest of Participants, Plan Sponsors cannot simply seize the lowest cost alternatives. The responsibility to be loyal to Participants often means bypassing low cost solutions for ones that provide greater value. For example, there may not be a reasonable expectation of high returns from the lowest cost investment option. Another form of value is in the area of Participant service, in which the lowest cost provider may also provide the poorest quality. In neither of these cases would it be appropriate to select the low cost option.

## Demonstrating Sound Judgment

The balance between value and cost is subjective and as such it is important to demonstrate that sound judgment was used and decisions made after careful consideration. Plan Sponsors need to use and then to document a formal decision making process in the exercise of their judgment of reasonableness.

**The easy decision of picking low cost solutions can be as hazardous as failing to comply with the regulations, both being breaches of fiduciary duty.**

## Values Affecting Reasonableness of Costs

Plan Sponsors should evaluate cost in the context of several factors that are valuable to Participants. Some of these factors enhance value, while others may lower the value.

### *Value Enhancers*

The following features, when considered essential, add to the value of a plan. This means that plan costs can be considered reasonable even when the costs exceed standard benchmarks that may not include an economic weighting for these enhancers. The economic value placed on these enhancers is based on the Plan Sponsor's judgment, using the care, prudence, skill and diligence of a prudent person:

- High participation and contribution rates
- Potential future investment return in relation to risk in each Plan Investment
- The quality of services that are valued by Participants such as phone centers and Websites
- Effectiveness of communications and materials
- The availability of services that are considered essential to the success of the plan, such as:
  - Effective Qualified Default Investment Alternatives
  - In-person investment advice to Participants
  - Retirement income alternatives and services
- Quality of investment advice provided to the Plan Sponsor
- Open architecture that permits use of Plan Investments from a wide variety of sources

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### *Value Detractors*

A plan may fall short of meeting the needs of all participants, but still be acceptable. Under these circumstances, Plan Sponsors can consider costs that are at or below standard industry benchmarks to be unreasonable.

The value detractors are areas where the current plan fails to fully meet Participants needs but lower plan costs can compensate for the deficiencies. As with Value Enhancers, the economic value placed on these detractors is based on the Plan Sponsor's judgment, using the care, prudence, skill and diligence of a prudent person.

Frequent value detractors are:

- Low participation and contribution rates
- Restrictions, penalties and difficulty of making changes
- Attention received from service provider… this could be undesirable because it is excessive or could be insufficient
- External factors that reflect on the image and reputation of the service provider

# Plan Sponsor Powers

Concurrent with the burdens of the New Fee Disclosures, Plan Sponsors have new as well as existing powers to operate their plans most effectively for Participants. These powers include the hiring and firing of experts, negotiating fees, changing Plan Investments and filing complaints against service providers.

Plan Sponsors who exert these powers, demonstrate compliance with ERISA and are better able to answer concerns of Participants and provide meaningful explanations. Plan Sponsors who exert these powers can also defend themselves against regulatory actions and/or litigation.

## Hiring & Firing Experts

ERISA regulations permit Plan Sponsors to use a number of experts and service providers that are needed to establish and operate a plan. The common thread in the use of experts and service providers is the need to prudently select and monitor all such third parties. Plan Sponsors are obligated to act when experts or service providers fail to meet reasonable standards. In addition to specific guidelines from the DoL, Plan Sponsors should consider the depth of the organization and contingency plans in the event of problems.

Guidance from the DoL for selection and monitoring to include:

An objective process to assess:

- Qualifications
- Quality of services offered
- Reasonableness of fees charged for the service
- Avoidance of self dealing
- Avoidance of conflicts of interest
- Avoidance of other improper influence

Such a process should take into account:

- Experience and qualifications
- Registration in accordance with applicable federal and/or state securities laws
- Willingness to assume fiduciary status and responsibility under ERISA
- Where applicable, use of generally accepted investment theories

The monitoring of experts and service providers should include a periodic review of:

- Changes in information that served as the basis for the initial selection
- Whether the expert or service provider continues to meet applicable federal and state securities law requirements
- Expert or service provider’s compliance with the contractual provisions of the engagement
- Level of utilization of services in relation to the cost of the services to the plan

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## Negotiating Fees

The regulatory concern about fees is evident in the New Fee Disclosure requirements. Much of the responsibility to detect and reduce high plan costs has been turned over to Plan Sponsors and Participants.

The ability to negotiate fees is an essential expectation of the New Fee Disclosure.

ERISA regulations do not protect service providers from negotiating fees in violation of securities and other laws[5] but do require the Plan Sponsor to change contracts or arrangements to bring unreasonable services or fees into line.

Complexities of securities laws and current business arrangements require fee negotiations to take one or more different forms:

- Unbundling Bundled Pricing. Plans that use one service provider for multiple services under a single fee arrangement may have to price individual components. Note that bundled pricing may sometimes produce lower overall costs.
- Changing Share Classes. Compensation of service providers is often paid by mutual funds that deduct expenses from the Plan Investments. These fees are lowered by changing the Plan Investments from more expensive share classes to less expensive ones.
- Removal of Unnecessary Services. For plans in which the costs of individual services can be separated, fee negotiations may involve evaluating the need for and removal of one or more services from the plan.
- Lowering Prices and Rates. In arrangements that involve direct payments at negotiated rates, the fee negotiation involves finding common ground.

## Changing Plan Investments

Plan Sponsors are ultimately responsible for designating appropriate investments for the plan. This requires continuous monitoring of Plan Investments to determine if and when changes are necessary.

This responsibility is often supported by an investment expert who may advise or alternatively take responsibility for selecting and monitoring the Plan Investments.

## Filing Complaints against Service Providers

The New Fee Disclosure regulations introduce an exemption that protects Plan Sponsors from the liability in the event of a failure to receive proper disclosures. This exemption is only granted if certain procedures are followed and a complaint is filed against a service provider.

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[5] Section 22(d) of the Investment Company Act of 1940 effectively prohibits the negotiation of mutual fund fees and expenses. Negotiation of mutual fund fees and expenses are limited to the selection among share classes that have different pricing.

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The exemption procedure starts with notifying the service provider in writing of a problem. The problem can be any non-compliance with the regulations, including the usability of disclosures. Service providers then have 90 days to correct the problem, after which the Plan Sponsor has 60 days to file for an exemption. The exemption filing identifies the service provider and describes the nature of the problem.

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# Applying Fiduciary Responsibility to New Fee Disclosure

The fiduciary responsibility of Plan Sponsors is an integral part of complying with ERISA. This section explains how the New Fee Disclosure regulations apply to the existing ERISA fiduciary requirements for Plan Sponsors.

ERISA imposes obligations on Plan Sponsors who are responsible for the administration and management of employee benefit plans such as 401(k) plans. As fiduciaries of 401(k) plans, Plan Sponsors are required to observe ERISA's "Exclusive Benefit Rule" and its "Prudent Man Rule". A Plan Sponsor must also administer the plan in accordance with its terms and is subject to ERISA's fiduciary liability and prohibited transaction rules.

## The Exclusive Benefit Rule

ERISA section 404(a)(1)(A) requires that a Plan Sponsor execute plan related duties for the exclusive benefit of Participants and for the purpose of defraying the expenses of administering the plan.

**Plan Sponsors are therefore obligated to apply the knowledge gained from the New Fee Disclosures to improving the success of the plan and/or lowering unreasonable plan expenses.**

Section 403(c) of ERISA states that "the assets of a plan shall never inure to the benefit of any employer and shall be held for the exclusive purposes of providing benefits to Participants in the plan and their beneficiaries and defraying reasonable expenses of administering the plan."

Although the "Exclusive Benefit Rule" is phrased in terms of "never", "solely" and "exclusively", the courts have found that incidental benefits may flow to the Plan Sponsor as long as the primary motivation is to benefit the plan.

**Plan Sponsors must change any arrangement in which the New Fee Disclosure reveals that more than incidental benefits of assets in a plan inure to the Plan Sponsor.**

## The Prudent Man Rule

Under the "Prudent Man Rule" of ERISA section 404(a)(1)(B), a Plan Sponsor must discharge his or her duties with the care, prudence, skill and diligence that would be exercised by a reasonably prudent person who is familiar with such matters. Plan Sponsors may delegate certain responsibilities to experts that have the appropriate skill.

**If Plan Sponsors do not possess the skill to evaluate the reasonableness of New Fee Disclosures, they must select an expert to perform the evaluation and make recommendations.**

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## Complying with the 404(c) Regulations

Under ERISA 404(c) regulations, a Plan Sponsor is relieved of responsibility and liability for a Participant's investment decision only if the Participant has exercised meaningful, independent control over the investment of his account. The regulations specify that for this standard to be met, the Participant must have the opportunity to obtain sufficient information to make informed investment decisions.

**New Fee Disclosure regulations amend existing 404(c) regulations so that they are aligned.**

## Case Law on Misinforming Participants

The duty to disclose material information to Participants has been established in case law.

In the Unisys Savings Plan Litigation the Third Circuit found that "a fiduciary may not materially mislead those to whom duties of loyalty and prudence are owed." Quoting from one of its earlier decisions, the court went on to hold as follows:

[The] duty to inform is a constant thread in the relationship between [Participant] and [Plan Sponsor]; it entails not only a negative duty not to misinform, but also an affirmative duty to inform when the [Plan Sponsor] knows that silence might be harmful.

**This finding of the court requires that costs, such as record keeping, that are disclosed to Plan Sponsors under 408(b)(2) cannot be reported differently to Participants, regardless of the permission to do so granted under 404(a)(5).**

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# Checks & Balances of New Fee Disclosure

The three New Fee Disclosure regulations contain checks and balances that permit a Plan Sponsor to reach a reasonable conclusion regarding the completeness, accuracy and usability of the disclosures. The use of these checks and balances are not prescribed in the regulations but are generally accepted business practices that are consistent with the "Prudent Man Rule".

Failing to use these checks and balances exposes Plan Sponsors to misinformation that should have been detected in the normal course of business.

**Such undetected errors may indicate a failure to use the care, prudence, skill and diligence that is required of Plan Sponsors.**

## Disclosures Should Agree

Much of the data contained in the three different disclosures have logical relationships to each other. At the most basic level, all three disclosures should be reporting similar:

- Total plan assets
- Total fees and expenses
- Number of participants

In addition to this very basic data, there are a number of other variables that should be consistent across disclosures. (See *Appendix A: ERISA Fee Disclosures Reconciliation Worksheet*)

**Plan Sponsors who use these checks and balances to detect discrepancies can initiate corrective steps and obtain an exemption from liability.**

## Providers Should Agree

The New Fee Disclosure regulations require that providers that compensate other providers, report all such payments and receipts. Using this requirement, Plan Sponsors would be expected to identify inaccuracies where paying providers disclosures disagree with providers receiving payments. Plan Sponsors would also be expected to recognize if a provider has failed to deliver a disclosure.

As is the case with the previous example, Plan Sponsors who detect discrepancies can initiate corrective steps and obtain an exemption from liability.

## Estimates Should Match Actuals

Estimates of fees and expenses are required from Covered Providers under 408(b)(2). In addition to determining whether these estimates are reasonable at the time they are made, Plan Sponsors should establish that actual costs remain true to these estimates over time.

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Actual costs are required by Schedule C and the quarterly reporting of 404(a)(5) so plans requiring these disclosures have a ready-made method of comparing estimates to certain actuals, if services providers present data in a comparable format. The actual costs reported should include all the fees and expenses included in the original 408(b)(2) estimates, even in cases where the Schedule C and 404(a)(5) do not explicitly require a cost to be disclosed as an actual.

Other arrangements are necessary for Plan Sponsors that do not file a Schedule C or do not report quarterly participant costs. Such arrangements may require Plan Sponsors to make specific requests for actual costs that match up with the 408(b)(2) estimates.

Note that according to the DoL, "*Service providers also must, upon request, disclose compensation or other information related to their service arrangements that is requested by the responsible plan fiduciary or plan administrator in order to comply with ERISA's reporting and disclosure requirements.*"

## Establishing Reasonable Belief

Plan Sponsors are expected to take routine steps to determine if service providers will or can provide disclosures that can reasonably be relied on. These steps include:

- Requesting a written response from each service provider about its readiness to meet the deadlines associated with the New Fee Disclosures.
- A periodic update on progress and any major delays that may have been encountered.
- Initiating corrective steps if failures do occur or can be expected to occur in order to obtain an exemption.

## Readiness Assessment Questions

The following specific questions help to establish the readiness of various types of service providers:

- How do our fees compare to other plans of our size with similar features?
- Can we eliminate any services to reduce our fees?
- Is your disclosure going to show that you act as a fiduciary?
- Will you provide a summary in dollars of the total annual cost of our plan as well as the cost of each optional feature that we use?
- Are you prepared to handle questions from our employees about their plan costs?
- What methods are available to us to allocate plan costs to participants?
- Is there an additional cost to prepare the employee disclosures?
- Will you provide actual costs that can be compared to estimates given under 408(b)(2)?

# Government Reporting Responsibilities

Changes to Schedule C of Form 5500 (the annual report for employee benefit plans) provide new insights to Plan Sponsors concerning costs associated with plans. This disclosure, however, is only applicable to those plans that are required to file Form 5500.

## Schedule C Requirements

Service providers with compensation of more than $5,000 are required to provide Schedule C for any plans that file Form 5500. This includes compensation paid directly and compensation received indirectly through other service providers.

Providers must associate their compensation with one or more service codes specified by the DoL.

Any relationship of the service provider to any known party in interest to the plan must also be disclosed.

## Duty of the Plan Sponsor

The obligation to complete and file the Schedule C and the responsibility for its accuracy rests with the Plan Sponsor. Service providers are required to cooperate in providing the required information to the Plan Sponsor.

## Applicable Compensation

Schedule C requires the reporting of fees by all who provide services directly to the plan or to any investment vehicle in which ERISA plans invest, whether or not the investment is otherwise subject to ERISA. These non-ERISA investments include:

- Mutual funds
- Hedge funds
- Private equity funds
- Fund of funds

Schedule C requires the reporting of fees paid by the plan, or fees paid by the investment vehicle, or fees paid to plan service providers by an advisor, a transfer agent or a distribution agent, including:

- Management fees paid by mutual fund to investment adviser
- Sub-transfer agency fees paid to broker or to recordkeeper
- Shareholder servicing fees paid to broker or to recordkeeper
- 12b-1 fees, not used to offset other fees
- Account maintenance fees

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All forms of value are considered to be compensation and are therefore reportable on Schedule C, if the compensation is in connection with services provided to the plan. This includes money and other items of value such as gifts, awards or trips.

## Direct Compensation

Direct compensation is defined as payments made by the plan for services to the plan, including:

- Direct payments from a plan account
- Charges to plan forfeiture accounts
- Charges to fee recapture accounts
- Charges to a trust account before allocations to participant accounts
- Charges to participant accounts

Direct compensation does not include payments made to service providers by the Plan Sponsor. If a Plan Sponsor pays a service provider from the Plan Sponsor's own funds, and not from the plan, that payment does not need to be reported on the Schedule C.

## Indirect Compensation

Compensation is indirect if made for services provided to the plan or for a transaction or series of transactions with the plan. Indirect compensation excludes compensation that would have been received had the service not been rendered or the transaction not taken place and that cannot be reasonably associated with services performed or transactions executed on behalf of the plan. Examples of indirect compensation include:

- Finders fees, revenue sharing, 12b-1 fees, sub TA fees
- Float revenue
- Brokerage commissions
- Soft dollar services
- Gifts and entertainment
- Fees and expense reimbursements that are deducted from a Plan Investment and is reflected in a reduction in value of the plan's assets.

## Alternative Reporting

Alternative reporting is an abbreviated form available to service providers who only receive indirect compensation from a Plan Investment.

- Gifts and entertainment and other nonmonetary compensation are not eligible for alternative reporting
- Plan Sponsors must have received written materials that disclosed and described:
    - The existence of the indirect compensation
    - The service provided for the indirect compensation

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- The amount or estimate of the compensation or a description of the formula used to calculate the compensation
- The identity of each party paying and each party receiving the compensation.

## Gifts and Entertainment

Reporting of gifts and entertainment as a form of compensation applies to both Plan Sponsors and service providers

Non-monetary compensation with a value of more than $50 or an aggregate annual value from any one source of more than $100 is reportable on Schedule C.

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# Specific Duties: 408(b)(2)

## Required Disclosures

Information that must be disclosed to Plan Sponsors include:

- A description of each service to be provided
- All direct and indirect compensation expected by the service provider, its affiliates or subcontractors.
- Whether recordkeeping services are to be provided and the attributable compensation, even when no explicit charge for recordkeeping is identified as part of a service contract.
- Whether services are provided as a fiduciary to the plan.

Information must also be disclosed about plan investments and investment options. Investment disclosure obligations are the responsibility of record keepers and brokers who, through a platform or other mechanism, facilitate the investment in various options by Participants.

A service provider must disclose changes as soon as practicable, but no later than 60 days after the provider has knowledge of the change.

See *APPENDIX D –Checklist of Required Disclosures* for full details of requirements.

See *APPENDIX E* for a Fee Disclosure Assessment Example.

## Plan Sponsor Duties

The first duty of the Plan Sponsor under 408(b)(2) is to receive disclosures.

Should a Covered Service Provider fail to make the required disclosure or if a disclosure is incomplete, inaccurate or unusable, the Plan Sponsor is required to take specific actions, and ultimately file a complaint notice to obtain an exemption from liability.

Plan Sponsor's next duty is to determine if the fees and expenses are reasonable for the services being provided and that the services are in fact needed by the plan. The regulation requires that the Plan Sponsor take action if the fees and expenses are not reasonable or if the determination cannot be made.

The required action by the Plan Sponsor if the services, fees and expenses are found to be unreasonable is to re-negotiate the terms of the agreement with the Covered Service Provider or to replace that provider. If the determination cannot be made then the disclosure is considered unusable and the specific actions referenced above are required.

### *How to Determine if Information is Complete and Accurate*

A Plan Sponsor may not be aware of all the information that should be expected but must make a "good faith" effort to obtain all that is needed. Unfortunately, these requirements are new and not yet fully understood by many industry experts, leaving Plan Sponsors with little guidance.

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The Plan Sponsor's "good faith" effort starts with understanding what the regulations require (See *Appendix D –Checklist of Required Disclosures*) and then applying the regulations to the specific situation. This approach can be time consuming and error prone and still may not be compliant with other regulations. The alternative is to use the summary of "Required Disclosures" at the start of this section and use the checks and balances as the "good faith" effort to establish completeness and accuracy.

The 408(b)(2) disclosures must be delivered by July 1, 2012 so that it would be appropriate to determine if delivery is complete and accurate a short time after that date.

**For Completeness, Plan Sponsors should:**

- Check on July 1, 2012 or soon after that fee disclosures were received from each covered service provider to their plan. Covered service providers include any fiduciaries, record keepers, brokerage firms and any firm receiving indirect compensation.
- Check disclosures received to see if other covered service providers are mentioned from whom no disclosure were received.
- Check that all categories of information are included in the disclosure (services provided, fiduciary status, costs, conflicts of interest, etc.)
- Check that the information is clear and usable in determining if services and costs are reasonable and if not request any needed information.

If there are missing fee disclosures, if information is missing or if disclosures are unclear, take the "Specific Corrective Actions" described in the section below.

**For Accuracy. Plan Sponsors should:**

- Compare information provided on disclosures to what is already known.
- Compare information for consistency across multiple providers. For example, if a record keeper reports it expects to pay a TPA $5,000, then the TPA should report that it expects to receive $5,000.
- Compare key information for consistency across multiple types of disclosures. Determine if Schedule C says the same thing as 408(b)(2) and the same as 404(a)(5). The worksheet format in Appendix A is intended to facilitate this process.

If there are inconsistencies, take the "Specific Corrective Actions" described in the section below.

### *How to Determine if Disclosure is Usable*

While usability will depend on the individual making the required assessment, there are objective guidelines that can be used to establish a framework. The guidelines presented here are based on a Plan Sponsor that is able to understand and interpret typical budget or other financial statements.

The first measure of usability is to determine what information will be necessary to make the decision, which in this case is to establish that the plan arrangement is reasonable from the perspective of Participants. The necessary information consists of:

- Annual cost to Participants to operate the plan, including the cost of each designated investment and the cost for each service provider.
- An understanding of what services are being provided. This includes the usage and necessity of those services.
- Fiduciary status of the service provider.

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- Potential conflicts of interest that could be harmful to Participants and methods of protecting Participants from these conflicts.

The second measure is for the Plan Sponsor to decide if help is needed in making this assessment. If the Plan Sponsor is unfamiliar with the information listed above, it is suggested that the assessment be turned over to an expert.

The third measure is the ability to extract the required answers from the disclosure provided. The required answers should be obtainable in less than one hour, without having to seek assistance from the service provider.

The fourth measure applies if the third measure is unsuccessful. In that case a written request for additional information or clarification is made to the applicable service provider.

### *Specific Corrective Actions in the Event of Disclosure Failure*

The DoL prescribed procedure relieves the Plan Sponsor of fiduciary liability in the event that disclosure requirements are not met. This procedure consists of:

- Request needed information in writing
- After 90 days, report failure of service provider to DoL using notice provided
- Replace service provider, if necessary

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# Specific Duties: 404(a)(5)

## Required Disclosures

### *Plan-Related Information*

There are three types of plan-related information that must be disclosed to Participants on or before the date they can first direct their investments, and then again annually:

- General Plan Information, such as an explanation of how to give investment instructions under the plan and a current list of the plan's investment options.
- Administrative Expenses Information, such as fees and expenses for legal, accounting, and recordkeeping services.
- Individual Expenses Information, such as fees and expenses for plan loans, hardship withdrawals, etc.

### *Actual Costs Incurred*

In addition to the plan-related information that must be furnished up front and annually, participants must receive statements, at least quarterly, showing the dollar amount of the plan-related fees and expenses actually charged to or deducted from their individual accounts, along with a description of the services for which the charge or deduction was made.

These specific disclosures may be included in quarterly benefit statements.

### *Investment-Related Information*

Investment-related information must be disclosed to Participants on or before the date they can first direct their investments, and then again annually. Investment related information consists of:

- Performance data
- Benchmark information
- Investment fee and expense information
- Internet Website address for more information
- A glossary

See *APPENDIX D –Checklist of Required Disclosures* for full details of requirements.

## Understandable Disclosures

Disclosures to Participants are intended to support making informed investment decisions, and regulations specifically require that information is understandable by average Participants.

This requires that Plan Sponsors review participant disclosures or have them reviewed and make any changes necessary to make them understandable to participants.

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## Disclosure to Eligible Employees

The Plan Sponsor's duty to provide information to Participants is expanded to include eligible employees before they make investment selections.

There is a "catch-up" provision to make initial disclosures to all non-participating eligible employees. Going forward the disclosure is needed only as employees become eligible.

## Allocating Expenses to Participants

Plan Sponsors must elect a method of allocating plan expenses to each participant to comply with the Actual Cost disclosure requirement of 404(a)(5). The usual alternatives are:

- Percentage based on Participant's account balance
- Pro rata based on specific investments held by each Participant
- Fixed dollar amount for each Participant (per capita)

The Plan Sponsor has the challenge to determine how the cost of record keeping services can be fairly allocated between low balance and high balance participants.

## Selection & Monitoring

The regulation explicitly reaffirms the Plan Sponsor duty to prudently select and monitor all service providers. The requirement includes any additional service providers used to comply with this regulation.

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# How to Measure Reasonableness

The emphasis on determining "reasonableness" is a central theme of the New Fee Regulations. The importance placed on reasonableness requires a uniform approach that can be adopted by a large number of Plan Sponsors. The adoption of a uniform approach will create a de facto standard.

Such an approach is offered here.

## Uniform Approach

(See *APPENDIX E* for a Fee Disclosure Assessment Example).

It is evident that several factors must be considered to determine if plan fees and expenses are reasonable. These factors are grouped into four categories:

- Size of Plan: Economies of scale permits larger plans to be more cost effective than the smaller counterparts.
- Services Provided: Plans elect and use different services and delivery methods that affect costs.
- Quality of Services: High quality service can be considerably more costly.
- Need/Usage: The value or benefit derived from a specific service is another determinant of the reasonableness of its cost.

Using these four categories, Plan Sponsors or experts determine if the fees and expenses are within norms and therefore reasonable. These norms may be based on a narrow universe, such as a particular service provider or specific industry; or norms may be based on national benchmarks.

The choice of norm that is used depends on cost, reliability and availability of data.

## Process for Determination

The determination or reasonableness is based on which features are considered to be in the interest of Participants. The four steps described below should be documented as the basis for the reasonableness determination.

1. **Necessity**: Examine plan features and decide which are essential. Features may be essential for one or more reasons, such as to:
    - Maximize retirement income for employees
    - Meet employee needs and preferences
    - Meet regulatory requirements
    - Comply with contractual obligations
    - Adopt an institutional policy
    - Reduce risk

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2. **Success**: Assess how well the current arrangement serves the essential needs of the plan. **If the current arrangement does not meet the essential needs then it should be considered unreasonable**.
3. **Comparability**: Determine what the costs are for comparable plans with those features considered to be essential. This will rarely produce an exact match so differences in features need to be addressed.
4. **Judgment**: Using the available comparisons, make adjustments for differences between comparable data and the current arrangement. **Costs that are within 20% of comparable data should be considered reasonable.**

New Fee Disclosure regulations require that Plan Sponsors amend or replace unreasonable arrangements.

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# Available Resources

The Plan Sponsor's fiduciary duty to evaluate the reasonableness of plan services and costs and take appropriate actions such as changing the service arrangement and renegotiating fees. Such an evaluation excludes the use of existing service providers to evaluate their own costs. The obvious conflict of interest is made even more egregious if the evaluator benefits from recommendations made to the Plan Sponsor.

Several independent services providers with expertise and data are available to support Plan Sponsors' evaluation. These independent service providers offer services to Plan Sponsors that are able to perform the evaluations themselves (Do-it-yourself Plan Sponsors) and to those who choose to engage a third party evaluator to make recommendations.

## Do-it-yourself Plan Sponsors

Do-it-yourself Plan Sponsors will need access to instructions, data and training to conduct the evaluations.

The DALBAR handbook, *How To Comply With Fee Disclosure, a Plan Sponsors Guide* provides a condensed set of instructions that do-it-yourself plan sponsors to follow.

Recognized Data providers include:

### *Fiduciary Benchmarks*

Fiduciary Benchmarks (FBi) The comprehensive nature of FBi's Benchmarks Reports supports the day-to-day management and oversight of a defined contribution retirement programs. While applications vary based on a plan sponsor's specific needs and objectives - here are three common ones:

- Many plan sponsors will use Benchmarks Reports primarily for fiduciary documentation as part of an annual plan review process.
- Others will rely on Benchmarks Reports as a means to compare their plan to other plans in their industry, possibly for application in labor relations.
- Still others will use Benchmarks Reports to guide their participant education and communication efforts.

**503-546-4909**

http://www.fiduciarybenchmarks.com/Plan_Benefits.html

### *Ann Schleck & Co*

Ann Schleck & Co. Fee BenchmarkerTM is an online tool that compares Advisor / Consultant fees (both commission and fee-for-service) to a database of industry norms for a selected plan size. It's easy to use, and is available on a one-time-use basis or through an annual subscription. In a few simple steps, you receive a comprehensive report comparing your fees to similar retirement practices.

**651-687-0118**

https://www.annschleck.com/networking/sites/250416903/AnnSchleck/pages/fafeebenchmarker.jsp

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### *Training*

Training is being offered by a number of trade groups and professional service firms, typically attorneys and accountants.

## Third Party Evaluator

Audit firms that specialize in ERISA plans are a potential resource for evaluation.

### *DALBAR, Inc.*

DALBAR is a Third Party Evaluator. DALBAR's Fee Disclosure Evaluation and Recommendation service is available to Plan Sponsors. The Fee Disclosure Evaluation and Recommendation service is designed to assist Plan Sponsors to perform the duties called for by the new Federal Regulations regarding fee disclosures in retirement plans.

Plan Sponsors that do not have the expertise, tools or available resources to perform the required evaluation may elect to engage an independent third party evaluator. The evaluator must have no financial interest or compensation that could be influenced by the results of the evaluation. Existing service providers are therefore disqualified as evaluators.

**617-723-6400**

http://www.dalbar.com/Portals/dalbar/Cache/Homepage/FeeDisclosureEvaluationRecommendation.pdf

## Implementation Services

ERISA consultants provide services such as investment selection and monitoring, reviewing plan design, obtaining competitive pricing, vendor selection and conversion management.

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# Appendix A
# Fee Disclosures Reconciliation Worksheet

April 2011

Three ERISA disclosures require that fees and expenses be disclosed. While each disclosure is made to a different party (government, plan fiduciary and participant) and each has different rules, the overarching requirement is that each is reasonably accurate.

The most well accepted method of determining accuracy is to establish that totals of common elements should agree after making adjustments for known differences. The worksheet below identifies the common elements among the three fee disclosures (Schedule C, 408(b)(2) and 404(a)(5) and the metrics that should be used for reconciliation.

This reconciliation is for each plan.

## WORKSHEET

| Reconciling Item | Schedule C | 408(b)(2) | 404(a)(5) | Potential Explanations of Differences |
|---|---|---|---|---|
| Designated investment alternatives | Number of alternatives | Number of alternatives | Number of alternatives | Changes made between reporting time frames |
| Investment Expenses | Total $$ paid | Total estimated $$ | N/A | Normal variance between estimate and actual |
| | N/A | Average expense | Average expense | |
| Total non-investment expense (administration) | Total $$ paid | Total estimated $$ | Total $$ annualized | Changes made between reporting time frames |
| Record keeping cost | Total $$ paid | Total $$ paid | Total $$ annualized | Changes made between reporting time frames |
| Service providers | Number of service providers | Number of service providers | N/A | Changes made between reporting time frames |
| For each service provider | Total $$ paid | Total estimated $$ | N/A | Normal variance between estimate and actual |

**Note**: Eligible Indirect Compensation under Schedule C, Investment Expenses need not be detailed if plan is relying on the alternative reporting option.

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## Appendix B
## 408(b)(2) Fact Sheet

# Fact Sheet

U.S. Department of Labor
Employee Benefits Security Administration
July 15, 2010

## Interim Final Regulation Relating to Improved Fee Disclosure for Pension Plans

***The Employee Retirement Income Security Act (ERISA) requires plan fiduciaries, when selecting and monitoring service providers and plan investments, to act prudently and solely in the interest of the plan's participants and beneficiaries.***

***Responsible plan fiduciaries also must ensure that arrangements with their service providers are "reasonable" and that only "reasonable" compensation is paid for services. Fundamental to the ability of fiduciaries to discharge these obligations is obtaining information sufficient to enable them to make informed decisions about the services, the costs, and the service providers.***

***This interim final rule represents a significant step toward ensuring that pension plan fiduciaries are provided the information they need to assess both the reasonableness of the compensation to be paid for plan services and potential conflicts of interest that may affect the performance of those services.***

### Background

- The Employee Benefits Security Administration (EBSA) is responsible for administering and enforcing the fiduciary, reporting, and disclosure provisions of Title I of the ERISA.
- The agency oversees approximately 708,000 private pension plans, including 483,000 participant directed individual account plans such as 401(k)-type plans.
- In recent years, the way services are provided to employee benefit plans and the way service providers are compensated (e.g., through revenue sharing and other arrangements) have become increasingly complex.
- Many of these changes may have improved efficiency and reduced the costs of administrative services and benefits for plans and their participants. However, the complexity resulting from these changes also has made it more difficult for many plan sponsors and fiduciaries to understand how and how much service providers are compensated.
- Although the Department has issued considerable guidance relating to the obligations of plan fiduciaries in selecting and monitoring service providers, this interim final rule establishes, for the first time, a specific disclosure obligation for plan service providers – a disclosure obligation designed to ensure that ERISA plan fiduciaries are provided the information they need to make better decisions when selecting and monitoring service providers for their plans.
- The Department published a notice of proposed rulemaking and related class exemption in December 2007 and held a public hearing on March 31 and April 1, 2008.

## Overview of Interim Final Service Provider Disclosure Regulation

- The interim final regulation applies only to defined contribution and defined benefit pension plans and focuses on the disclosure of the direct and indirect compensation certain service providers receive. The interim final regulation applies to plan service providers that expect to receive at least $1,000 in compensation in connection with their services and that provide:
  - certain fiduciary or registered investment advisory services;
  - recordkeeping or brokerage services to a participant-directed individual account plan in connection with the investment options made available under the plan; or
  - certain other services for which indirect compensation is received.
- The rule focuses on service providers and compensation arrangements that are most likely to raise questions for plan fiduciaries with respect to the amount of compensation being received by a service provider for plan-related services and potential conflicts of interests that might compromise the quality of those services.
- The interim final regulation also includes a class exemption from the prohibited transaction provisions of ERISA for a plan fiduciary who enters into a contract without knowing that the service provider has failed to comply with its disclosure obligations.

## Disclosure Requirements

### *Disclosure of Services and Compensation*

- Information required to be disclosed by plan service providers must be furnished in writing to the plan fiduciary. The rule does not require a formal written contract delineating the disclosure obligations.
- Information that must be disclosed includes a description of the services to be provided and all direct and indirect compensation to be received by the service provider, its affiliates or subcontractors. Direct compensation is compensation received directly from the plan. Indirect compensation generally is compensation received from any source other than the plan sponsor, the covered service provider, an affiliate, or subcontractor.
- Because certain services and costs are so significant or present the potential for conflicts of interest, information concerning those services and costs must be disclosed without regard to whether services are furnished as part of a bundle or package. For example, service providers must disclose whether they are providing recordkeeping services and the compensation attributable to such services, even when no explicit charge for recordkeeping is identified as part of the service contract.
- Service providers must disclose whether they are providing any services as a fiduciary to the plan.
- Information also must be disclosed about plan investments and investment options. These disclosure obligations are placed on the fiduciaries to investment vehicles that hold plan assets and on recordkeepers and brokers who, through a platform or other mechanism, facilitate the investment in various options by participants in individual account plans, such as 401(k) plans.

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### *Ongoing Disclosure Obligations*

- Changes: A service provider generally must disclose a change to the initial information required to be disclosed as soon as practicable, but no later than 60 days from the date on which the covered service provider is informed of such change.
- Reporting and Disclosure Requirements: Service providers also must, upon request, disclose compensation or other information related to their service arrangements that is requested by the responsible plan fiduciary or plan administrator in order to comply with ERISA's reporting and disclosure requirements.

### *Benefits of Interim Final Regulation*

- The Department estimates that the rule will be economically significant. The non-discounted costs for the first year are estimated to be approximately $153 million.
- The first year costs are attributable to reviewing and analyzing the regulation, conducting a compliance review to ensure that service providers comply with the regulation, and preparing any new disclosures required by the regulation. Costs in the second and subsequent years are expected to fall to an estimated $37 million.
- The Department estimates that benefits would result from reduced time and cost for fiduciaries to obtain compensation information needed to fulfill their fiduciary duties, the discouragement of harmful conflicts of interest, reduced information gaps, improved decision-making by fiduciaries about plan services, enhanced value for plan participants, and increased ability to redress abuses committed by service providers.

## Public Notice and Comment on the Interim Final Regulation

The interim final regulation will be published in the Federal Register on July 16, 2010. The Department invites public comments from interested persons on the regulation by August 30, 2010, and specifically requests input on the feasibility and cost effectiveness of requiring plan service providers furnish to plan fiduciaries a summary disclosure statement as part of the regulation.

Public comments can be submitted electronically by email to e-ORI@dol.gov or by using the Federal eRulemaking portal at www.regulations.gov. Persons interested in submitting comments on paper should send or deliver their comments to: Office of Regulations and Interpretations, Employee Benefits Security Administration, Room N-5655, U.S. Department of Labor, 200 Constitution Ave., N.W., Washington, DC 20210, Attention: 408(b)(2) Interim Final Rule. All comments will be available to the public, without charge, online at www.regulations.gov and www.dol.gov/ebsa, and at the EBSA Public Disclosure Room.

## Effective Date

The final regulation is effective for contracts or arrangements between plans and service providers as of July 16, 2011.

## Contact Information

For questions about the regulation, contact EBSA's Office of Regulations and Interpretations at

(202) 693-8500.

## Appendix C
## 404(a)(5) Fact Sheet

# Fact Sheet

## Final Rule to Improve Transparency of Fees and Expenses to Workers in 401(k)-Type Retirement Plans

***The Department of Labor's Employee Benefits Security Administration (EBSA) today released a final rule that will help America's workers manage and invest the money they contribute to their 401(k)-type pension plans. The rule will ensure: that workers in this type of plan are given, or have access to, the information they need to make informed decisions, including information about fees and expenses; the delivery of investment-related information in a format that enables workers to meaningfully compare the investment options under their pension plans; that plan fiduciaries use standard methodologies when calculating and disclosing expense and return information so as to achieve uniformity across the spectrum of investments that exist among and within plans, thus facilitating "apples-to-apples" comparisons among their plan's investment options; and a new level of fee and expense transparency.***

### Background

- EBSA is responsible for administering and enforcing the fiduciary, reporting, and disclosure provisions of Title I of ERISA.
- The agency oversees approximately 708,000 private pension plans, including 483,000 participant-directed individual account plans such as 401(k)-type plans.
- A "participant-directed plan" is a plan that provides for the allocation of investment responsibilities to participants or beneficiaries.
- An estimated 72 million participants are covered by these participant directed plans, which contain nearly $3 trillion in assets.
- While workers in these plans are responsible for making their own investment decisions, current law does not adequately ensure that all workers are given the information they need or ensure that information, when provided, is furnished in a format useful to workers, particularly information on investment choices including associated fees and expenses.
- In April 2007, EBSA published in the Federal Register a Request for Information (72 FR 20457) soliciting the views, suggestions and comments from participants, plan sponsors, plan service providers and members of the financial community, as well as the public in general, on whether and to what extent rules should be adopted or modified, or other actions should be taken, to ensure that participants and beneficiaries have the information they need to make informed decisions about the management of their individual accounts and the investment of their retirement savings.

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## Overview of Final Rule

- The final rule provides that the investment of plan assets is a fiduciary act governed by the fiduciary standards in ERISA section 404(a)(1)(A) and (B), which require plan fiduciaries to act prudently and solely in the interest of the plan's participants and beneficiaries.
- The final rule also provides that when a plan allocates investment responsibilities to participants or beneficiaries, the plan administrator must take steps to ensure that such participants and beneficiaries, on a regular and periodic basis, are made aware of their rights and responsibilities with respect to the investment of assets held in, or contributed to, their accounts and are provided sufficient information regarding the plan and the plan's investment options, including fee and expense information, to make informed decisions with regard to the management of their individual accounts.
- A plan administrator must provide to each participant or beneficiary certain plan-related information and certain investment-related information. These categories of information are described below.

## Plan-Related Information

The first category of information that must be disclosed under the final rule is plan-related information. This general category is further divided into three subcategories as follows:

### *General Plan Information*

- General plan information consists of information about the structure and mechanics of the plan, such as an explanation of how to give investment instructions under the plan, a current list of the plan's investment options, and a description of any "brokerage windows" or similar arrangement that enables the selection of investments beyond those designated by the plan.

### *Administrative Expenses Information*

- An explanation of any fees and expenses for general plan administrative services that may be charged to or deducted from all individual accounts. Examples include fees and expenses for legal, accounting, and recordkeeping services.

### *Individual Expenses Information*

- An explanation of any fees and expenses that may be charged to or deducted from the individual account of a specific participant or beneficiary based on the actions taken by that person. Examples include fees and expenses for plan loans and for processing qualified domestic relations orders.

The information in these three subcategories must be given to participants on or before the date they can first direct their investments, and then again annually thereafter.

### *Statements of Actual Charges or Deductions*

- In addition to the plan-related information that must be furnished up front and annually, participants must receive statements, at least quarterly, showing the dollar amount of the plan-related fees and expenses (whether "administrative" or "individual") actually charged to or deducted from their individual accounts, along with a description of the services for which the charge or deduction was made. These specific disclosures may be included in quarterly benefit statements required under section 105 of ERISA.

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## Investment-Related Information

The second category of information that must be disclosed under the final rule is investment-related information. This category contains several subcategories of core information about each investment option under the plan, including:

### *Performance Data*

- Participants must be provided specific information about historical investment performance. 1, 5 and 10-year returns must be provided for investment options, such as mutual funds, that do not have fixed rates of return. For investment options that have a fixed or stated rate of return, the annual rate of return and the term of the investment must be disclosed.

### *Benchmark Information*

- For investment options that do not have a fixed rate of return, the name and returns of an appropriate broad-based securities market index over 1-, 5-, and 10-year periods (matching the Performance Data periods) must be provided. Investment options with fixed rates of return are not subject to this requirement.

### *Fee and Expense Information*

- For investment options that do not a have a fixed rate of return, the total annual operating expenses expressed as both a percentage of assets and as a dollar amount for each $1,000 invested, and any shareholder-type fees or restrictions on the participant's ability to purchase or withdraw from the investment.
- For investment options that have a fixed rate of return, any shareholder-type fees or restrictions on the participant's ability to purchase or withdraw from the investment.

### *Internet Website Address*

- Investment-related information includes an internet Web site address that is sufficiently specific to provide participants and beneficiaries access to specific additional information about the investment options for workers who want more or more current information.

### *Glossary*

- Investment-related information includes a general glossary of terms to assist participants and beneficiaries in understanding the plan's investment options, or an Internet Web site address that is sufficiently specific to provide access to such a glossary.

## Comparative Format Requirement

Investment-related information must be furnished to participants or beneficiaries on or before the date they can first direct their investments, and then again annually thereafter. It also must be furnished in a chart or similar format designed to facilitate a comparison of each investment option available under the plan. The final rule includes, as an appendix, a model comparative chart, which when correctly completed, may be used by the plan administrator to satisfy the rule's requirement that a plan's investment option information be provided in a comparative format.

## Miscellaneous

- The rule provides plan administrators protection from liability for the completeness and accuracy of information provided to participants if the plan administrator reasonably and in good faith relies upon information provided by a service provider.
- After a participant has invested in a particular investment option, he or she must be provided any materials the plan receives regarding voting, tender or similar rights in the option.

- Upon request, the plan administrator must also furnish prospectuses, financial reports and statements of valuation and of assets held by an investment option.
- The general disclosure regulation at 29 CFR § 2520.104b-1 applies to material furnished under this regulation, including the safe harbor for electronic disclosures at paragraph (c) of that regulation.
- The final rule would also make conforming changes to the disclosure requirements for plans that elect to comply with the existing ERISA section 404(c) regulations.

## Economic Benefits of the Final Rule

- The Department estimates that the rule will be economically significant.
- The anticipated cost of the rule is $425 million in 2012 (2010 dollars), arising from legal compliance review, time spent consolidating information for participants, creating and updating websites, preparing and distributing annual and quarterly disclosures, and material and postage costs to distribute the disclosures.
- A significant benefit of this rule is that it will reduce the amount of time participants spend collecting fee and expense information and organizing the information in a format that allows key information to be compared; this time savings is estimated to total nearly 54 million hours valued at nearly $2 billion in 2012 (2010 dollars).
- Over the ten-year period 2012-2021, EBSA estimates that the present value of the benefits provided by the final rule will be approximately $14.9 billion and the present value of the costs will be approximately $2.7 billion.

## Contact Information

For questions about the rule, contact EBSA's Office of Regulations and Interpretations at 202-693-8500.

This fact sheet has been developed by the U.S. Department of Labor, Employee Benefits Security Administration, Washington, DC 20210. It will be made available in alternate formats upon request: Voice phone: 202.693.8664; TTY: 202.501.3911. In addition, the information in this fact sheet constitutes a small entity compliance guide for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

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# Appendix D
# Checklist of Required Disclosures

## 408(b)(2) –Disclosures to Plan Sponsors

### *(A) Services.*

A description of the services to be provided to the covered plan.

### *(B) Status.*

If applicable, a statement that the covered service provider, an affiliate, or a subcontractor will provide, or reasonably expects to provide, services as a fiduciary; and, if applicable, as an investment adviser registered under either the Investment Advisers Act of 1940 or any State law.

### *(C) Compensation.*

**(1) Direct compensation.**

A description of all direct compensation, either in the aggregate or by service, that the covered service provider, an affiliate, or a subcontractor reasonably expects to receive in connection with the services described.

**(2) Indirect compensation.**

A description of all indirect compensation that the covered service provider, an affiliate, or a subcontractor reasonably expects to receive in connection with the services described, including identification of the services for which the indirect compensation will be received and identification of the payer of the indirect compensation.

**(3) Compensation paid among related parties.**

A description of any compensation that will be paid among the covered service provider, an affiliate, or a subcontractor, in connection with the services described if it is set on a transaction basis (e.g., commissions, soft dollars, finder's fees or other similar incentive compensation based on business placed or retained) or is charged directly against the covered plan's investment and reflected in the net value of the investment (e.g., Rule 12b-1 fees); including identification of the services for which such compensation will be paid and identification of the payers and recipients of such compensation (including the status of a payer or recipient as an affiliate or a subcontractor). Compensation must be disclosed regardless of whether such compensation also is disclosed elsewhere. This paragraph shall not apply to compensation received by an employee from his or her employer on account of work performed by the employee.

**(4) Compensation for termination of contract or arrangement.**

A description of any compensation that the covered service provider, an affiliate, or a subcontractor reasonably expects to receive in connection with termination of the contract or arrangement, and how any prepaid amounts will be calculated and refunded upon such termination.

### *(D) Recordkeeping services.*

Without regard to other disclosure of compensation, if recordkeeping services will be provided to the covered plan--

> (1) A description of all direct and indirect compensation that the covered service provider, an affiliate, or a subcontractor reasonably expects to receive in connection with such recordkeeping services; and
>
> (2) If the covered service provider reasonably expects recordkeeping services to be provided, in whole or in part, without explicit compensation for such recordkeeping services, or when compensation for recordkeeping services is offset or rebated based on other compensation received by the covered service provider, an affiliate, or a subcontractor, a reasonable and good faith estimate of the cost to the covered plan of such recordkeeping services, including an explanation of the methodology and assumptions used to prepare the estimate and a detailed explanation of the recordkeeping services that will be provided to the covered plan. The estimate shall take into account, as applicable, the rates that the covered service provider, an affiliate, or a subcontractor would charge to, or be paid by, third parties, or the prevailing market rates charged, for similar recordkeeping services for a similar plan with a similar number of covered participants and beneficiaries.

### *(E) Manner of receipt.*

A description of the manner in which the compensation will be received, such as whether the covered plan will be billed or the compensation will be deducted directly from the covered plan's account(s) or investments.

### *(F) Investment disclosure--fiduciary services.*

In the case of a fiduciary to an investment contract the following additional information with respect to each investment contract, product, or entity that holds plan assets and in which the covered plan has a direct equity investment, and for which fiduciary services will be provided pursuant to the contract or arrangement with the covered plan, unless such information is disclosed to the responsible plan fiduciary by a covered service provider providing recordkeeping services or brokerage services--

> (1) A description of any compensation that will be charged directly against the amount invested in connection with the acquisition, sale, transfer of, or withdrawal from the investment contract, product, or entity (e.g., sales loads, sales charges, deferred sales charges, redemption fees, surrender charges, exchange fees, account fees, and purchase fees);
>
> (2) A description of the annual operating expenses (e.g., expense ratio) if the return is not fixed; and
>
> (3) A description of any ongoing expenses in addition to annual operating expenses (e.g., wrap fees, mortality and expense fees).

### *(G) Investment disclosure--recordkeeping and brokerage services.*

> (1) In the case of a recordkeeping or brokerage service provider, the additional information described in paragraph (F)(1) through (3) above, with respect to each designated investment alternative for which recordkeeping services or brokerage services will be provided.

(2) A covered service provider may comply with this paragraph by providing current disclosure materials of the issuer of the designated investment alternative that include the information, provided that such issuer is not an affiliate, the disclosure materials are regulated by a State or federal agency, and the covered service provider does not know that the materials are incomplete or inaccurate.

## 404(a)(5) –Disclosures to Participants

### *(c) Disclosure of plan-related information.*

**(1) General.**

(i) On or before the date on which a participant or beneficiary can first direct his or her investments and at least annually thereafter:

(A) An explanation of the circumstances under which participants and beneficiaries may give investment instructions;

(B) 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;

(C) 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;

(D) An identification of any designated investment alternatives offered under the plan;

(E) An identification of any designated investment managers; and

(F) 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.

(ii) If there is a change to the information, 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 such 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 of such change must be furnished as soon as reasonably practicable.

**(2) Administrative expenses.**

(i)(A) On or before the date on which a participant or beneficiary can first direct his or her investments and at least annually thereafter, an explanation of any fees and expenses for general plan administrative services (e.g., legal, accounting, recordkeeping), 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.

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(B) If there is a change to the information, 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 such 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 of such change must be furnished as soon as reasonably practicable.

(ii) At least quarterly, a statement that includes:

(A) 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 such services;

(B) A description of the services to which the charges relate (e.g., plan administration, including recordkeeping, legal, accounting services); and

(C) 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, Rule 12b-1 fees, sub-transfer agent fees).

### (3) Individual expenses.

(i)(A) On or before the date on which a participant or beneficiary can first direct his or her investments and at least annually thereafter, 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 qualified domestic relations orders, fees for investment advice, fees for brokerage windows, commissions, front or back-end loads or sales charges, redemption fees, transfer fees and similar expenses, and optional rider charges in annuity contracts) and which are not reflected in the total annual operating expenses of any designated investment alternative.

(B) If there is a change to the information, 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 such 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 of such change must be furnished as soon as reasonably practicable.

(ii) At least quarterly, a statement that includes:

(A) 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

(B) A description of the services to which the charges relate (e.g., loan processing fee).

### (4) Disclosures on or before first investment.

The requirements 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.

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## *(d) Disclosure of investment-related information.*

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:

### (1) Information to be provided automatically.

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—

**(i) Identifying information.**

Such information shall include:

(A) The name of each designated investment alternative; and

(B) 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).

**(ii) Performance data.**

(A) For designated investment alternatives with respect to which the return is not fixed, the average annual total return of the 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; and

(B) 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. 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 required under this section.

**(iii) 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, 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.

**(iv) Fee and expense information.**

(A) For designated investment alternatives with respect to which the return is not fixed:

(1) 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);

(2) The total annual operating expenses of the investment expressed as a percentage (i.e., expense ratio), calculated in accordance with paragraph (h)(5) of this section;

(3) 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 paragraph (2) above;

(4) A statement indicating that fees and expenses are only one of several factors that participants and beneficiaries should consider when making investment decisions; and

(5) 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.

(B) 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.

**(v) Internet Web site address.**

An Internet Web site address that is sufficiently specific to provide participants and beneficiaries access to the following information regarding the designated investment alternative:

(A) The name of the alternative's issuer;

(B) The alternative's objectives or goals in a manner consistent with Securities and Exchange Commission Form N-1A or N-3, as appropriate;

(C) 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;

(D) The alternative's portfolio turnover rate in a manner consistent with Securities and Exchange Commission Form N-1A or N-3, as appropriate;

(E) The alternative's performance data described in paragraph (d)(1)(ii) of this section updated on at least a quarterly basis, or more frequently if required by other applicable law; and

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(F) The alternative's fee and expense information described in paragraph (d)(1)(iv) of this section.

**(vi) 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.

**(vii) 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 in paragraph (i)(2)(i) through (i)(2)(vii) of this section with respect to the annuity option, to the extent such information is not otherwise included in investment-related fees and expenses.

**(viii) Disclosures on or before first investment.**

The requirement to provide information to a participant or beneficiary on or before the date on which the 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.

## (2) Comparative format.

(i) Furnish the information described in this section in a chart or similar 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, and that includes:

(A) 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;

(B) A statement that additional investment-related information (including more current performance information) is available at the listed Internet Web site addresses; and

(C) A statement explaining how to request and obtain, free of charge, paper copies of the information required to be made available on a Web site.

(ii) Nothing in this section 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.

## (3) Information to be provided subsequent to investment.

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.

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### (4) Information to be provided upon request.

Furnish to each participant or beneficiary, either at the specified times, or upon request, the following information relating to designated investment alternatives—

(i) 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;

(ii) 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;

(iii) A statement of the value of a share or unit of each designated investment alternative as well as the date of the valuation; and

(iv) A list of the assets comprising the portfolio of each designated investment alternative and the value of each such asset (or the proportion of the investment which it comprises).

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# Appendix E
## 408(b)(2) Fee Disclosure Assessment Example

This example provides a framework for making the required assessments of the 408(b)(2) fee disclosure. It should be used in conjunction with the handbook "*How To Comply With Fee Disclosure, a Plan Sponsors Guide*" (Available on www.DALBAR.com.) This table shown here provides the documentary evidence to establish that a prudent process was used in making the determinations and taking the actions indicated.

| | Covered Service Provider: | ABC Record Keeping Company | |
|---|---|---|---|
| | Date of Assessment: | July 15, 2012 | |
| | | Assessment | Explanation/Comment |
| Completeness, Accuracy and Usability | Disclosure is Complete: | Yes | This disclosure contains a description of services provided, fiduciary status, costs and how they are computed and describes possible conflicts of interest. |
| | Disclosure is Accurate: | Yes | Total assets, number of participants and total cost is consistent with totals from Schedule C and 404(a)(5) participant disclosure (after adjustments). Disclosure from DEF Investment Services and MNO Plan Advisors are consistent with this disclosure. |
| | Disclosure is Understandable: | Yes | Very clear presentation, including a summary containing essential information. |
| | Disclosure is Usable: | Yes | No difficulty finding all needed information in a form that can be used directly. |
| | Plan Assets in Designated Investments: | $306,452,980 | Provided in disclosure as of 11/30/2011 |
| | Number of Participants: | 727 | Provided in disclosure as of 11/30/2011 |
| | Total Annual Cost: | $1,135,254 | Provided in disclosure as of 11/30/2011 |
| | Annual Cost per Participant: | $1,562 | Provided in disclosure as of 11/30/2011 |
| Success | Participation Rate: | 73% | Obtained from service provider's Website |
| | Deferral Rate: | 4.8% | Obtained from service provider's Website |
| | % of Participants Projected to Achieve Goal: | 56% | Obtained from service provider's Website |

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| | Covered Service Provider: | ABC Record Keeping Company | |
|---|---|---|---|
| | Date of Assessment: | July 15, 2012 | |
| | | Assessment | Explanation/Comment |
| Necessity | Services Needed: | 5 | 1. Maintain records of Participant accounts and transactions<br>2. Phone center service for Participants and Plan Sponsors<br>3. Maintain Website for Participants and Plan Sponsors<br>4. Develop and prepare educational and enrollment materials<br>5. Conduct educational and enrollment meeting for Participants |
| | Quality of Service: | Very High | Positive reaction by participants and no complaints received.<br>Service provider has top rated Website. |
| | Fiduciary Status: | Non Fiduciary | Services do not include any that require fiduciary status |
| Comparability | Comparison with other source(s) | $1,019,500 | From proposal made in 2007 |
| | Percentage Difference: | 10.2% | The difference is considered reasonable based on the age of the proposal. |
| | Comparable Cost/source: | $1,487,320 | Calculated from purchased benchmarks using the asset size of this plan |
| | Percentage Difference: | -31.0% | The plan costs are considerable lower that comparable plans |
| Judgment | Other Service Providers Referenced: | 4 | 1. DEF Investment Services<br>2. GHI Trust Company<br>3. JKL Plan Administrators<br>4. MNO Plan Advisors |
| | Potential Conflicts of Interest: | None | Disclosures revealed no potential conflicts of interest. |
| | Method of Resolving Conflicts of Interest: | N/A | |
| | Determination of Reasonableness: | Reasonable | Based on the foregoing, necessary services, fiduciary status and costs are acceptable. |
| | Action Taken: | None | No action is necessary |
| | Performed By: | John Smith | Vice President, Finance |